



August 28, 2009

MEMORANDUM TO CLIENTS

Re: D.C. Circuit Vacates FCC's 30% Cable Subscriber Cap

Today, a unanimous 3-0 panel of the United States Court of Appeals for the District of Columbia ("D.C. Circuit") invalidated the FCC's latest attempt to impose a horizontal ownership cap of 30% on cable television operators. The Court found that there was "overwhelming evidence" of the "dynamic nature of the communications marketplace" at both the programming and service distribution levels. Accordingly, the Court determined that "it was arbitrary and capricious for the Commission to conclude that a cable operator serving more than 30% of the market poses a threat either to competition or to diversity in programming."

The D.C. Circuit's ruling marked the second time that court has invalidated a 30% cable subscriber cap, following its decision in 2001 to invalidate the cap on the grounds that the FCC had not properly accounted for increased competition from Direct Broadcast Satellite (DBS) providers. In 2007, in response to the 2001 decision, the Commission re-adopted the 30% cap on the grounds that it was necessary to prevent a single cable operator from having the power to cause a cable programming network to fail on account of the operator's refusal to carry the network. The 2007 FCC Order purposely did not take into account the impact of DBS competition, claiming that DBS competition was not significant, and in any event would be "difficult" to account for. This reasoning prompted Comcast and a coalition of other cable interests to ask the D.C. Circuit to overturn the FCC's 30% cap.

The Court harshly criticized the Commission for again ignoring the significance of DBS competition, stating that the FCC's "dereliction [was] particularly egregious." The Commission argued that DBS competition was insignificant because: 1) the cost of switching from cable to DBS was prohibitively high; 2) cable operators offered telephone and internet services that DBS did not; 3) customers would be reluctant to switch to DBS without having already consumed its product; and 4) competition from DBS would not assist a network that suffered from a lack of financing due to lack of carriage with the largest cable operator. The Court dismissed with ease the four FCC-proffered reasons for failing to take into account DBS, finding that the Commission's rationales were merely speculative, and often contradicted by clear record evidence. For instance, the Court labeled the "switching cost" argument "feeble" in light of record evidence demonstrating that 50% of DBS customers had switched from cable to DBS. Similarly, the Court noted that DBS companies were now offering telephone and internet service by partnering with local phone companies. Moreover, the Court found that an upstart network would not have trouble securing financing if it obtained carriage on DBS, which constitutes more than 30% of the video programming provider marketplace.

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While the D.C. Circuit's 2001 decision merely remanded the 30% cap to the Commission for reconsideration, in today's decision the Court had no trouble vacating the rule on the ground that "the Commission either cannot or will not fully incorporate the competitive impact of DBS and fiber optic companies into its open field model." If the rule was kept in place to give the Commission a third chance to support it, the Court found that the rule "would continue to burden [cable operator] speech protected by the First Amendment."

In response to the D.C. Circuit's decision, FCC Chairman Julius Genachowski stated that "FCC staff is currently reviewing the Court's decision with respect to the limit previously adopted and the Commission will take this decision fully into account in future action to implement the law." Thus, Chairman Genachowski has left open the possibility that the Commission will try once again to establish a horizontal ownership limit.

We would be pleased to respond to any questions regarding this matter.

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