CABLE TV: RESTRAINING PRICES BY COMPETITION, NOT RE-REGULATION

Cable television has become a major medium, bringing information and entertainment into 62 percent of American homes. This apparently is tempting Congress to mess with cable TV. Ostensibly concerned over rising prices charged by most local cable companies, Congress soon will act on legislation to re-regulate cable TV rates. Rather than lowering prices, however, this re-regulation would raise costs for consumers and reduce the quality of service and variety of programs offered. Instead of regulating rates, an approach that failed in the past, Congress and the Administration should try to remove barriers to competition imposed by state and local governments and by Congress itself. Allowing firms to compete for customers is the proven way to provide consumers better service and lower prices.

The current rules of the Federal Communications Commission allow local governments to regulate local cable rates only in communities where there are fewer than six over-the-air TV stations or fewer than two multichannel providers, such as a satellite broadcast system or competing cable service. Under these FCC rules, 61 percent of America's cable systems, serving 34 percent of all TV viewers, can be regulated. Under present law, meanwhile, only local governments regulate cable TV rates. This local control of cable TV would be transferred to the federal government by the "Cable Television Consumer Protection Act of 1991" (S. 12), introduced in the Senate by John Danforth, the Missouri Republican. The bill would impose federal rate regulation in any community in which there are not at least two multichannel video competitors available to a majority of homes; each of these competitors would have to have, moreover, at least 15 percent of the market. Since only a handful of communities have more than one multichannel provider, virtually all local cable markets would be subject to regulation by Washington.

The Bush Administration has threatened to veto S. 12. A few Republican senators, however, are working on a compromise bill that would be little better than S. 12. The Administration should reject this compromise.

Lack of Competition. Proposals to re-regulate cable TV have been prompted by concern over the seemingly sharp rise in cable rates since the federal government deregulated rates in 1986. According to the General Accounting Office, for example, average cable rates rose 39 percent during the first three years following deregulation. This rise was not unexpected, however, since regulation had kept rates well below the rate of inflation before 1986. Adjusting for inflation, the price per channel has increased only slightly if at all. The number of channels offered, moreover, has increased since deregulation. Where rates are high, the problem seems to be not lack of regulation, but lack of competition.

Some 99.5 percent of the cities that have cable have only one provider, usually because local governments restrict market entry. Sometimes local governments confer explicitly exclusive franchises and thus explicitly prohibit entry by other would-be service providers. In most instances, however, franchises are nominally available to more than one firm but are so difficult to get and have so many conditions attached to them, that effectively only one firm can obtain a franchise. Nine states have enacted legislation making it even more difficult for a second firm to obtain a franchise. And even where a franchise is not required because no public rights of way are crossed, cities have sued or changed their zoning ordinances in an effort to keep new entrants out of the market.

Cities that have done this include Chicago, Dallas, Los Angeles, New York, and Washington, D.C. Government-imposed barriers rather than economic factors are the true source of cable's monopoly status, and are the true cause of such pricing problems as may exist.

Cutting Costs. There are some fifty local jurisdictions, including Cleveland, Allentown (Pennsylvania), Orlando, Omaha, and Sacramento, that allow competition, with two and sometimes three cable TV providers serving the same geographic area. Several studies have found that prices in these markets for basic cable service are about 18 percent lower, or a little over $3 per month on average, than they are in markets where government prevents competition. Cable companies in competitive markets also tend to offer more channels than those with government-granted monopolies, 21 percent more on average. This makes the price per channel almost 33 percent lower in communities that allow competition. These data indicate that the real problem has not been the deregulation of cable rates in 1986 but the absence of competition.

Historical evidence suggests that rate regulation is not very effective at holding down prices. Although cable TV rates grew slower than the rate of inflation before cable deregulation in 1986, some 94 percent of all rate increase requests were granted in full by local governments. Since cities typically collect 5 percent of cable firms' gross revenues as franchise fees, it was in the cities' interest to grant rate increases. At the same time, the ability to deny or delay a rate increase enabled local politicians to extract valuable political concessions from cable companies, such as coverage of city council meetings, "local origination" shows extolling the mayor's new programs, "public access" programming that paying customers rarely watch, and even outright campaign contributions. Rather than limiting cable TV prices, a return to rate regulation would benefit mainly politicians.

At the same time, by limiting cable companies' prices, regulation would tend to limit the quality and expansion of service. If their revenues would be capped, cable firms could maximize their profits only by holding down their costs, for example, by not upgrading their equipment or adding new channels. By making cable markets less profitable, moreover, regulation would undermine the incentive for technological innovations that would enable new firms to enter the market in competition with existing cable providers.

Ending the Artificial Monopoly. The best way to hold down cable rates while maintaining or even expanding service is to remove cable's artificial monopoly status and to allow competition. Direct competition by a second or third cable company often will result. Even where it is impractical or inconvenient to string wires on utility poles or to dig up city streets to lay underground cable, local telephone companies, which already have their own sets of wires in place, could deliver video signals to the home. The technology for this promising alternative already exists, but federal law prohibits the telephone companies from offering such service.

Other technologies also can spur competition with cable companies. Satellite dishes can receive signals which are then sent over wires on private land, usually to residents of large apartment complexes. Such "private cable" systems have already been installed in parts of Chicago, Dallas, and New York. "Wireless cable," another alternative, uses microwaves to send signals to an antenna on the roof of the customer's home. Under a third approach, called "DBS" (for Direct Broadcast Satellite), about 600,000 homes in Britain receive broadcasts direct from a satellite.

The current legislation being considered by Congress or any "compromise" regulation bill will harm consumers. George Bush and Congress would do well to point out that local governments can help consumers by removing restrictions on competition. And Bush and Congress can help as well by removing restrictions on cable services provided by telephone companies. No kind or amount of regulation will help consumers. Only competition will.

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