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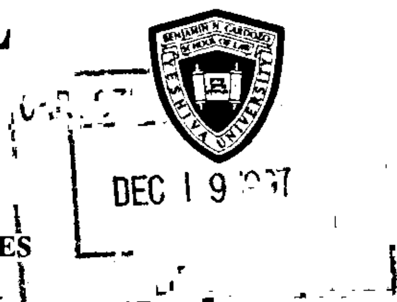

ARTICLES

The *Red Lion* of Cable, and Beyond? — *Turner Broadcasting v. FCC* .... *Laurence H. Winer*

Reflecting the Best of Our Aspirations: Protecting Modern and Post-Modern Architecture .... *Gregory A. Ashe*

THE JURISPRUDENCE OF RATINGS SYMPOSIUM PART I

On the Plurality of Ratings .... *Diane Roberts*

Motion Picture Ratings in the United States .... *Richard M. Mosk*

Reflections on the Ratings Craze .... *Senator Joseph Lieberman*

THE FOURTH ANNUAL HERBERT TENZER DISTINGUISHED LECTURE IN INTELLECTUAL PROPERTY

Copyright Without Borders? Choice of Forum and Choice of Law for Copyright Infringement in Cyberspace .... *Jane C. Ginsburg*

NOTES

The Repeal of the Financial Interest and Syndication Rules: The Demise of Program Diversity and Television Network Competition? .... *Marc L. Herskovitz*

Deaccession: Not Such a Dirty Word .... *Jason R. Goldstein*

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THE REPEAL OF THE FINANCIAL INTEREST AND SYNDICATION RULES: THE DEMISE OF PROGRAM DIVERSITY AND TELEVISION NETWORK COMPETITION?

INTRODUCTION

On January 4, 1996, shareholders of the Walt Disney Company approved the $19 billion purchase of Capital Cities/ABC[1] and ushered in what may turn out to be a new era in the television broadcasting industry. Until recently, creating a media behemoth such as this would have invited the close scrutiny of the Federal Communications Commission ("FCC"), armed with concerns for the protection of the public interest in maintaining market competition.[2] This is no longer the case. With the repeal of the Financial Interest and Syndication Rules ("fin-syn")[3] on September 21, 1995,[4] and the Prime Time Access Rule ("PTAR"),[5] which expired

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[1] *See Disney Wins Holder Votes For Capital Cities Purchase*, WALL ST. J., Jan. 5, 1996, at B12. The deal was structured such that Disney and ABC's parent company, Capital Cities, will become wholly owned subsidiaries of a holding company named "New Disney." Holders of Capital Cities stock will receive the option to convert their stock into $65 plus one share of Disney's stock, or the equivalent in all cash or all stock. *See* THE WALT DISNEY COMPANY, NOTICE OF SPECIAL MEETING OF STOCKHOLDERS—JOINT PROXY STATEMENT/PROSPECTUS 1, (Nov. 13, 1995) [hereinafter DISNEY PROSPECTUS].

[2] The Communications Act of 1934, 47 U.S.C. § 151 (1994), *as amended by* Telecommunications Act of 1996, Pub. L. No. 104-104, 110 Stat. 56 (codified as amended in scattered sections of 47 U.S.C.), granted the FCC the "authority over the use of the electromagnetic spectrum to propagate communications signals." Schurz Communications, Inc. v. FCC, 982 F.2d 1043, 1048 (7th Cir. 1992). The 1934 Act "provides no guidance for the exercise of this authority other than that the [FCC] is to act in accordance with the *public interest*, convenience, or necessity." *Id.* (emphasis added). Thus, with the blessing of the Supreme Court, the FCC has used this authority to closely regulate network activities by conditioning the renewal of broadcast licenses on the "networks' accepting constraints intended to maximize the [FCC's]' conception of the social benefits of broadcasting." *Id.* The FCC has justified the imposition of controls over the networks by declaring that "[d]iversity of programs and development of diverse and antagonistic sources of program service are essential to the broadcast licensee's discharge of his duty as trustee for the public in the operation of his channel." Amendment of Part 73 of the Commission's Rules and Regulations with Respect to Competition and Responsibility in Network Television Broadcasting, Report and Order, 23 F.C.C.2d 382, ¶ 37, at 400 (1970) [hereinafter 1970 Order], *aff'd sub nom.* Mt. Mansfield Tel., Inc. v. FCC, 442 F.2d 470 (2d Cir. 1971).

[3] The fin-syn rules were codified at 47 C.F.R. § 73.658(j) (1970). *See also* 1970 Order, 23 F.C.C.2d ¶¶ 27-32, at 397-99. The fin-syn rules will be further discussed *infra* in part I of this Note, but they may be summarily described as being designed to eliminate the networks from distribution and profit sharing in domestic syndication and to restrict their activities in foreign markets to distribution of programs of which they are the sole producers. *Id.* ¶ 28, at 397-98. The rules were to take effect September 1, 1971, in order that the networks should have "at least a year to allow for orderly phase out of their domestic syndication and foreign distribution activities." *Id.* ¶ 34, at 399.

[4] Network Financial Interest and Syndication Rules, 60 Fed. Reg. 48,907 (1995) (final rule repealing fin-syn). The Final Rule is a synopsis of the Report and Order adopted by the FCC on August 29, 1995, wherein the FCC accelerated the repeal of the fin-syn rules

on August 30, 1996,[6] the FCC has decided that the television industry will be better served with less regulation. Gone, or soon gone, are the restrictions on ABC, NBC, and CBS (collectively "the three networks") from entering the program production and syndication markets,[7] as well as on supplying programming to their affiliates for the one hour time slot of 7 p.m. to 8 p.m.,[8] dubbed the prime time "access" period.[9] These rules were enacted at a time when the entire national broadcast universe was occupied by the three networks.[10] The rules were an attempt to undermine their dominance of all aspects of television programming, from program creation to deciding which programs get aired and eventually syndicated.[11]

The FCC took the position that the repeal of these rules was

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from November 10, 1995 to the date of publication of said Report and Order in the above cited Federal Register. *See* Review of the Syndication and Financial Interest Rules, Sections 73.659—73.663 of the Commission's Rules, Report and Order, 10 F.C.C.R. 12,165, ¶ 2, at 12,165 (1995) [hereinafter 1995 Order].

[5] Prime Time Access Rule ("PTAR") was enacted concurrently with fin-syn with the similar goal of aiming to "correct the competitive imbalance between networks and their affiliates and increase diversity of program source." 1970 Order, 23 F.C.C.2d at 384 n.7. The rule provides that

> no television station, assigned to any of the top 50 markets in which there are three or more operating commercial television stations, shall broadcast network programs offered by any television network or networks for a total of more than 3 hours per day between the hours of 7 p.m. and 11 p.m. local time, except that in the Central time zone the relevant period shall be between the hours of 6 p.m. and 10 p.m.

Id. ¶ 5, at 384; *see* 47 C.F.R. § 73.658(k) (1970). The rule "exempts certain types of programming [such as] runovers of live sporting events, special news, documentary and children's programming, and certain sports and network programming of a special nature which are not counted toward the three hours of network programming." Review of the Prime Time Access Rule, Section 73.658(k) of the Commission's Rules, Report and Order, 11 F.C.C.R. 546, ¶ 1, at 547 (1995) [hereinafter PTAR Order]; *see also* 47 C.F.R. § 73.658(k)(1)-(6). In layman's terms, PTAR effectively prohibited the three networks, ABC, NBC, and CBS, from supplying their affiliates in the fifty largest television markets ("top 50 market affiliates") with programming for the 7 p.m. to 8 p.m. schedule slot. *See* PTAR Order, 11 F.C.C.R. ¶ 10, at 550. The FCC believed that by reducing the level of network control over their affiliates' programming decisions, there would be a natural increase in the diversity of programs available to the public. *Id.* ¶ 1, at 547. Furthermore, "PTAR also came to be viewed as a means of promoting the growth of independent stations in that they did not have to compete with the Top 50 Market Affiliates in acquiring off-network [*i.e.*, former network] programs to air during the access [the 7 p.m. to 8 p.m. time slot] period." *Id.*

[6] PTAR Order, 11 F.C.C.R. ¶ 4, at 548. Brief mention of PTAR is made at the outset in the interests of providing a complete picture, however, it will not be analyzed further in this Note. For some reason, PTAR has "escaped much of the harsh criticism levied at" fin-syn, commentators having chosen, by and large, to focus on fin-syn. Suzanne Rosencrans, *The Questionable Validity of the Network Syndication and Financial Interests Rules in the Present Media Environment*, 43 FED. COMM. L.J. 65 n.4 (1990).

[7] *See* 1970 Order, 23 F.C.C.2d ¶¶ 27-32, at 397-98.

[8] *See* PTAR Order, 11 F.C.C.R. ¶ 10, at 550.

[9] *See id.*

[10] *See* 1970 Order, 23 F.C.C.2d ¶ 6, at 385.

[11] *Id.* ¶ 11, at 389. The FCC found that "[t]he networks have gradually—since about 1957—increased their economic and creative control of the entire television program process. Between 1957 and 1968 the share of all network evening program hours (entertain-

warranted and even necessary, in the face of the changing broadcast media landscape.[12] Where at one time there were only three national networks broadcasting, there are now six.[13] Add nearly 500 channels of cable[14] and Direct Broadcast Satellite television[15] (to name just two alternate television outlets),[16] and the television landscape is immeasurably broader today than it was in 1970. The FCC found that because of these changes, the three networks no longer exerted the kind of market domination that justified continued retention of these rules.[17]

While the decline of network dominance cannot be seriously disputed, at least with regard to market share,[18] and perhaps also with regard to market influence, the FCC failed to foresee the consequences of its decision to repeal these rules. Fin-syn and PTAR were enacted to foster a more competitive and diverse programming climate,[19] wherein program producers with unique ideas

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ment and other) either produced or directly controlled by networks rose from 67.2 to 96.7 percent." *Id.*

12 *See* 1995 Order, 10 F.C.C.R. 12,165, ¶ 3, at 12,165 (1995).

13 The six are the well known ABC, NBC, CBS, the newer Fox Network, and the newest, UPN ("United Paramount Network") and WB ("Warner Brothers"). Both UPN and WB were launched in January 1995. PTAR Order, 11 F.C.C.R. ¶ 8, at 549. UPN is owned by Chris-Craft Industries, Inc., although the Paramount Pictures Corporation (a subsidiary of Viacom, Inc.) has provided funding and assistance in UPN's launch and holds a contingent ownership interest in UPN as well. *Id.* ¶ 8, at 549 n.8. Recent data show that UPN has a total audience reach of 86.5%. *Id.* WB is affiliated with Warner Brothers, which is, in turn, owned by Time Warner. *Id.* WB has an audience reach of 78%. *Id.* By comparison, ABC, NBC, and CBS each have over 200 affiliates nationwide, and reach 99% of U.S. television households. *Id.* ¶ 7, at 548. Fox has over 150 affiliates that together reach 97% of the country (as of February 1995). *Id.*

14 *See* Tamber Christian, *The Financial Interest and Syndication Rules—Take Two*, 3 COMMLAW CONSPECTUS 107, 107 (1995). With regard to what percentage of Americans actually subscribe to cable, Judge Posner made this observation in 1992: "Almost everyone in this country either now has or soon will have cable television . . . ." *Schurz*, 982 F.2d at 1055. Judge Posner, quite uncharacteristically, did not offer any empirical evidence in support of his claim, however.

15 *See* PTAR Order, 11 F.C.C.R. 546 (Separate Statement of Commissioner Rachelle B. Chong).

16 Additionally, video cassette recorders ("VCRs") are present in over 70% of American households. *See* Christian, *supra* note 14, at 107.

17 *See* In the Matter of Evaluation of the Syndication and Financial Interest Rules, 8 F.C.C.R. 3282, ¶ 1(k), at 3284 (1993) [hereinafter 1993 Rules] (establishing a two year phase-out of fin-syn); 1995 Order, 10 F.C.C.R. ¶ 2, at 12,165; PTAR Order, 11 F.C.C.R. 550 n.15; *Schurz*, 982 F.2d at 1045-48; Capital Cities/ABC, Inc. v. FCC, 29 F.3d 309, 311 (7th Cir. 1994).

18 For example,

> [l]ooking at prime time alone, the time period when the networks' viewing shares are the highest, each network's average share of the prime time audience declined from a 31.1 viewing share during the 1971/72 season to a 20.2 share during the 1993/94 season, a loss of almost one-third of each network's audience.

PTAR Order, 11 F.C.C.R. ¶ 29, at 561.

19 *See* 1970 Order, 23 F.C.C.2d 382, ¶ 1, at 382 (1970); PTAR Order, 11 F.C.C.R. ¶ 1, at 546.

would be able to have those ideas showcased on a national network without surrendering valuable syndication rights.[20] Additionally, independent stations[21] could compete on an equal footing with network affiliates[22] for the rights to broadcast popular program reruns. The theory was that with only three national broadcast outlets available, the autonomy and leverage of independent producers was severely compromised.[23] Independent producers faced the reality that in order for their programs to have national exposure, the programs would have to be aired on one or more of the three networks.[24] The networks, in return for national penetration, demanded that the producers surrender potentially valuable syndication rights,[25] as well as submit to the network's creative control over the show's formula.[26] Furthermore, the networks could theoretically bypass the independent producers entirely, opt-

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20 *See* 1970 Order, 23 F.C.C.2d ¶¶ 8-12, at 387-89. "Syndication is the industry term used to refer to the licensing of programs for exhibition to individual stations." 1995 Order, 10 F.C.C.R. at 12,165 n.6. The term "active" syndication refers to the direct negotiation with the individual stations for the exhibition of programs, and the term "passive" syndication refers to the holding of syndication rights that do not bestow the right to negotiate directly with the individual stations. *Id.*

21 Independent stations are those that do not affiliate with a network. Review of the Prime Time Access Rule, Section 73.658(k) of the Commission's Rules, Notice of Proposed Rule Making, 9 F.C.C.R. 6328, ¶ 7, at 6331 (1994) [hereinafter PTAR Notice]. As of mid-1995, there were over 450 local commercial stations that were not affiliated with the ABC, NBC, or CBS networks. *See* PTAR Order, 11 F.C.C.R. ¶ 9, at 549-50. However, "[w]hile these stations have traditionally been called 'independent' stations, approximately 300 of these commercial stations are now affiliated with and obtain several hours of prime-time programming from Fox, UPN, or WB networks." *Id.* Of these 300 stations, about 150 are affiliated with Fox. *Id.* According to the above statistics, that would leave just 150 truly independent stations, i.e., those that are unaffiliated with any network whatsoever. Since these stations are not affiliated with any network, they must obtain programming on their own. *Id.* "These programs include movies previously shown in theaters, television series previously aired on network affiliates [defined as 'off network programs'], and series produced for first-run viewing on the independent stations." *Id.*; *see* discussion *infra* part I. Throughout this Note, the term "independent" stations denotes these latter, truly independent stations.

22 Affiliates of a network are stations that are electronically connected to the network by cable or satellite. *Schurz*, 982 F.2d at 1045. Affiliated stations are further defined as

> station[s] having a regular affiliation with one of the three national television networks, under which it serves as that network's primary outlet for the presentation of its programs in a market. It includes any arrangement under which the network looks primarily to this station rather than other stations for the presentation of its programs and the station chiefly presents the programs of this network rather than another network.

47 C.F.R. § 73.658(l)(1)(iii) (1992); *see* Christopher J. Pepe, Comment, *The Rise and Fall of the FCC's Financial Interest and Syndication Rules*, 1 VILL. SPORTS & ENT. L. F. 67 n.2 (1994) (discussing the history of fin-syn and the FCC's response to the remand issued by the *Schurz* Court in 1992 (*see infra* part II.C. for a description)).

23 *See* 1970 Order, 23 F.C.C.2d ¶¶ 6-8, at 385-87.

24 *Id.* ¶ 7, at 386-87; *see* discussion *infra* part I.

25 *See* 1970 Order, 23 F.C.C.2d ¶ 28, at 397-98.

26 *Id.* at 397 n.27. To produce programming based on a "formula" means that a television show's or series' characters, theme(s), action, and general subject matter are produced to conform to tested commercial patterns. *Id.*; *see* discussion *infra* part I.

ing instead to produce all of their programming "in-house."[27]

In response to such bargaining inequalities, the three networks were legislatively prohibited from producing their own programming "in-house," so as to allow for the inclusion of outside and potentially diverse programming in their schedules.[28] For instance, since the three networks were forbidden to produce more than forty percent of their prime time programming "in-house,"[29] they had nothing to lose and everything to gain by accepting outside programming for their broadcast schedules. Furthermore, the networks were completely prohibited from entering the syndication market.[30] Consequently, for the first time, independent producers were bargaining from a position of relative strength, since the networks had to seek outside programming and were prohibited from acquiring syndication rights to such programming.[31]

However, with the repeal of these restrictions, the three networks are now permitted to broadcast as much in-house programming as they wish, as well as to retain and acquire the lucrative syndication rights for popular programming.[32] The newly presented opportunities presented by this have not gone unnoticed. Realizing the potential for the vertical integration of programming with its own national broadcast outlet, the Walt Disney Company made a successful bid for ABC, thus assuring itself of a viable outlet for its large slate of programming, as well as the cash generated by those programs in syndication.[33]

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27 *See supra* note 11 and accompanying text (describing the extent of network control over the production of its evening programming). "In-house" programming is defined as network programming that is "(1) solely produced by the network; (2) co-produced by the network with foreign production entities; or (3) co-produced by the network with outside domestic production entities that initiate such arrangements." 1993 Rules, 8 F.C.C.R. 3282, at 3313 n.72 (1993).

28 *See* 1993 Rules, 8 F.C.C.R. ¶ 3, at 3284-85.

29 Evaluation of the Syndication and Financial Interest Rules, Memorandum Opinion and Order, 7 F.C.C.R. 345, ¶ 5, at 349-50 (1992) [hereinafter 1991 Rules], *modified*, 1993 Rules, 8 F.C.C.R. 3282 (1993). This 40% cap on "in-house" productions was added by the 1991 Rules, and had no counterpart in the 1970 Order. *See Schurz*, 982 F.2d at 1047. This introduction makes no effort to identify particular restrictions with specific sets of fin-syn rules; instead it merely offers examples of the types of restrictions that were placed on the networks throughout the evolution of the different sets of fin-syn rules, each of which will be discussed *infra* in parts I.-II.

30 *See* 1970 Order, 23 F.C.C.2d ¶ 1, at 382 (codified at 47 C.F.R. § 73.658(j)(1)(i)-(ii) (1970)).

31 *Id.*

32 *See* 1993 Rules, 8 F.C.C.R. ¶ 1(a)-(c), at 3283; Network Financial Interest and Syndication Rules, 60 Fed. Reg. 48,907, ¶ 27, at 48,912 (1995). The 1993 Rules eliminated the 40% cap on network "in-house" program production, but maintained the prohibition on active network syndication. 8 F.C.C.R. ¶¶ 1(b)-(c), at 3283. The Network Financial Interest and Syndication Rules repealed all remaining vestiges of fin-syn. *See* Network Financial Interest and Syndication Rules, 60 Fed. Reg. ¶ 27, at 48,912.

33 *See* DISNEY PROSPECTUS, *supra* note 1, at 25, 113; *see* discussion *infra* part III.A. The

The problems presented by such a merger are twofold. First, the opportunity for independent program producers to provide programming to ABC has now been severely curtailed. The chances of an independent production gaining a schedule slot ahead of a Disney production are measurably lower.[34] Second, other networks and independent stations have been effectively cut off from a large supplier of programming, both for original programming and for acquiring syndication rights.[35] Disney most certainly will favor supplying programming to ABC over other outlets,[36] and would be foolish to sell syndication rights of popular programs to independent stations or other networks over ABC affiliates.

This Note will attempt to show that the above concerns are something more than just educated speculation. While the repeal of fin-syn is as yet too fresh for its ultimate effects to be felt, the problems presented are real and must be addressed now before all the progress in the television industry over the last twenty-five years unravels. Part I of this Note will trace the history of the fin-syn rules in light of market conditions in 1970, as well the structure of the television industry in general. Part II will describe the changing market conditions during the 1970s and 1980s leading up to the FCC's attempt at revising the rules in 1991. Part II will also discuss the *Schurz*[37] court's vacating of the 1991 rules and the FCC's subsequent enactment of a new set of rules in 1993. Finally, part III will analyze present and possible future effects of the 1995 repeal of the rules, and will propose an alternative to immediate, wholesale revocation.[38] Part III will also briefly note the passage of

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potential benefits of vertical integration in the cable industry are being pursued as well—witness the $7.6 billion acquisition of Turner Broadcasting System, Inc. by Time Warner, Inc. *See* Eben Shapiro, *Time Warner Posts Operating Gains, Resumes Discussions With US West*, WALL ST. J., Oct. 17, 1996, at B8. For a thorough discussion of the vertical integration issues as they relate to the cable industry, see James W. Olson & Lawrence J. Spiwak, *Can Short-Term Limits on Strategic Vertical Restraints Improve Long-Term Cable Industry Market Performance?*, 13 CARDOZO ARTS & ENT. L.J. 283 (1995).

[34] *See infra* notes 186-87 and accompanying text.

[35] *See infra* notes 186-87 and accompanying text.

[36] *See infra* notes 186-87 and accompanying text. There is, arguably, a greater tendency for a parent corporation to favor a subsidiary than for a network to favor an affiliate, yet even for the latter the FCC believes that there is "the natural tendency of an affiliate to do more business with its dominant supplier." 1970 Order, 23 F.C.C.2d 382, ¶ 7, at 386-87 (1970).

[37] *Schurz*, 982 F.2d 1043.

[38] The 1993 Rules actually provided for a two year "phase-out" of the rules which was to expire on November 10, 1995. 1993 Rules, 8 F.C.C.R. 3282, ¶ 1(k), at 3284 (1993). Notwithstanding the FCC's cautious approach, this Note will propose that the decision to ultimately repeal the rules was not wise, and that certain restrictions should be maintained. *See* discussion *infra* part III.C.

the Telecommunications Act of 1996[39] and how it may affect the evolution of the television industry.

PART I. HISTORY OF FIN-SYN

In 1970, the FCC determined that the three major networks at that time, ABC, NBC, and CBS, supplied the lion's share of prime time television programming, and that something had to be done to curtail their power.[40] The FCC was concerned that the networks had "monopsony" power, meaning the ability to acquire programming rights unfavorable to program producers.[41] In other words, since the networks were the only program providers that could reach virtually every American household, if an independent producer wanted to get a show broadcast to the largest market, he would be forced to comply with whatever terms the networks chose to impose on him.[42] For example, the networks could force him to relinquish his future rights to proceeds from syndication in return for the present ability to reach the largest audience for his program.[43] Furthermore, the FCC feared that the networks had and would exercise "monopoly" power by preventing independent stations from purchasing popular network programs.[44] The networks would withhold or "warehouse"[45] those programs, or grant more favorable syndication terms to its affiliates.[46] Such potential practices by the networks would decrease or perhaps even eliminate the supply of diverse programming available to television audiences, and would prevent the creation of a competitive syndication

[39] Pub. L. No. 104-104, 110 Stat. 56 (codified as amended in scattered sections of 47 U.S.C.).

[40] *See* 1970 Order, 23 F.C.C.2d ¶ 7, at 386-87; 1993 Rules, 8 F.C.C.R. ¶ 3, at 3284-85; Network Financial Interest and Syndication Rules, 60 Fed. Reg. 48,907, ¶ 1, at 48,908 (1995).

[41] *See* 1970 Order, 23 F.C.C.2d ¶ 8, at 387.

[42] *See* Christian, *supra* note 14, at 107.

[43] *See* 1970 Order, 23 F.C.C.2d ¶¶ 19-20, at 393 & nn. 29-31. The networks' financial interests in acquired programming took two forms: "(1) actual distribution of programs through their syndicated program divisions, and (2) profit sharing rights in domestic and foreign distribution carried on by others." *Id.* ¶ 20, at 393. For the years 1960-1964, of the 114 1/4 hours of independently produced programming that the networks acquired, 43 hours (37.6%) were acquired together with domestic and/or foreign syndication distribution rights, while 93 hours (81.4%) were acquired together with domestic and/or foreign syndication profit shares. *See id.* at 393 n.29; Rosencrans, *supra* note 6, at 67.

[44] *See* 1970 Order, 23 F.C.C.2d ¶ 12, at 389; *Schurz*, 982 F.2d at 1045 (tracing the history of the fin-syn rules, and vacating the FCC's attempt in 1991 at modification of those rules); Christian, *supra* note 14, at 107; Rosencrans, *supra* note 6, at 66-67 & n.13.

[45] Warehousing is the act of "delaying . . . the syndication of programming to the detriment of non-network stations. . . . The anti-warehousing safeguard required a network to release into syndication a program for which it held syndication rights four years after the program's network debut or within six months following the end of the network run, whichever was sooner." 1993 Rules, 8 F.C.C.R. ¶ 59, at 3313-14.

[46] *See* 1993 Rules, 8 F.C.C.R. ¶ 59, at 3313.

market.[47]

In order to better understand the extent of network dominance in 1970 and the FCC's attempt to curtail this dominance, some discussion of the structure of the television industry is warranted. Television stations may be divided into two categories: those that are "affiliated" with a national network, and those that are not. Those stations that are not affiliated with a national network are referred to as "independent" stations.[48] Network affiliates obtain an entire schedule or package of programming via satellite directly from the network.[49] This package is known as the network "feed."[50] In return for clearing airtime for the network programming, the affiliates are compensated according to the time of day they clear, the amount of time cleared, and the size of the affiliates' potential audience at that time.[51] The networks encourage their affiliates to carry the entire slate of prime time programming so as to maximize the size of the audience viewing these programs.[52] The larger the audience, the higher the prices the network can command from advertisers. These proceeds in turn are used to defray the cost of procuring programming.[53] However, network affiliates do not only broadcast the network feed. They also air "locally originated programming, primarily local news and sports programming,"[54] as well as programs purchased from "syndicators."[55] In the past, these syndicators supplied their programming to television stations by sending films or tapes of the programs.[56] However, with the advent of satellite technology, programs can be sent simultaneously to all of the syndicators' television station customers, similar to the network feed to its affiliates.[57]

Historically, only a small number of programs aired on the three networks were produced in-house by the networks.[58] For the most part, the programs aired on the three networks are supplied by outside production companies, primarily major movie studios

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47 *See generally* Christian, *supra* note 14; Rosencrans, *supra* note 6; Pepe, *supra* note 22.

48 *See* PTAR Notice, 9 F.C.C.R. 6328, ¶ 7, at 6331 (1974).

49 *Id.* ¶ 4, at 6330.

50 *Id.*

51 *Id.*

52 *Id.* ¶ 5, at 6330-31.

53 *Id.*

54 *Id.* ¶ 6, at 6331.

55 *Id.* "Syndicators" are defined as "entities that sell programming to television stations on an individual basis." *Id.* The well-known game show *Wheel of Fortune* is an example of such a program supplied by the syndicator, King World. *Id.*

56 *Id.*

57 *Id.*

58 *Id.* ¶ 8, at 6331-32. Fox, however, produces a large amount of its own programming because it is affiliated with a movie studio, Twentieth Century Fox. *Id.*

such as (Twentieth Century Fox, Time Warner, Sony, and Disney).[59] Other suppliers include independent producers, who often affiliate with movie studios in order to produce the program, and syndicators (such as King World).[60] Those programs that are slated for network distribution are sold directly to the networks, who air them through their respective national affiliates.[61] Those intended for off-network broadcasting or syndication are sold through the syndication "arm" of the production company, or, alternatively, the syndication rights to the program are sold to an independent syndicator who then negotiates with the independent stations.[62]

Independent stations are those not affiliated with a national network.[63] "The owner of an independent station is responsible for obtaining programming for the entire broadcast day."[64] While some of an independent station's programming—such as sports and local news—is locally originated, and some is from the networks, much of it is obtained from program producers or syndicators.[65] An independent station's programming typically includes movies that have previously been shown in theaters, television series that were previously aired on a network, and some series that are originally produced to be aired on independent stations—so-called "first-run syndication."[66] The independent station usually pays for the programming it obtains with cash, and, hopefully, recoups the investment by selling airtime to advertisers.[67] In some instances, programming is obtained by "barter," a process by which the independent station allows the syndicator or other program supplier to sell some of the advertising time directly to advertisers

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59 *Id.*
60 *Id.*
61 *Id.*
62 *Id.*
63 *Id.* ¶ 7, at 6331; *see also supra* text accompanying note 21.
64 PTAR Notice, 9 F.C.C.R. 6328, ¶ 7, at 6331 (1974).
65 *Id.*
66 *Id.* One such program is *Star Trek: The Next Generation. Id.* Other examples include *Jeopardy, Entertainment Tonight,* and *The Oprah Winfrey Show. See* PTAR Notice, 9 F.C.C.R. ¶ 19 & at 6340 n.43. Incidentally, Oprah Winfrey might never have acquired the fame and fortune that she enjoys today if not for fin-syn. According to *Forbes,* Winfrey had previously given up her syndication rights to the local ABC affiliate, WLS. Subsequently, Winfrey's agent "sensed he could do better" with *Oprah* by peddling it to the independent market, so, in 1985, he asked WLS if he could retrieve the syndication rights. Apparently, WLS either forwarded this request to ABC, or Winfrey's agent negotiated with ABC directly (the article does not elaborate), and ABC agreed, on the condition that ABC affiliates got first crack at airing the program. ABC's motivation was simple: "Prohibited by law from syndicating, ABC had nothing to lose [by returning the syndication rights] and something to gain [first crack at the program]." Robert La Franco & Josh McHugh, *"Piranha is good,"* FORBES, Oct. 16, 1995, at 66, 68.
67 *See* PTAR Notice, 9 F.C.C.R. ¶ 7, at 6331.

in exchange for a smaller cash outlay by the independent station for the programming.[68] The barter system serves two purposes. First, it allows a cash-strapped or smaller market independent station to obtain choice programming, since less cash (sometimes none) is required to obtain programming.[69] Second, it provides needed funds to the program producers by allowing them to get advertising dollars.[70]

Today there are six networks that broadcast nationally and have affiliates. They are the ABC, NBC, CBS, Fox, UPN, and WB networks.[71] Although the total national market coverage for each of them differs, even the smallest coverage by these networks is substantial.[72] An independent program producer is virtually assured of a national audience for his program no matter which network airs the program, although the three oldest networks still offer greater exposure.[73]

The above represents the reality of the broadcast industry as of today, after twenty-five years of fin-syn regulations. However, the picture was developing somewhat differently in 1970, prior to the rules' enactment. As noted above, in 1970 the national television industry consisted of only three networks: ABC, NBC, and CBS.[74] Each of these networks was actually composed of five television stations licensed to the network corporation and a large number of independent stations that were affiliated with the network corporation.[75] The networks produced or procured programs for broadcast and offered a "continuous, coordinated program schedule to its affiliated stations."[76] The production process of these programs was "for all practical purposes controll[ed] . . . [by the networks] from idea through exhibition."[77] The networks wanted creative

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68 *Id.*
69 *Id.*
70 *Id.*
71 *See supra* text accompanying note 13.
72 *See supra* note 13 (noting that ABC, NBC, and CBS each reached 99% of the country, Fox reached 97%, UPN reached 86.5%, and WB reached 78%).
73 *See supra* note 13.
74 *See* 1970 Order, 23 F.C.C.2d 382, ¶ 6, at 385-86 (1970).
75 *Id.* at 384 n.8.
76 *Id.*
77 *Id.* ¶ 11, at 389. The FCC added that "[b]ecause off-network programs constitute a principal staple of the nonnetwork program market, networks also control the production and hence, the form and content, of a large share of the syndicated programs exhibited by television stations." *Id.* Furthermore, the FCC noted a big increase in

> network controlled independently produced programs—the so-called joint venture programs with respect to which networks almost invariably acquire the first-run right in addition to some rights to share in the profits from the network run and the right to distribute and/or share in the profits from domestic syndication and overseas sales and other valuable subsidiary rights. This type of arrangement facilitates network control of the form, content, and creative as-

control over the content of their programming in order to increase advertising circulation.[78] Thus, programs were produced on the basis of "formulas" that were pre-approved by the three networks and their advertisers, such that the subject matter would satisfy tested commercial patterns.[79] This "allowed the networks to select and cancel programs on the basis of their own potential profit, without regard to the public interest."[80] Additionally, independent program producers typically required financial support from the purchasing network in order to produce programs.[81] This further tightened the network's control over the result. An independent producer had no incentive to create diverse programming since it would receive neither network funding nor exposure.

National exposure was crucial to independent producers so that the program, if successful, would generate the kind of national interest that would justify high prices in syndication.[82] In 1970, the three networks were the only ones who could claim truly national exposure. To illustrate this point, it is helpful to understand television market demographics. Typically, the television market is described as having an audience in the fifty largest television markets ("top fifty markets"),[83] and an audience consisting of the rest of the United States.[84] The stations in the top fifty markets in 1970

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pects of the show even though actual filming is done by a nominally independent producer.

Id. ¶ 12, at 389. The true extent of network control over programming is perhaps most vividly portrayed by the precipitous drop in the percentage of evening programs provided to the networks by independent producers and in which the networks had no financial interest or other control. The percentage fell from 32.8% in 1957 to just 3.3% in 1968. *Id.* at 389 n.17; *see also supra* text accompanying note 11.

78 *See* 1970 Order, 23 F.C.C.2d at 392 n.27. Network revenues from domestic and foreign sales of advertising time in 1967 amounted to $363.7 million. *Id.* at 392 n.28. Compare that figure to the $29.3 million collected from syndication activities during the same year. *Id.* One gets a good idea of how important it was for the networks to assure themselves of programming with a solid advertising base.

79 *Id.* at 392 n.27.

80 Rosencrans, *supra* note 6, at 67 (discussing the networks' control over the program production process, and their bargaining leverage over independent producers).

81 *See* PTAR Notice, 9 F.C.C.R. 6328, ¶ 8, at 6331-32 (1974); Rosencrans, *supra* note 6, at 69.

82 In order for a program to enter syndication, it usually must have had at least a four year run on a network. Christian, *supra* note 14, at n.52. Without a sufficiently large number of episodes, the purchasing stations will not have enough programming to fill their schedules. *Id.* The ability to provide a sufficient number of episodes can be difficult, due to the fact that nearly 80% of prime-time network programs fail to last three years. *Id.* Judge Posner of the Seventh Circuit Court of Appeals likens the risk of failure involved in program production to "wildcat drilling for gas and oil. Most television entertainment programs are money losers. The losses are offset by the occasional hit that makes it into syndication after completing a long first run." *Schurz*, 982 F.2d at 1046.

83 *See* 1970 Order, 23 F.C.C.2d ¶ 6, at 385-86; PTAR Order, 11 F.C.C.R. 546, ¶ 1, at 547 (1995).

84 *See* 1970 Order, 23 F.C.C.2d ¶ 6, at 385-86; PTAR Order, 11 F.C.C.R. ¶ 1, at 547.

reached over seventy-five percent of the available audience.[85] Of the 224 television stations in the top fifty markets in 1970, 153 were network affiliates.[86] Furthermore, only fourteen out of the top fifty markets had at least one independent VHF station.[87] Clearly, the independent stations were an inadequate means of displaying programming to the largest audience. Access to at least a substantial portion of the top fifty markets was imperative.[88] However, gaining access to a national market came with a price that effectively removed the independent producer's need for national exposure. The independent producer stood to gain the least from having the program aired nationally, since the networks demanded and usually got either the distribution rights or large shares of the profits from domestic and foreign syndication, or both, in exchange for airing the program.[89]

Once a program entered syndication, independent stations were at a significant competitive disadvantage vis-a-vis the network affiliates. Since the networks held all or most of the syndication and distribution rights, they tended to favor their affiliates in granting the right to air these programs in syndication.[90] The independent stations were forced to fill airtime with old movies or "off-network" programs.[91] They did not receive the network feed, they could not obtain popular syndicated programming, and they were unable to finance independent producers to produce their own programming.[92] In short, the independent stations were essentially locked out of the choice programming.

To summarize, there were two disturbing trends developing by 1970. First, independent producers had no incentive to create diverse programming for fear of having neither the necessary financial support of the three networks nor the concomitant national exposure. Second, to the detriment of program producers and in-

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85 *See* 1970 Order, 23 F.C.C.2d ¶ 7, at 386-87.

86 *Id.* ¶ 6, at 385-86.

87 *Id.* The VHF broadcasting band broadcasts a stronger signal than does the UHF band. *See* PTAR Order, 11 F.C.C.R. ¶ 73, at 583. Whereas affiliates of the three networks are predominantly VHF stations, most of the independent stations are in the UHF band, which puts independent stations at a structural disadvantage relative to the network affiliates. *Id.* This disadvantage is referred to as the "UHF handicap," which proponents of network regulation argued justifies the retention of PTAR and fin-syn to even the playing field. *Id.*

88 *See* 1970 Order, 23 F.C.C.2d at 394 n.32.

89 *Id.* ¶ 28, at 397-98; *see supra* text accompanying notes 42, 76.

90 *See* 1970 Order, 23 F.C.C.2d ¶ 7, at 386-87. The FCC explained that if the networks were to sell programs to independent stations, these programs would be in competition with the networks' own programs on their affiliates. *Id.* ¶ 21, at 394.

91 *Id.* ¶ 6, at 385-86.

92 *See* Pepe, *supra* note 22, at 69.

dependent stations, a competitive syndication market was simply nonexistent. Program producers were forced to turn over syndication rights to the three networks, who in turn funneled them to their respective affiliates. Independent stations never stood a chance of obtaining this programming.

In response to this perceived threat to the public interest, the FCC enacted the Financial Interest and Syndication Rules, which became known as the "fin-syn" rules.[93] These rules were designed to restrict the networks from syndicating or acquiring any financial interest in television programming. In particular,

> [t]he 1970 rules: (1) prohibited television networks from acquiring any financial interest in the broadcast of programs not solely produced by the network, but allowed these programs to be aired on the network; (2) prohibited networks from engaging in the domestic syndication business or from having an ongoing interest in the syndication of programs for non-network program distribution . . . .[94]

Fin-syn was aimed at alleviating the two primary concerns outlined above, namely diversity of programming and creation of a competitive syndication market where the independent stations could compete on even terms with network affiliates.[95] Independent producers, freed of the need to surrender syndication rights or other financial interests to the networks, would be free to create diverse programming and have it aired nationally.[96] In other words, since the networks were prohibited from having any financial interest in independent programs, the independent producers would not be subject to the creative control of the networks. Furthermore, since the networks were no longer the funnel for practically all syndication rights, the independent stations could bargain more competitively with network affiliates for the syndication rights to popular programs.[97] The hope was that these restrictions

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[93] *See id.* at 68-69.

[94] *Id.* at 73; *see also* 1991 Rules, 7 F.C.C.R. 345, ¶ 2, at 347 (1992).

[95] *See* Pepe, *supra* note 22, at 72.

[96] *See* 1970 Order, 23 F.C.C.2d ¶ 29, at 398 (1970). The FCC observed:

> Relieved of the need to grant a network a large portion of his potential profit the producer's ability [ ] to operate [profitably] in network television will be greatly enhanced. With the expanded syndication market as a feasible alternate to network exhibition his bargaining position will be improved and he can be expected to develop into a stable and continuing alternate source of programs and ultimately to compete for network time.

Id.

[97] *Id.* ¶ 30, at 398. Since the networks' competitive advantage stemmed in large part from its existing relationships with affiliates, the prohibition on syndication "will permit the networks to lend all their efforts to the sale of network programs," rather than acting as

on the three networks would help foster a more diverse and competitive television broadcast market.[98]

PART II. A CHANGING MARKETPLACE

A. *The 1983 Tentative Decision*

Not long after the adoption of the fin-syn rules, the marketplace conditions which precipitated, or, perhaps mandated the rules, changed.[99] As early as 1977, the FCC established a commission of experts, the Network Inquiry Special Staff ("NISS"), to evaluate how the marketplace for television programming had changed since the 1970 Order.[100] Based on the NISS findings, the FCC released a Tentative Decision in 1983 proposing to eliminate the fin-syn rules.[101] The NISS found that the networks

> no longer had the ability to control the price or conditions under which producers would sell their programs. The Commission [FCC] reasoned that: "In order for these concerns to be realized, two conditions regarding network behavior must be met. First, the three networks must be able to act in concert, either tacitly (by parallel behavior) or collusively (by active conspiracy). Second, the three networks together must comprise the sole purchasers of the program producers' product. If either of these conditions is not met, it is not likely that the networks could exert power over program producers. This is so because, if adequate alternative program purchasers exist, any producer who may be dissatisfied with the treatment he receives by a single broadcast network has the option of offering his product to a different network or some other program purchaser."[102]

The FCC determined that neither of the required conditions had been met.[103] According to the NISS, the networks did in fact com-

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brokers in acquiring syndication rights and reselling them to their affiliates. *Id.*; *see* PTAR Order, 11 F.C.C.R. 546, ¶ 16, at 553-54 (1995).

[98] *See* 1970 Order, 23 F.C.C.2d ¶¶ 1, 7, 8, 21, 22, 29, 30, at 382, 386-87, 394, 398.

[99] *See Schurz*, 982 F.2d at 1046, 1050-52. Judge Posner delivers a remarkably in-depth and colorful description of the television industry, and harshly criticizes the FCC's decision in 1991 to leave the fin-syn rules in place. *See generally* Rosencrans, *supra* note 6, for an excellent discussion of the questionable validity of the fin-syn rules in the face of marketplace conditions in 1990.

[100] Christian, *supra* note 14, at 108.

[101] *Id.*; *see* In the Matter of Amendment of 47 C.F.R. § 73.658(j)(l)(i) and (ii); the Syndication and Financial Interest Rules, Tentative Decision and Request for Further Comments, 94 F.C.C.2d 1019, ¶¶ 1, 10, at 1020, 1022 (1983) [hereinafter Tentative Decision].

[102] Christian, *supra* note 14, at 108 (quoting Tentative Decision, 94 F.C.C.2d ¶ 124, at 1063).

[103] *See id.*

pete with each other,[104] a finding which muted the concern about the networks acting in concert. Furthermore, the NISS noted that network dominance resulted primarily from entry barriers into the programming production industry,[105] which prevented the emergence of competition from new networks.[106] However, with the advent of satellite technology and the repeal of certain FCC rules in the area of cable and subscription television, new networks would develop and challenge the dominance of the three networks.[107] With more program purchasers looking to acquire programs to fill their airtime, the three networks would have less control over independent producers.[108] Fin-syn would be unnecessary to control network dominance; the market would do that on its own.[109]

Moreover, the FCC declared that it "found no credible evidence that the rules have . . . increased the diversity or competitiveness of the program supply market."[110] Although the restriction on the three networks from acquiring syndication rights was supposed to increase the bargaining power of program producers, in fact the opposite was true. Since the networks would not be receiving syndication rights together with the purchase of the program, they simply paid a lower price.[111] Program producers were left scrambling to cover their production costs with the hope of a successful run in syndication.[112] To avoid this situation, many small

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104 *Id.*

105 *See* Pepe, *supra* note 22, at 73 and n.38. The FCC described these entry barriers as follows:

> Through their de facto control of time-rental of evening hours on the vast majority of television stations throughout the country networks control market entry. In turn this enables them to dictate the form and content of the so-called creative efforts by writers, directors, and producers. Indeed, in most cases program form and pilot development are determined by the direct intervention or known preferences of the network managers. At the outset of the production process a formula is set out in terms of specifics designed to produce circulation through application of what network managers conceive to be the tastes and preferences of the largest undifferentiated mass audience. In this way networks make use of their economic power to dictate the terms of entry into television program markets and to prescribe the type and content of the product of that market.

1970 Order, 23 F.C.C.2d 382, app. II, ¶ 12, at 389 (1970) (footnotes omitted); *see also supra* text accompanying note 77 (describing the extent of network dominance over program production).

106 *See* Rosencrans, *supra* note 6, at 68.

107 *Id.* at 68-69.

108 *Id.* at 69.

109 *Id.*

110 Tentative Decision, 94 F.C.C.2d 1019, ¶ 195, at 1094 (1983).

111 *See* Rosencrans, *supra* note 6, at 69.

112 *Id.* The program producers were unable to cover their production costs with the reduced fees collected from the networks and had no additional financing, so they were hoping to make up the difference from a successful run in syndication (so-called "deficit financing"). *Id.*

program producers opted to create low-budget programming, which often translated into lower quality, risk-averse programming—the exact opposite result of the diverse, quality programming the FCC had hoped to promote.[113] Thus, the FCC reasoned that fin-syn had neither achieved nor was necessary to promote market competition and served no valid public service.[114]

However, despite the FCC's findings, the Tentative Decision was never adopted.[115] This was due in large part to an enormous lobbying effort by the movie industry,[116] which sought "to preserve their dominance . . . in the $5 billion-a-year syndication market"[117] and thus opposed any loosening of the fin-syn rules. The movie industry had long been a major supplier of programming to the three networks,[118] and argued that retention of the rules was essential to preserve creative flexibility.[119] The movie industry argued that without fin-syn, the television networks would have been reluctant to license the once revolutionary programs such as *All in the Family, The Jeffersons,* or *Hill Street Blues.*[120] Proponents of the rules' repeal argued that there was no legitimate issue of public interest involved, rather the issue "was one of big [syndication] dollars, and as long as [fin-syn] remained, the networks would be denied vital revenues to sustain commercial television."[121] Largely due to the movie industry's close ties with government representatives (including then President and former actor Ronald Reagan),[122] Congress entered the battle on the side of Hollywood and urged a compromise.[123] The compromise solutions suggested by the par-

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113 *Id.*

114 *See* Tentative Decision, 94 F.C.C.2d ¶ 195, at 1094.

115 *See* Christian, *supra* note 14, at 109.

116 *See* Michael R. Gardner, *Commentary: December 19, 1984—A Big Day in Telecommunications*, 34 CATH. U. L. REV. 625, 627-28 (1985).

117 Pepe, *supra* note 22, at 74.

118 *In the 1970 Order, the FCC listed eight motion picture companies that had supplied programming to the three networks since the late 1950's.* They were (1) Metro-Goldwyn-Mayer; (2) Paramount; (3) Screen Gems, a subsidiary of Columbia Pictures; (4) Twentieth Century Fox; (5) United Artists; (6) Universal Pictures; (7) Walt Disney; and (8) Warner Brothers. *See* 1970 Order, 23 F.C.C.2d 382, ¶ 9, at 388 (1970).

119 *See* Gardner, *supra* note 116, at 628.

120 *Id.* The movie industry was represented by a diverse coalition, known as the Committee for Prudent Regulation, "which had among its members major Hollywood studios, the trade guilds (Screen Actors, Directors, Producers, and Writers), independent television stations, and television celebrities such as Mary Tyler Moore, Alan Alda, Jean Stapleton, Henry Winkler, Charlton Heston, and Norman Lear." *Id.* at 627-28.

121 *Id.* at 628.

122 *See* Rosencrans, *supra* note 6, at 70. Then FCC chairman Mark S. Fowler met with President Reagan secretly for 45 minutes, 35 minutes of which were spent discussing fin-syn and Fowler's reasons for wanting to repeal the rules. *Id.* Fowler said the President smiled, nodded, and said little. *Id.* Soon after this meeting, Reagan announced that the FCC had agreed to a two year moratorium on further action regarding the fin-syn rules. *Id.*

123 *Id.* at 75; Christian, *supra* note 14, at 108.

ties may be summarized into two groups:

> The first of these would entail regulating in some fashion the negotiations that take place when a network is interested in purchasing a program from an outside producer for exhibition on its network. The second alternative is to somehow limit the number or types of programs in which a network could acquire financial interests.[124]

Examples of the first group include a mandate that the program producer has the exclusive right to initiate bargaining proceedings and proposals that separate the negotiations for licensing fees from negotiations for financial interests or syndication rights.[125] Examples of the second group include caps on the percentage of programs in the network's schedule in which the network may have financial interests, or caps on the percentage interest that a network may have in any of its programs.[126] The networks have tended to propose solutions for the second group,[127] to which the movie industry has responded that: "[U]nder such a scenario, the networks would insist on interest in the half-hour sitcoms ['situation-comedies'] in their schedules—which often do well in syndication—and leave producers with the remaining hour-long shows, which are more expensive to produce and haven't been performing well in syndication."[128] By contrast, one of the movie industry's proposals "would allow the networks to enter 50-50 joint programming ventures with producers for no more than five of the twenty-two weekly hours on prime-time."[129] As each side "vehemently rejected the other's proposals,"[130] a compromise proved elusive,[131] and so the status of the fin-syn rules remained in limbo until 1990, when the Fox Network "resurrected the debate."[132]

B. *The 1991 Rules*

In 1986, Fox launched a fourth network to compete with the three established networks.[133] Fox argued to the FCC that, as an

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124 Rosencrans, *supra* note 6, at 75.

125 *Id.* (citing Evaluation of the Syndication and Financial Interest Rules, 5 F.C.C.R. 6463, 6464 (1990)).

126 *Id.*

127 *Id.* For instance, the networks "have proposed loosening the rules to permit them to acquire a minority interest (less than fifty percent) in up to one-half—that is, eleven hours weekly—of the shows in their prime time schedules." *Id.*

128 *Id.* at 75-76.

129 *Id.* at 76.

130 *Id.*

131 *See* Christian, *supra* note 14, at 109; Pepe, *supra* note 22, at 75.

132 *See* Pepe, *supra* note 22, at 75.

133 *See* Christian, *supra* note 14, at 109.

emerging network, it should be exempt from the fin-syn rules on the ground that being subject to the rules would defeat their very purpose of promoting competition and diversity.[134] The fin-syn rules, in effect in 1990, applied to "any person, entity, or corporation which offers an interconnected program service on a regular basis for fifteen or more hours per week to at least twenty-five affiliated television licensees in ten or more States."[135] By 1990, Fox was close to exceeding the fifteen hour limit and had 129 affiliates.[136] Fox argued that the fin-syn rules tended to discourage diversity, since emerging networks, such as itself, would choose not to broadcast all their available programming so as not to be subject to the rules.[137] This in turn limited the number of broadcast outlets to which program suppliers could offer diverse programming.[138] The FCC responded to Fox's concerns by issuing a one year waiver permitting it to exceed fin-syn limits. More importantly, the FCC used the issues raised by Fox as an impetus to review the fin-syn rules once again.[139]

Not surprisingly, given the trends in the broadcasting industry that had already been identified by the NISS study in the late 1970s, the FCC discovered that network dominance had grown considerably smaller.[140] Among the FCC's findings regarding the changes in the television market since 1970 were:

> (1) the number of independent stations had increased from sixty-five to almost 340;
>
> (2) the proliferation of over ninety programming channels on cable;
>
> (3) close to sixty percent of American households subscribed to cable;
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> (4) perhaps the most telling change was that the share of the prime time viewing audience belonging to the networks had shrunk from nearly ninety percent in 1970 to less than sixty-two percent in 1990.[141]

However, regardless of these numbers depicting a sharp decline of

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[134] *See Schurz*, 982 F.2d at 1053.

[135] 47 C.F.R. § 73.658(j)(ii)(4) (1990).

[136] *See* Christian, *supra* note 14, at 109.

[137] *See Schurz*, 982 F.2d at 1053. The court noted that Fox "may be bluffing," but, nevertheless, sided with Fox since "the Commission failed even to mention the argument that its rules perversely limit competition with the established networks." *Id.*

[138] *See* Christian, *supra* note 14, at 108.

[139] *See* Pepe, *supra* note 22, at 75.

[140] *See* Evaluation of the Syndication and Financial Interest Rules, Report and Order, 6 F.C.C.R. 3094, ¶ 36, at 3108 (1991) (Sikes, J., dissenting) [hereinafter 1991 Report and Order]; Christian, *supra* note 14, at 108.

[141] *See* 1991 Report and Order, 6 F.C.C.R. ¶ 36, at 3108.

network dominance, the FCC decided to leave the rules essentially unchanged. The FCC theorized that although

> the networks faced greater competition in the media marketplace, [they] still retained an ability to manipulate the prime time entertainment and first-run programming market to the detriment of program source and outlet diversity. Consequently, it was still necessary to impose modified restraints on network acquisition of financial interests in programming and on network syndication activities.[142]

The modified rules somewhat relaxed the then existing restrictions. For example, while the 1970 Order prohibited network ownership of all programming not solely produced by the networks,[143] the 1991 Rules allowed the network to retain complete ownership rights in programming co-produced with a foreign production entity or even with a domestic production entity, *provided that* the domestic entity had initiated the arrangement.[144] Further, whereas under the 1970 Order networks were not allowed a financial interest even in non-network programming,[145] the 1991 Rules allowed the acquisition of such financial interests, including both foreign and domestic syndication rights.[146] The 1991 Rules also permitted the networks to tap "in-house programming" for up to forty percent of their prime time schedules.[147]

Most importantly for Fox, the 1991 rules created a loophole that would protect Fox from being subject to the rules altogether.[148] The 1991 rules redefined "television network" as "any . . . entity . . . [that] provid[es] more than fifteen (15) hours of prime time programming per week . . . to . . . affiliates reach[ing] seventy-five (75) percent of television households nationwide."[149] This new definition, like the old, still included Fox, and did not address Fox's argument that it would have to curtail programming to avoid being subject to the rules. Nonetheless, rather than increase the number of hours allowed before reaching "network" sta-

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142 1993 Rules, 8 F.C.C.R. 3282, ¶ 3, at 3284-85 (1993).

143 *See* 1970 Order, 23 F.C.C.2d 382, 383-84 (1970).

144 *See* 1991 Rules, 7 F.C.C.R. 345, ¶¶ 5, 12, at 348, 350-51 (1992). This modification bears a close resemblance to the first group of compromise solutions noted above that were proposed by the movie industry.

145 *See* 1970 Order, 23 F.C.C.R. ¶¶ 27-30, at 397-98.

146 *See* 1991 Rules, 7 F.C.C.R. ¶ 5, at 348.

147 *Id.* The 40% cap "had no counterpart in the old [1970] rules." *Schurz*, 982 F.2d at 1047. This provision seems to address the second group of proposals, championed chiefly by the networks. Thus, the 1991 rules were a legislated compromise of sorts between the interests of the movie industry and the networks.

148 *See* Christian, *supra* note 14, at 109.

149 47 C.F.R. § 73.662(i) (1991).

tus, or narrowing the definition some other way, the FCC elected to exempt "emerging networks" from the fin-syn rules. An "emerging network" was defined as an entity that "does not qualify as a network under [the new 1991 Rules] . . . as of the effective date of the [adoption of these new rules], even if it subsequently meets this definition."[150] This loophole was tailored for Fox, which still did not yet meet the hours requirement, and applied to any future upstart network.[151] The FCC explained the adoption of the loophole as "remov[ing] a significant impediment to the development of competition with the major networks, and [would] precipitate an increase in the amount of programming available to broadcast stations not affiliated with these major networks."[152] Thus, the adoption of the 1991 Rules aimed to loosen the fin-syn slightly with respect to the major networks, while protecting the interests of the emerging networks in order to promote diversity.[153]

C. *The* Schurz *Decision and Subsequent Enactment of the 1993 Rules*

The 1991 version of the fin-syn rules proved to be short-lived. In October of 1992, the networks petitioned the Seventh Circuit Court of Appeals, alleging that, in light of the FCC's findings with respect to the changes in the television marketplace since 1970, the decision to leave the fin-syn rules essentially unchanged was unjustifiable.[154] The networks argued that the rules should be repealed immediately. Judge Posner agreed. He stated "[w]hatever the pros and cons of the original financial interest and syndication rules, in the years since they were promulgated the structure of the television industry has changed profoundly."[155] Judge Posner concluded that in order for the rules to be upheld, "the statement accompanying its promulgation must show that it is rational—must demonstrate that a reasonable person upon consideration of all

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150 1993 Rules, 8 F.C.C.R. 3282, ¶ 99, at 3331 (1993).

151 *Id.* ¶ 104, at 3333.

152 *Id.* ¶ 99, at 3331.

153 *See id.* ¶ 98, at 3330. The Commission remarked about the 1991 rules that "the syndication rules are designed to foster . . . diversity specifically." *Id.*

154 *See Schurz*, 982 F.2d at 1049. Central to the FCC's decision to leave fin-syn essentially unchanged was its belief that the three networks still had the power to force independent producers to sell them programs at less than what it would cost if there was a truly competitive market. *Id.* at 1052. The networks refuted this argument by pointing to their decline in prime time audience to 62% from 90% in 1970, to the fierce competition between the three networks as evidence of no network collusion against independent producers, and to the emergence of Fox as a fourth network. *Id.* at 1046. Additionally, the three networks each commanded only 12% of total advertising revenues. *Id.* Together this is substantial, but hardly controlling.

155 *Id.* at 1046. Posner identified the spread of cable into 60% of American homes and VCRs found in 70% of American homes as the primary causes of the networks' decline. *Id.*

the points urged pro and con the rule would conclude that it was a reasonable response to a problem . . . . The new rules flunk this test."[156] The FCC, in Judge Posner's opinion, had merely thrown up its hands in the face of conflicting views and split the difference, rather than resolving the conflict in favor of the party with the stronger case, in this instance (in Posner's opinion), the networks.[157] He called the FCC opinion, "despite its length, . . . unreasoned and unreasonable, and, therefore, in the jargon of judicial review of administrative action, arbitrary and capricious."[158] Neatly condensing the FCC opinion into a paragraph, he remarked that "[s]tripped of its verbiage, the opinion, like a Persian cat with its fur shaved, is alarmingly pale and thin."[159] The FCC had not explained key concepts, overlooked key evidence, ignored arguments that had "formerly persuaded the [FCC] and that time had only strengthened," and had silently passed over "contradictions within and among [FCC] decisions."[160] Specifically, the *Schurz* court outlined five criticisms of the 1991 rules.

> First, the court charged the FCC with ignoring the networks' argument that the 1991 rules were unsuccessful because they did not, in fact, increase network access to the programming market. . . . Second, . . . the 1991 rules would not prevent the networks from using their market power to purchase programming at favorably low prices. . . . Third, . . . the 1991 rules limited competition with established networks by stunting the growth of new networks. . . . Fourth, . . . the court asserted that the FCC failed to reconcile its order supporting the 1991 rules with its Tentative Decision [of 1983]. . . . Finally, the court was concerned that the FCC never defined the word "diversity" as it applied to television programming.[161]

Accordingly, the court vacated the rules and remanded the matter to the FCC for further proceedings.[162]

The FCC responded by issuing a new set of modified fin-syn

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156 *Id.* at 1049-50.

157 *Id.* at 1050.

158 *Id.* at 1055.

159 *Id.* at 1050.

160 *Id.*

161 Pepe, *supra* note 22, at 82-86.

162 *See Schurz*, 982 F.2d at 1055. As the FCC understood it, the *Schurz* court's decision to vacate the rules and to remand the case was not a ruling that the 1991 Rules could not be justified, but rather that the FCC had failed miserably in providing adequate explanation for disregarding the networks' arguments. *See* 1993 Rules, 8 F.C.C.R. 3282, ¶ 18, at 3291 (1993). Nonetheless, upon further analysis, the FCC decided that fin-syn should be repealed. *Id.* ¶ 1, at 3282-83; see Pepe, *supra* note 22, at 82-86, for an analysis of the *Schurz* court's objections to the 1991 Rules.

rules ("1993 Rules"),[163] which still retained some restrictions. Some of the restrictions retained included the prohibition against network's "actively" syndicating programming domestically,[164] warehousing programming,[165] and on first-run domestically syndicated programming.[166] However, the restrictions imposed minimal restraints on the networks, and even these remaining restrictions were to be eliminated within two years.[167] The FCC decided upon this partial deregulation scheme for three reasons. First, the FCC wanted to observe the marketplace for a while to determine whether its "assessment that the networks would not act in ways detrimental to diversity and competition following deregulation was valid."[168] Second, the FCC believed that a two-year "sunset" period for the restrictions on active syndication was prudent given that the immediate lifting of these restraints posed a greater risk to outlet diversity than the other restraints did in the event that the FCC misjudged the network's role in the marketplace.[169] Finally, the FCC generally thought it wise not to order an immediate repeal of the rules to avoid disrupting the marketplace and perhaps causing "unintended and unforeseen negative effects."[170]

Commentators have applauded the FCC's response in 1993 for appropriately addressing the concerns raised in *Schurz*, and for recognizing that the profound changes in the marketplace mandated regulatory reform.[171] The FCC left the door open for propo-

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163 *See* 1993 Rules, 8 F.C.C.R. 3282. The Commission stated that it was amending "its financial interest and syndication rules, following the [Schurz] decision . . . ." *Id.* ¶ 1, at 3282-83.

164 *Id.* ¶ 1(c), at 3283; *see supra* text accompanying note 20.

165 *See* 1993 Rules, 8 F.C.C.R. ¶ 1(e), at 3283. For the definition of "warehousing," see *supra* text accompanying note 45.

166 *See* 1993 Rules, 8 F.C.C.R. ¶ 1(f), at 3283. First-run syndicated programs are those programs that are originally produced to be aired on independent stations. *See* PTAR Notice, 9 F.C.C.R. 6328, ¶ 7, at 6331 (1974).

167 *See* 1993 Rules, 8 F.C.C.R. ¶ 1(k), at 3284.

168 Network Financial Interest and Syndication Rules, 60 Fed. Reg. 48,907, ¶ 1, at 48,907 (1995).

169 *Id.*

170 *Id.*

171 After careful analysis of the FCC's response to the *Schurz* court's remand, one commentator had this to say:

> By promulgating the 1993 rules, the FCC sought to create a competitive balance between the networks and independent producers, without compromising the public's interest in programming selection. While the FCC's primary interest in modifying the 1991 rules was to increase programming for the television viewing audience, the FCC had a particular view towards maximizing programming diversity and increasing market competition. The 1993 rules are the cautious, but successful, result of the FCC's efforts. . . . [T]he FCC acknowledged that network dominance in the television industry had decreased significantly since 1970 and that intense competition between the networks existed. In adopting the 1993 rules, the FCC suggested that it was relying on these

nents of the rules to reargue their case by providing for a review six months before the rules' scheduled demise.[172] However, it placed the burden of proof on the proponents of the rules to convince the FCC of the continued necessity to promote diversity and competition through fin-syn.[173] Arguments both for and against retaining the rules were entertained by the FCC beginning on April 5, 1995 with the adoption of a Notice of Proposed Rule Making.[174] Absent convincing proof of its continued viability, fin-syn was set to expire on November 10, 1995.[175] However, on September 6, 1995, the FCC released an order effectuating the rules' demise as of the publication date of the order in the Federal Register. The order stated that supporters of fin-syn had failed to prove their case, and that there was no justification for extending fin-syn any longer.[176] On September 21, 1995, the Financial Interest and Syndication Rules

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> changes and safeguards on "emerging networks" to foster competition and increase diversity.

Pepe, *supra* note 22, at 90. Another commentator adds that "the [FCC's] stated purpose in enacting the fin-syn rules was to encourage competition and diversity. The marketplace itself has done more to accomplish this result than have the rules." Christian, *supra* note 14, at 117; *see* Rosencrans, *supra* note 6 (arguing in 1990 that the television market had already outgrown the need for fin-syn).

[172] *See* 1993 Rules, 8 F.C.C.R. ¶ 1(k), at 3284.

[173] *Id.*

[174] *See* Network Financial Interest and Syndication Rules, 60 Fed. Reg. 48,907, 48,907 (1995). A Notice of Proposed Rule Making is released by the FCC when it wants comments from interested parties concerning a particular rule or rules then under consideration. *Id.*

[175] *See* 1995 Order, 10 F.C.C.R. 12,165, ¶ 1, at 12,165 (1995).

[176] *Id.* ¶ 2, at 12,165. The FCC declared that since in its promulgation of the 1993 rules it determined that market conditions did not justify retention of the fin-syn rules, proponents of retaining fin-syn would have to "present evidence of networks' behavior and the status of program production and distribution markets since that time." *Id.* ¶ 5, at 12,166. The FCC set forth a list of fourteen factors that it deemed relevant to its review of fin-syn:

> (1) The extent to which a network-owned program is syndicated primarily to that network's affiliates.
>
> (2) Patterns that reveal delay in the introduction of network programs (in which the networks had financial interests or syndication rights).
>
> (3) The percentage of network programming in which a network has obtained a financial interest or syndication right.
>
> (4) The relative change in the number of independent producers creating and selling television shows to the networks.
>
> (5) Each network's share of the first-run syndicated programming domestic market.
>
> (6) Concentration of ownership in the program production industry.
>
> (7) Audience shares of first-run syndicated programming carried by non-network affiliated stations during prime time.
>
> (8) The overall business practices of emerging networks, such as Fox, in the network television and syndication business.
>
> (9) Network negotiating patterns, particularly the manner in which networks obtain financial interests and syndication rights . . . .
>
> (10) Network syndication practices, to the extent they are permitted.
>
> (11) The relationship and business arrangements between networks and third-party syndicators of off-network programming.
>
> (12) Mergers or acquisitions involving networks, studios, cable systems and other program providers since our 1993 fin-syn decision took effect.

were officially repealed.[177]

PART III. THE POST FIN-SYN TELEVISION MARKETPLACE

A. *The Independent Program Production Market—Source Diversity*[178]

Commentators have taken the position that the repeal of the rules was a prudent judgment in light of the present media environment.[179] They point to the prolification of broadcast outlets such as cable, VCRs, and direct broadcasting, as well as the addition of three new television networks.[180] They point to these as evidence of competition in the industry and an increasing supply of diverse programming. However, one commentator, while lauding the repeal of the rules as presently necessary, warned about the possibility that once the networks are

> freed of the fin-syn rules, [they] will quickly engage in anti-competitive behavior, perhaps by producing more of their own programs and then airing those programs exclusively on [their] station and cable affiliates. . . . [O]ne unfortunate result that could arise from the removal of these restrictions is the removal of several important "showcases" available to independent producers.
>
> UPN and WB will probably fill most of the air time on their networks with programs from their own production studios. ABC, NBC, and CBS are likely to follow . . . . All of this could signal trouble for small, independent producers because although there may very well be a virtual cornucopia of channels

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(13) The growth of additional networks, including the development of Fox and its position vis-a-vis the three major networks.

(14) The growth of the number and types of alternative outlets for sale of programming (*e.g.*, the development of the Direct Broadcast Satellite service; cable penetration; wireless cable development).

Id. ¶ 6, at 12,166. The FCC examined the evidence based on each of these factors and determined that proponents of retaining the fin-syn rules had failed to provide *current* empirical data or other evidence concerning the above factors that would justify the continued retention of fin-syn. *Id.* ¶ 9, at 12,167; Network Financial Interest and Syndication Rules, 60 Fed. Reg. ¶ 5, at 48,908.

177 Network Financial Interest and Syndication Rules, 60 Fed. Reg. 48,907.

178 Source diversity refers to programming sources, meaning program producers. *See Schurz*, 982 F.2d at 1054.

179 *See* Pepe, *supra* note 22; Christian, *supra* note 14.

180 *See supra* text accompanying note 171; *see also* Capital Cities/ABC, Inc. v. FCC, 29 F.3d 309 (1994) (The networks petitioned the Seventh Circuit for a review of the 1993 Rules, arguing that there was no reason to retain any restrictions even for so short a time as two years, considering the parameters of the television marketplace. Judge Posner denied the review, explaining that "these restrictions strike us as rather small beer when their temporary status—only sixteen months to go before they expire—is considered." *Id.* at 315. He added that the "precise timetable on which the Commission executes a major turn in regulatory policy is a matter of judgement and prudence . . . [that] is confided to the discretion of the Commission within broad limits not here exceeded." *Id.* at 316.).

> available on which they could display their programs, if independent producers do not receive financial support at the beginning, they will be unable to produce any programs. Many times, the networks are in the best position to provide this financing. Who knows if the "owners" of the remaining 497 channels will be able to afford the cost of producing a new television series.[181]

The above illustrates one of the concerns arising from the repeal of fin-syn. The networks, including the newer UPN and WB networks, can freeze out independent producers since they are now free to draw on their own production facilities for their programming. This underscores a very important point: the FCC has merely concluded that there is no *past* evidence of such behavior on the part of ABC, NBC, and CBS.[182] The FCC did not attempt to project how the networks, including Fox, UPN, and WB, will respond to the complete repeal of fin-syn. Regrettably, the anticipated market behavior has begun to occur. The media marketplace has begun to consolidate, with an eye toward the benefits of vertical integration.

A recent example is the acquisition of ABC by the Walt Disney Company.[183] The Disney/ABC merger has been called "a classic example of vertical integration in which a company moves into more than one stage of production or distribution."[184] In fact, with the acquisition of ABC, Disney "has now put together a leading Hollywood studio, a leading TV network and locally dominant phone companies covering 3/7 of the United States."[185] Disney's

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181 Christian, *supra* note 14, at 119.

182 *See* 1995 Order, 10 F.C.C.R. 12,165, ¶ 9, at 12,167 (1995) (stating that proponents of retaining fin-syn must show evidence of anti-competitive behavior by the networks between 1993 and 1995); *see supra* text accompanying note 176.

183 The FCC did, in fact, note the recent merger of ABC and Disney and stated that it "will, of course, be reviewing these acquisitions in the normal course of its regulatory business to ensure that they do not undermine the competitiveness of the production and distribution markets." Network Financial Interest and Syndication Rules, 60 Fed. Reg. 48,907, ¶ 25, at 48,912 (1995). Clearly, the FCC was aware of the potential problems that could arise as a result of the repeal, yet it issued the repeal nonetheless. One has to wonder why the merger announcement gave no pause to the FCC's drive to accelerate the repeal, considering that the merger announcement directly implicated factors 6 and 12, (relating to mergers and acquisitions involving networks, and concentration of ownership in the media industry, respectively) which the FCC listed as important considerations to be weighed in repealing fin-syn. *See supra* note 176. One may be truly puzzled by the fact that the FCC subsequently gave final approval to the merger in the midst of a flurry of recent network business activities discussed in this Note. Final approval of the merger was granted on February 8, 1996. *See* Albert R. Karr & Thomas R. King, *FCC May Toss Out Rules On Owning Competing Media*, WALL ST. J., Feb. 9, 1996, at B2.

184 Claudia MacLachlan, *TV Deregulation Is Driving The Deals*, NAT'L L.J., Aug. 14, 1995, at B1.

185 Tony Jackson, *Masters of the Moving Image: US Communications Mergers are Raising Fears for the Future of Competition and Creativity*, FIN. TIMES, Aug. 2, 1995, at 15. Disney also ac-

move was certainly "fueled by the expectation that the networks would no longer be locked out of the syndication market."[186] The repeal of two of the fin-syn rules were particularly crucial to Disney's decision to acquire ABC.[187] First, with the repeal of the rules, Disney will be able to fill as much of their prime time entertainment as they wish with in-house productions. Second, Disney can reap the full benefits of these programs through domestic and foreign syndication.[188] This may have a devastating effect on independent program producers, due to the possibility that Disney will give less consideration to outside producers whose "wares might have greater appeal, if they could only be seen."[189]

These concerns are beginning to materialize. Soon after announcing its deal to acquire ABC, Disney announced that it would provide programming for ABC's Saturday morning block of children's television by late 1996.[190] Disney has made no secret of the

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quired a few other choice media properties with its acquisition of Capital Cities/ABC. The ABC Cable and International Broadcast Group is the majority owner of cable networks ESPN and ESPN2, and is a partner in the A&E and Lifetime cable networks. ESPN reaches about 70% of American homes and is seen in 130 countries in 11 different languages. *See* The Walt Disney Company, 1995 Annual Report 9 (1995). Additionally, the Capital Cities/ABC Publishing Group owns and operates seven daily newspapers, including the nationally respected *Kansas City Star* and *Fort Worth Star-Telegram*. *Id.*

186 Bill Carter, *F.C.C. Speeds Repeal of Syndication Rules*, N.Y. Times, Sept. 7, 1995, at D6; *see* MacLachlan, *supra* note 184 (quoting Samuel C. Butler, presiding partner at the prestigious New York law firm Cravath, Swaine, & Moore) ("That's [the anticipated repeal of the fin-syn rules] definitely what's fueling this [referring to the $19 billion merger of Disney with ABC, and the $5.4 billion acquisition of CBS by Westinghouse Electric Corporation]"). The Walt Disney Company itself later confirmed these speculations. In a pamphlet distributed to its stockholders describing the history and details of the ABC acquisition, Disney stated, "[o]ne of the most significant regulatory changes was the FCC's tentative decision to repeal its financial interest and syndication rules . . . . Given Disney's syndication activities, the fin-syn rules would have hampered New Disney's [the name of the combined Disney and ABC] syndication and related businesses." Disney Prospectus, *supra* note 1, at 25. Moreover, "[i]f the fin-syn rules are still in effect upon the closing of the Acquisition, New Disney will not be in compliance with certain of such rules if Disney's current syndication activities are continued." *Id.* at 113.

187 *See id.* and accompanying text (observing that the lifting of the 40% cap on in-house productions and the prohibition on syndicating activities were crucial to Disney's acquisition).

188 *See* Jackson, *supra* note 185.

189 *Merger Frenzy*, Nat'l L.J., Aug. 14, 1995, at A18. The article opines that "[t]he ABC deal . . . through its vertical integration of interdependent industries, produces a media entity with the resources both to create and to distribute programming . . . . Vertical integration also means that this media combination will be able to rely on itself for products . . . ." *Id.*

190 *See* Karen Donovan, *Media Megamergers: No Problem?*, Nat'l L. J., Sept. 25, 1995, at A1. Donovan reports that the vertical integration of Disney/ABC invites antitrust questions, but that the prevailing view among antitrust lawyers is that "there are too many channels of distribution and too many sources of content, and nobody has enough control over either" for there to be an antitrust concern. *Id.* (quoting antitrust lawyer Joe Sims). As to whether the ABC merger means that independent producers will be squeezed out, the article quotes Sanford M. Litvack, Disney's general counsel and Chief of Corporate Operations, declaring "Hell, no." *Id.* ABC later announced that Disney was supplying three new chil-

fact that it "expected to find an outlet for some of its shows on ABC."[191] Other networks, as well, have increasingly relied on their respective production facilities.[192] Fox, for example, has already been producing its own programming (for example, *The Simpsons*), and has successfully begun syndicating *Married—with Children.*[193] The WB and UPN networks rely primarily on their movie studio parents to provide their programming.[194] This leaves the independent producers in a precarious position. With fewer network backers and a dwindling supply of independent television stations,[195] these producers will have neither the funds nor the outlets to showcase their goods. Furthermore, the present trend among the networks is to sign up as much programming talent as they can, thereby increasing the probability that all producers must join some network, preferably a major one, or risk not having the capital to continue producing diverse programming.[196]

An argument can be made that with six networks presently

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drens' series: *The Jungle Book's Jungle Cubs, The Mighty Ducks,* and *Gargoyles: The Goliath Chronicles. See ABC Saturday Lineup For Children Includes 3 New Disney Series,* WALL ST. J., Jan. 30, 1996, at B5. Incidentally, children's programming, whether on the networks or on cable, draws some serious advertising dollars. For the 1995-96 season alone, advertisers spent some $660 million in advance sales, and industry observers are expecting even more for the 1996-97 season. *See* Elizabeth Jensen, *Advertisers Get More Play Time On Kids' TV,* WALL ST. J., Feb. 6, 1996, at B1.

191 *Id.*; *see supra* note 186 and accompanying text. Contrast ABC's program changes with this observation from the FCC: "No party has presented any evidence indicating that the established networks [ABC, NBC, CBS] have allowed their financial interests in or syndication rights to programming aired during prime time to influence their decisions to either retain or cancel that programming." Network Financial Interest and Syndication Rules, 60 Fed. Reg. 48,907, ¶ 14, at 48,909 (1995). The previous statement was in response to proponents of fin-syn who could not, at that time, point to any specific actions by the established networks, but were expecting such actions to ensue as a result of the repeal.

192 The percentage of prime time entertainment series produced in-house by the three networks increased from less than 1% in 1993-94 to 6.3% in the 1993-94 season. *See* Network Financial Interest and Syndication Rules, 60 Fed. Reg. ¶ 17, at 48,910. In terms of the percentage of *hours* of such programming produced in-house, the figures vary. According to NBC, in-house productions accounted for 20.2% of the three networks' prime time hours in 1992-93, 19.0% in 1993-94, and 25.8% in 1994-95. *Id.* The remainder of programming is supplied by independent producers. Based on NBC's numbers, the FCC concluded that the networks were not precluding outside programming from their schedules. The flaw in this analysis is fairly obvious. One can hardly draw conclusions of future network behavior based on figures that represent network activity while fin-syn was at least partially in effect, nor does this conclusion allow for the possibility of the present vertical integrations that will substantially increase the number of in-house productions.

193 Telephone Interview with Jim Hedlund, President of the Association of Independent Television Stations ("INTV") (Nov. 30, 1995) [hereinafter Hedlund Interview]. Fox claims that it currently produces only three and a half hours of its 15 hours of weekly prime time programming. *See* Network Financial Interest and Syndication Rules, 60 Fed. Reg. ¶ 19, at 48,910.

194 Hedlund Interview, *supra* note 193; *see* Christian, *supra* note 14, at 118 (warning that The WB and UPN networks will "probably fill most of the air time on their networks with programs from their own production studios"). *Id.*

195 Hedlund Interview, *supra* note 193.

196 *Id.*

broadcasting, competition and diversity should be guaranteed.[197] However, this argument overlooks two important points. First, the two newest networks, UPN and WB, can hardly be considered viable alternative outlets at the present time. They do not supply a significant number of hours of prime time programming[198] and they are structurally disadvantaged, with fewer of their affiliates broadcasting in the stronger VHF band.[199] Considering the steep losses suffered by UPN and WB, it is doubtful that they will maintain the financial capability to effectively compete in the market for producers and/or programming.[200] Certainly, a company like ABC that can tap the deep pockets of Disney presents a formidable obstacle to the acquisition of quality programming. Inevitably, there will be "less competition . . . as [there is] more concentration."[201] With all or most program providers signed up with the major networks, it is likely that the public will be stuck with homogenous entertainment offerings and "the dull repetition of a single, corporate point of view."[202]

Second, there is also some concern in news-gathering.[203] If all news establishments are run by three or four "supercorporations, as opposed to 130 corporations, you're likely to have a great

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197 *See* Network Financial Interest and Syndication Rules, 60 Fed. Reg. ¶ 22, at 48,911; Christian, *supra* note 14, at 1.

198 UPN and WB currently supply only two to four hours of weeknight prime time programming. Network Financial Interest and Syndication Rules, 60 Fed. Reg. ¶ 22, at 48,911 (articulating the concerns of INTV). Moreover, while ABC, NBC, CBS, and Fox accounted for a combined 66% share of prime time viewing for the 1994-95 television season, UPN and WB managed to draw a meager *combined* nine percent share for the same period. *See* In the Matter of Annual Assessment of the Status of Competition in the Market for the Delivery of Video Programming, 11 F.C.C.R. 2060, ¶ 113, at 2114 (1995).

199 *See* Network Financial Interest and Syndication Rules, 60 Fed. Reg. ¶ 22, at 48,911 (articulating the concerns of INTV).

200 UPN reportedly lost $125 million in 1995, with wider losses expected for 1996. Undaunted, Chris-Craft Industries, Inc., parent of UPN, added a third evening of prime time programming to UPN's schedule. *See* Lon Grahnke, *Justice "Swift" on UPN; Renegade Cop Bashes Bad Guys*, CHI. SUN TIMES, Mar. 12, 1996, at 31; Eben Shapiro, *Chris-Craft's 4th Period Net Fell 67% On Losses at UPN, Weak TV Ad Revenue*, WALL ST. J., Feb. 15, 1996, at B6. Similarly, Time Warner announced that its network, WB, lost $66 million in 1995. These losses were due, at least in part, to weak advertising revenue. *See* Shapiro, *supra*.

201 141 CONG. REC. 10917 (1995) (comments of Sen. Dorgan). Senator Dorgan was voicing his concerns about how the creation of vast media enterprises will negatively affect free enterprise. *Id.* President Clinton also voiced his concern over the creation of media conglomerates during a press conference regarding what was later to become the Telecommunications Act of 1996. Mr. Clinton remarked, "I do think it would be an error to set up a situation in the United States where one person could own half the television stations in the country or half the media outlets." To Avoid Clinton Veto, Conference Committee May Change Bill, FCC Report, 1995 WL 2288037 (1995).

202 *Merger Frenzy*, *supra* note 189.

203 *See* Stephen Galloway, *If Americans are Fascinated with Filmmaking, They are Even More Fascinated with Tinseltown's Way of Doing Business*, HOLLYWOOD REP., Nov. 7, 1995, Cover Story.

homogeneity of product."[204] Additionally, there is the potential for conflicts of interest. Will the parent corporation censor news material if it is contrary to the views of the parent?[205] We have already seen some evidence of this with the Turner Broadcasting Company's decision not to allow its subsidiary, CNN, to run an advocacy advertisement (analogous to an editorial) opposing the then-pending telecommunications legislation.[206] Obviously, such concerns are real, although it is hard to predict whether they will actually be realized.

B. *The Syndication Market—Outlet Diversity*[207]

The Association of Independent Television Stations ("INTV")[208] argues that with the repeal of the restrictions on network syndication of programming, the networks will once again become a funnel for their affiliates, granting syndication rights to affiliates over independent stations.[209] The FCC refuted this claim by pointing to the lack of post-1993 empirical evidence supporting INTV's assertion,[210] and the fact that there was no evidence that "the Fox Broadcasting Company ('Fox'), which [has been] permitted under [fin-syn] to engage in active syndication, has favored its affiliates in syndicating Fox programming."[211] While there may not have been evidence of networks favoring affiliates then, there may be now, and this is not surprising considering that the networks are no longer prohibited from doing so. For example, one of today's most popular shows is a sitcom entitled *Friends*, aired on NBC.[212] The producer of this program is Warner Brothers, a unit of Time Warner, Inc.[213] With the show just midway through its second season, Warner decided to begin syndicating the program.[214] De-

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204 *Id.*

205 *Id.*

206 *See* Cheryl Bolen, *Media Concentration: Merger Mania or Myth*, BNA MGMT. BRIEFING, Nov. 20, 1995.

207 Outlet diversity refers to the distribution outlets, which are television stations. *See Schurz*, 982 F.2d at 1054.

208 *See supra* note 193.

209 *See* 1995 Order, 10 F.C.C.R. 12,165, ¶ 10, at 12,167 (1995).

210 *Id.* ¶ 12, at 12,167.

211 *Id.* ¶ 16, at 12,168.

212 *See* Elizabeth Jensen, *Television: New Market Rules Help Make "Friends" Quick Syndication Hit*, WALL ST. J., Jan. 15, 1996, at B1.

213 *Id.*

214 *Id.* Warner wants to capitalize on the red-hot demand for sitcoms. Reruns of two other highly popular programs, *Seinfeld* and *Home Improvement*, have been drawing huge audience shares, while stations are paying top dollar for the rights to *Frasier* and *Mad About You.* The estimated revenue from the sale of syndication rights to *Friends* is $2.2 million per episode with a minimum of 88 episodes expected to be produced. At this price, *Friends* would place among the top six highest-ever rerun-syndication prices. Presently, the all-

mand for the reruns was fierce, owing to the show's popularity and the number of stations bidding for them.[215] Rights to the reruns were eventually bought by seven stations owned by the Tribune Company of Chicago.[216] Coincidentally, those stations recently became affiliates of Warner's new WB network.[217] Though Warner "insists it didn't favor Tribune in the *Friends* bidding,"[218] one wonders whether that assertion can withstand further scrutiny.[219] At the very least, it raises the troubling specter of similar transactions that blatantly favor affiliates.[220]

C. *The Telecommunications Act of 1996*

Perhaps the wild card in this deck of market deregulation is the recent passage of the Telecommunications Act of 1996.[221] For over fifty years, lawmakers, regulators, and the courts have believed that the preservation of diverse media voices is not only in the public interest, but necessary to protect the rights guaranteed by the First Amendment.[222] The 104th Congress decided that the existing regulations were no longer necessary to meet those ends. Congress

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time price leader is *The Cosby Show*, which commanded $4.4 million for each of 200 episodes, for a total of $880 million. *Id.* at B5.

215 *Id.*

216 *Id.*

217 *Id.*

218 *Id.*

219 Notwithstanding the lofty price to be paid for the rights to *Friends*, Warner will not be surrendering those rights permanently. As a condition of sale to any station that purchases the rights to *Friends*, Warner has insisted that those rights are only exclusive through the year 2001, at which time the station(s) must share the reruns with cable network WTBS, whose owner, Turner Broadcasting System ("Turner"), has recently agreed to merge with Time Warner, parent of Warner. *Id.* This further leads one to consider whether this condition was a means of keeping the rights to *Friends* in the family, so to speak. Having to share rights with Turner may be a disincentive to all but affiliates of Warner who will be indirectly affiliated with Turner anyway as a result of the merger, and possibly heavily dependent on Turner's production facilities for their programming besides.

220 A related issue is the potential for aggressive expansion by the networks into syndication activities generally through the acquisition and consolidation of distributors, thereby wiping out competition and driving up prices. Though the networks would presumably have a hard time acquiring large syndicators such as King World, we may see the acquisition of smaller syndicating companies. For example, CBS (now a unit of Westinghouse Electric Company, having been acquired for $5.4 billion) has agreed to acquire MaXam Entertainment, a television syndication company, to be merged with Group W Productions, the syndication arm of Westinghouse. The new division "will produce, market, and distribute original programming for domestic and international syndication, and will handle sales of rerun of CBS-produced shows." *Westinghouse Electric Corp.: CBS Plans to Buy MaXam, A TV Syndication Concern*, WALL ST. J., Jan. 23, 1996, at B4.

221 Telecommunications Act of 1996, Pub. L. No. 104-104, 110 Stat. 56 (1996).

222 *See* Bolen, *supra* note 206. The author does an admirable job of compiling numerous interviews with lawmakers and industry people and contrasting their views on how the Telecommunications Act may affect the diversity of media voices. She also provides an excellent summary of media regulations prior to the enactment of the Act, as well as the House version of the Act versus the Senate's. Most of her discussion about the Act, while captivating, is beyond the scope of this Note.

cited the ever-rapid advance of technology and ways of delivering information to the public as reasons for loosening the reins on the broadcast market.[223] In fact, Congress declared that the purpose of the Act was "to promote competition and reduce regulation in order to secure lower prices and higher quality services for American telecommunications consumers and encourage the rapid deployment of new telecommunications technologies."[224] Whether the Congressional purpose will be served remains to be seen, and naturally, is hotly debated.[225] Since the Act affects numerous areas that do not fall within the scope of this Note, this subsection will focus on the part of the Act that presents similar uncertainties to the ones discussed above relating to the repeal of fin-syn.

The Act affects essentially three communications groups: the telephone industry, the cable industry, and the broadcast industry. For the telephone industry, the Act means that local phone markets previously served exclusively by Bell companies since the AT&T breakup in 1984 will be opened to competition from long-distance companies such as MCI, Sprint, LCI International, and, of course, AT&T.[226] As for the Bell companies, provided they prove to the satisfaction of the FCC that they have opened their local phone networks to new competition, they will be allowed to compete in the long-distance phone market.[227] The Act also mandates "universal service,"[228] which guarantees phone service even to the most remote rural areas but does not provide for its funding.[229]

For the cable industry, the Act removes the current rate regulations on cable systems that serve less than one percent of the na-

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[223] *Id.* Critics of the Telecommunications Act do not necessarily disagree that *eventually* no one media entity could control the market, due primarily to the increasing acceptance of the Internet as an alternate source of news and information and due to the increase in the capacity of broadcast delivery systems to supply channels. However, critics are concerned that *presently* these advances have not reached their potential, as the majority of Americans still turn to their local news sources, the newspaper or the television, and for at least the near term it is conceivable that, as a result of the Telecommunications Act, one entity can control the news content of any particular area. *Id.*

[224] Telecommunications Act of 1996, 110 Stat. 56, 56.

[225] *See* Bolen, *supra* note 206.

[226] *Likely Mergers Herald an Era of Megacarriers*, WALL ST. J., Feb. 2, 1996, at B1 [hereinafter *Likely Mergers*]. It is a shame that the author of the preceding article is not identified by name because the article masterfully presents a concise yet complete summary of the salient points of the Telecommunications Act. *See* Telecommunications Act of 1996 §§ 251-259.

[227] 47 U.S.C. § 271(d)(2)(B) (Supp. 1996). Critics of the Act see it as paving the way for "megacarriers," as local and long-distance companies will forge alliances rather than competing with one another. Thus, the Act will have served to lessen competition rather than to increase it. *Likely Mergers*, *supra* note 226, at B1.

[228] 47 U.S.C. § 254 (Supp. 1996).

[229] *See Likely Mergers*, *supra* note 226, at B1. The Telecommunications Act leaves the decision as to how to fund this mandate up to the states and the FCC. *Id.*

tion's subscribers.[230] The bigger cable companies will have to wait three years for their rate regulations to be lifted.[231] Additionally, the restrictions on "cross-ownership"[232] are removed, thus allowing a single company to provide both cable service and telephone service in the same community.[233]

Finally, for the broadcast industry, the Act allows any network to own as many television stations as it wants, as long as the stations do not reach more than thirty-five percent of the United States.[234] In an anticipatory gamble that the Act would pass and include this increase, Westinghouse bought CBS, a move that created a group of fifteen stations reaching thirty-three percent of the United States.[235] Also expanding its market reach was NBC, which, with the announcement of an acquisition on the same day that Congress passed the Act but prior to the President's signing it into law, now owns nine stations reaching twenty-three percent of the United States.[236]

The expansion of direct network broadcasting reach, coupled with the repeal of the cross-ownership restrictions, further inhibits the emergence of diverse programming sources and a healthy syndication market. Permitting television and cable companies to merge essentially returns the broadcast market to what it was before 1970, when a few companies dominated the playing field, dictated the types of programming that would be broadcast, and

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[230] 47 U.S.C. § 543(m)(2) (Supp. 1996); *see also Likely Mergers*, *supra* note 226, at B1.

[231] 47 U.S.C. § 543(c)(4); *see also Likely Mergers*, *supra* note 226, at B1.

[232] Cross-ownership refers to the restrictions on the consolidation of various media outlets. Cross-ownership restrictions prevented a telephone company from owning a cable system, and a television network from owning a cable system in the same community. *See* Bolen, *supra* note 206.

[233] As with the telephone market deregulation, critics of the Act are concerned that the repeal of the cross-ownership restrictions will result in the consolidation of vast media enterprises. *See Likely Mergers*, *supra* note 226, at B1. Another aspect of the repeal of the cross-ownership rules is that the same company may own a television network and a cable system, as noted *supra* note 232. If not for the repeal, the merger between Time Warner and Turner Broadcasting System would never have been contemplated, since Time Warner owns the WB Network and Turner is a large cable concern.

[234] Telecommunications Act of 1996, Pub. L. No. 104-104, § 202(c)(1)(B), 110 Stat. 56 (1996). Prior to the Act, networks were restricted to owning just 12 television stations reaching 25% of the United States. *Id.* § 202(c)(1)(A), (B) (eliminating restrictions on the number of television stations that one network may own, and increasing the percentage from 25% to 35%). *See Likely Mergers*, *supra* note 226, at B1-2.

[235] *See Likely Mergers*, *supra* note 226, at B1.

[236] *See NBC Buys Station Owner Outlet*, WALL ST. J., Feb. 5, 1996, at B7. NBC purchased Outlet Communications, Inc., a company that owns three television stations in Raleigh-Durham, North Carolina, Columbus, Ohio, and Providence, Rhode Island. *Id.* The Telecommunications Act of 1996 was passed by Congress on February 5, 1996, *see* S. 652, 104th Cong. (1996) (the Act was originally introduced on March 30, 1995, and went through five revisions before finally being passed) but was not signed into law by President Clinton until three days later, on February 8. *See* Karr & King, *supra* note 183 (reporting that the President had signed the Act).

controlled who would get subsequent syndication rights. In addition, allowing television networks to own, directly or indirectly, as many stations as they want[237] encourages them to seek out production/distribution alliances to maximize audience coverage[238] and simply refrain from selling any syndication rights at all. In light of the repeal of the cross-ownership restrictions, coupled with the repeal of fin-syn, independent stations face daunting challenges ahead in obtaining syndication rights to network-produced programming.

D. *Alternate Proposal to Repeal of Fin-Syn*

In view of the Telecommunications Act, a return to the full restrictive power of fin-syn is unlikely. However, the following two restrictions may coexist with the Act, and will protect the broadcast market without stifling it completely. These restrictions should apply equally to all current networks.[239] First, the forty percent cap on in-house productions as originally articulated in the 1991 Rules should be adopted. This will ensure that no matter how large a network's national coverage is as a result of alliances, it still must accept programming from outside producers. Furthermore, it will discourage the networks from their present objective of bringing such talent in-house, thus allowing independent producers to retain their creative autonomy while not risking the loss of network exposure.[240]

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237 *See* Telecommunications Act of 1996 § 202(c)(1)(A).

238 An early example of such an alliance is a joint programming partnership between New World (a television station group) and Fox, which together reach 40% of the United States. *See The Changing TV Landscape: Mergers, New Networks, and Alliances Highlight the Importance of Local Stations*, MEDIAWEEK, Nov. 13, 1995, at S1.

239 This would require redefining "network" to include "any entity that reaches 75% of the total U.S. viewing market," and disposing of the requirements regarding the number of prime time programming hours and the number of states in which the entity has affiliates. Such a definition would complement the Telecommunications Act's focus on percentage of national coverage, and allow for the emergence of new broadcast outlets that need not fear bumping up against programming hour limits (as Fox did under the original 1970 Order, and would have under the 1991 Rules had the FCC not grandfathered the clause). *See* discussion *supra* part II.B.

240 Under the 1991 rules, the prohibition on actively syndicating programming did not apply to in-house productions. *See* 1991 Rules, 7 F.C.C.R. 345, ¶ 5, at 345 (1992). Thus, in order to prevent the networks from loading up their prime time schedules with in-house programs and subsequently syndicating them, the FCC tacked on the 40% cap on prime time in-house productions. *See* 1993 Rules, 8 F.C.C.R. 3282, ¶ 68, at 3317 (1993). The *Schurz* court described this aspect of the rules "unwieldy and unduly restrictive." *Id.* Consequently, as part of the 1993 rules, the FCC eliminated the 40% cap and replaced it with a more stringent prohibition on the networks from actively syndicating any programming, whether it had been produced in-house or purchased from an outside producer. *Id.* According to the FCC, this eliminated the need for a 40% cap, since the networks could no more syndicate their in-house programs than anything else, and had no reason to load up their schedules with in-house productions over outside productions. *Id.* However, with

Second, the networks should be prohibited from actively syndicating all programming, whether produced in-house or otherwise procured.[241] This rule, while protecting independent stations from undue pressure from the networks, does not close the networks out of the syndication market entirely.[242] Moreover, it would prevent the networks from favoring their affiliates when selling syndication rights, since networks would be prohibited from controlling such sales. Control would remain with the independent syndicators, who would presumably entertain bids for syndication rights from both independent stations and network affiliates equally.

Finally, a procedural requirement should be imposed upon the networks that they submit periodical reports to the FCC describing their ownership of and involvement in broadcasting activities. This would include providing information about the number of television stations either owned by or affiliated with the network, any programming/distribution alliances forged (as allowed under the Telecommunications Act), and the categories of programming offered to the public (to determine if they are attempting to maintain a diverse programming schedule). This reporting requirement is important for the FCC to be able to monitor the networks' conduct and respond to any threats to programming diversity.[243]

These rules represent a logical alternative to the total repeal of fin-syn. As noted above, there is ample evidence that the networks are going about undoing competition in the television marketplace

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vertical integrations such as Disney/ABC, networks will still have incentive to produce their own programming, irrespective of whether they will be able to subsequently "actively" syndicate such programming, even if only to exploit the economic synergies that motivated the integration. Therefore, the 40% cap on in-house productions should remain in addition to the prohibition on active syndication.

241 This rule was originally part of the 1993 Rules. *See* 1993 Rules, 8 F.C.C.R. ¶ 67, at 3316-17.

242 *See supra* note 20 (describing "active" versus "passive" syndication). Furthermore, as under the 1993 rules, networks will not be prohibited from acquiring financial interests in all off-network programming, as well as in first-run programming produced in-house. *See* 1993 Rules, 8 F.C.C.R. ¶ 69, at 3317-18.

243 Ideally, all three proposals should be adopted, but at the very least the reporting requirements should be adopted so that the FCC can better monitor the effects of a deregulated market. The 1993 rules retained similar reporting requirements for that very reason. *See* 1993 Rules, 8 F.C.C.R. ¶ 109, at 3335-36 ("[W]e are retaining a set of reporting requirements tailored to facilitate our review of the effects that our actions here will have on network behavior."). The retention of reporting requirements was suggested by INTV in its Comments opposing the final repeal of fin-syn, but the FCC declared that proponents of fin-syn (including INTV) had failed to demonstrate a need for continuing such requirements. *See* Network Financial Interest and Syndication Rules, 60 Fed. Reg. 48,907, ¶ 26, at 48,912 (1995). As this Note has shown, network behavior in the form of mergers, programming alliances, and syndication activities requires that reporting procedures should be reinstated, so that the FCC can monitor the effects of this network behavior.

through large mergers and programming alliances. Irrespective of whether the FCC was correct in its conclusions regarding the marketplace when it accelerated the repeal, it did not give full consideration for the kinds of activities that are now taking place.

Conclusion

The broadcast market is evolving rapidly, encompassing more and more channels of information and entertainment delivery. Those who view the repeal of fin-syn and the passage of the Telecommunications Act as acts of a progressive government relying on self-regulating markets may have a valid argument, but only in the long run. As the market expands and the new technologies become widely available and accepted, the need for a regulatory body to ensure diversity greatly decreases. However, in the short run, even if only for a few years, some regulation is necessary to prevent a few "media 'mastodons' [from] eat[ing] their competition."[244] No doubt Disney would have thought twice before acquiring ABC if the combined company would have faced restrictions on the amount of in-house programming that it could broadcast and on the syndication of its programming over its newly assembled national outlet.[245]

The events presently unfolding, such as the Disney/ABC merger and the numerous other media alliances and purchases,[246] support the notion that the repeal of the fin-syn rules was premature, a product of the present deregulatory climate. The fin-syn rules were enacted to avoid precisely the kind of consolidation of power that we are currently witnessing. In the 1960s, "[p]ublic resentment eventually rose against such power,"[247] and the government responded with the fin-syn rules. It is very likely that public resentment will rise again against these "Goliaths" of media, and force the government to take action again.[248] Thus, a more sensible approach would be to maintain some regulation of the television industry until technological advances have truly made a Disney/ABC type merger inconsequential in terms of market influence. In the absence of any regulations, these consolidations will

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244 Bolen, *supra* note 206 (paraphrasing Larry Irving, Administrator of the National Telecommunications and Information Administration (NTIA)).

245 *See* discussion *supra* part III.A.

246 *See* discussion *supra* part III.A-C.

247 Bill Keveny, *Experts See Less Diversity In The Media*, HARTFORD COURANT, Sept. 23, 1995, at A1 (quoting Lee Brown, editorial consultant for the Center For Communication, and former *New York Times* television reporter).

248 *Id.*

continue and will subsequently foster a media climate that the FCC has sought to prevent.

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