

Time to rethink set-top box regulation

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Cable companies and telecommunications companies that have begun offering video services to consumers are asking the Federal Communications Commission to postpone the set-top box "integration ban," now scheduled to go into effect July 1, 2007.

Not only should the ban be delayed, it should be permanently rescinded.

The ban is a relic of a "managed competition" regulatory mindset that has been unsuccessful in other contexts and is entirely unsuited to the increasingly competitive converged world of video communications services. If it goes into effect, it will inhibit innovation in a variety of ways and impose significant costs on consumers.

The "integration ban" stems from the [Telecommunications Act of 1996](#), which sought to stimulate a competitive market in "navigation devices" such as set-top boxes. As a result, the FCC adopted rules that would require most multichannel video program distributors to separate (meaning to not integrate) the security functions (which are specific to the individual provider) from the other functions of the set-top box. Consumers would be able to purchase a set-top box commercially, but would have to get a card--[known as a CableCard](#)--from their video provider for the set-top box to work.

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The idea is that consumers should have the benefit of a competitive set-top box market and not be dependent on devices leased by their providers. However, the requirement also applies to those devices, so as not to place the independent providers at a competitive disadvantage. Cable companies and the new entrants such as AT&T and Verizon are covered by this requirement; direct-broadcast satellite providers apparently are not.

The integration ban is essentially a mandatory unbundling regime for manufacturers of navigation devices. The experience with the other, better-known unbundling regime established by the 1996 act—the effort to promote local telephone competition by requiring incumbent local exchange carriers to unbundle their networks—should give the FCC pause. That experiment ultimately proved unsuccessful, at a cost of tens of billions of dollars of economic activity. And, competition developed in other ways.

This is exactly what is happening in the video sector. The integration ban is based on the premise of a monopoly video provider, but we now have cable, direct broadcast satellite, traditional telephone companies and Internet video all scrambling for consumers' attention and dollars. This is all happening not by creating artificial regulatory advantages, but as a result of technological advances and by removing barriers to entry.

Moreover, a robust competitive market for cable-ready devices has apparently also developed, without the integration ban going into effect. This belies the notion that cable or other video providers have either the ability or the incentive to squelch competition in that area. Their major incentive is to increase the value of their video services to consumers. A competitive device market is entirely consistent with that goal. But it should not be mandated, because integrating the various navigation and video-provider functions may also sometimes be the best way to foster innovation, promote efficiency and best serve consumers' interests. Regulators are not in a position to determine the circumstances in which one alternative is better than the other.

Finally, the integration requirement has very tangible costs. It would [require consumers to transition to CableCard-ready boxes](#), which everyone expects to be superseded in a few years by more efficient downloadable security systems. This, at a cost of \$70 to \$90 per leased box (which inevitably will be passed on to consumers), according to industry estimates.

It would divert resources from the rollout of advanced broadband, video and voice services, which are really what consumers want. It would increase the cost of the digital-TV transition by slowing the migration to pay-TV services. And it would bias competition if some providers--such as cable--are subject to the integration ban, while others--such as direct broadcast satellite--are not.

The communications world has changed a lot since 1996. One way the FCC can recognize this is to rescind the non-integration requirement.

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