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April 10, 2019

EX PARTE COMMUNICATION
Chairman Ajit Pai
Commissioner Brendan Carr
Commissioner Michael O'Rielly
Commissioner Jessica Rosenworcel
Commissioner Geoffrey Starks
Federal Communications Commission
445 12th Street, SW
Washington, DC 20554

Re: MB Docket No. 05-311
Second Further Notice of Proposed Rulemaking
In the Matter of Implementation of Section 621 (a)(1) of the Cable Communications Policy Act of 1984 as Amended by the Cable Television Consumer Protection and Competition Act of 1992-City of Newton, Massachusetts Reply Comments

Honorable Chairman Pai and Commissioners Carr, O'Rielly, Rosenworcel and Starks:

The City of Newton, Massachusetts, acting by and through its Mayor Ruthanne Fuller as cable license Issuing Authority, submits these *ex parte* comments.

I. RESPONSE TO NCTA'S MARCH 13, 2019 *EX PARTE* COMMENTS

In its March 13, 2019 *ex parte* comments at pp.4-5, NCTA responded to the Reply Comments of the City of Newton at pp.6-9. NCTA maintains that the Commission's cable rate regulations and Form 1240 do not prevent the Commission from adopting its tentative conclusions regarding the treatment of franchise related costs (cable-related in-kind contributions) as franchise fees. NCTA is incorrect.

A. NCTA Admits that the Commission's Proposed Treatment of Franchise-Related Costs Conflicts with the Commission's Existing Cable Rate Regulations

NCTA admits that the Commission has distinguished between franchise fees and franchise-related costs under its current cable rate regulations. It incorrectly claims that the Commission may ignore this distinction. The distinction is grounded in the federal statute that directed the Commission to consider in setting cable rates costs which the Commission now has improperly proposed to treat as franchise fees. *See. e.g., Thirteenth Order on Reconsideration,* MM Docket No. 92-266 (Sept. 22, 1995) at ¶¶121-136.

47 U.S.C. §543(b)(2)(C)(vi) directs the Commission to take into account in developing cable rate regulations "any amount required, in accordance with paragraph (4), to satisfy franchise requirements to support public, educational, or governmental channels or the use of such channels or any other services required under the franchise…." 47 U.S.C. §543(b)(4) directs that these cable rate regulations "include standards to identify costs attributable to satisfying franchise requirements to support public, educational, and governmental channels or the use of such channels or any other services required under the franchise." The Commission's proposed counting of such costs against the 5% franchise fee cap would render nugatory Congress' cable rate regulation statute and conflict with the Commission's own cable rate regulations. *Thirteenth Order on Reconsideration,* MM Docket No. 92-266 (Sept. 22, 1995) at ¶¶121-136; 47 CFR §§76.922(f), 76.925.

B. This is not a Case where the Commission can Change its Mind Regarding the Treatment of Franchise-related Costs

This is not a case where the Commission is "free to change its mind," as NCTA suggests. *NCTA ex parte filing* at pp.4-5, note 25. The tentatively proposed recharacterization of franchise-related costs as franchise fees conflicts with existing cable statutes and regulations. It is well-settled that "[W]hen an agency reverses its course, a court must satisfy itself that the agency knows it is changing course, has given sound reasons for the change, and has shown that the rule is consistent with the law that gives the agency its authority to act." *Fox Television Stations, Inc., v. Federal Communications Commission,* 489 F.3d 444, 456 (2nd Cir. 2007) (quoting *Chevron, USA, Inc., Natural Resources Defense Council, Inc.,* 467 U.S. 837,863(1984)).

The Commission has not satisfied this standard. First, it does not appear from the *SNFPR* that the Commission was aware that its tentative proposal overlaps or conflicts with existing cable rate statutes and regulations. In its *Initial Regulatory Flexibility Analysis* (required by 5 U.S.C. §603(b)(5)) at 20, the Commission answered that there are no existing federal rules that conflict with the proposed rules. In addition, the Commission has been conducting a separate proceeding in which it is considering an overhaul of its cable ratemaking rules. *Further Notice of Proposed Rulemaking and Report and Order*, MB Docket No. 17-105 (October 23, 2018). Its proposed regulations in that proceeding do not change the existing treatment of franchise-related costs as a component of basic cable rates, separate from cable franchise fees. It is also notable that the Commission distinguished franchise-related costs and franchise fees when it adopted Open Video Systems ("OVS") regulations. *Second Report and Order, In the Matter of Implementation of Section 302 of the Telecommunications Act of 1996,* CD Docket No. 96-46 (June 3, 1996), 11 FCC Rcd 18223 at ¶¶134,141-146.

Second, the Commission has made no attempt to square its tentative proposal with 47 U.S.C. §543 and its existing cable rate regulations. The Commission has made no showing that its tentative conclusion is consistent with the Cable Act, which directs that franchise fees and franchise-related costs be treated separately.

Third, as discussed below, even if the Commission were "free to change its mind" there are no sound reasons to do.

Taking the action suggested by NCTA would violate the general legal requirement of reasoned, non-arbitrary decision making. *Fox Television Stations, Inc., v. Federal Communications Commission,* 489 F.3d 444, 456 (2nd Cir. 2007) (quoting *Chevron, USA, Inc., Natural Resources Defense Council, Inc.,* 467 U.S. 837,863(1984)). *Thompson v. Clark,* 741 F.2d 401, 405 (D.C. Cir. 1984).

The Commission's rulemaking actions in this matter are subject to judicial review in accordance with 5 U.S.C. §706(2)(A). A reviewing court shall "(2) hold unlawful and set aside agency action, findings and conclusions found to be.... (A) arbitrary, capricious, an abuse of discretion, or otherwise not in accordance with law ...." Commission regulations have the force and effect of law, and agency adoption of an inconsistent regulation- is not "in accordance with law." *Wilcox v. Ives,* 864 F.2d 915, 924-927 (1st Cir. 1988); *Bradley v. Weinberger,* 483 F.2d 410, 414 n.2 (1st Cir. 1973); *Robert E. Derecktor of Rhode Island v. Goldschmidt,* 506 F. Supp. 1059, 1063 (D.RI. 1980); *Raymond Proffitt Foundation v. U.S. E.P.A.,* 930 F. Supp. 1088, 1104 (E.D. Pa. 1996). Adoption of a rule in this proceeding which is inconsistent with other agency rules and enabling legislation would be invalid. *Covert v. Herrington,* 667 F.Supp. 730, 741-742(E.D. WA. 1987).

C. NCTA Arguments Related to Commission Form 1240 are Incorrect

NCTA is correct that a cable operator need not claim franchise-related costs on its Form 1240. *NCTA ex parte filing* at p.5, note 23. However, a cable operators' decision to omit these costs when completing Form 1240 does not afford a cable operator any basis under law for treating those costs as franchise fees and netting them against a franchise fee cap. What NCTA suggests is tantamount to not taking an itemized deduction on an income tax deduction and instead treating the omitted deduction as an income tax credit.

NCTA illogically dismisses the settled distinction between franchise fees and franchise-related costs on the ground that cable rate regulation affects only a small number of systems nationwide. The separation between these two categories remains very relevant to the integrity of the franchise renewal ascertainment process, whether or not regulated cable rates are involved. Moreover, the Commission's proposal would force cable operators whose rates are not regulated to identify and quantify the value of franchise-related obligations and net them against their franchise fees.

D. NCTA Distorts the *First Section 621 Order*

At page 9 of its *ex parte* letter, NCTA distorts the clear distinction between non-cable and cable-related in-kind obligations that was addressed by Newton.

The Commission's discussion in the *First Section 621 Order* of the manner in which cable-related in-kind obligations might be allocated between cable operators (*pro rata* or otherwise) signified that cable-related in-kind obligations are not offsets against the franchise fee. If the Commission treated cable-related in-kind contributions as subject to the franchise fee cap, there would have been no need to make any allocation of their cost between the incumbent and the new entrant (or two incumbents).

E. The Commission's Proposal is Unworkable, Will Impose Significant Burdens on LFAs and Cable Operators and Will Inflict Significant Harm Upon PEG Access Service Providers and the Public

1. The Cable Industry Previously Recognized Problems That Would be Created by the Application of the Commission's Proposal to Existing Franchise Agreements

NCTA's recent *ex parte* filing supports the use of market value to determine franchise fee offsets and urges the Commission to apply its tentative proposal to existing franchise agreements. NCTA has continued to ignore the material problems which stem from adoption of the Commission's proposed treatment of franchise-related costs. Newton identified a number of these problems in its Comments and Reply Comments and does not repeat them here.

In contrast, problems of this type were acknowledged by the cable industry in Massachusetts in 1995, when a MSO did not want to bear the burden of quantifying franchise-related costs for ratemaking purposes under its numerous existing franchise agreements. The MSO wrote to the Cable Television Commissioner, "assigning a value to existing franchise requirements can be problematic." The MSO added that assigning value to a PEG access channel "…may prove… contentious." And further, *"[i]t would be quite challenging to recreate franchise-specific costs with any real degree of* *accuracy.*" (May 5, 1995 letter from predecessor of Comcast to John D. Patrone, Massachusetts Cable Television Commissioner) (public record attached) (emphasis added).[1]

These and many other issues will arise where cable operators (whether or not rate-regulated) must identify in-kind cable related obligations and develop cost or other valuation data for purposes of applying the Commission's proposal to existing cable franchise agreements. Both LFAs and cable operators will incur costs and other burdens solely due to the Commission's uprooting decades of their compliance with federal statutes, Commission regulations and Commission orders. A vast number of cable franchise agreements are predicated upon these laws and decisions, as several commenting parties have explained.

2. Negative Consequences are Inevitable

Contrary to NCTA's recommendation, applying the Commission's proposal to existing cable licenses would be inordinately burdensome for both municipal and cable operator stakeholders. The valuation envisioned by the Commission would be a costly, imprecise exercise at best and would likely spawn litigation across the country. This outcome would threaten the shutdown of PEG Access service providers if their funding were tied up pending the resolution of protracted disputes between cable operators and local franchising authorities. Ultimately, cable subscribers and the public would be harmed.

3. Positive Consequences are Highly Unlikely

Prescinding from the City's disagreement with the Commission's legal analysis, it is highly unlikely that any benefits cited by the Commission would flow from its tentative proposal. The Commission posits that its proposal is needed to "...promote competition by fostering parity between incumbents and new entrants and helping to ensure that local franchising requirements do not discourage cable operators from investing in new facilities and services." *SNFPR* at ¶1.

a. The current treatment of franchise-related costs has not discouraged investment

There has been no showing that the historic and current treatment of franchise-related costs as a component of cable rates (which may be passed through to cable subscribers) has deterred competition

[1] The above MSO letter further illustrates that cable operators and regulators have historically treated franchise-related costs as a component of cable rates, separate from cable franchise fees, consistent with federal cable statutes and FCC regulations.

or discouraged cable operators from investing in new facilities and services. In fact, all evidence is to the contrary.

Newton, for example, is served by three cable operators, all of which offer high-speed Internet access, VoIP telecommunications and cable services, and all of which bear a proportionate share of franchise-related costs. Comcast has upgraded its network and both RCN and Verizon have kept pace. Local franchising requirements have not discouraged these cable operators from investing in new facilities and services.

b. Franchise-related costs are minimal and unlikely to affect network investment

Franchise-related costs represent a very small part of a cable operator's cost structure. They are passed through to cable subscribers. They do not materially influence its investment decisions, which are driven by other factors. The Commission has recognized that network investment decisions of cable operators are based on considerations other than franchise-related costs. The Commission's *Eighteenth Report* on video competition, MB Docket No. 16-247 (Jan. 17, 2017), states:

> **Video Margins** 72. **** According to SNL Kagan, MVPDs spent over half of their video revenues on programming in 2015. Although video margins are declining, most MVPDs also offer Internet services with margins near 60 percent and voice services with margins near 20 percent. When video, Internet, and voice services are combined, SNL Kagan states that 'cable remains a highly profitable business, with margins that would be the envy of many sectors.'

Placed in reasonable perspective, franchise-related costs, long-recognized as proper for cable ratemaking under federal statutes and the Commission's own rate regulations as separate from franchise fees, do not discourage cable investment.

c. The Commission's proposal would not benefit consumers facing ever mounting cable rates

The Commission's claim that its proposal would curb cable costs for consumers is without merit and devoid of record support. First, there has been no showing that the adoption of the Commission's proposal would result in a reduction in in cable rates-no rate reduction is mandated. Second, franchise-related costs are a miniscule component of cable rates and any rate reduction would be negated by cable rate increases. *See,* the Commission's *Eighteenth Report* on video competition, MB Docket No. 16-247 (Jan. 17, 2017) at ¶69 (Kagan notes "persistent rate hikes" by cable operators).

II. CONCLUSION

The Commission is not bound to adopt its tentative conclusions, where, as here, it has been presented with compelling legal, factual and policy reasons why it should not do so. The Commission should limit its action on cable franchise fees to the Commission's treatment of in-kind contributions unrelated to the provision of cable services as franchise fees subject to the statutory franchise fee percent cap. At the very least, the Commission should adopt the ramp-up, grandfathering and other recommendations of the City.

Respectfully submitted,

City of Newton, Massachusetts

By: Ruthanne Fuller
Ruthanne Fuller, Mayor and Issuing Authority

and

By: ________________________
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Attachment

Continental
Cablevision®

May 5, 1995

Mr. John D. Patrone
MA Cable Television Commissioner
100 Cambridge St., Room 2003
Boston, MA

Dear John:

We are writing to propose a method of streamlining Form 1210 filings in a manner which will save the Commission and Continental administrative time and expense.

As you know, FCC rules classify the costs of meeting franchise requirements as "externals" for purposes of assuring that any increase in the costs of meeting local franchise requirements are passed through to subscribers in the form of basic service increases.

The "external" calculations were first devised by the FCC in connection with Form 1200, a Form which required substantial rate readjustments in an extremely short period of time. In Massachusetts, Continental was faced with a considerable accounting burden to compute Form 1200 rates and to put them in place. Because there were no changes in "external" costs of meeting franchise requirements, Continental reported zero as the cost at both the initial date of regulation and at 3/31/94, netting out to zero change. This served to avoid needless valuation questions. Assigning a value to existing franchise requirements can be problematic. While direct cash support of local programming may be readily quantified, attempts to assign a fair portion of overhead time can prove controversial. Accounting for the capital side can be particularly problematic, because costs of replacement and additions to facilities would need to be isolated in upper level accounting books and allocated to the appropriate system. Broad categories of assets have historically been depreciated from which the appropriate depreciation assigned to franchise requirements would need to be determined. In some cases, more equipment was purchased than may have been "required" by license, and some equipment was made available on a centralized basis to more than one franchised community unit.

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Also, a great many licenses identify certain requirements but do not assign any cost to them. Examples include:

- "Licensee shall provide a color television production studio facility" (see section 23, Marblehead license);
- "Licensee shall provide a professional broadcast quality van for L/O programming, equipped with a minimum of 3 high-quality cameras, power generator, and switching and processing equipment." (See section 17.5, Cambridge license);
- "Licensee shall provide a separate institutional interconnect system permitting simultaneous two-way video, audio and data transmission" (See section 20, Middleboro license); and
- "Licensee shall provide a color television production studio facility...and Licensee shall provide a Public Access Coordinator who will be available in Hamilton and Wenham a minimum of 20 hours per week" (See section 21, Hamilton license).

In addition, assigning a value to local access channels may prove as contentious as has the pricing of leased access channels, to which such valuation is closely related. It would be quite challenging to recreate franchise-specific costs with any real degree of accuracy.

By assigning a zero value, we not only avoided needless allocation and valuation questions but also saved enough accounting time to permit us to complete our Form 1200's in a timely manner. On a going forward basis, Continental would prefer to carry forward with this treatment, and not to engage in such controversial ratemaking valuation when there are no changes in such costs which would be subject to passthrough.

Our proposal is that we continue to account for all present costs of meeting franchise requirements at zero in the rate Forms until there are changes in the cost of meeting franchise requirements or the Licenses are renewed. When the costs of meeting franchise requirements come into play, these costs could then be quantified and treated as passthrough, to the extent permitted by law.

Like Continental, the Commission would be spared considerable administrative work.

It is unlikely that we would achieve greater accuracy through rate calculation Forms if we attempted to account for embedded franchise requirements, and the savings of administrative expense more than justifies the treatment requested. By analogy, the FCC has forgiven "de minimis" refund obligations in order to spare cable operators the administrative costs and burdens of implementing minor adjustments.[1] Likewise, such exceptions are provided for administrative convenience in telephone accounting, such as the decision not to require formal allocations for contingent liabilities of less than $1 million in the AT&T Plan of Reorganization.[2] We believe that a similar rationale, which assigns real value to administrative convenience, should prevail here over the need for a detailed and controversial accounting which provides no net "passthrough" to customers.

We are therefore requesting that the Commission permit us to account for all present embedded costs of meeting franchise requirements as zero in the rate Forms, until such time as the License is renewed or the costs of meeting those requirements otherwise change.

Very truly yours,

Susan M. Eid
Vice President and Corporate Counsel

Joseph M. Galli
Vice President and Controller

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[1] See e.g., Viacom Cable, DA 95-351 (Feb. 24, 1995); Copley/Colony Harbor Cablevision, Inc. DA 95-337 (Feb. 24, 1995); King Videocable Company, DA 95-282 (Feb. 23, 1995); King Videocable Company, DA 95-278 (Feb. 23, 1995); Viacom Cable, DA 95-273 (Feb. 21, 1995); Viacom Cable. DA 95-272 (Feb. 21, 1995); Prime Cable of Hickory, L.P., DA 95-168 (Feb. 15, 1995); King Videocable Company, DA 94-1625 (Jan. 3, 1995)

[2] See Kellogg, Federal Telecommunications Law, §4.9.6, page 240 n. 20.