least, be required to respond in writing to any such showing, and any written denial of an operator's request for a higher rate should at least be reviewable by the Commission under an "arbitrary and capricious" test.

This would mean that where an operator's costs clearly and demonstrably exceed what the benchmark would allow, a reviewable procedure would be in place to enable the operator to gain approval of a higher rate. In addition, as previously described, the Commission should provide a mechanism by which operators whose rates are currently at or below benchmark levels can pass through any readily demonstrable cost increases for basic programming. This, too, would reduce the need for constitutional litigation.

In sum, the Commission is right to recognize that cable operators ultimately have a right to recover their costs plus a reasonable profit. Therefore, the Commission should complement its benchmark approach with a right of rebuttal, retiering and limited pass-throughs, that will minimize the likelihood of confiscatory rates -- and of the inevitably complex litigation to which operators will be entitled if their rates are not sufficiently compensatory.

5. Pass-Throughs for Franchise Fees, Taxes, Retransmission Consent, Access Costs and Other Costs Imposed by Government

In general, a "benchmark" approach is preferable to cost-of-service regulation because (1) accurately identifying a system's costs in the absence of a uniform accounting system is very

difficult; (2) ratemaking proceedings are extremely burdensome and complex; and (3) cost-of-service regulation provides perverse incentives to incur unnecessary or unreasonable costs in order to recover additional revenues and profits. But some costs incurred by cable operators are readily identifiable and, because they are imposed externally are beyond the control of the cable operator and cannot be attributed to perverse incentives of rate-of-return regulation. With respect to these sorts of costs, an approach that simply allowed operators to pass them through directly to subscribers would be more appropriate than a benchmark approach.

The Act identifies certain costs that are good candidates for such automatic pass-throughs. Specifically, the Act directs the Commission to

> take into account amounts assessed as franchise fees, taxes or charges of any kind imposed by a state or local authority on the transactions between cable operators and subscribers or any other fee, tax, or assessment of general applicability imposed against cable operators or cable subscribers. In addition, amounts required to satisfy franchise requirements for the support of public, educational and governmental (PEG) channels, or amounts for the use of such channels, or amounts for any other service required under the franchise shall be taken into account....[43/]

These governmentally imposed costs should not be subject to a benchmark approach based on average competitive systems. The amount of such fees, taxes and other assessments may, for some operators, be unreasonably and abnormally high -- but it is

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43/ House Report at 83 (emphasis added).

reasonable to allow operators to pass through such costs in their entirety, whether or not the costs are reasonable. The operator has no choice but to incur them, and simply being reimbursed for them by subscribers provides no excess or monopoly profits to the system.

Often, these expenses are broken out from basic rate charges and itemized separately on subscribers' bills. But even where they are not, such taxes and fees are not hard to identify and should be subtracted from the basic rates charged by systems when calculating benchmark rates. Benchmarks would then reflect reasonable rates for basic service in the absence of all such charges. Each system would then add to its relevant benchmark <u>its own</u> costs, prorated on a per-channel basis, for franchise fees, taxes, PEG access expenses all other governmentally imposed assessments. That total would be the maximum per-channel rate that the system could charge for basic service.

One possible caveat concerns expenses incurred to support PEG access channels. Those expenses may not be as readily identifiable as franchise fees and taxes and, therefore, may be more difficult to exclude from basic rates in calculating benchmarks. If current access expenses cannot be separated out from the basic rate calculations, it would be inappropriate to permit systems to pass such costs through in excess of their benchmark limit. In essence, this would allow a double recovery of such expenses. A more appropriate approach in such circumstances would be to allow systems to add to their benchmarks and pass through any <u>increases</u> in annual access

expenses beyond those incurred when benchmarks rates were initially calculated.

A similar pass-through should also be permitted for any fees that systems are required to pay to broadcasters for retransmission consent. Retransmission consent fees will be readily identifiable. They are new expenses which Congress has ruled to be legitimate. Since they will not have been included in the basic rate benchmark calculations, allowing them to be added to each system's maximum rate will not permit a double recovery but only a wholly appropriate single recovery of the operator's legitimate costs.[44/]

II. STANDARDS FOR REGULATING RATES FOR EQUIPMENT USED TO RECEIVE BASIC SERVICE

As part of its "establishment of basic service tier rate regulations,"[45/] the Commission is required to

> include standards to establish, on the basis of actual cost, the price or rate for --

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44/ The Act also requires the Commission to take into account any advertising revenues attributable to the basic tier. see 47 U.S.C. Section 543(b)(2)(C)(iv). But like costs for facilities and programming, these revenues will generally be taken into account in the rates that are charged by the competitive and non-competitive systems that are used to calculate benchmark rates. Unless such revenues are to be added to the rates of systems in calculating benchmarks (and therefore, like franchise fees and taxes, effectively excluded from the calculation), it would be inappropriate to deduct any particular system's advertising revenues from its allowable maximum rate. This would in effect be the opposite of a double recovery of costs; it would constitute a double offset for advertising revenues.

45/ 47 U.S.C. Section 623(b).

(A) installation and lease of the equipment used by subscribers to receive the basic service tier, including a converter box and a remote control unit and, if requested by the subscriber, such addressable converter box or other equipment as is required to access programming described in paragraph (8); and

(B) installation and monthly use of connections for additional television receivers.[46/]

Construing the scope and meaning of this provision requires, at the outset, some understanding of what Congress was meaning to accomplish. In this respect, the Commission's emphasis on the need to "unbundle" equipment from basic service rates seems to miss the mark. The fundamental purpose of this provision, as discussed below, appears instead to be to ensure that cable operators not evade basic rate regulation and extract excess profits by charging excessive rates -- far above costs -- for remote control devices and other equipment and for additional outlets.

The provision, as we show, applies only to equipment rates charged to those subscribers who purchase only the basic tier (and to those subscribers who exercise their right, under the "buy-through" provisions of the Act, to bypass other tiers of service and purchase per-channel or per-program services). For those subscribers, the cost of equipment that is not included in the charge for basic service may not exceed actual costs plus a reasonable profit. In establishing such charges, what ultimately

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46/ Id., Section 623(b)(3).

matters is that the overall price for all equipment, additional outlets and installation not included in the basic service charge not exceed the total costs for such equipment plus a reasonable profit.

A. The Purpose of the Provision: To Ensure Competitive Rates for Basic Service Subscribers

The Commission describes the equipment rate regulation provision of the Act as if it were, primarily, an "unbundling" requirement -- a requirement "to separate rates for equipment and installations from other basic tier rates," in order to "help to establish an environment in which a competitive mandate for equipment and installation may develop."[47/] But this is an improbable legislative intent, for which there is no evidence. For much of the equipment at issue -- such as, in particular, remote control devices -- competitive availability is no problem. Electronics stores vigorously advertise the availability of "universal remotes," which can be used not only with cable television converter boxes but also with video cassette recorders, audio equipment and other electronic devices.

For other equipment, such as descrambling devices, and for installations of additional outlets and equipment, competitive availability may never be a reasonable option for consumers for security reasons. To the extent that provision of particular equipment is itself the method for enabling subscribers to

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47/ Notice, para. 63.

receive the services they pay for -- and for ensuring that they not receive services that they have not purchased -- cable operators must retain control over its distribution and installation to prevent theft of service.

Thus, Section 623(b) the Act is concerned not with the competitive availability of equipment but with the regulation of rates for basic cable subscribers. Its purpose is to ensure that rates for basic service subscribers are regulated at a competitive level. And Section 623(b)(3) is designed to ensure that this is the case, not only with respect to the rates charged for the programming received by basic subscribers but also for the equipment used to receive it.

In this respect, Congress's concern was not that cable operators would bundle service and equipment at a single, regulated price. To the contrary, it was that cable operators would unbundle equipment from the regulated basic service and charge excessive rates for that equipment. If cable operators bundle their equipment with their basic service -- in other words, if they provide "free" remotes or additional outlets with their basic service -- the rates for such a bundled package would be subject to basic rate regulation. But, absent Section 623(b)(3), unbundling the equipment from basic service would remove the equipment from the constraints of rate regulation. It would do little good to regulate basic service rates in the absence of effective competition if there were no regulatory or competitive constraints on the price of equipment necessary or desirable to receive that basic service.

B. The Scope of the Provision: Rates Charged for Equipment and Installation to Those Who Subscribe Only to Basic Service (or to Basic Service Plus Premium or Pay-Per-View Channels)

As an adjunct to the requirement that basic service rates be regulated at competitive levels, Section 623(b)(3) is directed only at the equipment rates charged in connection with basic service. The rates charged to subscribers to non-basic service tiers -- including the rates for equipment used by such subscribers -- are separately subject to regulation under Section 623(c), which authorizes the Commission to deal with complaints regarding unreasonable rates for "cable programming services." Those services include

> any video programming provided over a cable system, regardless of service tier, including installation or rental of equipment used for the receipt of such video programming, other than (A) video programming carried on the basic service tier, and (B) video programming offered on a per channel or per program basis.[48/]

The Commission asks whether "the only equipment that should be subject to Section 623(b)(3), therefore, is equipment that is necessary to receive basic service tier programming, and whether equipment, if any, used only to receive cable programming services would not be subject to Section 623(b)(3)."[49/] The answer to the first question is no. Both the statute and the legislative history make clear that equipment leased or purchased

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48/ 47 U.S.C. Section 627(l)(2).

49/ Notice, para. 65 (emphasis added).

by basic cable subscribers need not be "necessary to receive basic programming" to be subject to "actual cost" regulation under Section 623(b)(3). Indeed, the Conference Committee specifically replaced language in the House bill that regulated only "equipment necessary by subscribers to receive the basic service tier" with the current language regulating "equipment used by subscribers to receive the basic service tier."[50/]

This change was necessary to reach remote control equipment, which Congress clearly meant to place within the scope of the provision. Remote control devices are virtually never necessary to receive basic -- or any other -- cable service. But if they are "used" by basic subscribers "to receive the basic service tier", they must be provided subject to the "actual cost" restrictions of Section 623(b)(3).

With respect to the Commission's second question, equipment that is used by cable subscribers to receive non-basic "cable programming services" should not be deemed subject to Section 623(b)(3). Moreover, even if that same equipment is also used to receive the basic tier, its rate to non-basic subscribers should not be subject to the "actual cost" constraints of the Act. Indeed, remotes and converter boxes, including descrambling converter boxes that are used by subscribers to receive non-basic services are virtually always "used" by those same subscribers to receive basic service programming -- even if they are not

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50/ See Conference Report, 102-862, 102d Cong., 2d Sess. 64 (1992) (emphasis added).

"necessary" to receive such programming, and even if they are not even available to subscribers to basic service alone. But Congress clearly intended that the rates charged to non-basic subscribers (including the rates that such subscribers pay for equipment) be subject to the standards of Section 623(c) and not to the standards of Section 623(b).

Thus, if an addressable converter box or any other piece of equipment is made available only to subscribers to non-basic cable programming services, it should not be regulated pursuant to Section 623(b)(3), even if it is "used" to receive basic programming as well. And if a remote control device or other piece of equipment is made available both to basic subscribers and to subscribers to optional tiers of cable programming services, Section 623(b)(3) should only apply to the rates charged to the basic service subscribers for such equipment.

What matters, under the Act, with respect to subscribers to non-basic programming tiers is only that their overall rates -- including rates for equipment -- not be unreasonable under Section 623(c). There is, therefore, no reason to require that one component of those rates (equipment) be priced at cost plus a reasonable profit. What matters with respect to basic subscribers, on the other hand, is that basic service be available at a competitive rate. Applying Section 623(b)(3) to the rates charged to those subscribers will ensure that the entire package of service and equipment purchased by basic subscribers will be available at a competitive rate -- which is

precisely what Congress sought, with the entirety of Section 623(b), to achieve.

Congress recognized and closed the only potential loophole under this approach. Pursuant to the "anti-buy-through" provisions of Section 623(b)(8), basic service subscribers may purchase per-channel or pay-per-view services without purchasing intermediate tiers of cable programming services. Section 623(b)(8) prevents operators from discriminating against these subscribers, vis-a-vis subscribers to intermediate tiers, "with respect to the rates charged for video programming offered on a per channel or per program basis." But unless the rates for equipment used for per-channel or pay-per-view programming were regulated with respect to basic subscribers exercising their option to bypass intermediate tiers, cable operators could conceivably use rates charged for such equipment to discriminate against such subscribers and deter such bypass.

Accordingly, Section 623(b)(3) applies to rates for installation and lease of (1) equipment used to receive the basic tier and (2) "if requested by the subscriber, such addressable converter box or other equipment as is required to access programming described in paragraph (8)".

C. A "Basket" Approach: Overall Rates for Equipment and Installation Should Not Exceed Actual Costs Plus a Reasonable Profit

The Commission recognizes that cable operators may sometimes provide certain equipment, installation or additional outlets at rates that are lower than their actual costs, and it wonders

whether such below-cost rates are permissible under the Act. Again, the Commission's concerns are based on its mistaken view that the purpose of this "actual cost" requirement was not to protect basic subscribers from equipment rates that are too high but to protect competitive suppliers of equipment, installation and additional outlets from predatory rates that are too low. To the contrary, as discussed above, what Congress sought to ensure was that cable operators, whose basic service rates would now be regulated, not be allowed to extract excessive profits by unbundling equipment and installation and offering them at unregulated, supracompetitive rates.

It follows that below-cost pricing of individual items of equipment and installation should not itself run afoul of the Act. Moreover, even above-cost pricing of individual items should not cause problems so long as, overall, the cable operator's charges for unbundled equipment, installation and additional outlets simply cover the operator's direct and indirect costs plus a reasonable profit and are not, therefore, a source of monopoly profits.

Sometimes below-cost pricing of individual items of equipment or installation may itself yield pro-competitive economies that benefit all consumers. For example, as the Commission suggests, "promotional offerings [of installation at less than cost] can increase cable service penetration, thereby resulting in economies of scale that could reduce costs overall

of providing equipment to subscribers."[51/] To the extent that such below-cost rates for installation -- which are, indeed, the norm in the cable industry -- effectively pay for themselves in increased penetration and sales, they could not reasonably be viewed as violating the Act.

But even if the below-cost rates for installation and some equipment were also subsidized to some extent by rates for other items of equipment that exceeded an amount reflecting costs plus a reasonable profit, this still should cause no problems, as long as the total charges were not excessive. First, if total rates do not exceed total costs plus a reasonable profit, there is no danger that the operator is somehow using his unbundled equipment rentals and sales to extract monopoly profits. If overall rates simply cover overall costs, there are no such profits.

Second, there are public benefits to allowing rates for certain equipment to subsidize other equipment and installation charges. Lower installation rates can, as the Commission has suggested, increase cable penetration. If the sale of certain non-essential equipment, such as remote control devices, to those who are willing to pay more for their cable service can be used to reduce installation charges and make cable services more attractive or affordable to more subscribers, that should be encouraged, not discouraged, by the Commission. Such subsidies serve the Act's policy objective of "promot[ing] the availability

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51/ Notice, para. 70.

to the public of a diversity of views and information through cable television...,"[52/] without allowing operators to exercise the "undue market power"[53/] that the Act is intended to prevent.

For these reasons, the Commission should rule that what matters, under the Act, is not whether individual items of equipment, installation and additional outlets are offered at rates that reflect actual costs. What matters is that the rates for equipment, installation and additional outlets combined do not exceed actual costs plus a reasonable profit.

III. STANDARDS FOR REGULATING RATES FOR "CABLE PROGRAMMING SERVICES"

The Commission's Notice properly gives the lion's share of attention to the standards and procedures for regulating rates for basic cable service, because only basic service will be subject to affirmative rate regulation under the Act. To ensure that a reasonably priced basic service was available and affordable to as many consumers as possible, Congress allowed local rate regulation of basic service in the absence of effective competition and directed the Commission to develop standards for such regulation that ensured that basic rates did not exceed what would be charged if there were effective competition.

52/ Act, Section 2(h)(1) (emphasis added).

53/ Id., Section 2(b)(5).

With respect to non-basic service offerings, Congress showed a significant but decidedly lesser concern. Services offered on a per-channel or pay-per-view basis are not to be regulated at all. Congress and the Commission have understood that these services operate in a competitive marketplace, where video rental stores and other competitive providers of movies and entertainment effectively remove any significant possibility of market power.

Congress also recognized that, in most cases, non-basic tiers of "cable programming services" need not be subject to regulatory constraints. Congress believed that "most cable operators have been responsible about rate increases" and that only a "minority of cable operators have abused their deregulated status and have unreasonably raised subscribers' rates" for such services.[54/] To prevent and correct abuses by such "renegades," Congress provided consumers and franchising authorities with a complaint procedure. Under that procedure, the Commission is authorized to determine, "in individual cases,"[55/] whether a cable system's rates for cable programming services are "unreasonable."

The regulatory approach for determining, on a case-by-case basis, whether such rates are unreasonable will, for several reasons, almost certainly need to be different from the approach

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54/ House Report at 86.

55/ Id.

selected for regulating basic rates. First, while Congress may have intended to affect most systems' rates for basic service by requiring that rates in the absence of effective competition be set at the presumably lower rates of systems facing effective competition, Congress intended to regulate the non-basic rates of only that minority of "renegades" that had raised their rates to unreasonable levels.

Second, the effects of restraining non-basic rates are different from the effects of regulating basic rates. Rate regulation is markedly less effective to the extent that the regulated entity is able to vary the content and quality of its product. Capping prices of a seller that supposedly possesses market power will not effectively eliminate excess profits if the seller is able simply to reduce its costs and offer an inferior product at the regulated price.

To the extent that basic cable service consists of broadcast channels and access channels, the ability of cable operators to reduce the quality of their service is limited. Cable operators have no control over the content of broadcast channels and access channels and cannot spend less on such services if their allowable rates are reduced to "competitive" levels.

But there are no similar constraints on the content and quality of non-basic services. Thus, even if cable operators were able to price such services at supracompetitive levels, rate regulation would not likely be effective in ensuring competitive rates. The more probable result is that rate reductions would be

matched by reductions in expenditures on programming and facilities.

In other words, rate regulation's effect would be primarily negative, thwarting improvements in programming and technology without significantly restricting market power. It would thus stall out the engine primarily responsible for driving the program services that are relied upon by all non-broadcast video distributors, including not only cable but MMDS systems and distributors to backyard dish owners. It was precisely for such reasons that, even before the 1984 Cable Act established the first statutory framework for cable regulation, the Commission had decided to preempt and prohibit regulation of cable rates for all services and tiers except for the basic tier that included the retransmission of local broadcast stations.[56/]

Finally, an approach to regulating non-basic tiers that, like the approach to basic rates, was aimed at affecting the rates and practices of a large number of systems would produce a monumental regulatory gridlock at the Commission. This would not occur to the same extent with respect to basic rate regulation. Basic rate regulation is decentralized. Local franchising authorities will, at least in the first instance, have primary responsibility for regulating their communities' cable systems.

56/ See Community Cable TV, Inc., 98 F.C.C.2d 1180 (1984).

Moreover, cable operators will have the ability to reduce their basic rates to the presumably lower benchmark levels by retiering non-broadcast services, as contemplated by the Act, as an alternative to challenging the basic benchmarks as non-remunerative. But operators will have no such recourse with respect to non-basic programming, decreasing the likelihood of rate reductions to meet benchmark levels -- and, therefore, increasing the likelihood of complaints and disputes to be resolved at the Commission.

If the Commission's standards for non-basic rates established benchmarks at the unrealistically low 75th percentile of all rates -- that is, at a level currently exceeded by 25 percent of all systems -- the rates of almost 2,800 systems would be subject to rate complaints at the Commission that met the threshold showing that rates exceeded benchmark levels. What is needed is an approach that reasonably ensures, at the outset, that only that minority of cable systems whose rates so exceed the norm as to be clearly unreasonable be required either to reduce their rates or be subject to complaint proceedings.

Cost-of-service regulation clearly would not meet this need. To require each cable system to demonstrate, in ratemaking proceedings, that its rates are cost-justified and reasonable would itself be unreasonable. As noted previously, the Commission has no uniform methodology for applying cost-of-service regulation to cable systems. And, in any event, it would lack the resources to regulate all the nation's cable systems on this basis, even if such a methodology existed.

Approaches based on the current rates for "competitive" systems or on the past rates for regulated systems would provide no way of ensuring that only the minority of "outliers" that Congress meant to regulate would become ensnared in complaint proceedings at the Commission. Such approaches may be appropriate where the task is to establish in advance a benchmark "competitive" rate, and where the expectation is that most systems will have to adjust their rates and/or tiers to meet the benchmarks. But they are inappropriate ways to devise a test where the statutory burden shifts from proving an operator's rates are reasonable to establishing that rates are unreasonable.

The best way to rein in renegade rates is to determine, at the outset, the distribution of rates for all systems and simply to rule that rates at the outer edge of the distribution so far exceed the norm as to be unreasonable. This is, in fact, one of the approaches proposed by the Commission: "[S]ystems which ranked among the highest few percent (e.g., top 2-5 percent) in terms of rates would be assumed not to have rates that were reasonable."[57/] As the Commission notes, this approach "would identify those systems whose rates were unnecessarily high or substantially above the average"[58/] -- which is precisely what the Commission's standards for regulating non-basic cable programming services are supposed to identify.

57/ Notice, para. 47.

58/ Id.

To rein in only the true renegades, such an approach should establish a benchmark for the combined rates charged not only for non-basic tiers but also for basic service and for all equipment, installation and additional outlets. The Act specifically directs the Commission, in establishing criteria for determining whether rates for non-basic tiers are unreasonable, to consider "the rates, as a whole, for all the cable programming, cable equipment, and cable service provided by the system other than programming provided on a per-channel basis."[59/] This reflects Congress's order of concern -- primarily that basic rates be reasonable, and secondarily that non-basic rates not be unreasonable. Given these priorities, a cable system should not be discouraged from charging lower basic rates and higher non-basic rates, so long as its overall rates are not unreasonable.

A benchmark rate that was based only on rates for non-basic service, as surveyed at this time, would in any event have to be adjusted to take into account the retiering and repricing that will be compelled by the Commission's benchmarks for basic service and equipment. Such retiering and repricing may result in generally higher rates for non-basic service and generally lower rates for basic service, without increasing overall revenue. Thus, a benchmark for non-basic rates that identified the 95th percentile of today's rates for tiers above the basic tier might subject a large number of cable operators to complaint

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59/ 47 U.S.C. Section 543(c)(2)(D)

proceedings, even though their overall revenues still place them well below that percentile level.

An easier way to accommodate this problem than seeking to determine the appropriate upward adjustment in the benchmark for non-basic rates is simply to base the benchmarks on total revenues from all regulated services and equipment. Such an approach would identify the outliers that Congress meant to constrain, while allowing operators the flexibility to recover more of their costs from non-basic tiers and less from basic -- an option that Congress contemplated.[60/] Systems still would not be able to recover a disproportionate share of their costs from their basic rates, because those rates would remain subject to benchmarks based on competitive systems.

The Commission's proposal to establish benchmarks at a level that treats rates of all but the "top 2-5 percent" of systems as presumptively not unreasonable makes sense. While variations in different systems' costs are likely to explain most of the variations in rates among systems, it may be reasonable to presume initially that rates beyond the 95th or 98th percentile cannot be explained by cost differences and do, indeed, reflect the abusive exercise of abuse of market power.

Moreover, simply as a practical matter, a benchmark that subjected more than five percent of all systems to complaints would create an unmanageable burden for the Commission. Even a

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60/ See e.g., House Report, supra at 63.

benchmark that allowed just one percent of all subscribers to file such complaints would create the potential for 552,000 complaints from 111 systems.[61/] And apart from the burden on the Commission, these complaints would create confusion, disruption and uncertainty for cable systems and programmers.

In any event, Congress meant only to restrain those systems whose rates were so far from the norm as to be clearly abusive. A benchmark that treated rates below the 95th percentile as not unreasonable, as the Commission suggested, would appropriately identify the "renegades" while limiting the potential for an unmanageable torrent of complaints. Rates beyond the 95th percentile would be viewed as presumptively unreasonable, but as in the case of basic rate regulation, the constitutional requirements that rate regulation not be confiscatory would require that this presumption be rebuttable in complaint proceedings.

Once established, the "bad actor" benchmark would, like the basic rate benchmark, have to be recalculated periodically to take into account increased costs and to prevent increased investment in programming and technology. But once an initial benchmark is established that drives the rates of "bad actor" systems down to acceptable levels, it no longer makes sense to view rates above the 95th percentile each subsequent year as excessive -- because, even apart from any increased costs that

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61/ See Owen, Baumann & Furchtgott-Roth, supra.

those systems might incur, those rates have already been determined to be not unreasonable. Such an approach would simply push the rate ceiling down each year, reclassifying reasonable rates as unreasonable and thwarting the increased investments in programming and technology that consumers have shown that they want.

To avoid this problem, a better approach would be to determine, after the first calculation of benchmark rates, the percentage difference between the median rate and the rate of the 95th percential. This difference would represent, for future calculations, the difference between the median rate and "unreasonable" rates. In subsequent years, the Commission would recalculate the median rate and increase it by the established percentage to determine the new benchmark for unreasonable rates. Such an approach would allow the ceiling on overall rates to increase to allow for increased cost and for investments in improved service, instead of operating like "musical chairs", always forcing some operators unnecessarily into the unreasonable zone. But it would still serve as a check on the sort of unreasonable rate increases that, in Congress's view, were inflicted on consumers by some cable operators after deregulation.

IV. PROCEDURES FOR RATE REGULATION

The Act divides jurisdiction over rates between local franchising authorities and the Commission. The Notice raises questions regarding the procedures to be adopted to permit the

exercise of regulatory authority over basic rates, which we address below.

A. Certification Requirements

1. Jurisdictional Division

The Act provides that "the rates for the provision of basic cable service shall be subject to regulation by a franchising authority, or by the Commission if the Commission exercises jurisdiction pursuant to paragraph (6)."[62/] The Commission correctly interprets the statute to grant it "quite limited" authority to regulate basic cable service rates directly.[63/] The FCC may regulate basic tier rates only where a franchising authority's certification is revoked or disapproved, and then only until approval of a new certification.[64/] If a franchising authority, therefore, elects not to apply for certification from the Commission to regulate basic rates, then the Commission has no independent authority to step in and regulate those rates.

62/ Section 623(a)(2)(A)(emphasis added).

63/ Notice, para. 15.

64/ See also House Report at 81 ("The FCC may exercise regulatory authority with respect to basic cable rates only in those instances where a franchising authority's certification has been disapproved or has been revoked and only until the franchising authority has qualified to exercise that jurisdiction by filing a valid certification.") (emphasis added).

To be sure, the Commission is generally charged, under Section 623(b), with establishing regulations to ensure that the rates for basic service are "reasonable". But to interpret this general provision as a source of independent Commission authority to exercise rate regulation at the local level where a franchise authority chooses not to do so would be "at odds" with the statute, as the Notice suggests. Moreover, the Act in Section 623(a) specifically prohibits the regulation of rates for the provision of cable service "except to the extent provided under this section and section 612." Congress, therefore, left no room for the assumption of jurisdiction in the area where it is not specifically granted by the Act.

2. Effective Competition

A threshold determination that must be made prior to the assumption of rate regulatory power by either a franchise authority or the Commission is the absence of "effective competition" to the cable system. The Act charges the Commission with making this finding. But the FCC proposes to base its determination on a franchising authority's findings as submitted on its certification form.

We appreciate the difficulties that the Commission would face if it were required to independently gather evidence of the competitive conditions in each community and itself determine whether effective competition is absent. But if the Commission chooses to rely on the franchising authority's initial conclusion, it must ensure that franchising authorities on their