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January 28, 1993

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FEDERAL COMMUNICATIONS COMMISSION
OFFICE OF THE SECRETARY

Ms. Donna R. Searcy
Secretary
Federal Communications Commission
1919 M Street, N. W.
Washington, D. C. 20554

Re: MM Docket No. 92-262

Dear Ms. Searcy:

Transmitted herewith on behalf of Encore Media Corporation, are an original and 10 copies of its "Reply Comments" in the above-captioned proceeding.

Should you require anything further, please contact the undersigned.

Sincerely yours,

James E. Meyers

James E. Meyers
Counsel for
Encore Media Corporation

Enclosures

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Before the
Federal Communications Commission
Washington, D.C. 20554

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JAN 28 1993
FEDERAL COMMUNICATIONS COMMISSION
OFFICE OF THE SECRETARY

In the Matter of:	)	
	)	
Implementation of Section 3 of the Cable Television Consumer Protection and Competition Act of 1992	)	MM Docket No. 92-262
	)	
Tier Buy-Through Prohibitions	)	

REPLY COMMENTS OF ENCORE MEDIA CORPORATION

ENCORE Media Corporation ("ENCORE Corp."), through undersigned counsel, submits its Reply Comments in this matter above captioned.

ENCORE Corp. agrees with the commenters that support a flexible interpretation of Section 623(b)(8)'s buy-through prohibitions. In keeping with the purpose, policy and objectives of the 1992 Act, cable operators must be afforded maximum flexibility in the manner in which they are permitted to present their per-channel and per-program offerings.

Attached hereto as Attachment 1 are our Comments in the rate regulation proceeding, MM Docket No. 92-266, which we incorporate by reference and make a part of the record herein.[1] Our comments in the rate regulation proceeding attempt to identify a unified approach for the Commission

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[1]Page 14 of our attached Comments contain the last line which did not print on the version filed in MM Docket No. 92-266. We are in the process of preparing an Erratum to that effect to submit in that proceeding.

with respect to both rate regulation and tier buy-through owing to the interrelatedness of the issues.

Respectfully submitted,

ENCORE MEDIA CORPORATION

By: James E. Meyers
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Its Counsel

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Re: MM Docket No. 92-266

Dear Ms. Searcy:

Transmitted herewith on behalf of Encore Media Corporation, are an original and 10 copies of its "Comments" in the above-referenced proceeding.

Should further information be required in connection with this matter, please communicate with this office.

Very truly yours,

James E. Meyers

James E. Meyers
Counsel for
ENCORE MEDIA CORPORATION

Enclosures

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TABLE OF CONTENTS

		Page
1.	Introduction.	1
2.	Policy of the Act	3
3.	Definition of Types of Cable Service. . . . . (USAGE BASED)	4
	a. Basic Service Tier ("BST".	5
	b. Per Channel Per Program ("PCPP")	5
	c. Cable Programming Service ("CPS").	5
4.	Legislative Intent of the Act	6
5.	Services That are not Subject to Rate . . . . . Regulation	8
	a. Per Channel Per Program, (PCPP).	8
	b. PCPP Packaging	8
	c. PCPP Discount.	9
	d. Equipment Packaged with PCPP	10
6.	Standards for Rate Regulation of BST and CPS. . .	10
7.	Universal Standard/Benchmark.	14
8.	Equipment	16
9.	Equipment "Used" by Subscribers to Receive. . . . BST, CPS, and "Required" to Access PCPP	18
10.	Any Subscriber Must Subscribe to BST.	20
11.	Negative Option Billing	21
12.	Conclusion.	22

Before the
Federal Communications Commission
Washington, D.C. 20554

In the Matter of	)	
	)	
Implementation of Sections of the Cable Television Consumer Protection and Competition Act of 1992	)	MM Docket 92-266
	)	
Rate Regulation	)	
	)	
To: The Commission	)	

COMMENTS OF ENCORE MEDIA CORPORATION

Encore Media Corporation ("ENCORE Corp.") submits its comments to the Notice of Proposed Rule Making, FCC 92-544, in this matter above-captioned ("Notice").

1. Introduction

Encore Corp. owns and operates the television entertainment service known as "ENCORE," which commenced service in 1991 and which selects and packages motion pictures from the 1960s and 1970s and 1980s, exhibiting them principally to cable television subscribers.[1] As described in its comments to the Commission's Tier Buy-Through Prohibitions proceeding (MM Docket No. 92-262) (attached hereto as Attachment 1 and incorporated herein by

[1]ENCORE is received in about 3.7 million households whereas there are about 55 million total cable television households. By comparison, premium video programming services such as HBO and Showtime have achieved subscriber levels of in excess of twenty million and seven million, respectively, and such "tiered" video programming services as TNT, the Discovery Channel, ESPN and USA Network have achieved subscriber levels exceeding 50 million.

reference), ENCORE may be offered over cable television systems in a variety of ways and has obtained carriage on many cable systems because of ENCORE Corp.'s successful efforts to develop ENCORE as a value-added programming service.

ENCORE is almost always offered both as a stand-alone premium (per channel) basis and also as part of a package of per channel offerings on the same system. Lately cable operators have found it attractive to offer ENCORE also as part of a "cable programming service" tier. Such trend is likely to increase in 1993 and beyond.

Both the rate regulation proceeding and the anti-buy through proceeding seek comment on issues that affect substantially the manner in which ENCORE may continue to be available to cable subscribers. By its comments here, ENCORE Corp. has attempted, in essay form, to address these issues from its viewpoint as a video programming vendor.

Our comments, analysis, and recommendations are based upon a careful reading of the statutory language, the Conference Report, the legislative history as embodied in the House and Senate Reports and verbal discussions with senior FCC staff officials[2] and senior staff of the House Subcommittee on Telecommunications and Finance and of the Senate Subcommittee on Communications.[3] Recognizing, as has the Commission,[4] that the

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[2]The discussions with FCC staff occurred prior to the opening of the "Sunshine Period" to the Commission's December 10, 1992, meeting.

[3]We recognize the axiom that statements of draftsmen are not legislative history or reflective of the intent of Congress in enacting legislation.

anti-buy through provisions of the Act are interrelated with the rate regulation provisions, ENCORE Corp.'s objective in this filing is to provide the Commission with the conceptual and analytical framework from which it can develop a uniform approach to rate regulation that is consistent with the Act's objectives.

2. Policy of the Act

It is important and relevant to restate the essence of the overall guiding policy for the entire Act, which is the Statement of Policy outlined in Section 2(b). Wherever there is room for interpretation, we must come back to this policy for guidance. The essence of the policy is:

- To rely on the [free] marketplace, to the maximum extent feasible to promote the availability to the public a diversity of video programming through cable television and other video distribution media.
- To ensure that cable operators continue to expand their capacity and the programs offered whenever economically viable.
- Until cable television systems, on a system-by-system basis, are operating under effective [or actual] competition, to ensure that consumer interests are protected in the receipt of cable service and the

[4]Notice at paragraph 96, note 133.

market power between cable television operators and video programmers or consumers is properly balanced.

3. Definition of Types of Cable Service [USAGE BASED]

A significant part of the Act is how it categorizes the types of cable service with regard to the nature and extent of regulation required. For the first time, cable service is defined[5] by how the cable operator on a specific cable system offers the service to the consumer, and not by the nature of the cable service as broadly defined in the past, i.e., basic programming, premium or pay programming, etc.

Under the Rate Regulation Section of the Act there are three types of cable services, the Basic Service Tier ("BST"), Cable Programming Service ("CPS"), and Per Channel Per Program ("PCPP"). Putting aside the equipment component, the definition of these types of cable service are:

a. Basic Service Tier ("BST")

Every cable system must provide its subscribers a separately available BST to which subscription is required for access to any other tier of service. The BST is required to contain a minimum complement of programming plus any additional video programming the cable operator chooses to carry in the BST. The minimum complement of programming includes all the

[5]By "defined," we mean how "cable service" offerings are evaluated to determine in which category they fall for purposes of the Act's application. We do not mean the statutory definition of "cable service" in Section 602(6).

must carry signals, all PEG access channels, and (if the operator wants to carry them) any other television broadcast channels that are not satellite delivered.

b. Per Channel Per Program ("PCPP")

At the other end of the cable service spectrum is video programming offered to subscribers on an "a-la-carte" basis, either on a per channel or per program basis.[6]

c. Cable Programming Service ("CPS")

CPS is video programming offered on tier(s) (with a minimum of two channels in any such tier) that is not BST or PCPP. CPS is only available as a tier.

Note by the usage-based definition, a specific national video programming service can be in any of the three types of cable service from system to system. For example, HBO, normally thought of as a per channel service, can be part of BST should the operator choose to include HBO as part of BST as is done in a system in Alaska. On the other hand, C-SPAN, normally on BST in most systems, can be classified as a PCPP service if the operator markets C-SPAN on an a-la-carte per channel basis on a system. We also interpret the word "tier" to cover BST and CPS,[7] but not PCPP services. We stated that CPS must be a tier

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[6]"A-la-carte" offerings are at the extreme end of the cable service spectrum. There are various manners of offering cable service that are not strictly a-la-carte but that are still PCPP, such as various packaging plans.

[7]When the Act uses the term "tier(s)" we interpret it to mean either BST or CPS, and not PCPP. See paragraph 10.

of at least two channels because otherwise it will be classified as a per channel service.

4. Legislative Intent of the Act

Consistent with its Statement of Policy, Congress deemed that, in the absence of "effective"[8] competition to a cable system, the franchising authority is conferred the jurisdiction to ensure the public is offered the lowest possible rate for the BST through tight regulatory guidelines set up by the Commission.[9] At the same time, however, at the PCPP end of the spectrum, the Act encourages cable operators to offer the public cable services on an a-la-carte rather than the traditionally bundled basis.[10] Even in the face of no effective competition, the Act stipulates that such offerings are not subject to any rate regulation, except with regard to any separately billed equipment charges. The Congress' rationale is clear: On a per

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[8]The statutory definition of "effective competition" is necessarily imperfect. The absence or presence of "actual" competition to a cable system does not necessarily correspond with whether the system's BST would be subject to rate regulation (e.g., the mere presence of an arbitrary penetration cut-off of 30%).

[9]Consistent with the Statement of Policy, the goal of Section 623(b) is to protect consumers to the extent the Commission's regulatory program can approximate BST rates of systems subject to "effective" competition (Section 623(b)(1).)

[10]Section 623(b)(7) and (8) provide the consumer the optimum opportunity to access PCPP. That section permits cable operators to attract video programming services in keeping with the Statement of Policy at Section 2(b)(3) (and 2(b)(1) and (2)). The exclusion of PCPP from CPS "unreasonable" rate formula further promotes unbundling (Section 623(c)(1)(2)). The exclusion of PCPP from rate regulation (Section 623(c) and (1)(2)) is in direct keeping with Section 2(b)(2).

channel basis, the various PCPP services will vigorously compete for business thereby ultimately reducing the prices to the public. Moreover, public interest is being served when they only purchase what they want to view. The Act's insistence that the charges for separately billed equipment be based on actual cost as well as the prohibition of buy-through of any tier other than BST to subscribe to PCPP is to ensure that cable systems expand through ever-increasing offerings of PCPP[11] for the benefit of consumers[12] by reducing the barrier to access PCPP.[13] These are all consistent with Congress' intent to encourage the upgrading of the cable plant, including the addition of expensive home terminals, to foster the success and penetration of all PCPP services.

For the middle of the spectrum, Congress directed the Commission to control or weed out egregious rate behavior by cable operators in what it charges for CPS tier(s). These are the so- called "bad actor" provisions discussed in the legislative history. The standard for the regulation of CPS rates is to be more benign than that to be used for the regulation of the BST. Below we will develop more in detail to support our interpretation of the legislative intent.

5. <u>Services That are not Subject to Rate Regulation</u>

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[11]See Section 2(b)(3).

[12]See Section 2(b)(1).

[13]See Section 623(b)(8).

a. Per Channel Per Program, (PCPP)

The Act clearly excludes PCPP from rate regulation. PCPP includes the rates charged by cable operators to subscribers for pay-per-view movies, sporting events, etc. that are not tiered.

b. PCPP Packaging

A cable operator may place several per channel offerings into a specific package with a package price lower than the sum of the price for the same channels if taken individually, i.e., lower than the sum of the component per channel pricing. For example, a system may charge its subscribers HBO, Showtime, Cinemax and The Disney Channel each at $10.00 per service per month. But a special package consisting of HBO and Showtime is only $16.00, or a $4.00 discount from the sum of the two individual per channel rates. As long as the customer has the right to subscribe to either Showtime or HBO without being forced to buy the package, then the package pricing is not subject to rate regulation.[14] Since it is the clear intent of the Act to encourage the offering and the success of PCPP services, then certainly granting a discount from the per channel pricing would incent consumers to purchase more PCPP services, satisfying Congressional intent.

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[14]These packages, accordingly, are not definitionally CPS. See Notice at paragraph 96 and note 133. See also our parallel discussion of anti-buy through discrimination in Attachment 1.

c. PCPP Discount

A widespread practice by cable operators is to offer incremental discounts as the subscriber subscribes to more and more per channel services without creating a specific package of named channel brands. Again each per channel service is always available on an a-la-carte stand alone basis. For example, a system may charge its subscribers HBO, Showtime, Cinemax, and The Disney Channel each at $10.00 per service per month on a stand-alone basis where the consumer only subscribes to only one service. But if the subscriber subscribes to two of the services, the incremental charge is only $8.00 for a total of $18.00 or a $2.00 discount. The incremental charges for each additional service thereafter is $6.00, etc. Therefore a subscriber to three per channel services will be charged a total of $24.00 or a $6.00 discount. Again the benefit of a multi-per-channel level discount is clearly beneficial to the public and not be subject to any rate regulation.

d. Equipment Packaged with PCPP

Oftentimes, cable operators package a per channel service with equipment necessary or desirable for the receipt of such service in a single, packaged price. For example, a system operator may offer ENCORE together with an addressable converter and the associated remote control, for $6.00 per month. Since there is no prohibition in the Act (nor should there be) against packaging equipment with PCPP service, then the very fact that

ENCORE, as a per channel service, is not rate regulated (the cable operator can charge any rate for ENCORE) renders the dissection of the cost of equipment used in the ENCORE package a moot point.[15]

6. Standards for Rate Regulation of BST and CPS

We interpret by the statutory language and the legislative history that the standards used for the rate regulation of BST must be more stringent than that used for CPS even if the Commission should choose to use a Benchmark approach using the same core formula. As stipulated in the Act, the Commission must develop its guidelines, criteria or formula, etc. so as to be easily used without burdening the subscribers, cable operators, franchising authorities and the Commission.[16] Therefore such formula must be capable of being adaptable to all systems.

- Reasonableness of BST

  The Act stipulates that the Commission must ensure that the rates for BST are reasonable. For a procedure to be broadly applicable, it must, when given the particulars of the cable system, yield a reference rate for BST that is definitely reasonable for that system, i.e., any BST rate that is equal to or below the reference rate is reasonable and there-

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[15]We do not contend that the same equipment would not be available to the subscriber under Section 623(b)(3).

[16]See Section 623(b)(2)(A).

fore acceptable. On the other hand, BST rates above the reference rate may be reasonable and presumably cable operators thus affected could put forth their cases accordingly.[17]

- Unreasonableness of CPS

Correspondingly, the Act stipulates that the Commission must prescribe criteria for identifying, for each cable system, rates for CPS that are unreasonable. Similarly, it must, when given the particulars of the cable system, yield a reference rate for CPS that is definitely unreasonable for that system, i.e., any CPS rate that is above the reference rate is unreasonable and therefore is subject to possible rollbacks. Similarly, CPS rates below the reference rate may be unreasonable in the absolute sense but the cable operator is not required to justify such.[18] Diagrammatically, the reference rates of a same complement of channels when placed in BST or when placed in CPS can be depicted as follows:

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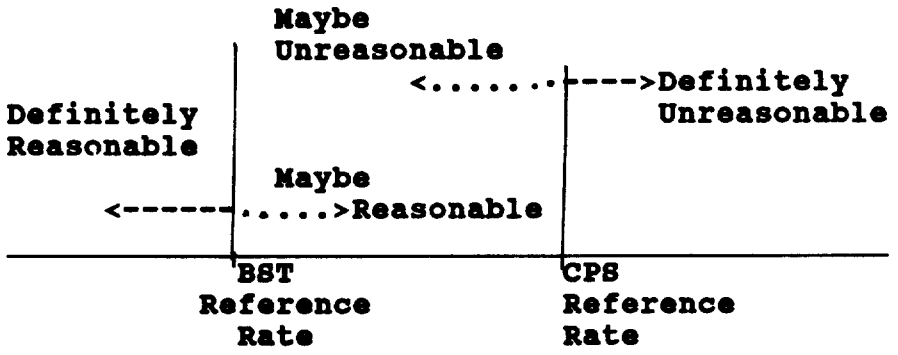
[17]See Notice at paragraph 61 proposing to permit cable operators that exceed the BST Benchmarks to demonstrate their costs.

[18]This statement is made in keeping with the intention of Section 623(c) to protect CPS subscribers from "egregious" rates. See House Report at 86. CPS rates serve a different purpose under Section 2(b) than BST rates. CPS rates can be seen as a fail-safe for consumers in the transition to a PCPP environment. See Footnote 10, supra.



It is quite clear from the above that there is a zone of maybes that separates the BST reference rate and the CPS reference rate, i.e., the "buffer zone." This comports with the legislative history that requires the Commission to provide the lowest possible rate protection for the consumer on the BST while the CPS rate regulation's objective is to weed out cable operators ("bad actors") that exhibit egregious rate behavior.

If the Commission decides to use a benchmark method which may include a rate-per-channel component for both BST and CPS, we recommend that there should be a multiplier of greater than one between BST and CPS to ensure that the "buffer zone" is maintained. For example, if the multiplier was determined to be 1.2 (or 120%), then a 20-channel component at say $0.50/channel would yield a $10.00 reference rate for BST while the same 20-channels placed in CPS would yield a reference rate of $12.00. It is beyond

ENCORE's scope or ability to determine what should be the specific multiplier. We believe however that the Commission, upon reviewing the results of its current rate surveys, can derive a normalized rate distribution curve. The multiplier can be derived by reviewing the normalized distribution curve for all rates and the percentage criteria for determining what is "definitely reasonably" and what is "definitely unreasonable." The multiplier is the ratio of the "definitely unreasonable" rate to the "definitely reasonable" rate.

It is of interest to note that a derived side effect of the multiplier is that the sum of reference rates for CPS and BST is greater if fewer channels were shifted to BST from CPS. This would encourage cable operators to not shift too many channels from CPS to BST, thereby ensuring the lowest possible rate for BST to the public.

7. Universal Standard/Benchmark

For the sake of deriving at workable formula so that any benchmark process can be applied to all cable systems, the Commission had alluded to treating all video programming services (particularly those that we have dubbed "cable programming channels" in the past) as "channels" without considering the content, nature, and, derivatively, the wholesale cost of

the channel to the cable operator. We believe this "universal" approach is inappropriate under the Act.

As pointed out in paragraph 3, above, that the Act would assign any video programming to the type of cable service, (BST, CPS, or PCPP) solely on how a cable operator markets such programming to the consumer in that system. To the extent that cable operators are free to use any video programming in fashioning a diverse offering to the public, a traditional view that a given video programming service should be in BST, CPS, or PCPP type of cable service is simply not reflective of the current marketplace and certainly would not be the case pursuant to the practices required under the Act.

In the marketplace today, a growing trend is to market ENCORE both as an a-la-carte service (PCPP) and as part of a new or existing tier (CPS) with other video programming services which more traditionally have been dubbed as "basic cable programming"[19] such as Sci-Fi, Comedy Central, The Learning Channel, etc., on the same cable system. The rationale to include a "premium service" such as ENCORE with traditionally "basic cable channels" in a "hybrid tier" is to provide a locomotive to increase consumer acceptance (penetration) at an affordable price which would permit cable operators to invest in

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[19]Pursuant to the environment created by the 1984 Act, many systems carry video programming as "basic cable service" that under present conventional wisdom of the 1992 Act would, upon re-tiering, be CPS.

marketing and technological resources to offer such a tier to the public.

For the Commission to treat all channels with a universal "cost per channel" regardless of content would definitely discourage cable operators from using ENCORE in a hybrid tier configuration thus dramatically decreasing the potential for diversity of programming to the public and to inhibit technological investment by cable operators all counter to the stated policy of the Act.

We recommend that the Commission perhaps should group the various programming services in accordance to their published or generally known "rate card" as compiled from time to time by trade publications, such as, Kagan's[20] newsletters. Using the average cost of such grouping by the Commission would be a far more accurate reflection of reality while still permitting the use of standard formulae for universal application.

8. Equipment

We interpret wherever the Act refers to the regulation of rates for the lease of equipment[21] that it only applies to such equipment as converters or associated remote control units which are technologically unique and are not readily available in the local retail consumer electronics market. This fully comports with the general policy for the Act (restated in paragraph 2

[20]Paul Kagan Associates, Inc.

[21]Section 623(b)(3) and (1)(2).

above) which brings the hands of government regulation into play only when there is no effective (and certainly no actual) competition in the marketplace. It also parallels the legislative intent of Section 3 of the Act which states that the overall rates for BST and CPS are not subject to any rate regulation when there is effective competition in the franchised area.[22]

This is particularly true in the area of remote control units. More and more consumer electronics retailers and national department stores are promoting a wide array of universal remote control units, and most of them are advertising the feature that they are fully compatible with cable's converter boxes, whether addressable or not, of the local cable systems. In many cases, the retailer actually offers features which are superior to what the cable operators are providing, e.g., a remote control unit that would permit volume control, TV set control, and VCR control. (See attached advertisements.) This growing but still nascent retail market is there precisely because the retailer believes that it can compete effectively with cable operators in offering the public a choice to purchase or lease such remote units from the retailer.

In fact, Section 17 of the Act contemplates and, indeed, would facilitate the growth of the consumer electronics retail industry by requiring that by no later than April 3, 1994, cable

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[22]Section 623(a)(2).

operators cannot take any action that prevents the functionality of commercially available remote control units with cable operator-supplied converter boxes. In a perverted way, if the Commission applied the "actual cost" approach to equipment which is readily available commercially, it would probably stop the growth of the retail consumer electronics industry in its tracks since the local retailers generally goes through several distributors while the cable operator deal directly with the manufacturers.

9. Equipment "Used" by Subscribers to Receive BST, CPS, and "Required" to Access PCPP

The Act stipulates that the lease of equipment "used" by a subscriber to receive BST or subscriber-requested equipment for "required" access to PCPP be rate-regulated on the basis of actual cost.[23] For CPS, which also includes the rental rate charged for equipment "used" for the receipt of CPS programming, the Act stipulates that the rate regulation criteria shall be based on unreasonableness.[24] One could posit that since practically all equipment can be used to receive BST signals, that there is an ambiguity or, worse, incompatibility of application

[23]Section 623(b)(3).

[24]Section 623(l)(2) and Section 623(c).

under the Act. A reading of the Conference Report clarifies this ambiguity.[25]

The statutory language made a clear distinction between equipment "used" to receive BST versus "addressable box[es] or other equipment as is required to access" PCPP.[26] Given the fact that all addressable converters can also receive BST signals, in the broadest sense they could be construed as being already covered by the "used" phraseology.

This specific bifurcation of BST and PCPP equipment and the exclusion of CPS equipment from "actual cost" regulation becomes clear with a reading of the Conference Report. It states that the original phrase "equipment necessary" is changed to "equipment used" to give the Commission greater authority to protect consumer interest. This change is intended to prevent cable operator from claiming for example, that if a converter is not definitely necessary by the subscriber if he/she has a cable-ready TV set, then such converter is not subject to regulation even though it is definitely used by those subscribers who have only the Commission approved minimum standard television set.[27] Therefore, we interpret the word "used" to mean "necessary for at least one subscriber on the system who has a Commission

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[25]Conference Report at Cong. Rec. H8324 (daily ed. September 14, 1992).

[26]Section 623(b)(3)(A).

[27]See 47 U.S.C. §303(s).

approved minimum standard TV set." For illustrative purposes, let's assume a system offers 30-channel converters for the receipt of BST and 50-channel converters for the receipt of CPS, and neither is necessary if the subscriber has a cable-ready set. Under the Act, the 30-channel converter is subject to "actual cost" regulation. The 50-channel converter, since it is not necessary for at least one subscriber on the system to receive BST because a 30-channel converter will do, is not subject to "actual cost" rate regulation, but would come instead under the criteria for unreasonableness or "bad actor" rate regulation proceedings.

10. Any Subscriber Must Subscribe to BST

The Commission inferred that a reading of Section (b)(7)(A) and Section (b)(8)(A) would indicate that any cable subscriber must first subscribe to BST. We interpreted that a cable operator may offer the consumer to subscribe to PCPP services without having to subscribe to the BST.

The statutory language of Section 623(b)(8)(A) yields two relevant facts. It reads in part, "A cable operator may not require the subscription to any tier other than BST . . . as a condition of access to video programming offered on a PCPP basis. . . ."

a. The word tier is limited to the video programming of BST or CPS tiers since PCPP is in addition to any and all tiers.

b. Any PCPP service must at least be available to BST subscribers; but the paragraph does not <u>require</u> the subscription of BST to receive PCPP.

The statutory language of Section 623(b)(8)(A) reads in part, "Each cable operator . . . shall provide its subscribers a separately available BST to which subscription is required for access to any other <u>tier</u> of services . . . ." We note that only CPS must buy-through the BST, but not necessarily PCPP services.

Our interpretation is fully in comport with the overall policy of the Act as stated in paragraph 2 above to create robust competition between cable operators and other distribution media. To the extent that there are no requirements on other multichannel video distributors such as Direct Broadcast Satellite distributor to offer BST before subscribing to PCPP, so the cable operators must have the same right in order to compete.[28]

11. <u>Negative Option Billing</u>

We fully agree with Commission's tentative finding that a change in the composition of a tier that was accompanied by a price increase justified under Commission's rate regulations would not be subject to the negative option billing prohibition.[29]

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[28]See also Attachment 1 for an additional rationale.

[29]Notice at paragraph 120.