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February 11, 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., Room 222
Washington, D.C. 20554

Re: Reply Comments of InterMedia
Partners, MM Docket No. 92-266

Dear Ms. Searcy:

Enclosed on behalf of InterMedia Partners, are the original and nine copies of InterMedia's Reply Comments in the above-referenced proceeding.

Please address any questions concerning this letter to the undersigned.

Sincerely yours,



Stephen R. Ross

KAH/mec
Enclosure

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Before the
FEDERAL COMMUNICATIONS COMMISSION
Washington, D.C.

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FEB 11 1993
FEDERAL COMMUNICATIONS COMMISSION
OFFICE OF THE SECRETARY

In the Matter of)
)
Implementation of Sections of)
the Cable Television Consumer)
Protection and Competition Act)
of 1992)
)
Rate Regulation)

MM Docket No. 92-266

REPLY COMMENTS OF INTERMEDIA PARTNERS

I. INTRODUCTION

InterMedia Partners ("InterMedia"), by its attorneys, hereby submits these reply comments to comments filed in response to the Federal Communications Commission's ("FCC" or "Commission") Notice of Proposed Rulemaking ("NPRM") in the above-referenced proceeding.

II. ADOPTION OF A RATE BENCHMARK METHODOLOGY

A. A "Benchmark" Method for Establishing Basic Tier Rates is Superior to Rate of Return Regulation

With the notable exception of some cities and the telephone companies, who are clearly interested in imposing the burdens of price cap regulation on potential competitors, the vast majority of comments supported the Commission's proposal to adopt a benchmark method of rate regulation. It was widely accepted that traditional rate of return regulation and its progeny, price cap regulation, are enormously complicated and expensive to administer.

Given the complexity and expense of administering, monitoring and holding lengthy public hearings to implement and adjudicate rate of return regulation, it was surprising to note that a number of cities

advocated traditional rate regulation.¹ InterMedia reiterates its position that franchise authorities should not be presumed to be competent to administer and enforce rate of return regulation, and should be certified for that process separately.

In addition, the Commission must make clear that cable operators are not required to absorb franchise authorities' costs of regulation. The franchise authority's costs associated with the administration of rate regulation, and any other costs of regulation under the Act, must be included in the franchise fee, which may not exceed five percent (5%) of the cable operator's gross revenues. 47 U.S.C. § 542 (1993). Attorney's fees, consultant's fees or other costs incurred in conjunction with awarding, renewing, administering and/or enforcing a cable television franchise, are impermissible additional franchise fees unless they are included in the 5% maximum allowable franchise fee. Time Warner Entertainment Company, L.P. v. The Towns of Athol and Orange, ___ F.Supp. ___ (D.Mass. 1993), slip. op., January 14, 1993 at p. 12-14.²

¹ See, e.g., Comments of the Mayor and the City of Baltimore, Comments of the City of Rocky Mount, Comments of the Political Subdivisions of the State of Minnesota.

² The Court also held that "the Towns . . . may not attempt to regulate cable service rates until the FCC has promulgated regulations and until they have filed certificates with the FCC. Because these preconditions have not been satisfied, the Towns may not regulate cable service rates under Post-amendment §543." slip. op. at 10.

B. Benchmark Rates Should Not Be Based on Past-Regulated Rates

As noted above, the initial comments filed in this proceeding generally indicated an overwhelming support for the adoption of a "benchmark" methodology. Comments varied, however, on exactly how such a benchmark should be developed. Several parties endorsed the benchmark alternative, offered by the Commission in the NPRM, to set benchmarks for the basic tier and for the cable programming services tier based on rates charged in either 1984 or 1986.³ The Commission had requested comment on whether 1984 or 1986 rates, which might be presumed reasonable, could be adjusted upward to establish a benchmark rate for 1993 rates. NPRM at ¶ 44.

InterMedia submits that benchmarks should not be based on either 1984 or 1986 rates. Proposals to merely adjust pre-deregulation rates by the rate of inflation or by the Gross National Product Price Index ("GNPPI") do not reflect the growth and development of cable television services since 1984. Such an approach might be appropriate for public utilities where the essential nature of the service does not change and rates are simply based on measurable units of output. In contrast, cable television services are comprised of program packages in which the value is largely determined by subscriber demand.

Benchmark rates based on past-regulated rates are not appropriate for several reasons. First, since 1984, the average number of channels on both the basic tier and the cable programming services tier have increased dramatically. On the cable programming services

³ See, e.g., Comments of Consumer Federation of America.

tier in particular, operators have added programming, such as regional sports programming, at a substantial cost to the cable operator. InterMedia has added many programs in response to a significant subscriber demand, despite the programming expense increases necessary to add these channels. The cost of such programming was not reflected in 1984 or 1986 rates. In addition, the cost of programs on existing channels, such as ESPN, has increased significantly as the quality of such programs has improved. Services such as USA Network have purchased expensive off-network programming and now produce expensive original programs. ESPN now carries NFL football games and NHL hockey games.⁴

Second, labor and benefits costs generally comprise the largest portion of a cable operator's expenses. These costs have greatly increased since 1984 at a much faster pace than inflation. Since 1984, insurance premiums paid by private sector employers have almost doubled -- from \$123.7 billion in 1984 to \$216.8 billion in 1990.⁵ Similarly, average labor costs in the communications industry rose 18% between 1985 and 1990.⁶ The Commission must factor these costs as well as all other relevant operating expenses into any

⁴ The ability of the programmers to raise their rates to cable systems operating in a free market has driven the quality improvements in programming.

⁵ Statistical Abstract of the United States, 112th Ed. (1992), Table No. 135 "National Health Expenditures: 1960 - 1990" at p.97.

⁶ Id., Table No. 649, "Average Annual Total Compensation and Wages and Salaries per Full-Time Equivalent Employee, by Industry: 1980 - 1990," p. 410.

benchmark established for the basic and cable programming services tiers.

Third, in contrast to the National Association of Broadcaster's ("NAB") position, retransmission consent fees cannot be viewed as "functionally identical to the direct costs of cable program services."⁷ Congress expressly separated the value of programming from the value of the unmodulated broadcast signal of the station. As the Conferees stated:

[c]able systems carrying the signals of broadcast stations [pursuant to retransmission consent] will continue to have the authority to retransmit the programs carried on those signals under the section 111 compulsory license.

Conference Report, p. 76 (emphasis added). Congress clearly intended that retransmission consent fees would be equivalent to the value of the unmodulated broadcast signal, not the programming for which cable operators currently pay substantial and growing copyright fees. Therefore, contrary to NAB's assertions, the equivalent of retransmission consent fees has never been included in cable operators' rate bases. Rather, retransmission consent fees are additional costs imposed on cable operators by the Act, which is why the Conferees specifically directed the Commission to "consider the impact that the grant of retransmission consent by television stations may have on rates for the basic tier" Id. Accordingly, InterMedia reiterates its concern expressed in its initial comments that the Commission must place some parameters on retransmission consent fees in

⁷ Comments of NAB at p. 5.

keeping with the Congressional mandate to establish "reasonable" basic tier rates. Cable operators should also be able to add retransmission consent fees to basic cable rates as a separate item, along with franchise fees, etc.

Fourth and finally, pre-1986 cable television rates were entirely subject to the local political decision-making process. As a result, cable television rates were kept artificially low by local franchising authorities, which historically delayed authorizing rate increases and often used the local political process to extract additional concessions from cable operators.

In sum, benchmark rates established by the Commission must take into account the growth and increased diversity of cable television services over the past 6-8 years, as well as the changed economic environment. Such benchmarks cannot be established by merely adjusting past-regulated rates. As Congress directed, the Commission must carefully review present direct and indirect costs associated with the provision of cable television service when setting benchmark rates.

III. RATES FOR LEASED ACCESS CHANNELS

There appeared to be a consensus among the majority of commenters that a "reasonable" rate for a leased access channel is largely a factor of what type of programming will be placed on the channel. In addition, the lack of historical leased access rate information makes it virtually impossible to use a benchmark approach to set leased access rates. In the context of such difficulties in establishing maximum reasonable rates for leased access channels, most commenters identified the key concern as the potential migration of

satellite programmers from the cable programming tiers and premium channels to leased access channels.

InterMedia agrees with this concern. The Commission should not establish a maximum rate for leased access channels that is lower than the highest "implicit leased access charge"⁸ paid by any programmer on the system. Such a rate could result in the migration of satellite programmers to leased access channels, which would reduce the diversity of programming available to subscribers and correspondingly reduce cable operators' ability to transmit lower-priced services.⁹ Therefore, InterMedia urges the Commission to adopt rules which recognize that a "reasonable" rate for a leased access channel should be based primarily on the intended use of the channel, but in no event should it be lower than the "highest implicit leased access rate" charged by the operator for a channel on that system.

V. SUBSCRIBER BILL LINE ITEMIZATION

Several comments addressed Section 622(C) of the Act, which permits cable operators to itemize the cable subscriber's bill to indicate those charges attributable to: (1) franchise fees; (2) PEG costs; and (3) any other governmental assessments on cable television services. Under the Act, line itemization would result in a pass-through of the charge over and above the "benchmark" rate. In

⁸ NCTA defines the "implicit leased access charge" as equivalent to the amount which the cable operator pays the programmer for the right to resell the program to subscribers. See Comments of NCTA at p. 91-92.

⁹ See, e.g., Comments of NCTA at p. 93, Comments of Continental Cablevision at p. 80.

particular, the National League of Cities raised the concern that cable operators in California abuse the line item provision by itemizing "taxes of general applicability including generally applicable property tax imposed on all property owners in the State of California."¹⁰ This practice is alleged to disguise rate increases and reduce gross revenues for purposes of calculating the franchise fee. Id.

It appears that the League is referring to California's "possessory interest tax," in which each county assesses and taxes cable systems for the use of public areas, such as "public streets, rights-of-way, or public easements contained in a cable television franchise or license."¹¹ Any California business which uses public rights of way (e.g., public utilities, shops in a public park) is subject to the possessory interest tax. For example, public utilities, which are also subject to possessory interest taxes, often incorporate such taxes into the rate base, and thus recover them through subscriber revenue.

While the possessory interest tax applies to businesses other than cable television, it is certainly not a generally applicable tax similar to social security tax or employee taxes. Unlike most other businesses, cable television systems extensively use public rights of way to lay cable under city streets or along telephone and utility lines, and as a result, cable operators pay to California counties

¹⁰ National League of Cities, comments at p. 22.

¹¹ California Revenue and Tax Code, § 107.7 (1993).

possessory interest taxes that are substantially higher than most other California businesses.

As an example of the possessory interest tax burden placed on cable operators, InterMedia operates a cable system in Newark, California. In 1990, the assessed value of the system was \$68,000. In 1992, the county re-assessed the value of the system at \$10,000,000, -- a nearly 15,000% increase -- for purposes of imposing the possessory interest tax. Moreover, the county applied the tax retroactively to 1990 when InterMedia first purchased the system. While InterMedia absorbs 40% of the new tax, the remaining 60% of the tax (\$1.52 per subscriber per month) is now collected from subscribers through line itemization charges.

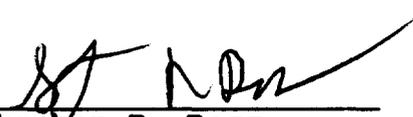
Assuming the Commission adopts national benchmark rates, specific state taxes would not be included in the rate unless the Commission makes such an allowances. If InterMedia is not permitted to add some or all of these taxes, especially possessory interest taxes, as a line item outside the benchmark (InterMedia, at present, is already absorbing 40% of this tax voluntarily) InterMedia will be unable to earn a reasonable profit as provided for under the Act. Such a result would be confiscatory. Therefore, the possessory interest tax set forth in Section 107.7 of the California Revenue and Taxation Code, among others, is directly attributable to cable operations and appropriately within the line itemization provision of the Act.

V. **CONCLUSION**

Based on the foregoing, InterMedia Partners respectfully requests that the Commission consider the concerns raised in these Reply Comments, and incorporate them into its final rules governing the regulation of cable television rates.

Respectfully submitted,

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By: 

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February 11, 1993

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I, Magdalene E. Copp, a secretary of the law office of Ross & Hardies, do hereby certify that I have this 11th day of February, 1993, served by first-class mail, postage pre-paid, a copy of the foregoing "Reply Comments of InterMedia Partners" to:

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