1992 Cable Act, i.e., converter box, remote control unit, connections for additional television receivers, and wiring that includes other inside cabling.[666] Commenters did not list additional equipment that we had overlooked. We also agree with NATOA that the Commission must establish guidelines for determining the actual cost of equipment used to receive the basic tier for all cable systems not subject to effective competition. Although we believe that Congress intended our regulations to encourage a competitive market in the provision of equipment and service installation, we do not have the information we would need to establish an effective competition test for equipment and installation at this time. We conclude that Congress, by specifically listing converter boxes and remotes in Section 623(b), expressed its opinion that these items were not subject to effective competition apart from a determination that the whole cable system is subject to effective competition.[667] Furthermore, Congress determined that developing a competitive market for equipment required additional study by this Commission.[668] We have begun a proceeding to investigate these issues and do not wish to prejudge that proceeding by making determinations here without sufficient data.[669]

283. We further believe that Congress intended the actual cost standard to apply broadly to all equipment used to receive basic tier service. The legislative history indicates that the statutory language was changed to give the Commission greater authority to protect the interests of the consumer.[670]

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[666] We adopt the same demarcation point for cable home wiring that we adopted in our proceeding on that subject. For single unit installations, that point is twelve inches outside of where the cable wire enters the outside wall of the subscriber's premises. For multi-dwelling units, the demarcation point is twelve inches outside of where the cable enters the outside wall of the subscriber's individual dwelling unit. See Report and Order in MM Docket 92-260, Implementation of the Cable Television Consumer Protection and Competition Act of 1992, Cable Home Wiring, FCC 93-73 (released Feb. 2, 1993), recon. pending.

[667] Section 623(b) of the Communications Act is designed to protect subscribers of cable systems not subject to effective competition. Communications Act, § 623(b), 47 U.S.C. § 543(b).

[668] See Communications Act § 624A, 47 U.S.C. 544A.

[669] See Notice of Inquiry in ET Docket No. 93-7, (Implementation of Section 17 of the Cable Television Consumer Protection and Competition Act of 1992, Compatibility Between Cable Systems and Consumer Electronics Equipment), 8 FCC Rcd (1993).

[670] See Conference Report at 64.

We find that this change in terminology was significant and was specifically intended to broaden the class of equipment subject to regulation on an actual cost basis. We interpret Congress' intent, therefore, to mean that we are obligated to give the term "used to receive basic tier service" an expansive reading as NATOA urges, rather than the narrow reading advocated by cable operators. Moreover, as the Notice discussed, the statute specifically included addressable converter boxes needed to access video programming on a per program or per channel basis. The inclusion of such equipment additionally reflects Congress' desire that we broadly interpret the phrase "equipment used to receive the basic service tier." We also agree with commenters who contend that regulating identical equipment differently depending on the level of service received by the subscriber will lead to customer confusion.[671] Congress expressed concern about the rates for equipment, particularly remote control devices.[672] If we narrowly define equipment used to receive basic tier service, operators might seek to evade regulation of remotes, for instance, by providing to basic subscribers converter boxes that do not have remote control capabilities.[673] Our broad interpretation of equipment used to receive basic tier service does not require a meaningless interpretation to the definition of cable programming services which includes equipment and installation. We believe that Congress included equipment and installation in the definition of cable programming services to prevent cable operators from avoiding regulation of equipment, if any, used to provide cable programming services alone or in conjunction with unregulated services.

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[671] We recognize that the technology for cable equipment is rapidly changing and Congress did not intend to inhibit innovation. Therefore, we note that in the future, cable operators may wish to provide converter boxes or remotes capable of numerous functions and that are used to receive the basic service tier. Initially, these devices might have very high costs. An operator would be entitled to recover actual costs, as we define them below, through monthly charges for the lease of this equipment. Alternatively, our rules will not preclude the operator from pricing these devices below-cost to encourage their use. The operator could recover the remainder of its costs in whole or in part through increased charges for unregulated services, per channel and pay-per view, that these devices also provide. See paras. 301-302, infra for a discussion of below-cost pricing.

[672] See, e.g., Communications Act, § 624A(c)(2)(D), 47 U.S.C. §544A(c)(2)(D); House Report at 27-28, 83-84, 108.

[673] See Simmons Comments at 1 (claiming that if a remote is not offered to basic subscribers, then remotes would not be subject to the actual cost standard).

(b) Unbundling

i. Background

284. The Notice tentatively concluded that Congress intended to separate rates for equipment and installations from other basic tier rates. The Notice relied on the fact that the statute addresses rates for equipment used to receive basic tier service and related installation in a subsection separate from those dealing with cable service rates. In addition, the statute establishes for basic tier equipment and installation a standard based on actual costs, which are only one of several factors used to evaluate the reasonableness of other basic tier rates. The Notice also requested comments on the feasibility of a competitive market developing for installation services in light of the potential for an increase in theft of service related to third party installations.[674]

ii. Comments

285. In general, cable operators argue that the Commission should not require operators to unbundle equipment and installation rates from other basic tier rates.[675] Other parties agree with the Commission's tentative conclusion to separate rates for equipment and installation from other basic tier rates.[676] For example, many municipalities claim that unbundling will not only impact rates for subscribers, but should assist in meeting the Congressional goal of promoting competition in subscriber technology.[677] Several operators counter that no evidence exists that a competitive environment for equipment and installation would be hindered by permitting operators to bundle

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[674] Notice, 8 FCC Rcd at 525 and n. 90.

[675] Armstrong Comments at 23; Carib Comments at 10-11; Continental Comments at 36; InterMedia Comments at 24; NCTA Comments at 46.

[676] Austin Comments at 55; Baltimore Comments at 9; BellAtlantic Comments at 11; CFA Comments at 132; Conn Comments at 11; Dade Comments at 10; Dover Comments at 19; EIA Comments at 4; Minn Comments at 14; Multiplex Comments at 12; NATOA Comments at 46; NYNEX Comments at 11; Rapids Comments at 34; SquareD Comments at 4; Bayonne Reply Comments at 9; GTE Reply Comments at 17; NYNEX Reply Comments at 13; USTA Reply Comments at 5; Watertown Reply Comments at 10.

[677] Laurinburg Reply Comments at 4; Laurens Reply Comments at 4; Owensboro Reply Comments at 4; Piscataway Reply Comments at 4; Reidsville Reply Comments at 4; Titusville Reply Comments at 4; Union Reply Comments at 4; Worthington Reply Comments at 4.

equipment and installation rates.[678] If bundling were prohibited, cable operators claim, they would face an unnecessary intrusion into their business practices.[679]

206. Several operators contend that even if the Commission prohibits bundling of basic service and equipment, it should allow operators to establish rates for equipment, installation, service calls and additional outlets, as long as rates remain within a reasonable rate pool or basket.[680] Many commenters believe that the Commission should not allow cable operators to bundle rates for installation with rates for lease of equipment.[681] Several parties agree with the Commission that unbundling may promote competition in the provision of equipment and installation.[682] Commenters did not express a great deal of concern about potential theft of service or signal leakage problems associated with third party installations.[683] Some commenters further argue that not only should rates for equipment and installation be unbundled, but charges for each individual item and activity should be unbundled.[684] CFA claims that this does not mean, however, that a cable operator may not offer a

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[678] AdelphiaII Comments at 81-82; Falcon Comments at 47; Nashoba Comments at 80-81; Newhouse Comments at 29-30; TimeWarner Comments at 64.

[679] AdelphiaII Comments at 82; Nashoba Comments at 81; Newhouse Comments at 30; TimeWarner Comments at 64-65.

[680] AdelphiaII Comments 82-83; Falcon Comments at 47-48; Nashoba Comments at 81-82; TimeWarner Comments at 65.

[681] Austin Comments at 55; Minn Comments at 14; NATOA Comments at 46; Schaumburg Comments at 9; SDA Comments at 11; Bayonne Reply Comments at 9; Watertown Reply Comments at 9.

[682] NATOA Comments at 47; Rapids Comments at 34; Schaumburg Comments at 9; Bayonne Reply Comments at 9.

[683] See, e.g., Armstrong Comments at 24 (most signal leakage occurs at the tap and the drop); EIA Comments at 8 (competition need not entail unacceptable risks of signal piracy); Multiplex Comments at 14-15 (Commission's concern that subscriber home wiring ownership might increase the risk of signal leakage is unfounded because virtually all subscriber owned equipment containing active components is governed by Commission technical standards controlling interference potential); SquareD Comments at 9 (cable industry has managed to deal successfully with theft of service in a competitive market place for the past several years).

[684] Conn Comments at 11-12; CFA Reply Comments at 14-15; see also Austin Comments at 55.

package of equipment at a single price in addition to offering each piece of equipment separately.[685]

iii. Discussion

287. We conclude that unbundling rates for equipment, installation, and additional outlets from the rates for basic service best comports with our Congressional mandate. As explained in the Notice, Congress discussed rates for equipment used to receive basic tier service and related installation in a subsection separate from those dealing with cable service rates. In addition, the statute requires an actual cost standard for basic tier equipment and installation, but includes several other factors for evaluating basic tier service rates. Accordingly, in order to apply the separate equipment and programming service standards, the rates for each must be unbundled from each other. Our decision to define the term "equipment used by subscribers to receive basic tier service" broadly also requires, at minimum, an unbundling from other cable system costs of costs related to specific types of equipment and installations. Once an operator identifies the costs associated with equipment and installation, developing cost-based charges should not burden the operator.

288. The Commission agrees with commenters who argue that we should require complete unbundling of the charges for equipment and installation. Therefore, we will require separate charges for each significantly different type of remote, converter box and installation. An operator may establish one charge for all other customer equipment or develop individual charges for specified other equipment. We believe that separate charges for individual pieces of equipment will help franchising authorities and subscribers to evaluate whether charges are set on the basis of actual costs. In addition, we think that this total unbundling is consistent with the development of a competitive market for equipment and installation.[686] We conclude that Congress intended that our rules implementing the Cable Act encourage competition.

(c) Actual Cost Standard

i. Background

289. The Cable Act directs the Commission to establish standards for setting, on the basis of actual cost, the rate for installation and lease of equipment used by subscribers to

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[685] CFA Reply Comments at 14.

[686] As noted above, commenters did not express concern over potential theft of service or signal leakage problems related to independent installations.

receive the basic service tier. The Notice proposed requiring operators to base charges for equipment covered by Section 623(b)(3) on direct costs, and indirect cost allocations, including reasonable general administrative loadings and a reasonable profit.[687] The Notice also proposed determining the actual costs for installation on the same basis as equipment. We recognized, however, that this determination would involve allocating many joint and common costs, and instead of proposing allocation rules, the Commission suggested requiring the cable operator to bear the burden of showing the reasonableness of its implementation of our general allocation rules.[688] The Notice concluded that it appears reasonable for our rules to permit cable systems to recover installation costs as a one-time charge.[689] The Commission recognized that costs for installation will vary depending on whether the dwelling has inside cabling already.[690] Therefore, we requested comment on whether costs vary enough to reasonably require cable operators to develop two separate rates for installation or to use an average rate and whether that decision should be left to the discretion of the local franchising authority. In addition, we requested comment on whether there should be provision for a surcharge when the distance between a customer's premises and the operator's distribution plant is substantial.[691]

290. As an alternative to leasing equipment, the Notice recognized that cable operators may wish to sell equipment to their customers.[692] We proposed limiting operators in these

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[687] Notice, 8 FCC Rcd at 526.

[688] Notice, 8 FCC Rcd at 526.

[689] Notice, 8 FCC Rcd at 526. The Notice based this conclusion on the extent to which installation costs have traditionally been recovered through a one-time charge and because the length of time a subscriber will continue service is unpredictable. We specifically noted, however, that we did not intend to require recovery of installation costs as one-time charges. Id. at 526 and n. 100.

[690] Whether the cable system is well-established in the community might be an important factor because dwellings in such areas are more likely to have been previously wired.

[691] Notice, 8 FCC Rcd at 526-27

[692] Although the statute refers to the lease of equipment, this alternative assumes that Congress's main concern was preventing customers from paying for equipment many times over through monthly rental fees. See House Report at 83-84. The sale may occur as a one-time payment or over a period of time. Notice, 8 FCC Rcd at

circumstances to the recovery of actual costs, however we define that term. We observed that actual costs may vary depending on the length of payment schedule. Where the operator sold equipment to subscribers, the purchaser would have responsibility for repair of the equipment, unless a service contract were also purchased. The Notice also took note of the potential competitive advantage cable operators would enjoy during the development of an alternative market for cable equipment. Therefore, we proposed that customers, purchasing on time from the cable operator, would be permitted to change their mind and purchase equipment from an alternative source. Under those circumstances, the cable operator must discontinue the equipment charge, but the equipment could be sold or leased to another customer as used equipment at a rate reflecting recovered costs.[693]

ii. Comments

291. We received various suggestions for determining the actual costs of equipment and installation. For example, some operators contend that rates must account for the following: installation; amortization; maintenance; financing; general administrative overhead; and a reasonable profit.[694] Other commenters would limit an operator's charges for equipment and installation.[695] In addition, some commenters describe limitations in operators' current accounting records.[696] Several parties suggest we establish a national average cost for each type of equipment.[697] CSC suggests we adopt a benchmark applicable to all basic equipment that would allow operators to

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526.

[693] Notice, 8 FCC Rcd at 526.

[694] See AdelphiaII Comments at 74-75; Falcon Comments at 42; Nashoba Comments at 73-74; Newhouse Comments at 23-24; TimeWarner Comments at 58. See also Armstrong Comments at 21; CIC Comments at 38-39; Cox Comments at 33-34; InterMedia Comments at 21-22, for similar lists.

[695] Baltimore Comments at 9 (charges should be no more than cost); CFA Comments at 132 (because Congress intended to promote a competitive cable equipment market, it makes no sense to allocate joint and common costs to equipment); Miami Beach Comments at 11 (actual cost does not include reasonable profit); Rapids Comments at 35 (charge should recover direct costs plus a nominal contribution to overhead).

[696] See Comcast Comments at 51-52; Multiplex Comments at 11.

[697] See, e.g., CIC Comments at 38-39; Cox Comments at 33-34.

retain their current equipment price structure.[698] TCI suggests competitive price benchmarks which can be presumed at cost.[699] NATOA contends the Commission should establish a benchmark rate or rates for installation because installation costs are not as readily identifiable as equipment costs.[700] Some operators propose applying a presumption that an installation rate is reasonable if it is no greater than the hourly rate charged for similar installations by the local exchange telephone carrier (LEC) that provides service in the area.[701] MCATC, however, recommends against a benchmark methodology, because a cost analysis of equipment and installation charges incorporates more discrete data, which would lend itself to manageable cost of service analysis.[702]

292. Commenters support the Commission's proposal to allow for recovery of installation costs as a one-time charge.[703] Cable operators generally prefer to average installation costs rather than establish separate rates for complete installations and previously wired homes.[704] Other parties, however, believe that installation rates should more closely reflect the cost of the actual installation.[705] On the other hand, operators support the application of a surcharge when the distance between a

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[698] CSC Comments at 12-13 n. 19.

[699] TCI Comments at 38-39; see also Multiplex Comments at 11 (if Commission does not adopt an allocation methodology, it should adopt a regional benchmark).

[700] NATOA Comments at 47.

[701] Falcon Comments at 44; Newhouse Comments at 26; TimeWarner Comments at 60-61.

[702] MCATC Comments at 11.

[703] See Armstrong Comments at 24; InterMedia Comments at 25; CATA Comments at 34; Continental Comments at 37 and Appendix D; Lenfest Comments at 7; NATOA Comments at 48.

[704] Carib Comments at 11-12; Continental Comments at 38 n.14; Lenfest Comments at 7.

[705] See Austin Comments at 56 (arguing that installation costs should be presumed nominal if the home already has cable home wiring); GTE Comments at 13 (Commission should unbundle installation into installation of service and installation of premises wiring); NMCC Comments at 4 (installation rates should reflect the amount of service that the customer actually needs).

customer's premises and operator's distribution plant is substantial.[706]

293. In general, commenters support the Commission's proposal to allow operators to sell equipment.[707] A few municipalities mention that the cable operator in their jurisdiction refuses to sell equipment.[708] Some commenters contend that the Commission should not allow third party vendors to supply addressable converters because of security and theft of service concerns.[709] In addition, cable operators disagree with the Commission's proposal to allow subscribers to cancel purchase agreements if the customer wishes to purchase the equipment from an alternative source.[710] Finally, several parties suggest that the Commission require cable operators to inform subscribers that alternative sources for equipment exist.[711]

iii. Discussion

294. We believe that, by requiring that charges for equipment and installation be based on actual cost, Congress intended that cable operators can recover the costs of leasing equipment and service installations from charges for those activities. Because the Act requires the Commission to establish standards for setting rates for lease of equipment and installation, we will require the local franchising authorities to follow the detailed guidelines we now adopt for identifying

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[706] See AdelphiaII Comments at 78-79; CATA Comments at 36-37; Falcon Comments at 45; Lenfest Comments at 7; Nashoba Comments at 77-78; Newhouse Comments at 27; TimeWarner Comments at 62.

[707] Austin Comments at 56; Continental Comments at 37; Lenfest Comments at 7; NMCC Comments at 5; ThousandOaks Comments at 22.

[708] Baltimore Comments at 3; Somerville Comments at 5.

[709] Armstrong Comments at 22; InterMedia Comments at 23; see also MediaGeneral Comments at 10-11 (Commission should not allow subscribers to purchase equipment from third party vendors unless controls exist to ensure equipment compatibility with the cable system); SquareD Comments at 9 (does not advocate subscriber ownership of descrambling devices without operator permission).

[710] Armstrong Comments at 22-23; Continental Comments at 38; InterMedia Comments at 23-24; see also Discovery Comments at 16; but see Austin Comments at 56.

[711] AdelphiaII Reply Comments at 37 (provided this is part of a standard that deregulates rates for such equipment); BellAtlantic Reply Comments at 20 n.49; GTE Comments at 14; ThousandOaks Comments at 23.

the costs to be recovered through equipment and installation rates and for calculating those rates. The Commission believes that our guidelines satisfy the statutory requirements, and thus a local franchising authority's proper use of them to determine reasonable rate levels cannot form the basis of a cable operator complaint to the Commission.[712]

295. Under our guidelines, a cable operator shall establish an Equipment Basket to which it will assign the direct costs of service installation, additional outlets, and leasing and repairing equipment.[713] The basket will include an allocation of all those system joint and common costs that service installation, leasing, and equipment repair share with other system activities, excluding general system overhead.[714] The costs contained in the Equipment Basket shall include a reasonable profit.[715] An operator must also calculate an Hourly

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[712] This will not preclude cable operators from complaining about whether the local franchising authority applied our methodology in a reasonable manner.

[713] The Equipment Basket shall not include the operator's direct costs of equipment sold to customers.

[714] Excluding general system overhead will simplify the cost showing for the Equipment Basket because a cable operator will not have to calculate these costs, unless the operator chooses to make a cost-of-service showing. In addition, this exclusion will reduce the burden for local franchising authorities because they will not be required to review and evaluate the methodology for determining general system overheads. We believe that this decision is consistent with Congress' intent to keep rates for equipment and installation low.

[715] The Commission has prescribed 11.25 percent as a reasonable rate of return for the provision of regulated interstate access service by local exchange carriers. Represcribing the Authorized Rate of Return for Interstate Services of Local Exchange Carriers, 5 FCC Rcd. 7507 (1990), on recon. 6 FCC Rcd 7193 (1991), aff'd sub. nom., Illinois Bell Tel. Co. v. FCC, No. 91-1020, Slip Op. (D.C. Cir. April 2, 1993). We believe that it is reasonable to utilize a similar return at the onset of regulation for installation of service and the provision of equipment by cable operators. Thus, at least initially, we will employ 11.25 percent as our standard. Cable operators therefore may incorporate a reasonable profit not to exceed 11.25 percent of the costs contained in the Equipment Basket. To the extent that a cable operator believes this standard, as applied in individualized circumstances, does not enable the operator to maintain the financial integrity of its regulated operations and attract new capital to the business, the cable operator may make a showing to justify an increase in the

Service Charge (HSC) through which it would recover all Equipment Basket costs (including a reasonable profit) except for the operator's capital costs of remotes, converter boxes and other customer equipment up to the time it is leased to the subscriber.[716]

296. Charges for leasing remotes[717] shall be designed to recover the operator's cost of purchasing and financing the lease of the remote and expected repair and service costs over the useful life of the equipment. Expected repair and service costs will be determined by multiplying the estimated number of repair and service hours per remote by the HSC. We anticipate that cable operators will use their past experience and historical data to make the best estimate of the number of service and repair hours for remotes. Charges for leasing converter boxes and all other equipment will be calculated in the

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permitted profit level. Through industry surveys, future reporting by cable operators, and the comments we will receive in our Second Further Notice on cost-of-service standards, we hope to refine our understanding of regulated cable operators' cost of capital and acquire more information concerning the risks of regulated provision of equipment. As we gain more experience in this area, we may revisit our initial determination regarding the reasonable profit standard for equipment.

[716] The HSC would be computed by taking the sum of all equipment basket costs except purchase cost of all equipment, and dividing that sum by the operator's total annual person hours dedicated to leasing, installing and equipment repair services. These estimates would be subject to verification using historical data.

[717] Some cable operators currently charge an additional monthly fee to enable converter boxes to work with a subscriber's universal remote control device. We recognize that not all converter boxes have the capability of working with a remote control device, and those boxes with remote capability may have higher costs. Therefore, we believe the cost of this service should be recovered in the charge for the type of converter box that is compatible with remote control devices instead of a monthly enabling charge. An operator may, however, require subscribers to pay a reasonable fee if a service call is necessary either to enable the converter box to work with the remote or to replace the subscriber's box with a converter that is compatible with the remote. At this time, we will not require cable operators to provide converter boxes that are compatible with universal remotes. But see Notice of Inquiry , ET Docket No. 93-7, supra note. 669.

same manner as for remotes.[718] For installation charges,[719] the cable operator must elect a uniform installation charge that is calculated based upon either: (1) the HSC times the person hours of the visit;[720] or (2) the HSC times the average hours spent per installation visit.[721]

297. The Commission believes that our guidelines comply with statutory requirements by developing charges for equipment and installation on the basis of actual cost. At the same time, this methodology strikes a balance between determining the actual cost for each type of equipment and installation, and simplifying the cost showing for operators and franchising authorities. The Hourly Service Charge Cost allows operators to aggregate certain joint and common costs that might be difficult to directly allocate, and then uses time spent in related activities as the factor for allocating these costs to the various charges.

298. These guidelines will not preclude an operator from selling equipment to subscribers.[722] Where an operator chooses to do so, the equipment price shall be set no higher than necessary to recover the operator's costs, including all costs incurred for storing and preparing the equipment for sale up to

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[718] For an explanation of calculating charges for additional connections, see paras. 306-307, infra.

[719] Consistent with our initial determination, an operator may elect to establish a one-time charge for service installation or recover the costs through a series of monthly charges. See Notice, 8 FCC Rcd at 526 and n. 100.

[720] This option would eliminate the need for lower charges for already wired homes and surcharges for extra long drops. Installations of already wired homes will involve less time and thus lower charges. Although the cost of the drop is not recovered as customer equipment, installations involving extra long drops will take more time, leading to a higher charge.

[721] Under this option, there must be several averages: one for unwired, another for prewired installations, one for installation of additional connections at the time of initial installation, and finally one average for installation of additional connections after initial service installation. In addition, an operator might wish to develop over average installation rates, such as one for installation, involving extra long drops.

[722] As stated in the Notice, this alternative is consistent with the view that Congress's main concern was preventing customers from paying for equipment many times over through monthly rental fees. Notice, 8 FCC Rcd at 526, n.100.

the time it is provided to the customer, plus a reasonable profit. The purchaser would be responsible for maintaining and repairing any purchased equipment, but cable operators may also sell service contracts. The price of these contracts shall be based on the HSC times the estimated average number of hours required for maintenance and repair over the expected life of the equipment. Although the Notice proposed allowing subscribers who purchase on time from the operator to change their mind and discontinue their monthly payments when competitive offerings become available, we believe that current information on the competitive marketplace for equipment is insufficient to justify imposing this condition upon operators.[723] Moreover, customers who purchase equipment must accept the risk of a cable system upgrade that might make their equipment incompatible with the new cable system technology. However, the operator must provide notice of these risks at the time of sale and notice of any pending changes that would make the equipment incompatible.

(d) Promotions

299. The statute is silent on the issue of promotional offerings for equipment and installation. The Notice observed that many operators charge less than actual costs for service installation as part of their marketing efforts. The Notice asked whether the Act's actual cost standard for equipment and installation reflects a legislative intent to prohibit such promotional offerings. We further asked whether it would be consistent with Congressional intent to permit promotional offerings to continue because they increase service penetration, thereby permitting operators to realize economies of scale that could reduce overall costs of providing cable services to subscribers.[724]

ii. Comments.

300. Virtually all commenters agree that Congress did not intend to prohibit promotional offerings.[725] Many commenters describe the consumer benefits from promotional offerings and the

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[723] See para. 282, supra discussing the Commission's rulemaking proceeding concerning equipment compatibility.

[724] Notice, 8 FCC Rcd at 527.

[725] See, e.g., AdelphiaII Comments at 76; TimeWarner Comments at 129; Carib Comments at 12-13; NATOA Comments at 50; CFA Comments at 133; Discovery Comments at 15; but see Multiplex Comments at 12 (Commission should not allow promotional offerings because they would be underwritten by the cable company's monopoly operation and used to suppress competition); SDA Comments at 12.

importance of expanding the customer base through promotions.[726] NCTA argues that the purpose of actual cost requirements was to protect basic subscribers from high charges for equipment and installation, rather than to protect competitive suppliers from predatory rates that are too low.[727] Parties to this proceeding, however, disagree over possible limitations on the recovery of the costs of promotional offerings. Several cable operators propose a basket or pool approach to the regulation of equipment and installation. That method would allow operators to recover the costs of promotional offerings from other equipment, installations, or additional outlets as long as the entire equipment basket recovered only its actual costs.[728] Other operators suggest allowing cable companies to recover the costs of promotional offerings through cable programming services rates.[729] Local authorities and consumer groups would limit an operator's ability to recover the cost of promotions. CFA and NATOA assert that promotional offering are acceptable only if operators absorb the cost of promotions from the reasonable profit they are permitted under the Act.[730] Similarly, Minn contends that the cost of promotional offerings should not be charged back as a loss or overhead cost applicable to the basic rates of other subscribers.[731] CFA further suggests that the Commission should monitor promotional pricing and reevaluate the issue if promotions interfere with the development of competition in the equipment and installation markets.[732]

iii. Discussion

301. The Commission agrees with commenters that Congress did not intend to prohibit promotional offerings. As the Notice and many parties discussed, promotional offerings help to increase subscribership that may permit the operator to

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[726] Armstrong Comments at 23; CATA Comments at 34; CIC Comments at 39; Cox Comments at 35; InterMedia Comments at 24; NCTA Comments at 52.

[727] NCTA Comments at 52; see also Discovery Comments at 16.

[728] AdelphiaII Comments at 82-83; Blade Comments at 13; Falcon Comments at 47-48; Nashoba Comments at 81-82; NCTA Comments at 53-54; TimeWarner Comments at 65.

[729] CIC Comments at 39 and n. 45; Cox Comments at 35 and n. 33.

[730] CFA Comments at 134; NATOA Reply Comments at 30, n. 64.

[731] Minn Comments at 15.

[732] CFA Comments at 135.

increase its overall revenue by increasing volume and its net revenue by realizing certain economies of scale. Accordingly, cable operators will be afforded substantial discretion to offer promotions, including a below cost offering of some equipment and installations.[733] However, while the statute does not preclude promotional offerings, neither does it envision that all equipment and installations can be offered at a below cost basis. We believe that the broad intent of Congress to protect consumers will be best served by an implementation of Equipment Basket rate regulation that affords subscribers a reasonable range of service options. Therefore, instead of allowing cable operators unlimited discretion to price all equipment and installation below cost, we will additionally require that below cost offerings be reasonable in scope in relation to the operator's overall offerings in the Equipment Basket.[734] This will afford operators the initial discretion to fashion the mix of promotional and actual cost offerings of equipment and installation, while permitting evaluation by regulators of the operator's overall Equipment Basket offerings to assure that they best serve the interests of subscribers.

302. In addition, certain limits on cable operator discretion to recover their costs should be imposed. If we accept the basket or pool proposal proffered by NCTA and individual operators, an operator would have the ability to recover all the cost of promotional offerings by increasing the price of one type of equipment, such as remotes. As discussed above, Congress expressed particular concern over the monthly rates charged for leased remotes. We think that Congress intended the actual cost standard for equipment and installations to prevent this type of pricing. Under a general cost-of-service showing we will allow costs of promotions to be recovered as general system overhead. Therefore, under our rules, cable operators cannot include costs of promotions as part of equipment charges.[735] We believe that below cost pricing for equipment and

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[733] As discussed, charges for equipment must be unbundled from basic service charges. This includes charges for equipment and installation offered on a promotional basis.

[734] These offerings must not violate any other regulations imposed upon cable operators. See, e.g., Report and Order, MM Docket No. 92-262, Implementation of Section 3 of the Cable Television Consumer Protection and Competition Act of 1992, Buy-Through Prohibition, FCC 93-143 (released April 1, 1993) (limiting to a reasonable length any discounts or special pricing to encourage nonsubscribers to become cable subscribers).

[735] The cost of a promotion is the difference between a charge based on our prescribed actual cost methodology and the promotional charge.

installation does not violate the actual cost standard incorporated in the Act as long as our regulations ensure that an operator does not charge other customers equipment or installation rates that would exceed our actual cost guidelines, and the total revenues for equipment and installation do not exceed actual costs.[736] In addition, the Commission recognizes that promotional offerings may interfere with the development of a competitive market.[737] We will review this treatment of promotional offerings as we address the issue of whether we should take steps to promote a competitive market for equipment.[738]

(e) Additional Connections

i. Background.

303. Section 623(b)(3)(B) of the Cable Act of 1992 specifically directs the Commission to establish, on the basis of actual cost, rates for installation and monthly use of connections for additional television receivers. The Notice tentatively concluded that cable operators should base the rates for installation of connections for additional receivers on the same costs associated with other installations. Thus, if additional connections are installed at the same time a subscriber's initial service is installed, cable operators would be limited to recovering the incremental costs of the additional installation. In addition, we requested comment on the costs associated with providing connections for additional television receivers and tentatively concluded that the cost of cabling used for additional connections should be recovered in the same manner as the costs of other equipment. We specifically requested comment on any costs associated with technical requirements, such

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[736] Under our rules, the cable operator must include the costs of all equipment and installations in the Equipment Basket. However, instead of recovering all such costs through our actual cost methodology, the operator may elect as a promotion to reduce charges for some of this equipment and installation. Because rates for cable service will be limited by benchmarks at levels not set to recover Equipment Basket costs, operators will not be able to increase rates for cable service to permit a recovery of those promotional costs, unless the cable operator can justify higher rates based on a cost-of-service showing. Thus, the Equipment Basket and our framework for regulation of equipment rates and service rates will serve as a cap on total equipment charges based on actual costs.

[737] See Multiplex Comments at 12; SDA Comments at 12.

[738] See Notice of Inquiry, ET Docket No. 93-7, supra n. 669.

as boosting a signal, involved in providing additional connections.[739]

ii. Comments.

304. Commenters disagree over the extent to which Section 623(b)(3)(B) of the Act governs rates for the provision of additional connections. Some operators claim that this provision covers service installation and equipment used with additional connections, but not the service or programming component of additional outlets. The type of regulation of the service component depends on the level of service being provided, they argue.[740] Other parties contend that operators should not charge for the programming services received over additional connections, because these programming costs are recovered in the charge for cable service at the primary receiver.[741]

305. Many operators argue that additional connections entail added costs, such as capital expenditure required to engineer the system to be capable of serving multiple sets in a home, extra power and plant costs needed to deliver adequate signal to additional outlets, additional repair and maintenance service.[742] Simmons estimates it costs an extra $1050 per mile

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[739] Notice, 8 FCC Rcd at 527.

[740] AdelphiaII Comments at 79-80; CSC Comments at 4; Falcon Comments at 45-46; Nashoba Comments at 78-79; Newhouse Comments at 27-28; Simmons Comments at 1 (those systems that offer the option of having only basic service on additional outlets should be allowed to charge the actual cost of the outlet to basic subscribers. Such systems should be able to make an additional charge for the cable programming service and premium television services provided on the same additional outlet); TimeWarner Comments at 62-63; see also SSO Comments at 17 (only the additional wiring required for reception of basic service on an additional outlet should be rate regulated on an actual cost basis. The other equipment associated with additional outlets, such as these converter boxes and remotes which are not necessary for the reception of basic service, should be "regulated as luxury items.")

[741] Multiplex Comments at 13; NATOA Comments at 50-51; SquareD Comments at 12; see also CalCities Comments at 19-20; Palm Comments at 17-18; Pappas Comments at 1.

[742] See Armstrong Comments at 25; Carib Comments at 14; Continental Comments at 37; InterMedia Comments at 26; Lenfest Comments at 8; Simmons Comments at 2. Because additional costs are related to extra trouble calls, more wiring and consumer equipment, and higher failure rates, operators suggest inside wiring

because of the additional signal power level required for additional outlets.[743] Armstrong and InterMedia assert that an operator should not be prohibited from folding the actual cost of additional outlets into basic service and offering whole house service without a direct charge for additional outlets.[744] On the other hand, Lenfest claims the Commission should adhere to its policy of unbundling, and require customers with additional outlets to bear the costs of providing and maintaining such service to their homes.[745] Some operators offer the same cost methodology for installation of additional connections as they propose for installation of other equipment.[746]

iii. Discussion

306. Commenters generally agree that Congress intended Section 623(b)(3) to cover the installation of, and equipment used with, additional connections. Therefore, the costs associated with additional connections will be included in the Equipment Basket. To simplify our regulation, we believe that operators should recover the costs of additional connections in the related equipment and installation charges. Thus, the installation costs would be recovered as an installation charge, as will the costs of remotes and other equipment. The installation charge for additional connections would be the HSC times the person hours of the visit or HSC times the average hours spent per visit. If the operator elects to use an average installation time, we would expect two rates: one for wiring additional connections at the time of installation and another if the operator makes a separate visit to install the additional connection. In either case, we anticipate a much smaller charge for installing additional outlets at the same time initial service installation occurs than for installations which require a separate visit to the subscriber's home. Remotes, converter

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maintenance agreements may be a better alternative to separate monthly charges for additional outlets. Armstrong Comments at 25; InterMedia Comments at 26.

[743] This includes the capital expenditure (including financing), the actual cost of wiring in the customers home, the additional cost of CLI compliance, the additional cost of service calls required to maintain the additional outlets, and a reasonable profit. Simmons Comments at 2.

[744] Armstrong Comments at 25; InterMedia Comments at 26.

[745] Lenfest Comments at 8.

[746] AdelphiaII Comments at 79; Falcon Comments at 45-46; Nashoba Comments at 78; Newhouse Comments at 27-28; TimeWarner Comments at 62.

boxes and other equipment involved would be leased to the customer at the same rate as equipment used with primary outlets.

307. The remaining issue is whether our guidelines should allow operators to charge for any other costs or services relating to additional connections. We disagree with commenters who argue that Section 623(b)(3) does not address the programming portion of additional connections. The statute specifically covers the "monthly use" of additional connections. These connections are used to receive programming. Thus, if an operator incurs additional charges for programming carried on basic or cable programming channels that it transmits to additional outlets, those charges would be properly recovered through a monthly charge levied for additional outlets in fact receiving that programming.[747] That monthly charge would be limited to the operator's additional programing costs. We recognize that there are costs associated with designing and building a cable system that can provide a signal strong enough to serve more than one outlet in a home. Any network costs for boosting the signal should be treated as part of general system overhead. If a subscriber requests additional connections that exceed network design capabilities and require additional customer premises equipment, the cable operator may recover the costs of the additional equipment through an additional connection charge. That charge would be developed using our actual cost guidelines for other customer equipment. An additional connection charge is permissible only to recover

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[747] We do not believe that the statute precludes cable operators from establishing reasonable categories of cable service customers with reasonable restrictions on the number of additional connections that may be obtained with each primary service outlet. While we believe that Congress intended that residential customers will generally be able to obtain the additional connections they need with one primary service outlet charge, we conclude that the statute does not prevent cable operators from establishing reasonable limits on the number of additional connections for each primary outlet in commercial or residential installations other than single family installations. Cable operators are thus permitted to establish reasonable multiple primary service charges, including reasonable discounted primary service charges, in non-commercial installations and residential installations other than single family installations. Single family installations would include residential units within a multifamily dwelling. Under the procedures we are establishing for the basic service tier, local franchise authorities will be able to review the operator's establishment of service categories along with other aspects of the operator's basic service tier offering. See also our discussion of geographically uniform rate structure and discrimination at Sections II.A.5, infra.

additional programming costs, if any, and the costs of additional customer premises equipment needed to boost the operator's signal.

(4) Costs of Franchise Requirements

i. Background

308. The Cable Act of 1992 requires that our rate regulations for the basic service tier include standards to identify costs that are attributable to satisfying franchise requirements to support public, educational and governmental channels, to the use of such channels or to any other services required under franchise.[748] The Notice tentatively concluded "that the purpose of this statutory requirement is to assure the establishment of standards that will permit the cable operator to identify on subscriber bills pursuant to Section 622(c)(2) the amount of the bill attributable to franchise requirements."[749] We also tentatively concluded that the costs attributable to satisfying franchise requirements should include:

> 1) any direct costs of providing any services required under the franchise; 2) the sum of per channel costs for the number of channels used to meet franchise requirements for public, educational, and governmental channels; and 3) a reasonable allocation of overhead.[750]

309. The Notice presented two proposals for determining the amount that could be reported on the franchise costs line of a subscriber's bill. Under the first alternative we would adopt, at least in part, a cost-based regulatory alternative, with the per channel costs and allocation of overhead, for purposes of implementing Section 622(c)(2) of the Communications Act, being determined in accordance with the proposed accounting and cost allocation rules set forth in Appendix A of the Notice.[751] In the alternative, if we decided not to adopt the accounting and cost allocation rules set forth in Appendix A, we proposed to require cable systems to use "reasonable methods to determine per channel costs and

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[748] Notice, 8 FCC Rcd at 527, para. 72 citing Communications Act § 623(b)(4), 47 U.S.C. § 543(b)(4).

[749] Notice, 8 FCC Rcd at 527, para. 73.

[750] Notice, 8 FCC Rcd at 527, para. 73.

[751] Notice, 8 FCC Rcd at 527, para. 73.

allocations of overhead."[752] We solicited comment on both of these proposals.

ii. Comments

310. Several municipalities state that cost of franchise requirements should include a reasonable allocation of overhead that is directly attributable to public, educational and governmental channels.[753] Most commenting municipalities maintain the position that cost of franchise requirements should be limited to direct costs directly required by the franchise.[754] These parties advocate differing methods on how to achieve this result. Minn argues that if any allocation is to be made for the costs of public, educational and governmental channels, the cable operator must show that absent the allocation for public, educational and governmental channels, the channel would have been used for a commercial purpose.[755] Minn disagrees with the Commission's tentative conclusion that cost of franchise requirements should include a sum for per channel costs for the number of channels used to meet franchise PEG requirements.[756] Minn further asserts that a cable operator should not be allowed to claim costs for public, educational and governmental channels unless the Commission's regulatory scheme also reflects benefits

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[752] Notice, 8 FCC Rcd at 527, para. 73.

[753] See, e.g., Minn Comments at 16; and Lakeville Reply Comments at 5.

[754] See, e.g., Austin Comments at 56; Minn Comments at 15; NATOA Comments at 53; Lake Forest Reply Comments at 4; Liberal Reply Comments at 5-6; Lincoln Reply Comments at 4-5; Louisville Reply Comments at 3-4; Madison Reply Comments at 3-4; Mankato Reply Comments at 4-5; Marshall Reply Comments at 3-4; Mentor Reply Comments at 4; MACC Reply Comments at 4-5; Dade Reply Comments at 9; Mt. Prospect Reply Comments at 4-5; Multnomah Reply Comments at 4-5; Niles Reply Comments at 4; Oakland Reply Comments at 4; Ottawa Reply Comments at 2; Owensboro Reply Comments at 4-5; Palm Desert Reply Comments at 4-5; Phillipsburg Reply Comments at 4-5; Piscataway Reply Comments at 4-5; Prince George Reply Comments at 5-6; Ramsey Reply Comments at 4-5; Reidsville Reply Comments at 4-5; Salina Comments at 4-5; San Antonio Reply Comments at 5; Tallahassee Reply Comments at 4; Titusville Reply Comments at 4-5; Union Reply Comments at 4-5; and Worthington Reply Comments at 5.

[755] Minn Comments at 16.

[756] Minn Comments at 16.

received from commercial cable television, such as advertising revenues.[757]

311. Several municipalities assert that the identification of costs related to a franchise should be reviewed in the regulatory process governing basic rates.[758] These same municipalities are concerned about consumers being billed twice for cost of franchise requirements.[759] They note that the Cable Act of 1984 provided that franchise fees that were already incorporated in the rates were not to be added to the subscriber's bill, while an increase in the franchise fee could be added.[760] These parties recommend that the Commission look to Section 622(c) of the Cable Act of 1984 for guidance on this issue.[761]

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[757] Minn Comments at 16.

[758] See, e.g., Atlanta Reply Comments at 4; Fairborn Reply Comments at 4; Georgetown Reply Comments at 4; Greensboro Reply Comments at 4; Greenville Reply Comments at 5; Henderson Reply Comments at 4; IowaCity Reply Comments at 4; Kinston Reply Comments at 4; Laurens Reply Comments at 4; Laurinberg Reply Comments at 4; Owensboro Reply Comments at 4; Piscataway Reply Comments at 4; Reidsville Reply Comments at 4; Titusville Reply Comments at 4; Union Reply Comments at 4; Worthington Reply Comments at 5.

[759] See, e.g., Atlanta Reply Comments at 4; Fairborn Reply Comments at 4; Georgetown Reply Comments at 4-5; Greensboro Reply Comments at 4; Greenville Reply Comments at 5; Henderson Reply Comments at 5; IowaCity Reply Comments at 4; Kinston Reply Comments at 4; Laurens Reply Comments at 4-5; Laurinberg Reply Comments at 4; Owensboro Reply Comments at 5; Piscataway Reply Comments at 4-5; Reidsville Reply Comments at 4-5; Titusville Reply Comments at 4-5; Union Reply Comments at 4-5; and NATOA Comments at 51-52.

[760] See, e.g. Atlanta Reply Comments at 5; Fairborn Reply Comments at 6; Georgetown Reply Comments at 5; Greensboro Reply Comments at 5; Greenville Reply Comments at 5; Henderson Reply Comments at 5; IowaCity Reply Comments at 5; Kinston Reply Comments at 5; Laurens Reply Comments at 5; Laurinberg Reply Comments at 5; Owensboro Reply Comments at 5; Piscataway Reply Comments at 5; Reidsville Reply Comments at 5; Titusville Reply Comments at 5; Union Reply Comments at 5; Worthington Reply Comments at 5.

[761] See, e.g. Atlanta Reply Comments at 5; Fairborn Reply Comments at 6; Georgetown Reply Comments at 5; Greensboro Reply Comments at 5; Greenville Reply Comments at 5; Henderson Reply Comments at 5; IowaCity Reply Comments at 5; Kinston Reply Comments at 5; Laurens Reply Comments at 5; Laurinberg Reply Comments at 5; Owensboro Reply Comments at 5; Piscataway Reply Comments at 5; Reidsville Reply Comments at 5; Titusville Reply Comments at 5;

312. AdelphiaII contradicts the assertion that the only costs that are addressed in Section 623(b)(4) of the Communications Act are those costs that are attributable to public, educational and governmental channel franchise requirements, which excludes costs attributable to franchise requirements in general.[762] AdelphiaII further alleges that the statutory language is clear and the Commission is to prescribe regulations that 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."[763]

313. For the most part, cable operators maintain that costs attributable to franchise requirements must include local origination, I-Nets and other municipal costs.[764] Several cable operators also feel that access costs should include capital, personnel and other related operating expenses.[765] Other cable operators argue that copyright fees should also be included as a cost of franchise requirement.[766]

314. Cable operators argue against the Commission adopting its proposed cost allocation and uniform accounting standards to identify costs and revenues, because they are too complex and burdensome.[767] Instead, these parties suggest, the Commission should rely on good faith allocation by cable operators, consistent with generally accepted accounting principles.[768]

iii. Discussion

Union Reply Comments at 5; Worthington Reply Comments at 5.

[762] AdelphiaII Reply Comments at 45.

[763] AdelphiaII Reply Comments at 45-46, quoting Communications Act § 543(h)(4), 47 U.S.C. § 623(b)(4).

[764] See, e.g., Continental Comments at 41; New England Reply Comments at 9-10; and Cole Comments at 32.

[765] See, e.g., Continental Comments at 41; and Cole Comments at 32-33.

[766] See, e.g., New England Reply Comments at 10.

[767] See, e.g., Nashoba Comments at 87; AdelphiaII Comments at 88; and Falcon Comments at 52.

[768] See, e.g., Nashoba Comments at 87; AdelphiaII Comments at 88; and Falcon Comments at 52.

315. We believe that we should adopt a standard for identification of costs attributable to franchise requirements that accurately reflects such costs without unduly burdening cable operators. Such costs should include any direct costs and per channel costs. We believe that overhead costs should be included because overhead costs are necessarily incurred in addition to indirect costs in satisfying franchise requirements. Further, the costs of franchise requirements can be determined in accordance with the general cost accounting rules we are adopting for implementation of other portions of the Cable Act of 1992. Thus, identification of the costs attributable to franchising requirements in accordance with these rules should not be unduly burdensome. Accordingly, we are adopting the proposal in the Notice that the costs attributable to satisfying franchise requirements shall include:

> 1) the sum of per channel costs for the number of channels used to meet franchise requirements for public, educational, and governmental channels; 2) any direct costs of providing any other services required under the franchise; and 3) a reasonable allocation of overhead.[769]

(5) Customer Changes

i. Background.

316. The Cable Act of 1992 requires that regulations for the basic tier include standards and procedures to prevent unreasonable charges for a customer changing equipment or service tiers. Charges for changing the service tier must be based on cost.[770] The Notice tentatively concluded that regulations adopted to implement Section 623(b)(5)(C) should apply to any changes in the number of service tiers that are initiated at the subscriber's request after installation of initial service.[771] Consistent with the language of the Act, we proposed to require that charges for changing service tiers not exceed a nominal amount "when the system's configuration permits changes in service tier selection to be effected solely by coded entry on a computer terminal or by other similarly simple method."[772] We

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[769] Notice, 8 FCC Rcd at 527, para. 73.

[770] Communications Act § 623(b)(5)(C), 47 U.S.C. § 543(b)(5)(C).

[771] Notice, 8 FCC Rcd at 527.

[772] Notice, 8 FCC Rcd at 527-28 citing Communications Act, § 623(b)(5)(C), 47 U.S.C. § 543(b)(5)(C).

requested comment on whether and, if so, at what level we should set the nominal amount when this condition is met.

317. For changes in service tiers at the subscriber's request, not made by coded entry and other simple methods, the Notice sought comment on two alternative proposals. Under the first proposal, we would require that charges be based on the actual costs of making service tier changes, including any direct costs and a reasonable allocation of indirect costs and overhead and a reasonable profit. Under the second alternative, we would require charges for all changes in service tiers to recover only nominal costs.[773] The Commission solicited comment on whether Congress intended for Section 623(b)(5) to apply to changes in equipment generally or only to changes in equipment associated with changes in service tiers. The Commission also solicited comment on applying our proposed alternatives to define reasonable charges for changing equipment, and whether Congress intended for cable operators to make a reasonable profit on changes in equipment. Finally, the Notice requested comment on whether the implementation of this rulemaking could encourage customers to change service tiers and whether costs associated with initial retiering should be treated in a different manner from subsequent customer changes in service.[774]

ii. Comments

318. Many commenters discuss whether the Commission should in some way limit the scope of regulations implementing Section 623(b)(5)(C) of the Cable Act. Several operators urge the Commission to limit its rules for service changes to those that affect basic service.[775] Other parties argue that the regulations should apply to any changes in the level of service

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[773] Notice, 8 FCC Rcd at 528. We noted that the latter alternative could help keep charges for changes in service tiers low, but could increase burdens and costs on cable operators for this activity by encouraging subscribers to order service changes more frequently. In addition, it would require that the costs of customer changes be recovered from other services. Id.

[774] Notice, 8 FCC Rcd at 528.

[775] CIC Comments at 39-40; Cox Comments at 36; see also TCI Comments at 40 (charges assessed for changes to or from basic tier or changes by customers receiving cable programming services must be based on the cost of such change); TimeWarner Comments at 66 (cable programming services should be regulated under an unreasonable standard outside of Section 623(b)(5)(C) of the Communications Act and charges for changes between and among expanded tiers and premium programming should be free of regulation).