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Before the
FEDERAL COMMUNICATIONS COMMISSION
Washington, DC 20554

In the Matter of	)	
	)	
Implementation of Sections of the	)	MM Docket No. 92-266
Cable Television Consumer Protection	)	
Act of 1992: Rate Regulation	)	

COMMENTS OF GTE

GTE Service Corporation, on behalf of its affiliated domestic telephone companies (GTE), respectfully submits these Comments in response to the Second Order on Reconsideration, Fourth Report and Order, and Fifth Notice of Proposed Rulemaking in MM Docket 92-266, Implementation of the Rate Regulation Provisions of the Cable Act of 1992, FCC 94-38, released March 30, 1994 (Fifth NPRM). GTE herewith responds to paragraph 256 of the Fifth NPRM.

I. INTRODUCTION

In the Docket 92-266 proceeding, the Commission adopted a regulatory framework to establish initial price levels and govern future rate adjustments of cable systems that are not subject to effective competition.[1] The principal elements of the Commission's cable rate regulation plan include a benchmark procedure to set initial rates and a price cap "going-forward" methodology to regulate future price adjustments

1 *See* 47 U.S.C. § 543(l)(1).

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resulting from channel additions or deletions or system upgrades and to adjust rates to reflect changes in inflation as measured by the GNP-PI.[2]

The Fifth NPRM requests comment on how the going-forward methodology should be modified to provide lesser or greater compensation to operators for adjustments to capped rates when channels are added to or deleted from regulated tiers. (Fifth NPRM, at ¶ 256.) The Commission also seeks comment on whether and how the benchmark methodology should apply to systems with more than 100 channels (Id.)

II. ADJUSTMENTS TO BOTH LEC AND CABLE PRICE CAP PLANS MUST BE MADE TO ACHIEVE REGULATORY SYMMETRY

The rapid growth of technology has made it possible for information of all types to be carried on most of the transmission media deployed today. These advances have enabled a wide variety of firms to enter interstate telecommunications market in recent years. Strategic alliances and mergers among telecommunications firms are taking place at a rapid rate, allowing these companies to capitalize on each firm's respective strengths. The result is a convergence of the previously separate telephone, cable, wireless, computer and information services industries.[3] Competition between the telephone and cable industries will intensify over the next few years as LECs begin to offer video programming distribution and cable operators seek entry into the local

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[2] These rules were established in the Commission's Report and Order and Further Notice of Proposed Rulemaking, MM Dkt. 92-266, released May 3, 1993 (*Rate Order*).

[3] For a listing of these alliances, *see* GTE's Comments, Attachment B, May 9, 1994, in *Price Cap Performance Review for Local Exchange Carriers*, CC Dkt. 94-1 (*LEC Price Cap Review*).

exchange markets. Potential entrants into LEC service markets are for the most part are large well-established firms that are well equipped to compete directly with the LECs. Given the dynamic convergence of the voice and video industries, the Commission can no longer avoid establishing rate regulations for one industry segment without considering the impact of its decisions on the others. The Commission must act now to eliminate regulatory asymmetries that inhibit competition and, in doing so, deny consumers the ability to select from a complete range of video service providers.

During this decade, the Commission has adopted as its primary regulatory tool incentive regulation plans which have proven to have achieved substantial benefits for consumers.[4] Under price cap regulation, the telephone industry has experienced an explosive growth of new technologies, services and price options. Logically, in the Docket 92-266 proceedings, the Commission once again turned to the price cap model as being the most effective alternative to traditional cost of service regulation to in order to fulfill its statutory obligation to regulate monopoly cable rates.[5]

In general, cable rates may be adjusted annually for changes in inflation (as measured by the GNP-PI index). This is done by first removing "external costs" from the rate for the tier and applying the GNP-PI factor to the residual. When new channels are added or deleted, the rate change is based on the current per channel price less current programming costs, adjusted for the proportional change in the benchmark rate (rates of competitive systems) for comparable size systems. New programming costs

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[4] *See Price Cap Performance Review for Local Exchange Carriers*, Notice of Proposed Rulemaking, CC Dkt. 94-1, FCC 94-10, released February 16, 1994, at ¶¶ 25-30; *Price Cap Performance Review for AT&T*, Notice of Inquiry, CC Dkt. 92-134, FCC 92-257, released July 17, 1992, at ¶ 13.

[5] *Rate Order*, at ¶ 228.

are then added to this "adjusted residual" rate in addition to a 7.5% mark-up on the programming costs for systems with 100 regulated channels or less. The Commission's rules do not address adjustments for systems over 100 channels.

Although the "going forward" methodology reflects some aspects of a "cost-plus" approach, in that it allows the flow-through of new programming costs, the Commission has generally adhered to a price cap methodology to regulate non-competitive cable rates. The Commission has a unique opportunity in this docket as well as in the LEC Price Cap Review proceeding to adopt symmetrical treatment for both LECs and cable operators.

GTE strongly urges the Commission to make several crucial changes in its regulatory policies to achieve this result. First, any adjustment to LEC or cable price cap plans must accommodate the increasing competition between the two industries. Once alternative video distribution services are present in a cable operator's market, it no longer is subject to any rate regulation, either from the local franchise authority or the Commission.[6] Just as important, LECs should be afforded the flexibility to meet competition as soon as competition is permitted. In its Comments in the LEC Price Cap Review proceeding, GTE has advocated the adoption of regulations which would allow greater pricing flexibility consistent with the level of competition present in the LEC serving area.[7] These recommendations should be expeditiously adopted by the Commission.

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[6] 47 U.S.C. § 543(a)(2).

[7] *Price Cap Performance Review for Local Exchange Carriers*, CC Dkt. 94-1, GTE's Comments, May 9, 1994, at 41.

Second, the price cap plans of the two industries should be de-coupled from traditional cost of service and rate of return methodologies. For cable operators, the Commission should affirm its earlier findings that the price cap/benchmark approach is the primary tool to govern regulated cable rates and that cost of service showings may only be used as a back-stop/last resort method to set initial rates. Once initial cable rates are set according to the benchmark or cost of service showing, future changes in cable rates are governed by the change in the GNP-PI factor, with no adjustment for earnings levels. The Commission should provide LECs with the same incentives to increase efficiency and retain higher earnings resulting from enhanced operations as allowed for cable. For LECs, eliminating the sharing mechanism and the regulation of depreciation rates would align the LEC price cap plan with the "competitive benchmark" approach of cable rate regulation.

Third, the Commission should adopt consistent policies relative to the use of a productivity factor for both industries. In recent months, Chairman Hundt has expressed his personal view that there may be no need for a productivity offset for cable operators.[8] In contrast, the Commission's LEC Price Cap Review notice asks for comments on the need to potentially increase the productivity factor of LECs to reflect higher average earnings achieved under price caps and declining interest rates. Maintaining no productivity factor for the cable industry while adjusting the LEC's productivity adjustment upward would indeed represent an odious disparity in Commission regulation. Increasingly efficient capital inputs in the form of advanced communications equipment such as compression technology, digital switches, and fiber

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8 Remarks of Hon. Reed E. Hundt at the National Cable Television Association Convention, New Orleans, LA, May 24, 1994.

optic technology provide opportunities for cable firms to realize substantial productivity gains over the next few years. Clearly, cable operators will achieve productivity levels that exceed those of the economy as a whole. LECs, on the other hand, have already deployed substantial fiber optic cable and advanced switching technology in their networks, precluding the ability to realize additional productivity gains from these technologies. Therefore, retaining no productivity offset for cable while increasing the factor for LECs makes no sense. GTE maintains that if the Commission retains a "0" productivity factor for cable, it should eliminate, or substantially reduce, the productivity factor for the LECs.

The price cap plan for LECs should also be improved to remove barriers that limit efficiency gains such as sharing and depreciation prescription and allow for greater pricing flexibility. Indeed, the dictates of a competitive marketplace require that the price cap rules which govern incumbents also be applied to potential competitors. Consequently, it is imperative that the Commission's evolving regulation of cable operators, as well as LECs, achieve consistency.

III. RATES FOR SYSTEMS IN EXCESS OF 100 CHANNELS SHOULD BE ESTABLISHED ACCORDING TO PRICE CAP PRINCIPLES

The Fifth NPRM requests comments on what regulations are needed to set rates for the addition of new channels for those systems in excess of 100 channels. (Fifth NPRM, at ¶ 256.) GTE advocates the use of price cap principles to govern the regulations for channels exceeding the 100 channel threshold. The Commissions's recommendation that channel rates be capped at 100 until a operator submits a cost of service showing is contrary to the price cap approach and effectively ties rates back to a rate of return/cost of service approach. This would provide cable operators with little incentive to deploy advanced technology and add new programming.

GTE believes that the advent of compression technology will play a significant role in altering cable offerings to consumers. Specifically, compression technology is expected to permit cable operators to increase channel capacity dramatically.[9] Compression will enable file servers to store movies and other programming for instant availability by customers. Continued improvements in compression and larger, lower cost storage devices will also enhance on-demand capability. Compression will play a large role in making far more programming available to the public.

It is likely that competitive alternatives to entrenched cable operators with system capacities in excess of 100 channels will develop in major markets in the next few years. While establishing rates under benchmark approach would be ideal, competitive benchmark rates for cable systems of that size generally do not exist in the market today. Therefore, the Commission should adopt a more flexible pricing approach, similar to that extended to the pricing of new LEC services. Rather than establishing additional costs of service regulations or complex rules for systems in excess of 100 channels, GTE urges the Commission to allow cable operators to submit rates for new channels based on the long run incremental cost (LRIC) of achieving channel capacity of that size. Operators should be allowed to price in order to cover the direct cost of providing a new channel service plus the allocation of reasonable joint and common costs. This approach, while allowing the operator to recover its costs, would be consistent with the manner in which LECs price new services.

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[9] Compression will also enable LEC video dialtone (VDT) platforms to meet channel capacity requirements as demand from multiple programmer/packagers increases.

IV. CONCLUSION.

For the reasons stated hereinabove, GTE respectfully urges that Commission (1) to adopt consistent policies for cable and LECs price cap regulation on a "going forward" basis, and (2) to permit cable operators to submit rates for new channels based on the long run incremental cost for systems over 100 channels.

Respectfully submitted,

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Certificate of Service

I, Ann D. Berkowitz, hereby certify that copies of the foregoing "Comments of GTE" have been mailed by first class United States mail, postage prepaid, on the 29th day of June, 1994 to all parties of record.

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