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July 11, 1994

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FEDERAL COMMUNICATIONS COMMISSION
OFFICE OF SECRETARY

EX PARTE

Hand Delivery

William F. Caton, Secretary
Federal Communications Commission
1919 M Street, NW
Washington, D.C. 20554

Re: **Ex Parte Presentation in MM Docket 92-266**

Dear Mr. Caton:

Submitted herewith, on behalf of Continental Cablevision and pursuant to 47 C.F.R. §1.1206, are an original and two copies of written ex parte comments to be included in the above referenced docket.

Should there be any questions concerning these comments, please contact the undersigned.

Sincerely,

James F. Ireland

James F. Ireland

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BEFORE THE
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FEDERAL COMMUNICATIONS COMMISSION
OFFICE OF SECRETARY

In the Matter of	)	
	)	
Implementation of Sections of the Cable Television Consumer Protection and Competition Act of 1992:	)	MM Docket No. 92-266
	)	
Leased Access	)	

EX PARTE COMMENTS

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July 11, 1994

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SUMMARY

Continental Cablevision ("Continental") submits these ex parte comments concerning the pending reconsideration of the leased access rules. As explained in the comments, the current leased access record is inadequate for the Commission to establish rules that both comport with Congressional intent for leased access and the "going-forward" rules that are currently under consideration by the FCC. Moreover, the Supreme Court's recent decision, *Turner Broadcasting System, Inc. v. Federal Communications Commission*, 62 U.S.L.W. 4647 (June 27, 1994), establishes a new First Amendment standard that the present record does not satisfy.

For example, the present record does not address the heavy use by local, non-profit programmers of cable operators' local origination and public access channels. The Commission should not be mislead into believing that access is unavailable to such programmers when operators like Continental routinely provide *free access*. Similarly, the record does not address the impact of leased access on the fate of the over 120 new programming services currently ready for launch or under development, such as The History Channel and Ovation, that will be unceremoniously denied access to cable systems that have become glutted with additional shopping services that subscribers simply are not interested in.

The present record also does not adequately address the impact on cable systems that more liberal access by the current glut of home shopping channels will have. If current rules are liberalized to ease access by shopping channels all leased access channels will quickly be filled by shopping services. The following shopping services (other than QVC and HSN) are now in existence or near launch: TV-Macy's, ATV, Black Shopping Network, Catalog 1, FYI Q&A, Valuevision, Merchandise Entertainment Television, Product Information Network, Telecompras, Telefashion Net, Via-TV, Video Catalog Channel, Fingerhut and Shop at Home. In addition, there are specialized infomercial programs on several more established networks such as MTV, BET and MOR-Music. Such programming

hurts the growth and development of cable relative to its competitors, and serves as an obstacle to other parties interested in gaining access to cable capacity.

The Commission should reject the suggestion that previously negotiated agreements with lessees reflect a marketplace rate for leased access in today's market. The fact is that agreements negotiated years in the past, in a rate deregulated environment where channel capacity was far less scarce, did not reflect a "market" rate. Certainly such agreements were not negotiated with the expectation that the terms of the agreement would be extended by government fiat beyond the term provided for in the agreement.

The Commission must also act to protect the growing cable advertising business from migration to leased access based upon artificially low rates. Current leased access rates are absurdly low when reduced to an hourly or per minute charge.

The Commission should also clarify that leased access is no longer required once a cable operator is subject to effective competition. None of cables' competitors are subject to leased access requirements, although such competitors have as many or more channels as cable operators who are subject to the requirements. The fact is that, once competition is available, the perceived "bottleneck" that Congress feared is no longer present and there is no longer a need to shackle cable relative to its competition.

The record was inadequate in the leased access proceeding last year when the formal comment process closed. Given the events that have transpired since that date, there is simply no way that the Commission can responsibly or legally craft rules based on the current record. The Commission should adopt a Further Notice of Proposed Rulemaking to harmonize the leased access rules with its "going-forward" rules, and to establish a basis for rules that can survive scrutiny under *Turner*.

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In the Matter of	)	
	)	
Implementation of Sections of the Cable Television Consumer Protection and Competition Act of 1992:	)	MM Docket No. 92-266
	)	
Leased Access	)	

EX PARTE COMMENTS

Continental Cablevision submits these comments in the above captioned docket related to commercial leased access. Continental is currently the nation's third largest operator of cable television systems, serving nearly 3 million subscribers nationwide in 16 states and over 650 communities. The Company participated in the FCC's rulemaking on this issue, and in the reconsideration of the FCC's initial decision. As the Commission itself has recognized, however, commercial leased access rules were adopted as a small part of the broader rate regulation rules during the first 180 days after the effective date of the 1992 Cable Act. As a result, affected parties necessarily focused less attention on this area than on the many other critical issues presented in that rulemaking.

The inadequacy of the original record in this proceeding has been exacerbated by three other factors. First, the Commission has recognized the pivotal importance of the so called "going-forward" rules to the future growth and development of both the programming and cable industries. The Commission is currently engaged in crafting rules that will encourage the development of new programming services, and the creation of adequate incentives for cable operators to add new services, and where necessary, expand capacity to accommodate the addition of new programming services. The revisions to the present leased access rules suggested by certain existing and prospective lessees (in formal comments and in numerous ex parte presentations) will undermine the critical objectives that the going-forward rules could otherwise accomplish.

Second, in light of the Supreme Court's recent decision, *Turner Broadcasting System, Inc. v. Federal Communications Commission*, 62 U.S.L.W. 4647 (June 27, 1994) (*"Turner"*), the Commission must ensure that the record is sufficient to support leased access rules that impinge upon the First Amendment right of cable operators to program their channels. Even assuming that the leased access requirements are content-neutral, and further an important or substantial governmental interest, the existing record is inadequate to satisfy the requirements of *Turner*.

Finally, it appears that there has been a steady stream of ex parte contacts with the Commission since the official reconsideration comment period ended last August. In particular, a review of the ex parte record indicates that existing and prospective lessees have maintained regular contact with the Commission on a variety of leased access issues. Certain of these commenters did not bother to participate in the official comment period yet have subsequently submitted substantive comments urging actions that are far beyond the scope of the FCC's original rulemaking.

Perhaps more troubling is the potential impact from the recent submission of certain leased access complaints by various programmers, including a company known as TeleMiami. The disputes involve bitter local confrontations between individual parties, yet the lessees are urging the Commission to take sweeping actions in areas that have never been open to public comment. Continental has serious concern that the Commission could be unduly swayed in its rulemaking by these localized flare ups that are not representative of the experience of the vast majority of the cable industry.

In an effort to balance the record in this area, Continental recently met with various members of the Commissioners' staffs, as well as members of the Cable Services Bureau, to address matters Continental had raised during the formal comment cycle. In that process, the Bureau Staff requested Continental to submit additional written comments addressing leased access. This submission is made in response to the Staff's request.

I. Statutory and Policy Framework.

In pushing forward in the leased access rulemaking, it is critical for the FCC to consider the broad legal context, as enunciated through Congressional intent. The purpose of the leased access provision is set forth in the statute itself:

> "to promote competition in the delivery of diverse sources of video programming and to assure that the widest possible diversity of information sources are made available to the public from cable systems <u>in a manner consistent with the growth and development of cable systems.</u>" 47 U.S.C. § 532(a). (Emphasis added).

To this end, the law directs the Commission to establish price, terms and conditions for leased access in a manner "at least sufficient to assure that [the leased access arrangement] will not adversely affect the operation, financial condition or market development of the cable system." 47 U.S.C. § 532(c)(1). The legislative history makes it absolutely clear that "[n]othing in these provisions is in any way intended to deprive a cable operator from receiving a **fair profit** from the use of this designated channel capacity." H.R. Rep. No. 98-934, 98th Cong., 2d Sess. 52 (1984) (Emphasis added).

The concern expressed by Congress is not academic. The 1992 Act included not only sweeping rate regulation provisions that would dramatically lower cable operators' revenues, but also reimposed must carry. Thus, a cable operator with 36 activated channels could be required to set aside up to 1/2 of its channel capacity for program services that it has not chosen itself (1/3 of capacity for commercial must carry, up to 3 channels for non-commercial must carry and 10 percent of available channels for leased access). In addition, local PEG access channels, which are standard requirements of practically any renewal franchise, remove typically 1 to 3 additional channels from the operator's control. Of course, these requirements affect cable operators differently in different markets, but the fact remains that the Congress wanted to protect operators from adverse economic consequences of leased access in this precise context.

Moreover, the competitive world in which cable operates is moving at a dramatic pace. In mid-June, Direct TV, a DBS company controlled by a subsidiary of

General Motors initiated service to several markets, and estimates that it will have 10 million subscribers by the end of the decade. The Commission has already authorized the first commercial offering of video dialtone services by a local telephone company. Furthermore, if the US West and C&P court cases are upheld, or if pending legislation in Congress passes, telephone companies will enter directly into the cable business in their own service territories in the near future. These are exceedingly well funded and sophisticated competitors, none of which are required to provide the access channels that cable operators do.

This is the context in which the Commission is currently developing its "going-forward" methodology. As the Commission has recognized, these rules are critical to the continued growth and development of the programming and cable industries.

> In addition, we believe that the cable industry can, and should, continue to grow and provide new and additional services to subscribers. In particular, operators should be given incentives to participate fully in the development of an advanced telecommunications infrastructure. Accordingly, a goal of our "going-forward" methodology is to allow cable operators to grow and develop new facilities and services, including new and innovative regulated programming services.

Second Order on Reconsideration, Fourth Report and Order and Fifth Notice of Proposed Rulemaking, MM Docket No. 92-266 at ¶238, released March 30, 1994.

Continental is greatly concerned that the Commission's leased access rulemaking will work at cross purposes with the going-forward rules now under consideration. There is a severe channel capacity shortage on cable systems throughout the country. If the Commission does not harmonize the goals of the two rulemakings, the policy concerns that the going- forward rules seek to address will be a moot point. Even with the best incentive plan, cable operators will be unable to add any of the more than 120 new programming services under development simply because channel capacity will be occupied by commercial lessees, which more often than not will be shopping services. This result will be bad for cable operators who are unable to deliver exciting new services demanded by subscribers, bad for subscribers that are denied those services, and bad for the programmers who will lose the incentive to produce new programming.

In this context it is imperative that the Commission move carefully, and only with the benefit of a properly developed record that fully takes into account the impact of its actions on cable operators, programmers and subscribers in this new regulatory and competitive environment.

II. The Existing Record Is Distorted By Ex Parte Presentations

As previously noted, since the formal comment period ended last year, numerous parties have made ex parte presentations concerning the leased access rules. These presentations are not subject to the same degree of open criticism and review by other interested parties as in the formal rulemaking process. In some cases, parties who never filed formal comments have submitted substantive written ex parte comments. *See Informal Comments of United Broadcasting Corporation, d/b/a TeleMiami*, filed April 8, 1994. These ex parte contacts, together with certain local confrontations brought to the Commission for resolution by complaint, provide an inaccurate and misleading record upon which the Commission cannot rely in establishing leased access rules. Continental responds below to a number of the issues raised by various ex parte comments.

A. There is no legal basis or policy need for the Commission to establish artificially low rates for shopping channels.

Valuevision International, Inc., a home shopping service **with affiliation agreements with a number of cable operators**, including Continental, has urged a leased access formula for shopping channels that is utterly at odds with the intent of Congress. Valuevision asserts that there is an explicit marketplace price for shopping services that amounts to 5% of the revenues that the service generates from cable system subscribers. Although Valuevision claims to be seeking a "marketplace" rate, in fact the Company misstates the pricing and competitive nature of the home shopping market.

First, the formula urged by Valuevision is extremely misleading, as Continental pointed out in its initial comments. There is no magic marketplace number of 5% of revenues irrespective of what those revenues are. Continental carries QVC and HSN because of the revenue potential that the 5% represents, not because 5% is the uniform home shopping number. Indeed, Continental's contracts (and the industry's generally) are more complex than Valuevision suggests to the Commission. Both QVC and HSN are subject to minimum guaranteed payments, marketing support and other consideration as part of their carriage agreements. Simply fixating on a percentage, rather than the legitimate revenue stream needed to compensate a cable operator for the loss of a channel, would deprive the operator of the "fair profits" the 1984 Act guarantees under a leased access regime.

Moreover, the Commission should be aware of Valuevision's place in the market. Valuevision and Continental recently executed an affiliation agreement in the free marketplace covering nearly 1 million Continental subscribers (1/3 of the Company's subscribers), and Valuevision has other MSO affiliate agreements as well. It is unclear why Valuevision is even the type of entity that should be eligible for leased access space when it can negotiate for channels in the same way that other commercially viable programmers must do. Commission intervention lowering access rates for home shopping services will interfere with free market transactions such as the Continental/Valuevision agreement.

Valuevision would have the FCC believe that it is a struggling David against a monolithic goliath cable industry. However, most cable systems in the country are not affiliated with QVC and HSN as Valuevision suggests. Continental, today the third largest cable operator with over 3 million subscribers, has no ownership in HSN and about a 1% interest in QVC. It is not influenced, as Valuevision claims, to discriminate against other shopping services, as the new affiliation agreement with Valuevision demonstrates. Moreover, Continental has more affiliations with HSN than with its "affiliate" QVC. In fact, Continental **benefits** from vigorous competition among programmers.

Valuevision also overstates the lack of competition in shopping services. Its comments suggest that it is the lone source of competition to QVC and HSN, and that there is a special public interest benefit for the FCC to promote Valuevision's successful access on cable systems. However, this is simply not the case. Continental recently affiliated with a new shopping service owned by Fingerhut called the "S Channel". In addition, there are a flood of other shopping services existing or planning launch, such as TV-Macy's, ATV, Black Shopping Network, Catalog 1 (a joint venture of Time Warner and Spiegel), FYI, Q&A, Merchandise Entertainment Television, Product Information Network, Telecompras (Spanish language), Telefashion Net, Via-TV, Video Catalog Channel and Shop at Home, as well as specialized infomerical programming on more established networks such as MTV, BET and MOR-Music. This is hardly the type of programming the FCC needs to promote through special, below market rates.

Given the glut of home shopping programming on the horizon, following the Valuevision formula will not only violate Congress' intention that operators receive a fair profit for their capacity, but will also unwittingly lead to all leased access space on cable systems quickly filling with shopping services. These services are precisely the ones most able to immediately take advantage of any channel leasing scheme, yet as Valuevision has demonstrated, are very capable of obtaining standard affiliation agreements in the marketplace. Of course, this is not the diversity that Congress had in mind in establishing leased access. This glut of shopping services will not benefit cable subscribers and will result in significant harm to the financial, operational and market development of cable systems as they try to compete with DBS, telcos and wireless operators that are able to provide services that subscribers actually demand.

B. Preexisting Agreements With Lessees Are Irrelevant In Setting Current Rates.

In informal ex parte comments submitted earlier this year, TeleMiami asserts that the Commission can derive a "marketplace" rate for leased access based on agreements that were negotiated years ago, and in many cases have expired. See *Informal Comments of United Broadcasting d/b/a TeleMiami*, at 16, filed April 8, 1994. There is no basis for TeleMiami's assertion that past agreements are a "reliable indicator of market rates." Id. at 17. The fact is that there are many reasons why a cable operator likely would have negotiated a below market rate historically. Moreover, tying current rates to old agreements freezes rates in perpetuity despite the competitive and marketplace changes that are sweeping across the cable industry.

First, in a rate deregulated environment it was far less critical than it is today for operators to be fully compensated for their channel capacity. Thus, it is more likely than not that previous agreements tend to be lower priced than would otherwise be appropriate today. Second, the Commission has no way of knowing the circumstances of each preexisting agreement. For example, a local general manager may have signed a deal 5 years ago when channel capacity was more plentiful, and that deal was intentionally one of limited duration. Such arrangements were not negotiated with any expectation that operators would be locked into them indefinitely. Finally, many such deals are negotiated at artificially low levels to give the lessee an opportunity to build a business. If after the initial contract term the lessee has become successful, then the cable operator can renew the arrangement at a higher rate.

The irony of the TeleMiami example is that apparently unsuccessful programmers are seeking subsidized rates and may be artificially kept on cable systems to the exclusion of more talented and ambitious newcomers that would make more of the valuable opportunity of leased access. As the Commission observed in its recent decision, New England Cable News, CSR-4190-P, released June 1, 1994, it takes years to build a successful programming business and programmers may not realize a profit for years. Id. at 935. But the Commission would be acting entirely inconsistently with this principle if it forced leased access rates to artificially low levels based upon what lessees claim they are able to pay and denied the cable operator reimbursement for its ongoing subsidies if and when the programmer does become successful. If the programmer remains unsuccessful, the cable operator subsidies would just extend indefinitely into the future. This is unfair, eliminates incentive for lessees to improve and excel, and is clearly contrary to what Congress had in mind.

III. The Commission Should Not Destroy the Emerging, Non-Regulated Cable Advertising Business.

In today's regulated environment, cable operators will rely more on unregulated streams of revenue to grow and develop. One such area is advertising, yet the leased access rules pose an imminent threat to this critical developing business.

An example will illustrate the problem. Presently, advertisers and infomercial providers are arguably included in the home shopping category for pricing. If cable operators are required to break the leasing of channels down to the hour and minute, and simply apply pro-rata shares of a full-month channel lease to that time allotment, then the following scenario applies. A 10,000 subscriber cable system that receives $0.50 per subscriber for its most lucrative unaffiliated shopping service would be required to offer prime time hourly rates of $6.94. By the minute this is $0.12. Obviously, any commercial advertising department ceases to exist under such circumstances. Moreover, such a rate is inconsistent with the Congress' intent to permit a fair profit for use of our facilities, as previously discussed.

To prevent the migration of this advertising business to leased access, the Commission has several alternatives. It could explicitly require lessees to lease an entire channel at a time, particularly commercially oriented programmers. Alternatively, the Commission should decouple the full-channel use rate from the part-time rate. The cable operator should be able to sell leased access time to advertisers and infomercial providers at the commercial rate offered by the cable company's advertising department. This is the real "market" for this usage and this would serve as the "implicit net fee" for this type of programming.

IV. The Current Record Is Silent Concerning The Impact Of The *Turner* Decision.

On June 27, 1994 the United States Supreme Court decided the *Turner* case and established new legal standards that the Commission must follow in developing leased access rules. In *Turner*, the Supreme Court reaffirmed the First Amendment rights of cable operators in the context of reviewing the FCC's must carry rules. However, because the Court determined that the must carry rules are content-neutral, it decided that the constitutionality of those rules must be evaluated under the intermediate scrutiny test. Following the dictates of Turner, because the leased access rules are *at best*[1] a content-neutral intrusion on the First Amendment rights of cable operators, those rules must be crafted, at minimum, to satisfy intermediate scrutiny.

[1]Continental believes that the leased access rules are content based regulations, particularly as they have been applied by the Commission, and are therefore subject to strict scrutiny. Specifically, in its recent *TeleMiami* decisions, the Commission refers to the content of the lessee's programming in granting waivers that entitle the lessees to remain on the cable system at a rate lower than the rules otherwise permit. *See United Broadcasting Corporation d/b/a/ TeleMiami v. Rifkin/Narragansett South Florida CATV Limited Partnership, d/b/a/ Gold Coast Cablevision*, CSR-4261-L released June 30, 1994; *United Broadcasting Corporation d/b/a/ TeleMiami v. TCI/TKR of South Dade, Inc.*, CSC-366, released June 10, 1994. However, because the existing leased access record fails to satisfy even the lower intermediate scrutiny test, it is not necessary to establish the appropriate First Amendment test at this time.

Under the intermediate scrutiny test, a content-neutral regulation will be sustained if:

> it furthers an important or substantial governmental interest; if the governmental interest is unrelated to the suppression of free expression; and if the incidental restriction on alleged First Amendment freedoms is no greater than is essential to the furtherance of that interest. *Turner* at 4658, quoting *United States v. O'Brien*, 391 U.S. 367, 377 (1968).

Even with the extensive Congressional findings supporting must carry, the Supreme Court was not satisfied, based on the record in *Turner*, that the must carry rules satisfied this test, and the case was remanded to the district court for further fact finding. Obviously, the record in the leased access proceeding, at the Commission's own admission, is lacking and is woefully inadequate in light of the substantial legal test applicable under *Turner*.

For example, the Commission has expressed concern that local, non-profit programmers are not obtaining leased access to cable systems. However, the Commission should be aware that significant amounts of non-profit programming is retransmitted over cable operators' local origination and public access channels **at no charge to the non-profit programmers**. It is Continental's standard practice to inform non-profit programmers of the availability of such free channel capacity, and such programmers typically take advantage of that option. To the extent the record is silent on this point, and suggests there is no outlet for such programming, the record is seriously inadequate.

V. Miscellaneous Issues.

A. The Commission should reject a first-come, first-served policy for access to cable systems. Such an approach will conflict with Congress' desire to promote diverse programming on cable systems because such an approach will favor commercially oriented programmers, those most likely to be able to compete for actual affiliation agreements with operators (like a Valuevision) over less organized non-commercial programmers. Continental fully expects that any such rule will result in the vast majority of leased access capacity being occupied by home shopping services to the detriment of non-commercial lessees, cable subscribers and the competitive position of cable operators.

B. The Commission should reverse its earlier determination that leased access obligations continue even where effective competition exists. The Commission and Congress have repeatedly pointed to the benefits that competition will bring to the video marketplace. There is no reason to impose leased access on cable operators who compete with other multi-channel video providers. The goal of access to diverse programming is present with the competitor, and the competitor removes the concern that a vertically integrated operator will improperly deny a community access to competitive programming. The competitive multichannel provider will provide a safety valve for alternative programming if it is attractive to carry in the marketplace. It should be noted that cable competitors have no leased access obligations themselves, and in most cases will actually have more channel capacity than the cable operator.

VI. Conclusion

While leased access issues were part of the rate regulation docket, they were not thoroughly addressed by commenters and the FCC itself in this proceeding. This initial inadequate record has been exacerbated by events that have transpired since the comment periods have closed. Cable operator revenues have been further reduced, and competitive DBS systems that were only planned last year are now operational. In addition, the FCC is currently crafting its "going-forward" rules that will provide the opportunities for new programming distribution through financial incentives for operators to expand subscriber service offerings. Perhaps most significantly, the Supreme Court has established a new legal standard that the present record does not satisfy.

There is currently a serious capacity problem on most cable systems. At the same time there are a host of new attractive programming services that will enrich the lives of subscribers if they can gain access to already congested cable systems. Among the reported 120 new programming services in development are the History Channel and Ovation, which should not be kept off systems as the result of improperly conceived leased access rules that merely encourage the fast prolification of home shopping programming.

The current state of the record in this proceeding requires that the Commission seek additional comment before changing the current rules. While the FCC has heard individual reports of highly charged controversies in specific markets, there is no evidence that in the main the current system is not operating adequately at present. Continental has serious concerns with the Commission revising its leased access rules based upon the present incomplete rulemaking record and the anecdotal flare ups in individual communities.

This is a critical transition period for cable operators in the new regulated environment, and it is clear from the concerns expressed above that the industry can be seriously adversely affected by ill conceived leased access rules. Continental urges the Commission to issue a Further Notice of Proposed Rulemaking in order to establish a suitable record in this area. Such an approach would also allow the Commission to reconcile the leased access rules with the going-forward rules that are so critical to the future of the industry as well as with the recent *Turner* decision.

Respectfully submitted,

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