Before The
FEDERAL COMMUNICATIONS COMMISSION
Washington, D.C. 20554

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In the Matter of	)	
Implementation of Sections of the Cable Television Consumer Protection and Competition Act of 1992	)	MM Docket 93-215
and	)	
Adoption of a Uniform Accounting System for Provision of Regulated Cable Service	)	CS Docket 94-28

REPLY COMMENTS OF BELL ATLANTIC

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REPLY COMMENTS OF BELL ATLANTIC[1]

1. Introduction and Summary

At every turn, the cable industry continues to push for preferential regulatory treatment compared to telephone companies. They do so, moreover, despite the fact that cable and telephone companies will compete with one another to an ever increasing degree using the same technologies to provide the same services.

In particular, the cable commenters in this proceeding claim that no productivity offset should be included in the price cap rules for cable, that the rate of return for cable should be set substantially higher than for telephone companies, and that

[1] The Bell Atlantic telephone companies are Bell Atlantic - Delaware, Inc., Bell Atlantic - District of Columbia, Inc., Bell Atlantic - Maryland, Inc, Bell Atlantic - New Jersey, Inc., Bell Atlantic - Pennsylvania, Inc., Bell Atlantic - Virginia, Inc., and Bell Atlantic - West Virginia, Inc.

any accounting, cost allocation and affiliate transaction rules for cable should be more lenient than those for telephone companies.[2] In addition, the cable commenters completely ignore the issue of what accounting and other safeguards should be adopted for cable companies that provide both cable and telephone services. They do so, moreover, despite their own arguments elsewhere that telephone companies should be subject to numerous additional regulatory burdens when they provide both video and telephone services.

The Commission must reject the efforts of the cable industry to obtain an artificial advantage in the developing competitive struggle between cable and telephone companies, and impose rules on cable companies that are equivalent to those for telephone companies.

2. The Commission Should Establish Parity of Regulatory Treatment Between Cable and Telephone Companies

The cable commenters repeat their usual arguments here that the Commission should not establish parity between direct competitors, and even suggest the Commission can not apply any rules to the cable industry that also apply to telephone

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[2] The cable commenters here advance many of the same arguments as in prior rounds of this proceeding; in the interest of brevity, Bell Atlantic hereby incorporates its prior pleadings addressing these arguments by reference. See Comments of Bell Atlantic, et al., Dkt. No. 93-215 (filed Aug. 25, 1993); Joint Comments of Bell Atlantic, et al., Dkt. No. 93-215 (filed Sept. 14, 1993).

companies.[3] But as the Commission itself has correctly recognized,[4] the cable commenters are wrong.

First, as explained by Drs. Harris and Vander Weide,[5] parity of regulatory treatment is critical to avoid artificially favoring or handicapping one competitor over another as cable companies move into increasingly direct competition with telephone companies -- both in the consumer market and in capital markets where they compete for investor dollars.[6] The Commission

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[3] See, e.g., Comments of Time Warner Entertainment Co., L.P. at 11-14 ("Time Warner Comments"); Comments of Tele-Communications, Inc., at 14-16 ("TCI Comments"); Comments of the Nat'l Cable Television Ass'n, Inc. at 22 ("NCTA Comments").

[4] See, e.g., Implementation of Sections of the 1992 Cable Act - Rate Regulation, MM Dkt No. 93-215 & CS Dkt No. 94-28, Report and Order and FNPRM at ¶ 26 (rel. Mar. 30, 1994) (holding that Congress "did not intend that we produce a system that is far more generous to operators, and less generous to customers, than the result produced by the telephone model"); Implementation of Sections of the 1992 Cable Act - Rate Regulation, MM Dkt 92-266, 2d Order on Recon., 4th Report and Order, and 5th NPRM at ¶ 24 (rel. Mar. 30, 1994) (holding that it is important to treat the cable and telephone industries "with as much regulatory parity as is possible").

[5] See Declaration of Robert G. Harris, attached to Comments of Bell Atlantic (July 1, 1994) ("Harris Decl."); Affidavit of James H. Vander Weide in Support of Reply Comments of Bell Atlantic ("Vander Weide Reply Aff.") (Aug. 1, 1994) (attached).

[6] As Bell Atlantic pointed out in its opening comments, the convergence of these previously separate industries is accelerating and major new announcements reflecting cable's move into telephony occur almost daily. Just last week, for example, several of the country's largest cable operators announced they jointly would purchase $2 billion worth of equipment to upgrade their networks to provide two-way telephone services. See J. Keller, "Cable TV Industry Solicits Bids to Buy Phone, Data Gear," Wall St. J. at B3 (July 29, 1994).

and the Administration agree. To cite just a couple of examples, the Commission itself has held that it is important to treat the converging cable and telephone industries "with as much regulatory parity as possible,"[7] and the Administration has explained that drawing arbitrary distinctions between converging industries will "harm consumers by impeding competition and discouraging private investment in networks and services."[8] In fact, even the cable commenters concede that "[r]egulatory parity is an appropriate objective where similarly situated companies seek to compete to provide the same services."[9]

Nonetheless, despite this concession, the cable commenters claim that parity is inappropriate here because of supposed "differences" between the cable and telephone industries.[10] But these claimed differences cannot and do not justify preferential regulatory treatment on the issues before the Commission.

For example, the fact that cable was not regulated historically means only that cable has operated as an unregulated

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[7] Rate Regulation, MM Dkt 92-266, 2d Order on Recon., 4th Report and Order, and 5th NPRM at ¶ 24.

[8] Testimony of Larry Irving, Asst. Commerce Secretary, Before the House Subcommittee on Economic and Commercial Law at 7 (Jan. 26, 1994).

[9] See Time Warner Comments at 11.

[10] Id. at 11-14; TCI Comments at 14-16.

monopoly with no meaningful restraints on its prices and no competitive or regulatory prods to improve efficiency. As a result, cable operators were free to jack up their rates by three times the rate of inflation while providing poor quality service in an inefficient manner.[11] In addition, the argument that cable should not be regulated because it is not a traditional "utility" was lost nearly two years ago when Congress directed the Commission to regulate cable rates in the absence of effective competition.[12] The only question here is how to implement these regulations in a manner that will eliminate cable's ability to

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[11] See Section 2(a), Cable Television Consumer Protection and Competition Act of 1992, Pub. L. 102-385, 106 Stat. 1460 (1992). In contrast, telephone companies have been subject to price cap regulation with a productivity offset for over three years, and unlike cable, which still faces little competition, telephone companies already face rapidly increasing competition from cable and other sources. The result is that telephone companies have been driven to increase efficiency, and consumers of telephone services have received the benefit of reasonable prices that have declined in real terms.

[12] 1992 Cable Act, Section 3. Moreover, cable claims it is not a utility because it does not provide an "essential" service. Given a choice between their telephone and their television, however, it is questionable which consumers would consider to be more essential. And while cable claims its less than universal penetration proves it is not essential, the current take rate for cable is largely a function of the exorbitant prices charged during the period that cable operated as an unregulated monopolist. Competitive pricing is likely to lead to an increase in penetration, an increase which can be conservatively estimated at 20 percent or more. See also Thomas W. Hazlett, "Telco Entry Into Video," Paper presented at the Annual Public Utilities Research Center Conference, University of Florida at 12-17 (Apr. 24, 1992).

exercise market power.[13] And while cable claims it cannot be subject to uniform price cap, cost of service or accounting rules because of the lack of "homogeneity" in the cable industry,[14] the fact of the matter is that cable is no different than the telephone industry in this respect. On the contrary, the telephone industry itself is a diverse group of large and small companies with a varied mix of business interests and organizational structures.

Second, contrary to the claims of the cable commenters, the 1992 Cable Act itself requires the Commission to establish regulatory parity between the cable and telephone industries. This is so because a "principle goal of the Act is to encourage competition from alternative and new technologies."[15] Arbitrarily giving cable preferential regulatory treatment will undermine this Congressional goal by giving cable an unwarranted competitive advantage and interfering with the development of true competition.

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[13] See 1992 Cable Act, Section 2 (b)(5) (a principal purpose of the 1992 Act is to "ensure that cable operators do not have undue market power vis-a-vis programmers and consumers").

[14] See, e.g., TCI Comments at 14-16; Time Warner Comments at 11-12.

[15] See H.R. Rep. No. 628, 102d Cong., 2d Sess. 27 (1992); see also H. Conf. Rep. No. 862, 102d Cong., 2d Sess. 93 (1992) (directing the Commission to adopt rules to "encourage arrangements which promote the development of new technologies providing facilities-based competition to cable").

In contrast, the cable industry has repeatedly sought to distort the 1992 Act to support its claim that any regulations that apply to telephone companies cannot be applied to cable companies. Cable's claim is based on a provision of the 1984 Cable Act that says cable operators should not be regulated "as a common carrier or utility by reason of providing any cable service."[16] But applying price cap, cost of service and accounting rules to cable that are comparable to those for telephone companies would not subject them to common carriage obligations. Nor would it subject them to the types of obligations traditionally imposed on utilities -- such as universal service obligations or a requirement to provide a basic class of service at subsidized rates. On the contrary, as required by the 1992 Act, it simply would ensure that cable operators are not able to exercise market power.

Moreover, as Bell Atlantic previously pointed out, cable companies no longer provide just "cable service," but also provide traditional telephone services.[17] In this respect, there can be no dispute that cable operators are common carriers subject to the full range of the Commission's own Title II

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[16] 47 U.S.C. § 541(c).

[17] See Bell Atlantic Comments at 2-3.

regulations, and to the jurisdiction of the states for any intrastate communications services.[18]

3. The Commission Should Adopt Equivalent Productivity Offsets for Cable and Telephone Companies

The cable industry here continues to argue for a productivity offset of zero in its own price cap plan, while simultaneously arguing elsewhere that the telephone company offset of 3.3 percent should be increased.[19] The only empirical study offered in support of its position here, however, actually shows that the offsets for cable and telephone companies should be equivalent.

Specifically, the cable industry relies here on a study of productivity growth for three small cable operators to argue that cable has historically experienced a negative rate of productivity growth.[20] As Dr. Harris explains in his attached reply affidavit,[21] this study has two important limitations --

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[18] The 1984 Cable Act preserved the authority of the states and the Commission to regulate any communications services other than cable service that are offered by cable operators. See 47 U.S.C. § 541(c)-(d).

[19] See Comments of the California Cable Television Ass'n, Price Cap Performance Review for Local Exchange Carriers, CC Dkt 94-1 (filed May 9, 1994).

[20] Comments of NCTA at Attach. B.

[21] See Declaration of Robert G. Harris in support of Reply Comments of Bell Atlantic at ¶¶ 4-11 (Aug. 1, 1994) ("Harris Reply Decl.") (attached).

both of which are attributable to the cable industry's failure to provide data needed to conduct a reliable study. First, the study is based on a small sample of three self-selected cable companies[22] -- presumably the ones that could lay claim to the lowest rates of productivity growth. Second, the study measures output solely in terms of the number of subscribers served by these companies, and ignores other measures of output such as numbers of channels and increasing per channel revenues.[23] As a result, it does not necessarily present an accurate measure of cable's historical rate of productivity growth.

But more fundamentally, the cable industry's own study shows that the productivity offsets for cable and telephone companies should be comparable, and that, to the extent the two differ, the offset for cable should be higher.[24] As Dr. Harris explains, if productivity for the local telephone industry were measured solely based on number of subscribers as it is in the cable study, then the rate of productivity growth for telephone companies would be a negative number and telephone companies would be equally entitled to an offset of zero.[25] Alternatively,

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[22] Harris Reply Decl. at ¶¶ 6-7.

[23] Id. at ¶¶ 8-11.

[24] See Comments of Bell Atlantic at 2-6, and Harris Decl. attached thereto.

[25] Harris Reply Decl. at ¶ 10.

adjusting the cable industry's own study to reflect even one additional measure of output -- namely, numbers of channels -- produces an historical rate of productivity growth for cable that not only is positive, but that also exceeds the rate of productivity growth historically experienced by local telephone companies.[26]

And as Dr. Harris previously explained,[27] cable companies also should experience a higher rate of productivity growth in the future than do telephone companies. This is true because cable companies historically have deployed fewer productivity enhancing technologies than telephone companies (such as digital switching), and will experience greater productivity growth in the future as their deployment of these technologies accelerates.[28]

4. The Commission Should Adopt Cost of Service Standards for Cable That Are Comparable to Those Historically Applied to Telephone Companies

The cable commenters also claim they are entitled to preferential treatment in terms of the standards that will apply in any cost of service proceedings that cable operators initiate to justify rate increases. Again, they are wrong.

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[26] Harris Reply Decl. at ¶ 11.

[27] Harris Decl. at ¶ 3.

[28] Id.

First, cable claims that it is subject to greater risk than telephone companies, and therefore should be entitled to earn a higher overall rate of return. But as Bell Atlantic previously demonstrated,[29] the notion that cable companies face greater business or regulatory risk than telephone companies is fanciful.

In particular, while cable faces the prospect of competition in the future, telephone companies already face rapidly increasing competition for their most profitable services.[30] And while cable operators are expressly exempted from rate regulation where they face competition, telephone companies continue to be subject to rate regulation even for their most competitive services.

Moreover, not only do existing Commission rules give cable operators preferential treatment in any number of respects,[31] but the risk facing telephone companies is further

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[29] See Comments of Bell Atlantic at 7-9.

[30] Id. at 2-9.

[31] As Bell Atlantic has pointed out previously, examples abound of the preferred treatment that cable operators currently enjoy: cable benefits from pure price caps with no sharing provisions but telephone companies currently do not; cable can set its own depreciation rates subject to the dictates of the market, but telephone companies can not; cable can pass through costs in higher rates that are within its power to control, but telephone companies can not; and cable stands to benefit from a proposed productivity offset of 2 percent that is more reasonable than the one currently applied to telephone companies. See Petition of Bell Atlantic for Further Reconsideration, MM Dkt. Nos. 92-266 and 93-215, at 2-3 (filed May 15, 1994) (and authorities cited therein).

heightened by the fact that rates for basic telephone services are often kept artificially low for public policy reasons. At the same time, however, the profitable services that have historically paid to keep these basic rates low also are the ones subject to the greatest competitive attack. Cable operators, however, face no such problems; they are entitled under the Commission's rules to charge remunerative rates for all their services.

Second, the cable commenters argue that the overall rate of return for cable should be increased to a number ranging anywhere from 13 to 16 percent.[32] As Dr. Vander Weide explains,[33] however, the only real empirical evidence offered by the cable commenters[34] is inconsistent with the Commission's method of determining a cost of capital for telecommunications companies, and misapplies the methods it does use in several significant respects. In fact, if the errors in cable's own study are corrected, it produces an average overall rate of return of 11.83 percent[35] -- roughly comparable to the interim rate established by the Commission of 11.25 percent.

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[32] See, e.g., Comments of Continental Cablevision, et al. at 45-52 (13 percent); NCTA Comments at 42 (13.5 percent); Viacom Comments at 17 (14 to 16 percent).

[33] Vander Weide Reply Aff. at ¶¶ 3-18.

[34] See Comments of Continental Cablevision, et al., Exh. G at 26-51.

[35] Vander Weide Reply Aff. at ¶ 18.

In addition, if cable's average cost of capital is calculated in an economically correct manner -- using a corrected estimate of cable's cost of equity, the actual embedded cost of debt, and the industry's actual capital structure -- the result is nearly 200 basis points lower than the interim rate established by the Commission.[36] As a result, in the event the Commission were to adopt different allowed rates of return for the cable and telephone industries, the rate of return for cable would have to be lower than for the local telephone industry -- not higher.

Third, the cable commenters attempt to inject issues into this proceeding concerning the valuation of assets included in cable's rate base. In particular, they claim that cable should be permitted to recover in regulated rates the full cost of any "intangible" assets -- including the cost of monopoly acquisition premiums. These issues, however, already have been

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[36] **Id. at ¶ 19.** This is attributable largely to the fact that cable relies much more heavily on low cost debt than does either the telephone industry, or the subjective capital structure of 50 percent debt and 50 percent equity that was assumed by the Commission in establishing an interim rate of return. While it is true that this high degree of leverage results in a higher cost of equity for cable, the net effect of cable's heavy reliance on low cost debt is to reduce its overall cost of capital.

fully briefed by the parties,[37] were decided by the Commission,[38] and are not part of the further notice in this proceeding.[39] As a result, these issues are not properly part of these proceedings, and the cable industry's attempt to reargue points it has already lost is unavailing.

5. Cable Companies Should be Subject to the Same Affiliate Transaction, Uniform Accounting and Cost Allocation Rules as Telephone Companies

The comments filed by the cable industry largely ignore the two most fundamental issues raised by the Commission's proposal to adopt affiliate transaction, uniform accounting and cost allocation rules for cable.

First, declining to look a gift horse in the mouth, the cable commenters are silent on the Commission's proposal to limit the application of any such rules to instances where cable companies initiate a cost of service proceeding or seek to pass through external costs in rates. Unlike the rules for telephone companies, cable would be subject to none of these rules when

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[37] See Joint Comments of Bell Atlantic, et al., MM Dkt 93-215 at 22-26 (filed Aug. 25, 1993); Joint Reply Comments of Bell Atlantic, et al., MM Dkt 93-215 at 11-19 (filed Sept. 14, 1993).

[38] See Rate Regulation and Adoption of a Uniform Accounting System, MM Dkt. No. 93-214 and CS Dkt. No. 94-28, Report and Order and FNPRM at ¶¶ 37-119.

[39] Id. at ¶ 305 (limiting the further notice to an examination of whether the interim rate of return adopted for cable should be modified or made permanent).

they operate under price caps. This disparity cannot be justified.

Cable companies today provide a varied mix of regulated and unregulated services; engage in a significant number of transactions with affiliates that provide programming, telephony and other services; and are subject to regulatory oversight that is split between the Commission and local regulatory authorities. These are the same conditions that resulted in the adoption of cost allocation, affiliate transaction and uniform accounting rules for the telephone industry. And while it may well be true that many of the rules for telephone companies are unnecessarily burdensome or have outlived their usefulness, there is no justification for arbitrarily giving cable preferential treatment in this respect.

Second, the cable commenters ignore the issue of what accounting and other safeguards should be applied to cable companies that also provide telephone services. This is especially surprising given that the cable industry has argued strenuously in other proceedings that even the existing rules for telephone companies are not adequate when applied to an entity that provides both video and telephone services.[40]

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[40] See Petition for Rulemaking of NCTA, et al., Amendment of the Commission's Rules to Establish and Implement Regulatory Procedures For Video Dialtone Service, RM 8221 (filed Apr. 8, 1993).

It seems the cable industry believes that if a company starts as a regulated cable operator and moves into telephony, no accounting or other rules are necessary. But if a company starts as a regulated telephone company and moves into video, it should be saddled with a host of intrusive and burdensome regulatory constraints. Cable cannot have it both ways. While Bell Atlantic has shown that the existing rules for telephone companies are more than adequate for an entity that provides both video and telephone services,[41] any rules that are ultimately applied to telephone companies as they move into video services must be applied equally to cable companies as they move into telephony.

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[41] Comments of Bell Atlantic, RM 8221 (filed May 21, 1993); Reply Comments of Bell Atlantic, RM 8221 (filed June 7, 1993).

CONCLUSION

For the reasons set forth above and in Bell Atlantic's previous filings in this proceeding, the Commission should adopt rules here that are comparable to those that already apply to local telephone companies.

Respectfully submitted,

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AFFIDAVIT OF JAMES H. VANDER WEIDE
IN SUPPORT OF REPLY COMMENTS OF BELL ATLANTIC

I. INTRODUCTION

1. I have been asked by Bell Atlantic to respond to issues raised by the commenters in the cable TV industry concerning an appropriate rate of return for use in cost of service proceedings, and in particular to comment on studies by the Brattle Group in response to the Federal Communication Commission's Report and Order and Further Notice of Proposed Rulemaking in MM Docket No. 93-215 and CS Docket No. 94-28 released March 30, 1994.[1] As part of my response, I will discuss the Brattle Group's estimate of the cable companies' average cost of capital and their estimate of the cable companies' beta and cost of equity using the hypothetical 50—50 capital structure that

[1] Attached to Comments of Continental Cablevision, Inc., *et al.* (filed July 1, 1994).

was used by the Commission to set an initial rate of return for cable. In addition, I will also explain why the cable companies' actual capital structure should be used to accurately determine cable's overall rate of return; and I will update my estimate, previously presented in this proceeding, of a rate of return for cable computed on this basis.

2. I am Research Professor of Finance and Economics at the Fuqua School of Business, Duke University. I previously submitted testimony in this proceeding on August 25, 1993.

II. THE COMMISSION SHOULD ESTABLISH REGULATORY PARITY BETWEEN CABLE COMPANIES AND TELEPHONE COMPANIES BY USING THE SAME METHOD TO SET THE RATE OF RETURN FOR CABLE COMPANIES AS HAS BEEN USED FOR TELEPHONE COMPANIES.

A. The Brattle Group's 13.1 percent recommended rate of return would give cable operators an artificial advantage in the marketplace.

3. In setting the fair rate of return for the cable industry, the Commission must recognize that the cable and telephone industries are rapidly converging, and that companies in these two industries compete for funds in the capital markets. Large cable companies are developing plans to offer telecommunications services to residential and business customers over their own networks, which provide access to millions of customers. For example, just this week, a group of the country's largest cable operators announced plans to purchase billions of dollars of equipment to upgrade their networks to

provide two-way telephone service. In a similar manner, local telephone companies are making plans to offer video services over their networks.

4. Given the rapid convergence of the cable and telephone industries, it is essential that cable operators' and telephone companies' rates of return be determined on a consistent basis. If one side were to gain an advantage through the regulatory process, the benefits of competition could be lost. Since the Commission set an 11.25 percent benchmark for local telephone companies, based on a traditional cost of capital methodology, the Brattle Group's recommended 13.1 percent rate of return, based on an alternative methodology, would provide a significant and artificial advantage to the cable operators in their competition with the telephone companies.

B. The Brattle Group's recommended cost of capital methodology is inconsistent with the Commission's preferred methodology for determining the telephone companies' cost of capital.

5. In setting the fair rate of return for the cable industry, the Commission correctly recognized the need to apply the same regulatory principles and methodologies to set the cable companies' fair rate of return as they apply to the telephone companies. Thus, in its Report and Order and Further Notice of Proposed Rulemaking, the Commission calculated the cable companies' average cost of capital based on: 1) a ***discounted cash flow*** ("DCF") estimate of the cable companies' cost of equity; 2) an estimate of the cable companies' ***embedded*** cost of debt; and 3) a hypothetical 50—50 ***book value*** capital structure. In contrast, the Brattle Group's estimate of the cable companies' average cost of capital is based on: 1) a ***capital asset pricing model*** ("CAPM") estimate of the cable companies' cost of equity; 2) an

estimate of the cable companies' cost of ***newly-issued long-term*** debt; and 3) an estimate of the cable companies' ***market value*** capital structure. The Brattle Group's recommended methodology is inconsistent with the Commission's preferred methodology for estimating telecommunications companies' cost of capital -- applicable to both cable and telephone companies.

III. THE BRATTLE GROUP OVERSTATES THE CABLE COMPANIES' AVERAGE COST OF CAPITAL.

6. In addition to using a methodology for estimating the cable industry's cost of capital that is inconsistent with that used by the Commission, the Brattle Group estimate also misapplies its own methodology in several important respects. By way of background, the cable companies' average cost of capital is the sum of their weighted cost of debt and their weighted cost of equity. The Brattle Group, however overstates the cable companies' cost of equity, overstates the cable companies' cost of debt, and understates the amount of debt in the cable companies' capital structure. The net effect is that the Brattle Group's estimate significantly overstates the cable companies' average cost of capital. Even with a 50-50 capital structure, correcting the Brattle Group's estimate of an appropriate rate of return for the remaining errors produces a rate of return that is close to the interim rate of 11.25 percent that was previously adopted by the Commission.

A. The Brattle Group overstates the cable companies' cost of equity.

7. The Brattle Group estimates the cable companies' cost of equity by using the Capital Asset Pricing Model (CAPM), which states that:

Cost of equity = Risk-free rate + Beta (Market Risk Premium)

Since the Brattle Group overstates both the risk-free rate and the cable companies' beta, they overstate the cable companies' cost of equity.

8. In the context of the CAPM, the term "risk-free rate" refers to the expected rate of return on a financial investment with zero risk. The Brattle Group defines the risk-free rate as the expected yield on short-term Treasury bills. Instead of directly using the current yield on Treasury bills as an estimate of the expected yield, however, the Brattle Group obtains its estimate of the yield on Treasury bills by subtracting the Ibbotson Associates' estimate of the long-run "maturity premium" on one- to five-year Treasury notes from the yield on those notes; they assume the continuance of this premium.[2] The Brattle Group's unusual procedure produces their estimate of the risk-free rate, 5 percent. If the Brattle Group had used the contemporaneous yield on short-term Treasury bills as their estimate of the risk-free rate, their cost of equity estimate would have been 126 basis points lower.[3]

9. The Brattle Group obtained their estimated beta of 1.82 for the cable companies by regressing the excess return for cable stocks on the excess return for the S&P 500. The Brattle Group fails to adjust their estimated beta, however, for the well-documented tendency of betas to move over time toward the mean beta of 1.0. Recognizing this tendency of betas to

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[2] The current yield on Treasury bills is the best estimate of the return current Treasury bill investors can expect to receive on their investment. Since interest rates fluctuate without a pattern, the current yield on Treasury bills is also the best forecast of the future yield on Treasury bills.

[3] The Brattle Group used data from the Federal Reserve. The Federal Reserve *Statistical Release* reports a yield on short-term Treasury bills equal to 3.74 percent for the latest month (June 7, 1994 report).