Companies Under $100 Million In Regulated Revenues		
	Companies	
Classification	Number	Percentage
Telephone[46]	1,329	98.5
Cable Television	1,661	98.3

B. A Small Cable Company Needs Revenues Of At Least $40 Million To Access Capital Markets.

One of the factors listed by the Commission as a relevant measure of company size is the ability to attract new capital[47]. In the *Broadband PCS Order*, the Commission established a bright line at $40 million of gross revenues between those entities that have access to capital markets and those that do not. Therefore, at a minimum, cable operators with revenues of less than $40 million (approximately 110,000 subscribers)[48] should, without question, qualify as small operators. This measure, in and of itself, is insufficient as it fails to consider the ability to absorb the burdens of administering regulation.

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[46]The number of telephone companies that qualify as small is actually understated as this data was accumulated based on the total revenues, not merely regulated revenues.

[47]*Second Reconsideration Order* at ¶120.

[48]Smaller operators have lower average per subscriber revenues as they generally offer fewer premium services. SCBA estimates that smaller operators average no more than approximately $30 per month per subscriber in total revenue. The $40 million gross revenue standard, when divided by $30 per month equates into 111,111 subscribers.

C. When Adjusted For Unique Characteristics Of The Cable Television Industry, The Number Of Access Lines Is In Line With The $100 Million Regulated Revenue Standard.

1. The Basic Standard - A Small Telephone Company is One With 100,000 Or Fewer Access Lines.

As previously stated, the minimum telephone company small business standard is 50,000 access lines per study area. Because the access line count is a limitation only for a study area, total company size can exceed the 50,000 limitation.

Also, for purposes of determining the impositions of regulatory burdens,the most recent Commission pronouncement used a measure of 100,000 access lines as the relevant measure of a small business[49]. This 100,000 access line measure, is not translatable directly into 100,000 cable television subscribers.

A 100,000 access line telephone company is roughly equivalent to a 100,000 subscriber telephone company[50]. It is interesting to note that the Commission has characterized areas served by these companies as being truly rural in nature. If an operator served 100,000 subscribers, assuming 2.63 persons per household[51], an area with 263,000 individuals is deemed "truly rural" by the Commission.

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[49]*Broadband PCS Order* at ¶193.

[50]Industry statistics suggest that only 3 percent of telephone access lines are multiple lines. Therefore, 100,000 access lines might translate into approximately 97,000 subscribers.

[51]U.S. Department of Commerce, 1990 Census, Summary of Population and Housing Characteristics for the United States (March 1992).

2. The Telephone Company Standard Must Be Adjusted For Lower Penetration Rates Of Cable Television Operators.

Before comparing to a cable television operator, however, it is important to note that a telephone company has virtually 100 percent penetration because it is providing an essential service. The same is not true for cable television operators[52]. Average penetration for cable operators is 60 percent, and sometimes less in rural areas. Therefore, a cable operator has to build twice as much plant in a given community to serve the same number of subscribers served by the local exchange carrier, thereby making the venture much riskier and in need of greater protection from unnecessary regulatory burden. Therefore, taking the differences in density into consideration, the number of subscribers must be approximately doubled from 100,000 to 200,000.

3. The Telephone Standard Must Also Be Adjusted For The Inherent Riskiness Found In Cable Television Companies Because They Are Not Utilities.

In addition to having a two to one disparity in customer density, the price elasticity of demand[53] must also be taken into consideration. The price elasticity of a utility is close to zero because, by definition, it provides an essential service. Cable, on the other hand, according to the Commission has a price elasticity which is substantially higher[54].

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[52]Even the Commission conceded that cable television demand is elastic, meaning that as price increases, demand decreases. *Second Reconsideration Order* at ¶20.

[53]Price elasticity of demand is the relationship between price and demand. A price elasticity of -1 means that for every percent increase in price, demand will decrease by one percent.

[54]The Commission asserts a direct relationship between price and demand when it states "when the rates for regulated services fall as a result of the application of the competitive differential, the quantities of these services demanded by consumers should rise as new subscribers are added, fewer subscribers disconnect, and individual subscribers purchase

Price elasticity is important for several reasons. First, the incremental cost of regulation cannot be passed on to cable television subscribers or the subscriber base will shrink. A utility with inelastic demand does not face this concern, it can, and is often legally obligated[55] Therefore, operators are forced to reduce their profitability for the costs of regulation. Second, the need to regulate is lessened in that the Commission has recognized the existence of economic forces that limit a cable operator's ability to increase rates without losing subscribers. Therefore, the definition of a small cable operator should be more expansive than that of a small telephone company which, by the Commission's own admission, operates as a total monopoly[56].

The higher demand elasticity adds proportional risk to the operation of a cable television company. It is much easier for an operator to enter an uncontrollable death spiral if the cost of regulation becomes too great because it cannot recover such costs in its rates. The Commission cites economic studies which estimate the demand elasticity of cable television to range between -1 and -4[57]. The midpoint of that range is -2.5. Even using the conservative assumption that small telephone companies had a demand elasticity of -1[58], the elasticity for cable television operators is at least two and a half times as great; a

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additional programming services." *Second Reconsideration Order* at ¶20.

[55]Consider the Filed Rate Doctrine that requires electric power and natural gas providers to charge rates that recover all costs incurred during a year during that year. *Montana-Dakota Utilities Co. v. Northwestern Public Services Co.*, 341 U.S. 246 (1951).

[56]*Small Telephone Company NPRM* at ¶48.

[57]*Second Reconsideration Order at fn.60.*

[58]The actual demand elasticity is much closer to zero.

factor that should be reflected in the size determination of what constitutes a small business. Applying a factor of 2.5 to the 200,000 subscriber amount listed above yields a small business definition of 500,000 or fewer subscribers.

4. A 500,000 Subscriber Small Business Definition Only Slightly Exceeds The $100 Million Regulated Revenue Standard.

While a 500,000 subscriber small business definition may seem large to some, its validity can easily be verified by comparing it to the Commission's revenue standard for measuring small telephone companies. The Commission's small telephone company definition contained in 47 C.F.R. §32.11(a) converts from $100 million in regulated revenue to 416,000 subscribers, without any of the adjustments necessary to equate the number of telephone subscribers to cable television subscribers. Clearly both the 500,000 subscriber and $100 million regulated revenue measures are within the zone of reasonableness.

VI. THE SMALL MSO CAP ON SMALL SYSTEM RELIEF SHOULD BE REMOVED, OR AT A MINIMUM GREATLY ENLARGED.

A. The MSO Cap Was Imposed In Direct Conflict With Congress' Mandate To Provide Relief To All Small Systems.

The Commission imposed a cap on the size of the cable operator that can qualify for relief for any of its small systems. A small cable system must either be independently owned, or owned by a Small MSO. SCBA renews the objections it raised to the imposition of an MSO subscriber cap on the provision of small system relief[59]. Congress mandated that all small systems, not just some systems should receive relief from administrative burdens.

Congress recognized that the compliance burdens on a per subscriber basis were enormous for small systems. That was why the mandate was made to provide relief for all systems. The Commission, on the other hand, expects that the cost of regulating these systems will effectively be subsidized by larger systems owned by the same operator. While cross-subsidization is possible for larger operators, it is not even for a "larger" operator provided it is an operator of many small systems.

The only solution above reproach is to eliminate the MSO subscriber cap placed on small system relief.

B. Any Subscriber Cap Needs To Be Significantly Expanded.

While not supporting an MSO cap, if the Commission is determined to retain a cap, it must be substantially increased. The current subscriber cap provides relief to only 16

[59]*Reply Comments* of the Small Cable Business Association in MM Docket 93-215 dated September 13, 1993.

companies with more than 15,000 total subscribers[60]. At a minimum, MSOs that meet the small business definition adopted in this rulemaking should be able to take advantage of whatever relief is made available. If the Commission limits relief to those small systems owned by small operators, it will essentially have equated small systems and small operators, thereby obliterating the distinction between the two.

Just as the Commission adopted a sliding scale for companies to avail themselves of benefits for broadband PCS providers[61], the Commission can craft a different standard for the relief for the owners of small systems.

C. The Appropriate Measure of Cable System Size Is Each Franchise Area, Not The Franchise Areas Connected To A Common Headend.

The cost of administering regulation is fixed on a franchise level. To determine whether rates are justified, operators must complete a myriad of rate computation forms. The forms must be completed on a franchise level[62]. This means that if a single headend serves five communities, separate rate justifications must be computed for each community, even if the communities have identical channel line-ups and rates[63].

Assuming that an operator needs to use a cost-of-service justification to demonstrate the reasonableness of its rates, the operator is required to complete at least three forms: (1) FCC Form 1220 (10 hours); (2) FCC Form 1205 (20 hours); and (3) FCC Form 1220 (80

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[60]Based on a review of statistics from the A.C. Nielsen Cable On-Line Data Exchange (CODE DATABASE) (8/25/94).

[61]The Commission adopted different relief for systems with gross revenues of $40 million, $75 million and $125 million.

[62]*Order*, MM Docket 92-266 (Released May 23, 1994)

[63]*Id.*

hours) or FCC Form 1225 (60 hours). If an FCC Form 1210 is also required, an additional 10 hours must be added to the equation. This means that total preparation time for each franchise area can range between 100 and 120 hours.

Assume cable System "A" has a single headend serving five franchises of 250 subscribers each. It will have 1,250 subscribers with a total forms compliance time of 600[64] hours using the current definition of a system[65]. This compliance burden consumes one quarter of one full-time employee's efforts. Assuming a nominal employee cost of $20.00 an hour with benefits but no overhead, the cost of compliance is $18,000, or $14.40 per subscriber. This is just the cost of preparing the filings. It ignores the cost of explaining them to franchise authorities and the Commission.

Contrast this to System "B" serving only one community with 1,000 subscribers. This system will have a total compliance burden of only 100 hours at a cost of $2,000 or $2.00 per subscriber. System "B" qualifies for small system relief even though the burdens are much greater on System "A" which is classified as a large system and is entitled to no relief.

Although the Commission chose to adhere to its historic definition of what constitutes a system, it created a compliance system that is based on a different measure -- franchise areas. The Commission needs to resolve the conflict by either requiring compliance only on a system level or by determining small system qualification on a franchise area by franchise area basis.

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[64]This assumes time to prepare the basic tier filings. Additional time would be necessary if the operator has cable programming service tiers.

[65]It will require completion of FCC Form 1220 as opposed to 1225 because the system will be classified as a large system.

The risk to consumers of expanding the definition to the franchise area is minimal at best as the Commission currently provides very little administrative relief to small systems. Aside from the availability of streamlined relief[66] which was too expensive for virtually any cable operator to adopt, the only benefit remaining is the ability to use a "simplified" cost-of-service justification form[67] which only allegedly reduces compliance costs by 20 labor hours, or 17 percent. As discussed later in these comments, to comply with its Congressional mandate, the Commission must provide real relief from administrative burdens.

The headend definition of system size provides a disincentive to reduce costs of providing service. Prior to the onset of regulation, many operators were planning to interconnect systems in close geographic proximity to one another. Interconnection provides opportunities to substantially reduce both capital investment and operating costs on a per subscriber basis. Such interconnection, however, will jeopardize classification as a small system and the loss of any benefits related to small system status. The benefits would not be so easily lost if system size were measured using the more relevant franchise area measure.

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[66]Streamlined relief is very close to voluntarily adopting full reduction rates immediately in return for not having to complete rate justification forms until the end of the transition period.

[67]i.e., FCC Form 1225.

D. Relief Is Needed Because Of The High Per Subscriber Cost Of Regulation For Small Systems.

As the foregoing analysis demonstrates, the costs of regulation can be very high on a per subscriber basis if the franchise areas are very small. These costs do not decrease substantially just because an operator might have another system with more than 10,000 subscribers, or if its average system size (measured on a headend basis) is 1,250 subscribers.

If the Commission is intent for political or other reasons to limit small system relief, it must craft an MSO cap using relevant measures. For example, the MSO cap must measure only the total number of subscribers nationally. That number must exceed the small operator definition.

VII. SUBSTANTIVE RATE RELIEF MUST BE PROVIDED SMALL OPERATORS AND SMALL SYSTEMS.

SCBA and others have expended significant effort to persuade the Commission to issue the *Notice of Proposed Rulemaking* and to provide initial comments on necessary revisions to the regulatory framework. Even if the Commission is finally persuaded to adopt appropriate company and system size definitions, one must ask the rhetorical question "So What?"

If the Commission adopts, as we ask, new business and system size definitions prior to completion of the cost studies, all that means is that a greater number of operators will qualify for transitional rate relief. If the Commission does not change any of the current rate structure, adoption of new business size standards effective upon completion of the cost studies will render the new standards totally meaningless.

The real solution lies in action that SCBA and the U.S. Small Business Administration have been advocating repeatedly in their comments. Smaller systems and companies must be allowed to charge higher rates and computing such rates must be substantially simplified. Even though the scope of such changes may lie outside the instant *Further Notice of Proposed Rulemaking*, SCBA takes this opportunity to urge the Commission to provide meaningful relief to small operators and systems prior to completion of the cost studies.

While SCBA does not provide specific suggestions for change in these Comments, SCBA refers to the myriad of suggestions that it and others, including the U.S. Small Business Administration have placed on the table. Consider the following:

A. National Cost Averaging.

National cost averaging for rate setting purposes on the order of the National Exchange Carrier Association ("NECA") that is currently available to virtually every "small" telephone company. Although the Commission has permitted company-wide cost averaging for certain operators, there is no benefit for small operators of single systems since there is no reduced burden (i.e., a single system cannot be averaged).

B. Benchmark Adjustments.

On February 15, 1994, after expending significant Association resources and extensive discussions with Cable Service Bureau staff, all of which was performed at their request, SCBA submitted a comprehensive schedule of cost-sensitive benchmark adjustment add-ons which serve to make the benchmark system more realistic for many small systems. Once again, despite development of these adjustments at the request of the Cable Services Bureau Staff, the data and proposals submitted by SCBA were not so much as referenced in the *Second Reconsideration Order*. Despite the Commission's rework of the underlying benchmarks in its *Second Reconsideration Order*, the premise underlying these adjustments remains valid. SCBA incorporates those comments by reference and requests that the Commission reevaluate on its own motion their validity.

C. Net Income Tests.

Other commentors such as the Coalition of Small Cable Operators has submitted on several occasions a rate setting methodology based on net income. SCBA supports reevaluation of any such methods.

D. Revised Interim Cost-Of-Service Rules.

SCBA has called to the Commission's attention the fact that the interim cost-of-service rules contain no safety net for small operators or small systems. It is essential that if the primary system (i.e., benchmark/full reduction) has safeguards built in to protect small operators and small systems, the safety net procedure (i.e., cost-of-service) must also afford such operators and systems special treatment. Currently, they do not. As pointed out in SCBA's Comments in Docket 93-215[68], the interim rules and associated presumptions impose disparate burdens on small operators and small systems. These need to be addressed and immediately revised by the Commission.

E. Cash Flow Considerations.

The Commission recently adopted a hardship standard based on cash flow needs[69]. Cash flow measures are the lowest common denominator to measure economic viability. SCBA urges the Commission to consider making such easily computed adjustments to rates available to all small operators and small systems through a standard adjustment mechanism, rather than forcing such operators to file petitions for hardship relief.

F. Burden Reduction.

Many of the proposed methods of making the substantive rate determination process produce realistic results for small operators and small systems have the potential of

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[68]*Reply Comments* of the Small Cable Business Association in MM Docket 93-215 dated September 13, 1993.

[69]In the Matter of Implementation of Sections of the Cable Television Consumer Protection and Competition Act of 1992: Rate Regualtion, *Fifth Order On Reconsideration*, MM Docket Nos. 93-215 and 92-266 (Released September 26, 1994).

significantly reducing administrative burdens. A major way to reduce the administrative burdens of small operators and systems is to avoid forcing them on a wholesale basis into cost-of-service showings. Avoiding the preparation of cost-of-service showings alone would substantially reduce the administrative burdens. Cost averaging on an industry basis would also help reduce burdens.

G. Other Methodologies.

SCBA is aware that other industry groups may have proposals to alter substantive rate regulation and reduce procedural burdens for cable operators. SCBA urges the Commission to quickly adopt proposals that would result in realistic rates for small operators and small systems while also reducing administrative burdens.

As it has in the past, SCBA stands ready willing and able to provide the Commission with input as it seeks to revise and possibly reshape the way it regulates small operators and small systems.

Respectfully submitted,

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