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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: Rate Regulation	)	MM Docket No. 92-266
Implementation of Sections of the Cable Television Consumer Protection and Competition Act of 1992: Rate Regulation	)	MM Docket No. 93-215

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COMMENTS OF DISCOVERY COMMUNICATIONS, INC.

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COMMENTS OF DISCOVERY COMMUNICATIONS, INC.

Discovery Communications, Inc. ("Discovery"), by its attorneys, hereby submits its comments on the Commission's *Seventh Notice of Proposed Rulemaking*[1] to implement the rate regulation provisions of the Cable Television Consumer Protection and Competition Act of 1992 ("Cable Act").

Discovery urges the Commission to allow cable operators that select the newly revised going-forward rules the opportunity to retain a 7.5 percent markup on programming cost increases for channels carried before May 15, 1994. In similar fashion, the Commission should also allow operators continuing to use the first set of

[1] *Implementation of Sections of the Cable Television Consumer Protection and Competition Act of 1992: Rate Regulation*, FCC 94-286 (released Nov. 18, 1994) (*Sixth Reconsideration Order, Fifth Report and Order, and Seventh Notice of Proposed Rulemaking*) (*"Sixth Reconsideration Order"* or *"Seventh Notice"*), *summary published*, 59 *Fed. Reg.* 62,703 (Dec. 6, 1994).

going-forward rules to markup new programming cost increases after the initial markup of programming costs of new channels.

Discovery owns and operates The Discovery Channel,[2] The Learning Channel[3] and several brand new program services: QUARK!, Animal Planet, Living, and Time Traveler.[4] As the provider of both established and emerging program services, Discovery has consistently emphasized throughout these proceedings the vital importance of regulations that preserve the financial incentives of cable operators to support quality programming.[5] This issue is at stake in the *Seventh Notice* as well.

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[2] The Discovery Channel features nonfiction documentaries about science, nature, technology, human events, and history. The Discovery Channel now reaches about 62 million subscribers and is one of the most enjoyed and appreciated cable networks in the country.

[3] The Learning Channel features educational programs on subjects such as history, science, archeology, and anthropology for viewers of all ages. It also provides six hours of commercial-free educational programming for preschoolers every weekday morning.

[4] QUARK! will focus on science and technology. Animal Planet will feature animals and their environments, people and pets, and nature programs for children. Living will feature cooking programs, how-to shows, travel, crafts, gardening, fashion, and collectibles. Time Traveler will feature programs covering events and stories from history.

[5] *See, e.g.*, *Comments of Discovery Communications, Inc.*, Docket No. 92-266 (June 29, 1994); *Comments of Discovery Communications*, Docket No. 92-266 (Jan. 27, 1993) (urging Commission "to allow cable operators automatically to flow-through their *net* increased costs for programming and system improvements").

I. THE COMMISSION's PREVIOUS DECISIONS HAVE RECOGNIZED THE NEED TO ALLOW CABLE OPERATORS SUFFICIENT INCENTIVE TO SUPPORT QUALITY PROGRAMMING

Consistent with the intent of Congress to foster the availability to consumers of diverse, quality program services,[6] the Commission's previous decisions in this docket have recognized explicitly the importance of programming investment by cable operators. In particular, the Commission has recognized the need for rate regulations to preserve incentives to encourage cable operators both to launch new cable services and to support financially the continued and heightened quality of material carried on established channels.

The Commission first acknowledged the need for financial incentives to improve programming when it allowed operators an opportunity to markup their investments in program services by 7.5 percent.[7] It recently reaffirmed this policy in the more recent decision revising the "going-forward" rules to authorize a 20 cent increase in program licensing fees and establishing an "operator cap." Indeed, the Commission

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[6] *See Cable Television Consumer Protection and Competition Act of 1992*, Pub. L. 102-385, §§ 2(b)(1), 2 (b)(3), 106 Stat. 1460 (1992).

[7] Whether the 7.5 percent return on programming investment currently authorized by the Commission is adequate to achieve this congressional goal, particularly in a time of rising interest rates, is another matter. Discovery has previously explained why a larger return on investment would better serve the public interest. *See Comments of Discovery Communications, Inc.*, Docket No. 92-266 at 8-10 (June 29, 1994).

"supplemented"[8] the going-forward rules largely because it recognized that the previous rules in many instances provided inadequate incentives for service upgrades.[9]

While it is important to encourage cable operators to add nascent program services, such as The Learning Channel or Discovery's other new programming services, it is equally important to encourage continued investment in the quality of programming already carried on a cable system. Accordingly, the Commission should not act to create incentives for cable operators to favor new channels over existing ones -- or *vice versa. Rather, the Commission should establish and preserve incentives for cable operators to invest in programming on terms fair to programmers, and without regard to how long their channels have been carried on a particular cable system.*

II. THE PROPOSAL TO DISALLOW THE 7.5 PERCENT MARKUP FOR INCREASED LICENSE FEES OF PROGRAM SERVICES CARRIED BEFORE MAY 15, 1994, WOULD THREATEN THEIR CONTINUED VIABILITY BY UNFAIRLY FAVORING EMERGING CHANNELS

In the *Seventh Notice*, the Commission tentatively concluded that "the 7.5% markup on programming cost increases for channels offered before May 15, 1994 may no longer be necessary given the total incentive structure provided in our revised going

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[8] *Implementation of Sections of the Cable Television Consumer Protection and Competition Act of 1992: Rate Regulation*, MM Docket No. 92-266, FCC 95-8 at ¶ 3 (Jan. 5, 1995) (*Seventh Order on Reconsideration*).

[9] *See Implementation of Sections of the Cable Television Consumer Protection and Competition Act of 1992: Rate Regulation*, 9 FCC Rcd 4119 (1994) (*Second Order on Reconsideration, Fourth Report and Order, and Fifth Notice of Proposed Rulemaking*); *Sixth Reconsideration Order*, ¶¶ 64-83.

forward rules."[10] Discovery submits that this conclusion is flawed, and that the proposal would undermine the Congressional goal of preserving quality programming.

First, it must be clearly understood that, under the proposal in the *Seventh Notice*, cable rate regulations would treat cable operator investment in programming differently based entirely on when the operator first began to carry a particular channel.[11] If adopted, the proposal would leave operators with a substantially enhanced incentive to increase programming investment by adding channels and no incentives to increase programming investment in channels carried prior to May 15, 1994. This is because cable operators could pass through increases in license fees for new channels, but would be denied any margin on such increased investment in program services carried before May 15, 1994.[12] This differing incentive structure

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[10] *Seventh Notice*, ¶ 133.

[11] While costs of programming undoubtedly vary between program channels, such differences are caused by the type of programming the channel carries and its operations. It is obvious that how long the channel has been on a particular cable system has nothing to do with the costs the channel incurs in providing programming. In every instance such cost increases are reflected in increases in the license fees negotiated with cable operators.

[12] In effect, a cable operator would see that its return on its investment in programming carried before May 15, 1994, would steadily decline if it were to agree to increased license fee support. As licensing fees rise, what was once a 7.5 percent return will inexorably shrink as a percentage, because the proposal would forbid operators from "marking up" the incremental programming expense increases. Over time, this will make further investments in the "old" programming less and less attractive, especially in comparison to the greater percentage returns possible under the revised going forward rules.

would be manifestly unfair to those program services carried before May 15, 1994, and would pose a threat to their continued quality.[13]

The likely consequence of such skewed incentives for operators is that program channels carried before May 15, 1994, will eventually wither. As cable operators, facing steadily smaller incentives, resist increases in licensing fees for the financially less attractive "old" channels, the reduced licensing revenues received by programmers will impair *their* financial ability to sustain programming quality, in turn forcing them to look even more to advertising revenue to support programming costs.[14] As programming quality declines, the American public will suffer. Such a result certainly cannot be intended by the Commission.

Moreover, the Commission should avoid creating any incentive for operators to "churn" program channels. The proposal to treat investment differently depending upon the length of time that channels have been carried could create an unfair incentive

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[13] While the Commission presumably fears that operators would simply raise rates without compunction, it has recognized previously in this proceeding that "cable operators also have incentives to assure that service rates are not excessive since excessive programming costs, if passed on to subscribers, may cause them to lose subscribers." *Implementation of Sections of the Cable Television Consumer Protection and Competition Act of 1992: Rate Regulation*, 8 FCC Rcd 5631, 5787-88 ¶ 251 (1993) (*Report and Order and Further Notice of Proposed Rulemaking*). Moreover, the Commission's rate regulations "must balance the interest in protecting consumers with the need to allow the regulated entity sufficient revenue, including a return on investment." *Federal Power Commission v. Hope Natural Gas Company,* 320 U.S. 591, 603 (1943).

[14] For example, under such circumstances it is conceivable that The Learning Channel could no longer afford to maintain its current six hour advertiser-free block of educational programming.

for operators to discontinue carriage of "older" channels, only to resume carriage at some later time when the channel might be considered a "new" one. This would serve no one's interest.

The *Seventh Notice* suggests no valid public policy reason for distinguishing the rate regulation of the investments by cable operators in programming services on the basis of how long a channel has been carried on particular systems. Contrary to the supposition in the *Seventh Notice*, the "total incentive structure" created by the newly-adopted going-forward rules does not provide operators with adequate incentives, for by their very terms the recently-adopted operator cap and licensing fee adjustments apply only to *new* channels on cable programming tiers.[15] They simply are not applicable to channels carried before May 15, 1994. Thus, the incentives that cable operators would face under the proposal would be unbalanced and would ultimately work to the detriment of programming quality.

The Commission should avoid these results by setting a cable operator's incentives in a program-service neutral manner. While Discovery recognizes that the Commission perceives a need for different sets of rules to govern channels carried before and after May 15, 1994, both sets of rules should provide operators with incentives to maintain and enhance their programming investments. As the "total

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[15] *See* 47 C.F.R. § 76.922(e)(3). Indeed, that is plainly the intent of the new rule, for the Commission states elsewhere that "the per channel adjustment of up to 20 cents for additional channels, in addition to the License Fee Reserve, will provide full and fair compensation to operators adding channels to CPSTs." *See Sixth Reconsideration Order*, ¶ 83.

incentive structure" does not preserve such incentives with respect to channels carried before May 15, 1994, Discovery respectfully submits that a percentage markup on increases in the programming costs of such channels remains necessary.

III. CONCLUSION

For the foregoing reasons, Discovery respectfully urges the Commission not to create an artificial incentive for cable operators to favor new channels over those carried before May 15, 1994. The Commission should not adopt its proposal to discontinue allowing operators from earning a 7.5 percent markup on increased costs of program channels carried before May 15, 1994, but rather should continue to allow cable operators to earn a return on their added investments in such services.

Respectfully submitted,

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