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

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FEDERAL COMMUNICATIONS COMMISSION
OFFICE OF SECRETARY

In the Matter of	)	
	)	
Implementation of Sections of the	)	
Cable Television Consumer Protection	)	MM Docket No. 92-266
and Competition Act of 1992:	)	
Rate Regulation	)	
	)	
Leased Commercial Access	)	CS Docket No. 96-60

COMMENTS OF COX COMMUNICATIONS, INC.

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May 15, 1996

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SUMMARY

The Commission has proposed in its leased access *Further Notice* to adopt a cost-based methodology to compute leased access rates. Cox urges the Commission to retain its existing "highest implicit fee" formula, with modifications. The current formula generally establishes reasonable rates for leased access programming while the more complex proposal in the Commission's *Further Notice* generates rates that do not reasonably estimate the costs of leased access programming.

The Commission suggests that the current formula is flawed because it permits cable operators to "double recover" leased access fees — once from the programmer and again from subscribers. But, it is highly unlikely that operators recover more than the fair value of leased channels under the current formula because the amount that cable operators receive from subscribers for carrying leased access programming is, in reality, *de minimis*.

The Commission also suggests that the *highest* implicit fee may overcompensate operators. This belief is misguided because operators do not recover certain revenue — such as advertising availabilities and additional revenues from increased subscribership — that they otherwise would recover by carrying programming which they select. Because comparing the *average* per-channel costs to subscribers with the *actual* cost of each channel of programming does not yield a result that reflects either the actual value of each channel or the average value of all channels to cable operators and programmers, the current formula could be revised by comparing the average per-channel cost to subscribers with the *average* cost of the programming on the tier. This will produce a rate that accurately reflects the average amount by which subscriber fees for a tier exceed programming costs.

While the current methodology can be adjusted to assure reasonable leased access rates, the proposed cost-based formula will not permit operators to recover all costs of

leasing capacity, and will result in rates which are far below reasonable levels. The proposed formula also is complex and burdensome, while the current formula is easily applied. Moreover, the Commission proposal that operators be required to specify in advance those channels that will be leased would provide a competitive advantage to other video providers and would financially harm cable operators.

The Commission suggests setting part-time leased access rates by *pro rating* full-time rates. This proposal is flawed because it fails to recognize that these are additional costs associated with carrying part-time programming and that revenue is lost because cable operators often cannot program all 24 hours of a channel. Some of these problems could be addressed by implementing the Commission's proposal to require that a minimum of eight hours of programming be provided on part-time leased access channels before dark channels or channels that carrying existing programming must be made available for leased access use.

The Commission also requests comment on whether not-for-profit entities should be offered preferential rates. The Commission is not authorized to require operators to offer reduced rates to not-for-profit organizations, and, in fact, the Communications Act and its legislative history suggest that such preferential rates are not permissible.

Finally, the Commission should not permit leased access programmers to resell time to other programmers. Allowing leased access users to resell time undercuts congressional policy. Moreover, it would be unfair to cable operators, which, in practice, would subsidize resellers of time rather than provide leased access time at reasonable rates to leased access programmers.

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COMMENTS OF COX COMMUNICATIONS, INC.

Cox Communications, Inc. ("Cox"), by its attorneys, hereby submits its comments in response to the Federal Communications Commission's (the "Commission's") *Order on Reconsideration of the First Report and Order and Further Notice of Proposed Rulemaking* in the above-referenced proceeding.[1/]

INTRODUCTION

In its *Further Notice*, the Commission tentatively concludes that its "highest implicit fee" formula to establish the maximum reasonable rates that cable operators may charge for commercial use of its channels is not working properly. Specifically, the Commission believes that the formula overcompensates cable operators and inhibits the use of leased access capacity by unaffiliated programmers. It therefore proposes to replace the formula

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1/ *Order on Reconsideration of the First Report and Order and Further Notice of Proposed Rulemaking*, MM Dkt. No. 92-266, CS Dkt. No. 96-60, FCC 96-122 (rel. Mar. 29, 1996) ("*Order on Reconsideration*" and "*Further Notice*").

with a new formula based on the costs incurred by operators in substituting leased access channels for existing programming.

As a general matter, it is not at all clear that leased access, as contemplated by the Communications Act, is not currently working. In seeking revision of the existing formula for determining leased access rates, some petitioners alleged that the "highest implicit fee" formula establishes prohibitively high rates that make leased access unaffordable to most programmers.[2/] Cox's experience as an operator of over 30 cable systems with 3.2 million subscribers indicates that, where sufficient demand for their programming exists, leased access programmers are both willing and able to lease channels under the current rules. Indeed, it has not been Cox's experience that "relatively little leased access capacity is being used by unaffiliated programmers."[3/]

For example, Cox's Pensacola, Florida cable system currently leases four channels on a full-time basis and uses a fifth channel for part-time leased access programming. Similarly, Cox's Myrtle Beach, South Carolina system leases three channels to full-time services and uses a fourth channel for part-time leased access. Cox's Hampton Roads, Virginia cable system currently leases five channels on a full-time basis. Cox's Cleveland, Ohio system has filled its statutory allotment of leased access channels.

These systems provide a variety of programming on their leased access channels, much of it locally oriented and produced. Exhibit A to these Comments lists the variety of leased access programming currently offered by a representative Cox cable system.

2/ *Order on Reconsideration* at ¶ 19.

3/ *Id.* at ¶ 6.

The current rules do not, of course, *require* cable operators to charge the highest implicit fee. Cable operators may negotiate rates for leased access that are lower than the highest implicit fee when business considerations warrant, and Cox has done so on many occasions. Fore example, Cox charges ValueVision rates lower than the highest implicit fee for full-time access on cable systems that Cox feels can support another shopping channel.

There are many virtues to the "implicit fee" approach, including its simplicity and ability to set rates that reflect the actual value of channels in the video programming marketplace. The Commission's cost-based approach, on the other hand, (1) is exceedingly complicated and burdensome to apply; and (2) despite its complexity, fails to measure and thus drastically understates the costs associated with leased access because it treats as "too speculative" most of the true costs of adding leased access programming. As a result, the cost formula would distort the programming marketplace and would "adversely affect the operation, financial condition, or market development"[4/] of cable systems — precisely the effects that Congress sought to avoid. Therefore, it makes more sense to modify and correct any perceived problems with the implicit fee approach than to replace it with a complicated cost formula that creates more problems than it solves

I. THE PERCEIVED PROBLEMS WITH THE CURRENT LEASED ACCESS REGIME CAN BEST BE ADDRESSED BY MODIFYING, RATHER THAN REPLACING, IT.

An implicit fee approach recognizes that the amount that programmers implicitly pay for channel access is determined, in large part, by the nature of the program service and its

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4/ 47 U.S.C. § 532(c)(1).

perceived value to subscribers and to cable operators. For this reason alone, an implicit fee approach is far superior to a cost-based approach that focuses solely on the direct costs incurred by the operator in making a channel available and on the differences in the operator's costs and revenues between the leased access programmer and the former occupant of the channel. Moreover, the implicit fee formula is as easy to calculate as the proposed cost formula is difficult.

The Commission has expressed concern that the current "highest implicit fee" formula overcompensates cable operators, both because it gives operators a "double recovery" from lessees and subscribers and because operators do not always recover the *highest* implicit fees from the programmers that they choose to carry on their systems. As discussed below, these concerns are overstated and largely unwarranted. The current formula may not, however, accurately measure implicit fees, and some revisions to that formula may be appropriate. But there is no basis for discarding the implicit fee approach altogether in favor of a cost formula based approach.

A. Any "Double Recovery" by Cable Operators is *De Minimis*.

The implicit fee approach seeks to identify the range of rates that traditional cable programmers "implicitly" pay cable operators to be carried on their systems. Programmers typically do not pay for carriage. Usually the cable operator pays for the programming and then resells it programming to subscribers. But what the Commission recognized in adopting the implicit fee approach was that this purchase and resale of programming by the operator could have been structured as a functionally equivalent lease agreement. Under such an agreement, the programmer would have paid the operator for carriage, and then would itself

have resold the programming to subscribers, perhaps using the cable operator as a marketing and collection agent.

If a traditional programming agreement were restructured or recharacterized in this manner, the amount paid by the programmer to lease a channel (the implicit fee) would be equal to the amount that the operator charges subscribers for the programming *minus* the amount that the operator pays for the programming. This is the amount that the operator receives for carrying the programming — and under a market-based approach, the operator should receive an equivalent amount for leasing a channel to the same programmer pursuant to its leased access obligations.

Under an implicit fee approach, therefore, operators are expected to recover from leased access programmers the difference between what they currently charge subscribers for similar programming and what they currently pay for such similar programming. Leased access programmers, meanwhile, are supposed to recover from subscribers the amount that cable operators currently charge subscribers for similar programming.

For *à la carte* leased access programmers, this is exactly how the current rules work. The programmer leases a channel at a rate that reflects the net amount that the cable operator typically receives from offering other à la carte program services on its system. Then, the programmer sells its service directly to subscribers and, depending on the value on the service to subscribers, receives more or less than the typical premium programmer on the system. But leased access programmers that choose to be placed on a tier and do not market their service directly to subscribers may have no way to recover any subscriber fees for the

service. Instead, the *cable operator* recovers subscriber fees for the tier that includes the leased access channel.

In the Commission's view, this is a critical flaw insofar as it "appears to allow double recovery of subscriber revenues (or 'double billing') by the operator."[5/] In fact, however, it is extremely unlikely that the amount that the cable operator receives from subscribers for carrying the leased access channel will constitute a *double* recovery; in most cases, that additional amount will be close to or equal to zero. For purposes of calculating the implicit fee paid by each channel on a tier, the Commission's current formula assumes that the amount paid by subscribers is the same for each channel on the tier — specifically, the total price for the tier divided by the number of channels. But, in fact, subscribers do not value all channels equally and services do not all receive equal amounts in subscriber fees from cable operators. Some services receive substantial per-subscriber payments from operators; others receive nothing at all. The value of leased access programming to subscribers is likely to be significantly lower than the average per-channel price for the tier on which it is carried; it may be nothing at all. This is, after all, programming that the operator has chosen for marketing reasons not to pay for and not to carry, even at no charge.

Therefore, while it is likely that a channel selected by the operator on the basis of consumer demand might add value to the tier (and therefore might generate immediate or future subscriber revenues), adding or substituting a leased access channel is unlikely to have such an effect. Neither the leased access programmer nor the operator recovers subscriber fees when leased programming is included on a tier — because subscribers simply do not pay

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5/ *Further Notice* at ¶ 29

any incremental fee for such programming. The implicit fee formula is intended to compensate cable operators for the foregone implicit access fees that they might have received from entering into carriage agreements with programmers of their choice. But while *those* programmers might, in a leased access environment, be able to recover an equivalent amount from subscribers, it is extremely doubtful that *other* leased access programmers could. Thus, it is reasonable to assume that the amount of tier subscriber fees attributable to leased access programmers that opt to be included on *tiers* — and therefore the alleged magnitude of the "double recovery" — is *de minimis*.

B. It is Reasonable to Allow Cable Operators to Charge the *Highest* Implicit Fee.

The Commission also is concerned that allowing operators to charge the *highest* implicit access fee from individual leased access programmers overcompensates cable operators because, by definition, operators are "accepting less than the highest implicit fee from many non-leased access programmers."[6] According to the Commission, this means that the highest implicit fee "is likely to overcompensate the operator compared to the amount the operator is *willing to accept*."[7] The Commission is correct that operators are often "willing to accept" less than the highest implicit fee from a programmer that it *chooses* to carry — but this does not necessarily mean that operators should be *required* to accept less from individual leased access programmers.

6/ *Id.* at ¶ 30.

7/ *Id.* (emphasis added).

Cable operators typically receive benefits from carrying programmers of their choice, in addition to any implicit fees that they receive — benefits that may not accrue from the carriage of leased access programming. For example, operators often receive local advertising availabilities from cable programmers and may accept less than the highest implicit fee from programmers that offer such availabilities. They generally receive no such advertising availabilities and revenues from leased access programmers.

Moreover, cable operators typically select programming that appeals to diverse audiences to maximize their subscribership and their advertising revenues. They may accept less than the highest implicit fee from a programmer that appeals to an unserved niche audience and complements their existing offerings. Leased access programmers, however, need not be concerned with the effect that their service may have on the system's subscriber penetration, its rates, or its advertising revenues.

In addition, cable operators may be willing to accept less than the highest implicit fee from services that are not yet profitable and have not yet attracted significant viewership but are expected to blossom into popular, high-quality services. Leased access program services are not subject to any such editorial expertise and judgment. Indeed, one of Congress' primary goals in adopting leased access was to "separate[] editorial control over a limited number of cable channels from ownership of the cable system itself."[8/] Cable operators certainly would factor this inability to exert editorial control over leased access channels into the fee they would be willing to accept from leased access programmers.

8/ H.R. Rep. No. 934, 98th Cong., 2d Sess. 31 (1984) ("House Report").

For these reasons, it is not at all unreasonable to permit cable operators to charge leased access programmers up to the highest implicit fee that they receive from non-leased access programmers. The highest implicit fee is intended to approximate the marketplace value of a channel to cable operators. It is also intended to approximate the marketplace value of a channel to leased access programmers that do not supply operators with the benefits that operators typically receive from other programmers on their systems. This marketplace approach is preferable to the proposed cost-based approach, because it takes into account the opportunity costs that the cost-based approach and distinguishes among premium per-channel services, shopping services, and tiered services in a manner that reflects the different economics of the three types of services

C. The Method of Calculating Implicit Fees Should be Revised to Better Reflect the Marketplace Value of Leased Access Channels.

The implicit access fee for each channel is the amount that the operator charges subscribers for a channel minus the amount that the operator pays the programmer for the service. For tiered services, it is impossible to determine exactly how much subscribers pay for each channel.[9/] To deal with this uncertainty, the Commission's formula simply assumes that all subscribers pay the same rate for each channel, based on the average per channel price for the tier, instead of apportioning the total price for the tier among the various channels.

9/ It is clearly not the case that all subscribers value all channels on the tier equally — some may be more valuable to all subscribers than others and others may be extremely valuable to some subscribers and not at all valuable to others.

But no such averaging is required to determine what cable operators pay for the programming on each tiered channel. It is not difficult to determine the actual amounts that operators pay programmers for their services, and these actual amounts are used to determine each channel's implicit fee. This comparison of *average* per-channel revenues with *actual* per-channel costs distorts the use of the highest implicit fee to determine reasonable leased access rates.

For example, under the current approach, the highest implicit fee will always be the fee associated with programming for which the cable operator pays nothing; *i.e.*, the average per-channel charge for the tier (minus the amount that the operator pays for the programming, which is zero). But the actual implicit fees for some services for which operators *pay nothing* — if they could be measured accurately — may be very low because their value to subscribers may be less than the average per-channel price for the tier. On the other hand, the actual implicit fees for services for which operators *pay high licensing fees* may in some cases be higher than the actual implicit fees for services for which they pay nothing — because the value of this high-cost programming to subscribers is very high.

Thus, comparing the *average* per-channel cost to subscribers with the *actual* cost of each channel's programming does not yield a result that reflects either the actual value of each channel or the average value of all channels to cable operators and programmers. A more reasonable and principled approach is to calculate the implicit fee for channels on a tier by comparing the *average* per-channel cost to subscribers with the *average* cost of the

programming on the tier. This will produce a rate that accurately reflects the average amount by which subscriber fees for a tier exceed programming costs.[10/]

II. THE PROPOSED COST-BASED APPROACH FAILS TO FULFILL THE STATUTORY DIRECTIVE THAT LEASED ACCESS NOT ADVERSELY AFFECT THE FINANCIAL CONDITION OF CABLE OPERATORS.

The Commission has tentatively concluded that the objective in establishing maximum reasonable rates for leased access should be to "promote the use of the leased access set-aside channels without imposing an undue financial burden on the operator [and] without giving programmers a subsidy."[11/] Indeed, Congress did not intend leased access to impose *any* financial burden on the operator, much less an "undue" burden. Thus, cable operators are to establish prices, terms and conditions for leased access that are "at least sufficient to assure that such use *will not adversely affect the operation, financial condition, or market development* of the cable system."[12/] A rate that enables cable operators to recover all the costs associated with making a channel available to a leased access programmer, plus a reasonable profit, would accomplish this objective. But the Commission's cost-based approach would not establish such a rate. It would instead produce maximum reasonable

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10/ For the reasons previously discussed, this average amount may not adequately compensate cable operators for leased access, since leased access programmers do not provide cable operators with all the benefits that operator-selected program services provide and may, indeed, impose costs on the system. Therefore, operators should be permitted to impose a reasonable surcharge on this implicit fee to account for such costs.

11/ *Further Notice* at ¶ 65.

12/ 47 U.S.C. § 532(c)(1) (emphasis added).

rates that *do* unduly burden cable operators and that result in unfair subsidies to leased access programmers.

A. The Proposed Approach is Administratively Burdensome and Undercompensates Cable Operators for the Costs of Leased Access.

The proposed approach recognizes only two types of costs incurred by cable operators in making capacity available to leased access programmers — "operating costs" and "net opportunity costs."

With regard to "*net opportunity costs*," the *Notice* acknowledges that the proposed formula "does not incorporate all opportunity costs."[13/] That is an understatement; in fact, the formula ignores *most* of the opportunity costs associated with leased access, because they are supposedly "speculative"[14/] and "not easily quantified."[15/]

The only opportunity costs that the proposed formula recognizes are the costs associated with the *particular channel* on which the leased access programming is to be placed. Thus, if an operator bumps a service from which it received advertising revenues to make room for a leased access service, the foregone advertising revenues would be viewed as an opportunity cost. Similarly, if an operator bumps a shopping service that pays sales commissions to the operator, any foregone commissions would be counted as an opportunity cost. On the other hand, any licensing fees that the operator had been required to pay for

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13/ *Id.*

14/ *Id.* at ¶ 86.

15/ *Id.* at ¶ 79. The fact that the Commission acknowledges that certain costs are not recovered under the proposed formula raises serious constitutional takings issues. *See Federal Power Comm'n v. Hope Natural Gas Co.*, 320 U.S. 591 (1944); *Bluefield Water Works and Improvement Co. v. Public Serv. Comm'n*, 262 U.S. 679 (1923).

the bumped service would constitute a negative opportunity cost — a cost savings that would offset any foregone advertising revenues.

But the economic effects of adding or substituting a leased access service on a tier cannot be measured simply by calculating the foregone revenues, commissions and licensing fees associated with the previous use of the channel. Unless the leased access programming is as valuable to subscribers as the programming that it replaces, the system's subscriber revenues will be adversely affected. Either the system will reduce its rates to reflect the diminished value to subscribers, or it will lose subscribers. The Commission acknowledges that this could occur but refuses to take any such effect into account in its cost formula because it "is too speculative to measure accurately."[16/]

While it may be difficult to quantify the precise effects of replacing a tiered service selected by the operator with a leased access service, there is no doubt that there will be such effects — and that they will be substantial. As the Commission and the courts have repeatedly recognized, selecting and packaging programming is the core activity of the business of cable television and is widely believed to be instrumental in maintaining and attracting subscribership.[17/] Moreover, whether or not the leased access service is as valuable to subscribers as the service it replaces, dropping *any* service from a tier invariably

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16/ *Id.* at ¶ 86.

17/ *See, e.g., City of Los Angeles v. Preferred Communications*, 476 U.S. 488, 494 (1986); *Leathers v. Medlock*, 499 U.S. 439, 444 (1991).

causes dissatisfaction among some subscribers — and there are costs associated with dealing with and attempting to minimize the extent of this dissatisfaction.[18/]

Furthermore, to the extent that the leased access programming is at all valuable to subscribers and attracts any significant viewership, the cable operator's opportunity costs will not be limited to any foregone revenues from the service that the leased access programming *replaces*. If such programming diverts viewership from other services on the system, it may diminish any advertising revenues or shopping commissions that the operator derives from those services. In addition, to the extent that such diminished viewership reduces the potential advertising revenues of the programming services, they may insist on recovering more from the operator in subscriber fees — that is, they may increase their licensing fees to the operator.

The proposed cost formula accounts for none of these costs, and therefore the formula is virtually certain to under-compensate cable operators. And, contrary to the Commission's objectives, it will surely subsidize certain programmers. By focusing solely on the costs and foregone revenues associated with the particular programming that is replaced by a leased access programmer, the formula establishes the same maximum reasonable rate regardless of the type of leased access programmer that may use the channel.

Suppose, for example, that an operator bumps a new, struggling tiered service that produces very little advertising revenues for either the programmer or the system. And suppose that the channel is then used by a leased access programmer to provide either a

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18/ In Cox's experience, system managers are often inundated with complaints from subscribers for removing even their least-watched programming.

tiered sports service that generates substantial advertising revenues or a premium movie channel that produces substantial subscriber fees. Under the proposed formula, the operator could not establish a leased access rate that accounts for these additional advertising revenues or subscriber fees — and this could give the leased access programmer a windfall and competitive advantage over similar programmers carried on the system. Services that attract substantial advertising often share potential advertising revenues with the cable operator by providing the operator with local advertising availabilities. And premium services typically split subscriber fees with the operator; the operator might, for example, collect $10 per subscriber per month for a movie service and pay the programmer half that amount. The leased access programmer, however, would not share any of these advertising revenues or subscriber fees with the operator. In these circumstances, the leased access programmer could underprice its competitors in the sale of advertising or in the sale of programming to subscribers, or it could use its windfall to spend more on its product than its competitors

Another example further illustrates the impracticality and unreasonableness of the proposed cost formula. Cable operators pay the steepest licensing fees for the tiered channels that are most valuable to subscribers In some cases, those licensing fees exceed the average per-channel subscriber fee attributable to that channel under the proposed cost formula. Therefore, the cost formula would suggest that cable operators would sustain a *net benefit* (reflected by a negative opportunity cost) by bumping one of its most popular — and correspondingly, most expensive — programming services, such as ESPN or CNN. The formula would suggest that a cable operator should *pay a leased access programmer* for the privilege of bumping a system's most popular programming services. Of course, no rational

cable operator would replace ESPN or CNN with a leased access programmer, because cable operators — unlike the flawed cost formula — take into consideration the effect of those services upon subscriber penetration and upon subscriber goodwill.

When applied to actual figures from cable systems, the proposed cost formula produces anomalous rates. The following chart compares the maximum monthly rates established by the current implicit fee formula and the proposed cost-based formula in several Cox cable systems.

System	Subscribers	Implicit Fee Rate (per channel)	Cost Formula Rate (per channel)
Myrtle Beach, SC	40,000	$4,188	($1,579)
Hampton Roads, VA	200,000	$87,174	($771)
San Diego, CA	330,000	$140,000	($61,464)

As the chart illustrates, the cost formula suggests that a *negative* monthly leased access rate would be appropriate for all three systems. Clearly, these rates are unreasonable, and, if part-time rates are prorated, the new formula would require Cox to provide access at nominal (or even *negative*) rates.

Establishing reasonable rates for leased access requires far more than a simple balancing of the costs incurred and revenues received by an operator in connection with the previous use of the particular channel designated for leased access. To replicate or even approximate the terms and conditions entered into by operators and programmers in the video programming marketplace also requires taking into account the content and economics of the leased access programmer, as well as that programmer's effect on the economics of the

system as a whole. As noted above, Congress *expected* the cable operator to take such matters into account in establishing reasonable rates.[19/]

Any formula aimed at identifying all the costs incurred by an operator in making a leased access channel available would have to consider all these matters — and Congress did not expect the Commission to impose such a complicated cost-based ratemaking. Congress specifically prohibited the Commission from requiring cable operators to lease channels on a common carrier basis[20/] (unless "cable systems with 36 or more activated channels are available to 70 percent of households within the United States and are subscribed to by 70 percent of the households to which such systems are available").[21/] And, in any event, any effort to identify and quantify all such costs in a formulaic manner would be impossible.

Instead of seeking to set cost-based rates, a more fruitful approach would be to establish maximum reasonable rates by examining the rates, terms and conditions of channel use in the video programming marketplace. That is precisely what an "implicit fee" approach does. An implicit fee formula for full-time leasing modified in the manner Cox proposes — to compare *average* per-channel programming costs with average per-channel

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19/ *See* 47 U.S.C. § 532(c)(1), *supra*. *See also* 47 U.S.C. § 532(c)(2) ("A cable operator shall not exercise any editorial control over any video programming provided pursuant to this section, or in any other way consider the content of such programming, *except that an operator may consider such content to the minimum extent necessary to establish a reasonable price* for the commercial use of designated channel capacity by an unaffiliated person.") (emphasis added).

20/ *See* 47 U.S.C. § 541(c).

21/ 47 U.S.C. § 532(g).

subscriber fees — would work far better as a surrogate for marketplace rates than would the Commission's cost-based formula.

B. The Commission Cannot Require Cable Operators to Identify in Advance the Channels to be Used for Leased Access.

To derive a leased access rate under the proposed cost-based formula, operators will be required to designate the channels which may be used for leased access, should such requests arise.[22/] Therefore, the Commission proposes to require operators to select enough channels to satisfy the leased access set-aside amount, and to identify these channels in the systems' public files.[23/] However the language of the Communications Act prohibits the Commission from imposing these requirements. Additionally, such a designation would financially harm operators because potential programmers and competitors would be able to review this information in systems' public files.

First, the Communications Act states that an operator may establish the price, terms, and conditions of leased access use only "[i]f a person unaffiliated with the cable operator seeks to use channel capacity . . . ."[24/] The statute does not authorize the Commission to require that cable operators establish specific prices, terms, and conditions of use, in the form of published rates and specific channel set-asides, prior to receipt of a leased access request.

22/ *Id.* at ¶ 76.

23/ *Id.*

24/ 47 U.S.C. § 532(c)(1).

The Commission's channel designation proposal is inconsistent with existing law because it would "adversely affect the operation, financial condition, or market development of the cable system."[25/] Section 612(c)(1) of the Communications Act specifically prohibits the price, terms and conditions of leased access from creating these types of hardships for cable operators.[26/] If operators were required to designate and disclose certain channels that may be used for leased access purposes in the future, negotiations with non-leased access programmers for use of these channels would be affected. Programmers would insist on more favorable terms for use of these channels than for channels which are not designated for leased access use. Even if no leased access programmer requested the use of these channels, operators would still be forced to accept less favorable terms from non-leased access users of these channels.

Second, adoption of a specific channel designation rule also would render operators unable to respond to customer demand in programming Operators' choices of what channels to use or what existing programming to bump could depend upon the type of programming to be placed on a leased access channel. Operators might want to bump similar programming, even if this programming were not located on a designated leased access channel, to avoid having duplicative programming on their systems Rigid adherence to previously designated leased access channels would limit cable operators' abilities to make business decisions regarding their systems and would hamper their ability to compete with other sources of programming.

25/ *Id.*

26/ *Id.*

Operators would be adversely affected by the forced disclosure of their business plans. If operators must designate specific channels for leased access use and make this information public, other competing multichannel video programming distributors would gain access to this confidential business information. Competitors would be able to determine which channels are designated for leased access use and what programming is currently carried on these channels and could use such information to their advantage.[27/] The statute does not authorize the Commission to adopt procedures that would harm the operation of cable systems' business in this manner, and it would not, in any event, be in the public interest to do so.

The Commission also seeks comment on its proposal to restrict operators from designating their highest valued channels to inflate the leased access maximum rate.[28/] As a practical matter, cable operators would not be willing to designate and take the risk of having to bump their most valued services for leased access programming, which has little or no value to subscribers. Any loss in subscriber penetration and goodwill could not be recovered through any charge to the leased access programmer. Customers would take their business elsewhere rather than subscribe to a cable system with no valued programming. Operators would lose much more than they would gain by employing this tactic.

27/ For example, a competing MMDS operator could add programming that a cable operator bumps to attract subscribers. The MMDS operators also could lease a channel from the operator to advertise its services and, perhaps, require the operator to bump programming that the MMDS operator will carry to lure subscribers.

28/ *Further Notice* at ¶ 76.

III. PART-TIME LEASED ACCESS RATES CURRENTLY ARE TOO LOW AND MUST BE HIGHER THAN THE RATES FOR FULL-TIME LEASED ACCESS.

The Commission has concluded, for purposes of its current "highest implicit fee" approach, that "proration of the maximum rate with time of day pricing is an appropriate method for establishing *part-time* rates."[29/] It seeks comment on whether such a method would also be appropriate under the proposed cost formula. Even under the current approach, proration of maximum full-time rates is the wrong way to establish reasonable rates for part-time leasing of channels. Using such proration under the proposed cost formula, which would lower part-time rates even further, would be especially inappropriate.

The notion that part-time rates should be set so that, if all time is leased, the operator's total revenues will be no greater than the rate for full-time lessees does not reflect the additional costs inherent in providing part-time leased access *i.e.*, the "break-up value" of a full-time channel. Simply in terms of the costs imposed upon cable operators, it seems obvious that part-time rates should be substantially *higher* than the prorated rates for full-time use.

First, part-time programming substantially increases the transactional costs of leased access. Instead of negotiating with a single programmer to lease all 24 hours of programming on a channel, cable operators must reach separate leased access agreements with a number of programmers who wish to use only a portion of the available time. Negotiating costs are increased further by the need to coordinate among the various part-time programmers to ensure that their programming time slots do not overlap. The costs of

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29/ *Further Notice* at ¶ 102 (emphasis added).