

company A's horizontal share under the rules would not be 25% but would be 22%.<sup>145</sup> Bell Atlantic argued that horizontal ownership limits are only required to combat the local monopoly and "gatekeeper" power of cable systems, so that the justification for these limits disappear where local distribution markets are competitive.<sup>146</sup>

61. Bell Atlantic argued that subjecting systems under "effective competition" to the horizontal ownership limits will harm competition in the industry. Bell Atlantic contends that, in exempting competitive markets from rate regulation, Congress recognized that competition eliminates the ability of cable operators in those markets to exercise market power and that continued regulatory constraints hinder flexibility in those markets. According to Bell Atlantic, Congress found that cable operators' ability to exercise market power arises from lack of competition in local service areas. As a result, Bell Atlantic asserts, national market power over programmers is diminished by the presence of competition at the local level.<sup>147</sup>

62. CME/CFA argued that Bell Atlantic's argument ignores Congress' well-founded concern that MSOs exercise market power at the national level by dint of sheer size.<sup>148</sup> Congress did not provide an "effective competition" exception here, as it did for rates in Section 3 of the 1992 Cable Act, indicating that Congress did not intend such an exception.<sup>149</sup> CME/CFA noted that Bell Atlantic provides no evidence that the presence of local competition diminishes the incentive or ability of cable operators to favor affiliated programmers and disfavor independents.<sup>150</sup> CME/CFA argued that it is not clear how sporadic local competition seriously undermines the power which flows from "being able to provide ready-made subscriber levels."<sup>151</sup> CME/CFA also pointed out that, because years and "billions of dollars" were required before VDT was to become operational, VDT systems at that time could not compete with cable or offer independent programmers a viable alternative to delivery by cable.<sup>152</sup> Since broadcasters are subject to analogous limits despite vigorous competition from local stations, CME/CFA stated that there

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<sup>145</sup>To see how this result is reached, assume that 100 million homes are passed nationally, and cable company A serves 25 million of these. If 10% of the nation were in "competitive" markets, the number of households not subject to competition would be 90 million. Cable company A serves 20 million of these, resulting in a percentage of 20/90 or 22%.

<sup>146</sup>*Id.* at 2-5.

<sup>147</sup>*Id.* at 1-3, 4-6.

<sup>148</sup>CME/CFA Opposition to Bell Atlantic Petition at 3.

<sup>149</sup>*Id.*

<sup>150</sup>*Id.* at 4.

<sup>151</sup>*Id.* at 6-7.

<sup>152</sup>*Id.* at 5.

is no reason for making local competition a basis for dropping the horizontal ownership limits on MSOs.<sup>153</sup>

63. Bell Atlantic responded to the CME/CFA opposition by stressing that it was not asking the Commission to eliminate the ownership limits where only a "theoretical" possibility of competition exists. Instead, Bell Atlantic argued, it simply proposed that these limits not apply where actual head-to-head competition exists. Where competition exists, according to Bell Atlantic, distributors have strong incentives to ensure that consumers obtain the programming they value, regardless of source. The only effect of applying these limits in competitive markets, Bell Atlantic contended, would be to prevent established companies from invading each others' territories and to inhibit entry by those companies that are best equipped to compete with existing MSOs.<sup>154</sup>

#### b. Discussion

64. We agree with Bell Atlantic that the concern that cable operators may "unfairly imped[e] . . . the flow of video programming from the video programmer to the consumer"<sup>155</sup> will be reduced when there is sufficient competition at the local distribution level. If there is sufficient local distribution competition, the local cable operator will no longer be a "gatekeeper" over that particular audience and video programmers would have alternative means to reach that audience.<sup>156</sup> We disagree with Bell Atlantic's conclusion that horizontal ownership limits are only required to combat the local monopoly of cable systems, so that the justification for these limits disappears where there is sufficient local competition to satisfy the "effective competition" standard applicable to rate deregulation.

65. A level of competition sufficient to support rate deregulation is not necessarily sufficient to address the public policy objectives of the horizontal ownership rules. As we observed in the *First Order on Reconsideration* in rejecting Bell Atlantic's similar argument in the context of channel occupancy limits, "the effective competition standard was not adopted for this specific purpose and [] it is not clear that the presence of effective competition for any cable system will address all of the relevant concerns that Congress expressed in enacting Section 11 of the 1992 Cable Act."<sup>157</sup> As an example, we noted that, if both the cable system and the competing MVPD are vertically integrated, unaffiliated programming services may continue to be denied access from either outlet, thus frustrating the diversity and competition objectives of the 1992 Act.<sup>158</sup> We agree with CME/CFA that, had Congress intended to eliminate all cable regulations where systems face effective competition, the effective competition

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<sup>153</sup>*Id.* at 8-9.

<sup>154</sup>Bell Atlantic Reply at 1-3.

<sup>155</sup>47 U.S.C. § 533(f)(2)(A).

<sup>156</sup>See *Second Report and Order* at ¶ 29.

<sup>157</sup>*First Order on Reconsideration* at ¶ 47.

<sup>158</sup>*Id.*

exemption would have been drawn much more broadly. Instead, the exemption is expressly limited to rate regulation; nowhere in either its language or legislative history does it state that the presence of head-to-head local distribution competition will render the horizontal ownership rules unnecessary.<sup>159</sup>

66. The "effective competition" standard determines when there is sufficient local competition to prevent an incumbent cable operator from exercising market power in setting local rates for cable services sold to local subscribers. In contrast, the horizontal ownership limit was designed to ensure that no cable MSO acquires a sufficiently large share of subscribers nationwide to exercise undue market power at the national level in its purchase of programming from networks, which generally sell their programming nationwide.<sup>160</sup> In the *Second Report and Order*, the Commission rejected an argument similar to that of Bell Atlantic, stating: "The presence of effective competition in any given system or group of systems does not, however, directly respond to Congress' concern about the exercise of undue control by a single entity at the national level."<sup>161</sup> We reaffirm that decision today. We will not assume that, in their bargaining, programming networks and cable MSOs do not consider an MSO's total subscribership, but only its subscribers in areas not subject to "effective competition." There may be grounds for revising the 30% horizontal ownership limit, however, as more systems become subject to effective competition.

### 3. Attribution Rules

#### a. Background

67. CME/CFA asked that the Commission tighten its attribution rules by eliminating the single majority shareholder exception, which provides that minority interests will not be attributed where a single shareholder owns more than 50% of the outstanding voting stock.<sup>162</sup> CME/CFA argued that this exception to the attribution rules is "unduly mechanistic" and ignores the minority shareholder's "ability to influence the actual operation of the property" even when a majority shareholder is present. CME/CFA posited that there are situations where a single majority shareholder may be forced to accommodate minority shareholders.

68. Responding to the CME/CFA proposal, NCTA noted that the attribution rules address the ability of an MSO to influence in a meaningful way the programming decisions of an individual cable system. NCTA argued that the single majority shareholder exception appropriately recognizes that the

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<sup>159</sup>*Id.* at ¶ 48.

<sup>160</sup>*See Second Report and Order* at ¶ 29; *see also* 47 U.S.C. §§ 533(f)(2)(A), (B) & (C).

<sup>161</sup>*Id.*

<sup>162</sup>CME/CFA Petition at 22-23 (incorporating by reference CFA's September 1993 Reply Comments at 4-5).

influence of non-majority shareholders is significantly attenuated when a majority shareholder exists, such that attribution is not required.<sup>163</sup>

**b. Discussion**

69. In the *Second Report and Order*, the Commission adopted the broadcast attribution rules, which contain the single majority shareholder exception,<sup>164</sup> in the cable horizontal ownership context because "the objectives of the broadcast attribution model are consistent with our goals in establishing ownership standards for subscriber limits."<sup>165</sup> The Commission explicitly stated that the broadcast rules "focus on ownership thresholds that enable a broadcast licensee to influence or control management or programming decisions" and that "these same issues are also relevant to addressing the concerns at issue in this proceeding relating to the ability of cable operators to unduly influence the programming marketplace."<sup>166</sup>

70. The Commission does not believe there is enough evidence in this docket to justify reversing our prior opinion that, in single majority shareholder situations, ownership of minority voting stock alone is unlikely to grant sufficient "influence" over programming decisions to warrant attribution. The single majority shareholder provision of the rules is currently under review in the broadcast context in MM Docket Nos. 94-150, 92-51 and 87-154.<sup>167</sup> In that proceeding, the Commission sought comment on the nature of "influence" and "control" and the connection between equity ownership and such influence and control. The Commission is also issuing a Notice of Proposed Rulemaking seeking comment on whether and how the cable attribution rules should be revised. Given the paucity of information in this proceeding from which to make an informed decision as to the need for changes in the attribution standards, that appears to be the preferable course.

71. This determination regarding the cable attribution rules applies to both our horizontal ownership rules and channel occupancy limits. As we noted in the *First Order on Reconsideration*,<sup>168</sup> that

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<sup>163</sup>NCTA Opposition at 15-16.

<sup>164</sup>47 C.F.R. § 73.3555 n. 2(b).

<sup>165</sup>*Second Report and Order* at ¶ 35.

<sup>166</sup>*Id.* at ¶ 35.

<sup>167</sup>See *Notice of Proposed Rulemaking, In the Matter of Implementation of the Cable Television Consumer Protection and Competition Act of 1992, Review of the Commission's Cable Attribution Rules*, MM Docket Nos. 94-150, 92-51 and 87-154, FCC 94-324, 10 FCC Rcd 3606 (1995); *Further Notice of Proposed Rule Making, In the Matter of Implementation of the Cable Television Consumer Protection and Competition Act of 1992, Review of the Commission's Cable Attribution Rules*, MM Docket Nos. 94-150, 92-51 and 87-154, FCC 96-436, 11 FCC Rcd 19895 (1996).

<sup>168</sup>*Memorandum Opinion and Order on Reconsideration of the Second Report and Order* in MM Docket 92-264, FCC 95-147, 10 FCC Rcd 7364, n. 3 (1995).

order addressed the issues on reconsideration regarding our cable channel occupancy limits, but left issues concerning the cable attribution standard for the current proceeding.

#### IV. MOTION TO LIFT STAY

##### a. Background

72. In the *Second Report and Order*, the Commission voluntarily stayed the effective date of the cable horizontal ownership rules pending final judicial resolution of the District Court decision in *Daniels* that the underlying statute violates the First Amendment.<sup>169</sup> While the *Daniels* Court had stayed further District Court proceedings pending interlocutory appeal of its judgment, it had not enjoined the Commission from adopting and enforcing horizontal ownership rules under the statute.<sup>170</sup> CME/CFA filed a motion to lift the Commission's voluntary stay, which was opposed by NCTA.<sup>171</sup>

73. CME/CFA argued that, because the *Daniels* Court elected to stay further District Court proceedings pending appeal, the Commission's stay "cancels out the Court's stay, resulting in a situation where there are no regulations controlling the growth of cable systems while the constitutionality of the limits is being appealed."<sup>172</sup> As a result, CME/CFA argued, while stays are generally granted to preserve the status quo, the Commission's stay does not preserve the status quo.<sup>173</sup> CME/CFA further argued: (1) that the Commission and the United States are likely to prevail on the merits on appeal;<sup>174</sup> (2) that lifting the stay during the litigation will not result in irreparable harm to cable operators because the current rule still allows expansion for all cable systems and only causes "a temporary inability to expand beyond the 30% limit;"<sup>175</sup> (3) that continuance of the stay could result in harm to video programmers and the public;<sup>176</sup> and (4) that the public interest in "achieving competition and diversity in the cable television marketplace" requires that the rules be enforced while the constitutionality of the limits are under review.<sup>177</sup>

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<sup>169</sup>*Second Report and Order* at ¶ 109.

<sup>170</sup>*Daniels*, 835 F.Supp. at 12.

<sup>171</sup>CME/CFA Motion to Lift Stay; NCTA Opposition to Motion to Lift Stay.

<sup>172</sup>CME/CFA Motion to Lift Stay at 1-2.

<sup>173</sup>*Id.* at 2.

<sup>174</sup>*Id.* at 2-4.

<sup>175</sup>*Id.* at 4.

<sup>176</sup>*Id.* at 4-6.

<sup>177</sup>*Id.* at 6.

74. In its opposition, NCTA argued that the case for a stay is one of "surpassing strength." NCTA stated: (1) that it is "far from clear" that the cable horizontal ownership limits will be upheld; (2) that "irreparable injury will result if cable systems are prevented from lawfully expanding their operations;" (3) that continuance of the stay during the litigation will not harm other interested parties, such as video programmers and the public; and (4) that the public interest favors the stay because the stay avoids "potential confusion and uncertainty during the period of judicial review."<sup>178</sup>

**b. Discussion**

75. In August 1996, the D.C. Circuit Court consolidated the *Daniels* appeal regarding the facial validity of the statute and the *Time Warner* challenge to the Commission's rules, and determined to hold court proceedings in abeyance while the Commission reconsidered the horizontal rules.<sup>179</sup> In light of the continuing pendency of the judicial proceedings relating to the underlying provision, we will retain the voluntary stay of the 30% horizontal ownership limit at this time.<sup>180</sup> That decision has been appealed and the Commission has argued that the provision in question is indeed constitutional.

76. In order to facilitate monitoring of MSOs' ownership interests, we will lift the stay insofar as it applies to the information submission provisions of 47 C.F.R. § 76.503(c) that are applicable when any person or entity holding an attributable interest in cable systems reaching 20% or more of homes passed nationwide acquires additional cable systems. The existing rules require a certification that no violation of the 30% limit will occur as a result of such acquisition. In light of the continuation of the stay, however, the certification should only specify the incremental change the acquisition makes in terms of the 30% of household passed standard, i.e. specifying the ownership in terms of homes passed before and after the acquisition is complete.

77. Affected parties will be required to come into compliance with the horizontal ownership rules within 60 days of the appellate court's issue of a mandate upholding Section 613(f)(1)(a) and the rules, unless the Commission determines as part of this ongoing proceeding to lift the stay at an earlier date. Interested parties, including in particular parties that are now entering into business arrangements that would violate the rules but for the existence of the stay, should be well aware of the existence of the rules and thus have a full opportunity to be prepared to comply with them.

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<sup>178</sup>NCTA Opposition to Motion to Lift Stay at 3.

<sup>179</sup>*Time Warner*, 93 F.3d at 979-80.

<sup>180</sup>Consumers Union/CFA filed a petition for rulemaking on September 23, 1997, requesting, among other things, that the Commission lift its voluntary stay. *Petition to Update Cable Television Regulations and Freeze Existing Cable Television Rates*, RM-9167, MM Docket Nos. 92-264, 92-265, 92-266, at 14-15 (filed Sept. 23, 1997) ("CU/CFA Petition for Rulemaking"). This *Second Order on Reconsideration* denies that particular request.

## V. FURTHER NOTICE OF PROPOSED RULEMAKING

78. We stated in the *Second Report and Order*, adopting the rules in question in this proceeding, that

we plan to review subscriber limits every five years to determine whether such limits are reasonable under the prevailing market conditions and whether such limits continue to serve the objectives for which they were adopted. We regard such periodic review as an important means of addressing Congress' intent that such rules reflect the "dynamic nature of the communications marketplace."<sup>181</sup>

The rules in question were adopted in 1993, and it is appropriate that we undertake this review to address intervening changes in the communications marketplace. We seek comment on whether 30% remains the appropriate horizontal ownership limit in light of evolving market conditions. In addition, the current rules allow ownership of additional cable systems reaching up to 35% of cable homes passed, provided such additional cable systems are minority-controlled.<sup>182</sup> The purpose of the minority-control allowance was to encourage diversity of viewpoints by fostering increased minority participation and ownership in the cable industry, through increased MSO investment in minority-owned cable systems.<sup>183</sup> Recognizing that the minority-control allowance has never been utilized by any MSO, we seek comment on the effectiveness of this rule and on the development of alternative rules to serve our purpose of promoting minority participation. We also recognize that, since this rule was adopted, the Supreme Court issued *Adarand Constructors, Inc. v. Peña*, 515 U.S. 200 (1995). We seek comment on the constitutionality of the minority-control allowance in light of that decision. We also seek comment on how we can develop our policies consistent with the standards set forth in *Adarand*.

79. We also seek comment on two specific issues concerning the method of ownership calculation: (1) whether the rules should consider the presence in the market of all MVPDs rather than cable operators alone, and (2) whether the rules should be based on actual subscriber numbers rather than on homes passed.<sup>184</sup> The rules proposed here would provide that, in calculating a cable MSO's market share, the numerator would consist of the MSO's cable subscribers plus its non-cable MVPD subscribers, and the denominator would consist of the total number of cable subscribers plus non-cable MVPD subscribers nationwide. In addition to these proposed rule changes, we seek comment as to whether the method of ownership calculation should be modified in some way to support cable overbuild competition.

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<sup>181</sup>*Second Report and Order* at ¶ 40 (citing 47 U.S.C. § 533(f)(2)(E)).

<sup>182</sup> 47 C.F.R. § 76.503(b).

<sup>183</sup> *Second Report and Order* at ¶ 28.

<sup>184</sup>The Commission also has issued a *Notice of Proposed Rulemaking, In the Matter of Streamlining of the Commission's Rules for the Direct Broadcast Satellite Service*, FCC 98-26, IB Docket No. 98-21 (rel. Feb. 26, 1998), requesting comment as to whether limitations on cable/DBS cross-ownership are necessary to address horizontal concentration in the MVPD market.

80. The MVPD market has continued to evolve since our adoption of the horizontal ownership rules. The *1997 Competition Report* noted the growth of MVPDs other than cable operators and suggested that a true measure of horizontal concentration ought to take into account all MVPDs and MVPD subscribers, rather than cable operators and cable subscribers alone:

[I]n assessing the impact that national concentration may have in the MVPD programming market, we believe that it is appropriate to consider the presence of all MVPDs and MVPD subscribers in national concentration figures, and not just cable MSOs and cable subscribers. As non-cable MVPD subscribership increases, the significance of DBS, MMDS and SMATV operators in the MVPD program purchasing market also increases.<sup>185</sup>

With the growth of alternative MVPDs, network programmers gain alternative avenues for distribution of their products, thus reducing cable operators' market power or influence in the purchase and distribution of network programming. Conversely, just as growth in alternative MVPDs' subscribership can reduce a cable MSO's market power, a cable MSO also can increase its market power by acquiring interests in alternative MVPDs.

81. We seek comment on a proposal to revise the rules to include alternative MVPDs in the measure of horizontal concentration in order to reflect the emergence of competitors to cable in the video marketplace, as well as potential MSO increases in market power through acquisition of interests in other MVPDs. By recognizing the impact of all purchasers of video programming, not just cable operators, this rule revision would provide a more accurate measure of MSOs' market power.

82. We seek comment on whether the proposed revision of the horizontal ownership rules is consistent with the Commission's authority under Section 613 of the Communications Act to "prescribe rules and regulations establishing reasonable limits on the number of cable subscribers a person is authorized to reach through cable systems . . ." <sup>186</sup> This proposal would result in a sliding or adjustable cable horizontal ownership limit, under which the number of subscribers a cable operator is authorized to reach through cable systems would decrease in proportion with any increase in the number of subscribers that entity reaches through other MVPD systems. Conversely, the cable horizontal ownership limit would rise for a cable operator that reaches fewer subscribers through other MVPD systems. The proposed rules would impose no limit on the number of subscribers a cable operator may reach through alternative MVPD systems. These rules also would not apply to persons who have no attributable ownership interests in cable systems. We seek comment on this proposal and on whether it is consistent with the terms of the underlying statute, given Section 613's focus on the cable industry and the establishment of a cable subscribership limit rather than an MVPD subscribership limit.

83. We also seek comment on the possibility of changing the method of calculating the basis of the horizontal ownership limits from potential reach, i.e., number of homes passed, to actual reach, i.e., number of MVPD subscribers served. In the *Second Report and Order*, we stated that the homes passed

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<sup>185</sup> *1997 Competition Report* at ¶ 150.

<sup>186</sup> 47 U.S.C. § 533(f)(1)(A).

standard reflects a cable operator's potential reach and constitutes a more stable basis on which to impose horizontal limits than a subscriber based standard.<sup>187</sup> We also noted some commenters' argument that a subscriber based standard may have the effect of discouraging subscriber growth.<sup>188</sup> In revisiting the horizontal ownership rules, we seek comment on whether the homes passed standard continues to be an accurate measure of horizontal concentration and market power in today's marketplace, and whether the easier to measure subscriber standard can be adapted for use in a fashion that will not require an abrupt halt to the addition of new subscribers to established cable systems.

84. While homes passed reflect the number of subscribers an MVPD has the potential of reaching, the MVPD often secures only a fraction of those potential subscribers. The MVPD typically does not purchase programming for all potential subscribers, only for those subscribers that it actually has. As alternative MVPDs continue to grow in the future, the number of homes passed by a cable operator may become an increasingly inaccurate measure of its actual subscribership and thus of its actual market power. We seek comment on whether the ownership calculation should be based on the number of actual subscribers, rather than homes passed, in order to reflect an MVPD's actual purchasing power.

85. The homes passed standard is also difficult to apply if we revise the horizontal ownership rules to consider all MVPDs in the calculation, since several different MVPDs may pass the same homes. Furthermore, the homes passed standard is a particularly inaccurate measure of market power for a new MVPD whose actual subscribership is only a small fraction of its potential reach in terms of homes passed. For example, under a homes passed standard, each direct to home satellite service provider, no matter how weak or new an entrant, could be deemed to pass virtually all homes in the country and thus be deemed to have far greater market power than an established cable operator passing 30% of homes nationwide. We ask commenters to comment on the best method for counting subscribers, including those residing in multi-dwelling units and commercial subscribers such as hotels, bars, etc.

86. We seek comment on whether the greater accuracy provided by a subscriber based standard outweighs the greater stability provided by a homes passed standard. With regard to the argument that a subscriber based standard may have the effect of discouraging subscriber growth, we seek comment on whether system operators would have a sufficient opportunity to anticipate the approaching limit and to dispose of systems sufficient to stay under the limit rather than to simply cease the addition of new subscribers.

87. We ask commenters to address whether these proposed revisions will serve the public interest objectives that Congress directed the Commission to consider and balance in implementing the horizontal ownership limits, particularly the objectives "to ensure that no cable operator or group of cable operators can unfairly impede the flow of video programming from the programmer to the consumer,"<sup>189</sup>

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<sup>187</sup>*Id.* at ¶ 24.

<sup>188</sup>*Id.* at ¶ 19.

<sup>189</sup>47 U.S.C. § 533(f)(2)(A).

"to ensure that cable operators do not favor affiliated video programmers in determining carriage . . .,"<sup>190</sup> "to take account of the market structure, ownership patterns, and other relationships of the cable industry, including the market power of the local franchise . . .,"<sup>191</sup> and "to make rules and regulations that reflect the dynamic nature of the communications marketplace."<sup>192</sup>

88. We ask commenters to address whether the proposed revisions are consistent with the Commission's legal authority under Section 613 and other provisions of the Act<sup>193</sup> and are reasonable and appropriate given our objectives. We seek comment on whether the proposed horizontal ownership rules would provide a more accurate measure of horizontal concentration and market power than the current rules. We also seek comment on the practical impact of the proposed rule changes on MSO ownership and operation. In particular, we ask that commenters address whether the proposed changes would place any cable MSO in violation of the 30% horizontal ownership limit and to provide specific factual information in support of any such conclusions. We seek comment on whether we should develop special rules to address situations where a cable MSO may exceed the 30% limit as a result of subscriber growth within an existing area of homes passed. We further invite comment on any other matters relevant to our proposals and tentative conclusions.

## VI. INITIAL REGULATORY FLEXIBILITY ANALYSIS

89. As required by Section 603 of the Regulatory Flexibility Act, 5 U.S.C. § 603 ("RFA"), the Commission is incorporating an Initial Regulatory Flexibility Analysis ("IRFA") of the expected impact on small entities of any policies or proposals contained in this *Further Notice of Proposed Rulemaking* ("*Further Notice*"). Written public comments concerning the effect of the proposals in the *Further Notice*, including the IRFA, on small businesses are requested. Comments must be identified as responses to the IRFA and must be filed by the deadlines for the submission of comments in this proceeding. The Secretary shall send a copy of this *Further Notice*, including the IRFA, to the Chief Counsel for Advocacy of the Small Business Administration in accordance with paragraph 603(a) of the Regulatory Flexibility Act.<sup>194</sup> In addition, this *Notice* and IRFA will be published in the Federal Register.<sup>195</sup>

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<sup>190</sup>47 U.S.C. § 533(f)(2)(A).

<sup>191</sup>47 U.S.C. § 533(f)(2)(C).

<sup>192</sup>47 U.S.C. § 533(f)(2)(E).

<sup>193</sup>*See, e.g.*, 47 U.S.C. §§ 151, 154, and 303.

<sup>194</sup> 5 U.S.C. § 603(a).

<sup>195</sup> *See id.*

**A. Need for, and Objectives of, the Proposed Rules**

90. The 1992 Cable Act and subsequent actions to implement it, and Section 11(c) of the 1992 Cable Act in particular, are intended to encourage competition in the cable industry and prevent the exercise of undue market power by large cable multiple systems owners. The Commission issues this *Further Notice* to obtain comment on whether certain aspects of the Commission's horizontal ownership rules should be revised to make them more effective in serving the public interest objectives Congress charged the Commission with protecting in Section 11(c).

**B. Legal Basis**

91. Authority for the actions proposed in this *Further Notice* may be found in Sections 1, 4, 303, and 613 of the Communications Act of 1934, *as amended*, 47 U.S.C. §§ 151, 154, 303, 533.

**C. Description and Estimate of the Number of Small Entities to Which the Proposed Rules Will Apply**

92. The RFA generally defines "small entity" as having the same meaning as the terms "small business," "small organization," and "small governmental jurisdiction" and "the same meaning as the term 'small business concern' under the Small Business Act unless the Commission has developed one or more definitions that are appropriate for its activities.<sup>196</sup> A small business concern is one which: (1) is independently owned and operated; (2) is not dominant in its field of operation; and (3) satisfies any additional criteria established by the Small Business Administration ("SBA").<sup>197</sup> Pursuant to 5 U.S.C. § 601(3), the statutory definition of a small business applies "unless an agency after consultation with the Office of Advocacy of the SBA and after opportunity for public comment, establishes one or more definitions of such term which are appropriate to the activities of the agency and publishes such definition(s) in the Federal Register."<sup>198</sup>

93. The SBA has developed a definition of small entities for cable and other pay television services under Standard Industrial Classification 4841 (SIC 4841), which covers subscription television services, which includes all such companies with annual gross revenues of \$11 million or less.<sup>199</sup> This

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<sup>196</sup> 5 U.S.C. § 601(3) (incorporating by reference the definition of "small business concern" in 15 U.S.C. § 632).

<sup>197</sup> 15 U.S.C. § 632.

<sup>198</sup> While we tentatively believe that the SBA's definition of "small business" greatly overstates the number of cable entities that are small businesses and is not suitable for purposes of determining the impact of any proposals on small cable entities, for purposes of this *Notice*, we utilize the SBA's definition in determining the number of small businesses to which proposed rules would apply. However, we reserve the right to adopt a more suitable definition of "small business" as applied to cable or other entities subject to our rules, and to further consider in the future the number of existing small cable entities.

<sup>199</sup> 13 C.F.R. §121.201.

definition includes cable systems operators, closed circuit television services, direct broadcast satellite services, multipoint distribution systems, satellite master antenna systems and subscription television services. According to the Census Bureau, there were 1,323 such cable and other pay television services generating less than \$11 million in revenue that were in operation for at least one year at the end of 1992.<sup>200</sup>

94. The Commission has developed its own definition of a "small cable company" and "small system" for the purposes of rate regulation. Under the Commission's rules, a "small cable company," is one serving fewer than 400,000 subscribers nationwide.<sup>201</sup> Based on our most recent information, we estimate that there were 1,439 cable companies that qualified as small cable companies at the end of 1995.<sup>202</sup> Since then, some of those companies may have grown to serve over 400,000 subscribers, and others may have been involved in transactions that caused them to be combined with other cable companies. Consequently, we estimate that there are fewer than 1,439 small entity cable companies that may be affected by the proposal adopted in this *Notice*. The Commission's rules also define a "small system," for the purposes of cable rate regulation, as a cable system with 15,000 or fewer subscribers.<sup>203</sup> We do not request nor do we collect information concerning cable systems serving 15,000 or fewer subscribers and thus are unable to estimate at this time the number of small cable systems nationwide.

95. The Communications Act also contains a definition of a "small cable operator," which is "a cable operator that, directly or through an affiliate, serves in the aggregate fewer than 1 percent of all subscribers in the United States and is not affiliated with any entity or entities whose gross annual revenues in the aggregate exceed \$250,000,000."<sup>204</sup> The Commission has determined that there are 61,700,000 subscribers in the United States. Therefore, we found that an operator serving fewer than 617,000 subscribers is deemed a small operator, if its annual revenues, when combined with the total annual revenues of all of its affiliates, do not exceed \$250 million in the aggregate.<sup>205</sup> Based on available

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<sup>200</sup> 1992 Census, *supra*, at Firm Size 1-123. See *Memorandum Opinion and Order and Notice of Proposed Rule Making, Implementation of Sections of the Cable Telecommunications Consumer Protection and Competition Act of 1992, Rate Regulation and Cable Pricing Flexibility*, MM Docket No. 92-266 and CS Docket No. 96-157, 11 FCC Rcd 9517, 9531 (1996).

<sup>201</sup> 47 C.F.R. § 76.901(e). The Commission developed this definition based on its determinations that a small cable company is one with annual revenues of \$100 million or less. *Sixth Report and Order and Eleventh Order on Reconsideration, Implementation of Sections of the 1992 Cable Act: Rate Regulation*, MM Docket Nos. 92-266 & 93-215, 10 FCC Rcd 7393 (1995).

<sup>202</sup> Paul Kagan Associates, Inc., *Cable TV Investor*, Feb. 29, 1996 (based on figures for Dec. 30, 1995).

<sup>203</sup> 47 C.F.R. § 76.901(c).

<sup>204</sup> 47 U.S.C. § 543(m)(2).

<sup>205</sup> 47 C.F.R. § 76.1403(b).

data, we find that the number of cable operators serving 617,000 subscribers or less totals 1,450.<sup>206</sup> Although it seems certain that some of these cable system operators are affiliated with entities whose gross annual revenues exceed \$250,000,000, we are unable at this time to estimate with greater precision the number of cable system operators that would qualify as small cable operators under the definition in the Communications Act. We are likewise unable to estimate the number of these small cable operators that serve 50,000 or fewer subscribers in a franchise area.

#### **D. Description of Projected Recording, Record keeping, and Other Compliance Requirements**

96. If our horizontal ownership rules are changed, the Commission may have to change certain cable reporting requirements. Cable entities also may have to adjust the organization of their business interests in order to comply with any new rules that we may adopt.

#### **E. Steps Taken to Minimize Significant Economic Impact on Small Entities, and Significant Alternatives Considered**

97. The actions proposed in the *Further Notice* are intended to ensure that the Commission's horizontal ownership rules are effective in preventing the exercise of undue market power by large cable multiple systems owners and promote a competitive, diverse and fair marketplace. Accordingly, as discussed in the above descriptions of the proposed rule changes, the approaches proposed in this *Further Notice* should promote fairness and diversity for all cable systems, including the small entities listed above. We invite comments on these approaches, including comment on whether alternative approaches will mitigate any unwarranted expenses incurred by smaller entities by virtue of their size alone.

#### **F. Federal Rules that Overlap, Duplicate or Conflict with the Proposed Rules**

98. None.

### **VII. PAPERWORK REDUCTION ACT**

99. The proposals contained herein in the *Further Notice* have been analyzed with respect to the Paperwork Reduction Act of 1995 (the "1995 Act") and found to impose modified information collection requirements. Implementation of any new or modified requirements will be subject to approval by the Office of Management and Budget ("OMB"). The Commission, as part of its continuing effort to reduce paperwork burdens, invites the general public to take this opportunity to comment on the information collection requirements contained in this *Further Notice*, as required by the 1995 Act. Comments should address: (1) whether the proposed collection of information is necessary for the proper performance of the functions of the Commission, including whether the information shall have practical utility; (2) the accuracy of the Commission's burden estimates; (3) ways to enhance the quality, utility, and clarity of the information collected; and (4) ways to minimize the burden of the collection of

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<sup>206</sup> Paul Kagan Associates, Inc., *Cable TV Investor*, Feb. 29, 1996 (based on figures for Dec. 30, 1995).

information on the respondents, including the use of automated collection techniques or other forms of information technology.

100. Written comments by the public on the modified information collection requirements are due 45 days from date of publication of this *Second Order on Reconsideration and Further Notice* in the Federal Register. OMB comments are due 60 days from the date of publication in the Federal Register. Comments on the information collection requirements contained herein should be submitted to Judy Boley, Federal Communications Commission, Room 234, 1919 M Street, N.W., Washington, DC 20554, or via the Internet to [jboley@fcc.gov](mailto:jboley@fcc.gov) and to Timothy Fain, OMB Desk Officer, 10236 NEOB, 725 - 17th Street, N.W., Washington, DC 20503 or via the Internet to [fain\\_t@al.eop.gov](mailto:fain_t@al.eop.gov). For additional information on the information collection requirements, contact Judy Boley at 202-418-0214 or via the Internet at the above address.

### VIII. PROCEDURAL PROVISIONS

101. *Ex parte Rules - "Permit-but-Disclose" Proceeding.* This proceeding will be treated as a "permit-but-disclose" proceeding subject to the "permit-but-disclose" requirements under Section 1.1206(b) of the rules.<sup>207</sup> Ex parte presentations are permissible if disclosed in accordance with Commission rules, except during the Sunshine Agenda period when presentations, ex parte or otherwise, are generally prohibited. Persons making oral ex parte presentations are reminded that a memorandum summarizing a presentation must contain a summary of the substance of the presentation and not merely a listing of the subjects discussed. More than a one or two sentence description of the views and arguments presented is generally required.<sup>208</sup> Additional rules pertaining to oral and written presentations are set forth in Section 1.1206(b).<sup>209</sup>

102. *Filing of Comments and Reply Comments.* Pursuant to applicable procedures set forth in Sections 1.415 and 1.419 of the Commission's Rules,<sup>210</sup> comments are due August 14, 1998, and reply comments are due September 3, 1998. To file formally in this proceeding, you must file an original plus four copies of all comments, reply comments, and supporting comments. If you want each Commissioner to receive a personal copy of your comments and reply comments, you must file an original plus nine copies. You should send comments and reply comments to Office of the Secretary, Federal Communications Commission, 1919 M Street, NW, Washington, DC 20554. Comments and reply comments will be available for public inspection during regular business hours in the FCC Reference Center, Room 239, Federal Communications Commission, 1919 M Street NW, Washington DC 20554.

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<sup>207</sup>47 C.F.R. § 1.1206(b), as revised.

<sup>208</sup>See 47 C.F.R. § 1.1206(b)(2), as revised.

<sup>209</sup>47 C.F.R. § 1.1206(b).

<sup>210</sup>47 C.F.R. §§ 1.415 and 1.419.

**IX. ORDERING CLAUSES**

103. Accordingly, IT IS ORDERED that the petitions for reconsideration filed in this proceeding ARE DENIED.

104. IT IS FURTHER ORDERED that the Motion to Lift Stay filed December 15, 1993 by the Center for Media Education and Consumer Federation of America IS GRANTED as to the Commission's voluntary stay on enforcement of 47 C.F.R. § 76.503(c), and IS DENIED as to the Commission's voluntary stay on enforcement of 47 C.F.R. §§ 76.503(a), (b), (d), (e) and (f).

105. IT IS FURTHER ORDERED that, pursuant to Sections 1, 4, 303 and 613 of the Communications Act of 1934, as amended, 47 U.S.C. §§ 151, 154, 303 and 533, NOTICE IS HEREBY GIVEN of proposed amendments to the Commission's rules, in accordance with the proposals, discussions and statements of issues in the *Further Notice of Proposed Rulemaking*, and COMMENT IS SOUGHT regarding such proposals, discussions and statements of issues.

106. IT IS FURTHER ORDERED that the Commission SHALL SEND a copy of this *Report and Order and Second Further Notice of Proposed Rulemaking*, including the Initial Regulatory Flexibility Analyses, to the Chief Counsel for Advocacy of the Small Business Administration.

FEDERAL COMMUNICATIONS COMMISSION



Magalie Roman Salas  
Secretary

**APPENDIX A**

List of Commenters

Petitions for Reconsideration of Cable Horizontal Ownership Rules

Bell Atlantic

Center for Media Education and Consumer Federation of America (joint petition)

Comments in Support of Petition(s) for Reconsideration

Viacom International, Inc.

Oppositions to Petition(s) for Reconsideration

Bell Atlantic

BellSouth Telecommunications, Inc.

Center for Media Education and Consumer Federation of America (joint opposition)

GTE Service Corporation

Liberty Media Corporation

National Cable Television Association, Inc.

Tele-Communications, Inc.

Time Warner Entertainment Company, L.P.

Turner Broadcasting System, Inc.

US West Communications, Inc.

Replies to Comments and Oppositions

Bell Atlantic

Center for Media Education and Consumer Federation of America (joint reply)

Liberty Media Corporation

National Cable Television Association, Inc.

Time Warner Entertainment Company, L.P.

Turner Broadcasting System, Inc.

Viacom International, Inc.

Motion to Lift Stay

Center for Media Education and Consumer Federation of America (joint motion)

Opposition to Motion to Lift Stay

National Cable Television Association, Inc.

Separate Statement of Commissioner Harold Furchtgott-Roth

In re: Implementation of Section 11(c) of the Cable Television Consumer Protection and Competition Act of 1992, Horizontal Ownership Limits, *Second Memorandum Opinion and Order and Further Notice of Proposed Rulemaking*.

I am pleased that the Commission seeks comment on the constitutionality of the 35% "minority-control allowance," 47 CFR section 76.503(b), for cable subscriber limits. *See supra* at 32. In my view, the constitutionality of this provision in light of intervening judicial decisions -- most notably, *Adarand v. Peña*, 515 U.S. 200 (1995) -- is, at best, dubious.

Accordingly, while it certainly does no harm to seek comment on the efficacy of this regulation, I believe that such comment is entirely unnecessary and I would not have sought it. If a regulation appears to violate the Constitution, that is all we need to know in order to decide whether to affirm it on reconsideration.

At the outset, I note that the Commission's statutory authority to promulgate the minority-control allowance (or any other race-based cable subscriber limits, for that matter) is scant. Section 613(f)(1)(a), which orders the Commission to set horizontal ownership rules, is *entirely race-neutral*. Its plain language supports no rational inference that Congress intended different subscriber limits to apply to different people based on nothing other than their race:

"[T]he Commission shall . . . prescribe rules and regulations establishing reasonable limits on the number of cable subscribers *a person* is authorized to reach through cable systems owned by *such person*, or in which *such person* has an attributable interest."

47 U.S.C. section 613(f)(1)(a)(emphasis added).

Nor do the "public interest" factors that Congress outlined make any distinctions between people based on minority or non-minority status. *See id.* section 613(f)(2)(A)-(G). To be sure, one of the factors states that the Commission shall "not impose limitations which would impair the development of diverse and high quality programming." Section 613(f)(2)(G). Congress clearly meant for the Commission to protect cable operators' ability to show a wide variety of choice programming by not setting subscriber limits so low as to dry up concentration-based efficiencies that facilitate costly programming investments. *See House Report at 43; Senate Report at 33; see also 8 FCC Rcd at 8571* (observing that "higher concentration levels enable[] cable companies to take advantage of economies of scale and foster investment in more and better original programming and a wealth of viewing options for consumers"). But there is no indication in the statute, or even its legislative history, that Congress meant for the Commission to view the issue of subscriber limits and varied, quality programming through the historically troubled lens of race.

In short, we simply do not have a clear Congressional directive that the Commission, in setting horizontal limits, make race-based distinctions among cable system owners. Given the weighty constitutional issues that arise whenever government employs such classifications, we should be reluctant

to read them into statutes. See generally *United States v. Thirty-Seven Photographs*, 402 U.S. 363, 369 (1971) (statutes should be construed to avoid, not to create, constitutional problems).

## II.

Section 76.503(b), which on its face employs racial classifications, raises grave constitutional questions. In particular, *Adarand v. Peña*, 515 U.S.200 (1995), which was decided after the Commission promulgated section 76.503(b), casts substantial doubt upon its constitutionality under the Equal Protection component of the Fifth Amendment.

In *Adarand*, the Supreme Court held that *all* governmental action based on race is subject to strict scrutiny. *Id.* at 226. This standard of review obtains, the Court made clear, whether or not the government's motives can be characterized as "benign." *Id.* at 227. Thus, the use of racial classifications by any governmental actor is now constitutionally permissible only where the measure is narrowly tailored to serve a compelling government interest. *Id.* at 235.<sup>1</sup>

With respect to the government interest in section 76.503(b), the Supreme Court has never held that diversity of programming -- the Commission's purported goal in adopting the minority-control allowance, see 8 FCC Rcd 8565, 8578-79 (1993) -- qualifies as a compelling government interest. See *Lutheran Church-Missouri Synod v. FCC*, No. 97-1116, slip op. at 20-21 (D.C. Cir. April 14, 1998) (observing that in *Metro Broadcasting, Inc. v. FCC*, 497 U.S. 547 (1990), the Court held programming diversity to be an important but not a compelling government interest). There is simply no affirmative authority for the proposition that the interest that has been asserted by the Commission in support of its regulation is legally sufficient under strict scrutiny.<sup>2</sup>

Furthermore, as in other contexts, the Commission's stated goal is something of a moving target. The Second Report & Order adopting the allowance does not explain what the Commission actually intends to accomplish when it speaks of promoting "diversity" in cable programming. *Cf. id.* at 19 ("The Commission never defines exactly what it means by 'diverse programming.'"). Of course, were "diversity"

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<sup>1</sup>As an initial matter, this regulation plainly requires the government to engage in race-based decisionmaking. In situations where a cable operator has more than 30% but less than 36% of national subscribers, the question whether that person is within legal limits for subscribership depends entirely on the racial identity of those who own or control affiliated systems. Therefore, whatever claims might be advanced with respect to the applicability of *Adarand* to other Commission regulations, *cf. Lutheran Church-Missouri Synod v. FCC*, No. 97-1116, slip op. at 13 (D.C. Cir. April 14, 1998) (summarizing and rejecting argument that FCC's equal employment opportunity rules do not involve race-based decisionmaking), it cannot be maintained that government action under this regulation does not turn expressly and precisely upon considerations of race.

<sup>2</sup>In fact, this legal problem -- *i.e.*, the lack of a compelling government interest -- would arise with respect to any regulation created in order to foster programming diversity. I thus find it hard to see how any horizontal ownership rule intended to advance such a goal could be fashioned under *Adarand*, as the Commission suggests. See *supra* at 32 ("We seek comment on how we can develop our policies consistent with the standards set forth in *Adarand*").

defined in a content-specific way, such an interpretation would trigger the First Amendment, as the D.C. Circuit has noted. *See id.* at 19-20 ("Any real content-based definition of the term may well give rise to enormous tensions with the First Amendment.").<sup>3</sup>

With respect to the second step under strict scrutiny, the fit between the means and ends here is loose, if not sloppy. The Commission has stated that the 5% allowance will foster investment in minority-owned cable systems, in turn create more minority ownership, and ultimately result in more minority "viewpoints" in programming. *See* 8 FCC Rcd at 8578-79. But the record in this proceeding is devoid of any evidence to support the Commission's predictive rationale, particularly the assumption that cable system ownership by a person of a certain race will lead to an identifiable type of programming content. *Cf. Lutheran Church*, slip op. at 22-23 (faulting Commission, in overturning EEO rules as unconstitutional, for lack of evidence "linking low-level employees [at broadcast stations] to programming content"); *Lamprecht v. FCC*, 958 F.2d 382 (D.C. Cir. 1992) (criticizing Commission, in finding gender preferences in licensing hearings unconstitutional, for lack of evidence of connection between female ownership of broadcast stations and "female programming").

Nor has the Commission made any attempt to explain why a 5% allowance is a more appropriate remedy for the posited diversity problem than a more limited allowance of, say, 3%. To the contrary, the flat 5% of extra passage for minority-controlled systems seems an exceedingly blunt instrument for achieving the Commission's goal (even if that goal were a legally compelling one, which, under current precedent, it is not). For instance, I can find no connection in the record between the particular percentage of extra subscribers that minority-controlled companies may serve under this regulation and the degree to which that allowance furthers ownership and programming. The 5% allowance thus appears to be a rigid numerical preference, with no record evidence to support either its necessity or efficacy in relation to the purported goal.

Relatedly, there appears to have been no consideration in this docket of race-neutral alternatives for increasing minority ownership or programming participation, as required under the narrow-tailoring prong of strict scrutiny. *See Adarand*, 500 U.S. at 237-38 (citing *Richmond v. J.A. Croson*, 488 U.S. 469, 507 (1989)). The Commission seems to have approached the use of this explicit racial classification as a foregone conclusion, rather than as an alternative approach after first evaluating the utility of rules that do not draw lines among citizens based on their race. Indeed, in the notices of proposed rulemaking and the order of adoption, the Commission never even broached the possibility of race-neutral rules. *See* 8 FCC Rcd 210, 217 n. 58 (1992); 8 FCC Rcd 6828, 6850-51 (1993); 8 FCC Rcd at 8678-79. This is perhaps understandable given that *Adarand* had not been decided at the time these documents were issued, but that fact does not solve the basic deficiency in this proceeding that now exists under that case.

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<sup>3</sup>In contrast to broadcasters, cable operators receive full First Amendment protection with respect to their transmission and selection of programming. *See Turner Broadcasting System, Inc. v. FCC*, 512 U.S. 622, 636-41 (1994). Accordingly, the First Amendment "tensions" referred to in *Lutheran Church*, which involved broadcasting, would be even stronger here.

## III.

For the foregoing reasons, governing judicial precedent strongly suggests that section 76.503(b), which literally creates two sets of rules for regulated entities based solely on the racial identity of those who own or control related systems, constitutes a denial of equal protection of the laws. The Commission has failed to articulate either a compelling government interest or to achieve a carefully crafted fit between the means it has chosen and the ends it says it intends to promote. The regulation therefore appears to be, at this juncture, facially unconstitutional.

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As indicated above, I certainly cannot object to my fellow Commissioners asking questions about the practical workings of the rule. The significance of such information, however, pales in comparison to the strong indication under existing caselaw that the regulation is unconstitutional. As the courts have admonished us, "[f]ederal officials are not only bound by the Constitution, they must also take a specific oath to support and defend it." *Meredith Corp. v. FCC*, 809 F.2d 863, 874 (D.C. Cir. 1987). If a regulation appears to be unconstitutional, I believe that is reason enough -- indeed, it is the most important reason that I can imagine -- to eliminate the rule.

**PARTIAL DISSENT OF COMMISSIONER GLORIA TRISTANI**

*In the Matter of Implementation of Section 11(c) of the Cable Television Consumer Protection and Competition Act of 1992 -- Horizontal Ownership Limits, MM Docket No. 92-264*

I would have lifted the Commission's voluntary stay on the enforceability of the horizontal ownership rules. In 1993, when the stay was imposed, a stay may have made sense: the largest cable operator, TCI, still controlled significantly less than 30% of cable subscribers nationwide and appellate review of the *Daniels* decision could have been expected well before the horizontal limit was threatened. In the past five years, that situation has changed dramatically. By the middle of 1997, TCI controlled 29.3% of cable subscribers, and with the flurry of deals announced over the last several months, it is clear that TCI has breached, or will soon breach, the 30% limit. Moreover, the anticipated appellate review never happened and may not happen anytime soon -- the D.C. Circuit has been waiting for the Commission to release this reconsideration of our rules before examining the underlying statute's constitutionality.

Under these circumstances, the 30% limit we are reaffirming today may be rendered moot unless the stay is lifted. To the extent that TCI already exceeds the 30% limit, I would identify those cases and address them separately. That task may be difficult, but not nearly as difficult as the situation we will face if TCI's dealmaking continues and a year from now the D.C. Circuit upholds the statute. Then we will face a situation in which the "facts on the ground" may severely hamper our ability to implement the right policy.

I recognize that the majority has put cable operators on notice that they must be prepared to come into compliance within 60 days if our rules are upheld. I am supportive of such an admonishment, but I am not convinced that it will be enforced. I therefore dissent on this part of the item.