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

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In the Matter of	)	
	)	
Annual Assessment of the Status of	)	CS Docket No. 98-102
Competition in Markets for the	)	
Delivery of Video Programming	)	

COMMENTS OF MEDIAONE GROUP, INC.

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MediaOne Group, Inc. ("MediaOne") submits these comments in response to the Federal Communications Commission's (the "FCC's" or "Commission's") Notice of Inquiry in the captioned matter.[1] MediaOne is the parent company of the third largest multiple system operator ("MSO") in the United States, providing a full range of broadband communications services to approximately 4.9 million customers. Through its subsidiary, MediaOne Telecommunications, Inc., MediaOne also provides residential facilities-based competitive local telephone service in several large U.S. markets.

I. INTRODUCTION AND SUMMARY

Pursuant to federal law, the Commission is required to report annually to Congress on the status of competition in the market for the delivery of video programming.[2] In its NOI, the Commission seeks information to assist in its preparation

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[1] In the Matter of Annual Assessment of the Status of Competition in Markets for the Delivery of Video Programming, CS Docket No. 98-102, Notice of Inquiry, FCC 98-137, rel. Jun. 26, 1998 ("NOI").

[2] 47 U.S.C. §548(g).

of the fifth annual report on competition in markets for the delivery of video programming ("1998 Competition Report"). The 1998 Competition Report will update the Commission's assessment of the status of competition and report on changes in the competitive environment since the Commission submitted its 1997 report to Congress.[3] In particular, the Commission seeks data, information, and comment regarding the cable industry, existing and potential competitors, and the prospects for increasing competition in markets for the delivery of video programming. The Commission also seeks to examine interservice competition, including the extent to which cable operators are providing telephone service and telephone companies are providing video services.

In these comments, MediaOne provides examples of direct competition in its video programming business and discusses how competition in the areas where it provides service has intensified over the past year. MediaOne details how it is meeting these competitive challenges. MediaOne also describes its facilities-based telephony initiatives which will provide the true local telephone competition envisioned by the 1996 Telecommunications Act, and certain factors hindering the delivery of such service to potential customers. As evidenced herein, the Commission should report to Congress that there is healthy competition in the multichannel video marketplace which is continuing to increase in magnitude throughout the United States.

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[3] Annual Assessment of the Status of Competition in the Market for the Delivery of Video Programming, CS Docket No. 97-141, Fourth Annual Report, 13 FCC Rcd 1034 (1998) ("1997 Competition Report").

II. DISCUSSION

A. MEDIAONE IS EXPERIENCING INCREASED COMPETITION IN EVERY MAJOR GEOGRAPHIC AREA IN WHICH IT PROVIDES VIDEO PROGRAMMING SERVICES.

MediaOne provides multichannel video service to subscribers domestically in 17 states. Within these states, MediaOne's major markets are Atlanta, Georgia, Eastern Massachusetts, Los Angeles County, California, Jacksonville Florida, Detroit, Michigan, and Minneapolis/St. Paul, Minnesota. As the Commission noted in its 1997 Competition Report, cable's competitors currently control 13 percent of the multichannel video market and have been growing their subscribership at an average annual rate of over 20 percent since 1990.[4] At midyear 1998, the number of direct broadcast satellite ("DBS") subscribers had reached 7.3 million – up from 5.1 million in 1997 – and continues to experience record growth every month over year-earlier figures.[5] Satellite subscribership is expected to reach 10 million by the end of 1998.[6] At the same time, the private cable industry has seen significant growth with SMATV subscribership growing 10.7% over the past year.[7] Furthermore, Ameritech has obtained 76 franchises in three Midwestern states in competition with MediaOne and other cable operators; the Commission has certified Open Video Systems in several of MediaOne's markets; and digital MMDS service has been introduced in still more of MediaOne's markets. Consequently,

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4 1997 Competition Report.

5 "DBS Sales Heat Up in June," Multichannel News, July 20, 1998, at 54.

6 CableFAX Daily, July 27, 1998, at p.4.

7 1997 Competition Report.

MediaOne is facing competition from a multitude of multichannel video programming distributors in each of its major markets.

1. Local Telephone Companies Are Overbuilding MediaOne's Cable Systems.

Incumbent local exchange carrier Ameritech, through its cable subsidiary, Ameritech New Media, Inc. ("Ameritech"), has been granted franchises for nine communities served by MediaOne, representing nearly 130,000 homes passed. The Commission has found effective competition to exist in five of these franchise areas (Plymouth, Plymouth Township, Northville, Northville Township, and Canton Township).[8] In the past year, Ameritech has launched service in competition with MediaOne in Madison Heights, Roseville and Westland. Ameritech has been receiving franchises on terms which can be less onerous than those applied to the incumbent franchisee.[9]

Southern New England Telephone ("SNET") has been granted a statewide franchise from the Connecticut DPUC, which allows it to compete directly with MediaOne's systems located in ten communities: East Granby, East Windsor, Enfield, Granby, Hartland, Somers, Stafford, Suffield, Union, and Windsor Locks.

BellSouth, through its subsidiary, Bell South Interactive Media Services, Inc. ("BellSouth"), is competing with MediaOne in parts of Florida and Georgia. BellSouth is employing a strategy of using both wireline and wireless delivery systems to provide

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8 In the Matter of Continental Cablevision of Southeast Michigan Petition for Determination of Effective Competition, Memorandum Opinion and Order, 12 FCC Rcd. 1467 (1997).

9 See, e.g., Cable TV Fund 14-A d/b/a Jones Intercable v. City of Naperville, Case No. 96C5962, 1997 U.S. Dist. LEXIS 7336 (N.D.Ill. May 21, 1997).

competing video services. In wireline delivery, BellSouth has been granted Title VI cable franchises in a number of Florida communities where MediaOne currently provides service. For example, BellSouth has been granted a county-wide franchise for Dade County, Florida which allows it to compete in all areas of the County that MediaOne services.[10] BellSouth has also been granted a county-wide franchise for St. John's County, Florida, and provides cable service to a private development known as World Golf Village in St. John's County. BellSouth also holds a ten-year county-wide franchise for Gwinnett County, Georgia.

2. Local Telephone Companies Are Competing With MediaOne's Cable Systems Using Wireless Technology.

BellSouth has also been acquiring wireless cable companies in Florida and Georgia, and has begun its initial rollout of digital wireless cable service in its home market of Atlanta, Georgia. Wireless video services are easier to deploy in urban areas because entry costs are not prohibitive: they don't require cable franchises or time-consuming and expensive street cuts to build infrastructure. Indeed, BellSouth is able to offer digital wireless service to Atlanta with only four transmission towers.[11] BellSouth has offered a similar service in New Orleans since November, 1997, and claims that the number of subscribers are exceeding company expectations.[12]

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[10] Yet another cable provider, Strategic Technologies, Inc. ("STI") has been granted a cable franchise for a smaller portion of Dade County that overlays MediaOne's existing franchise.

[11] "BellSouth MDS Offering Battles MediaOne in Atlanta," Video Competition Report, June 22, 1998, at p.10.

[12] "Bell South Brings Digital Cable To Atlanta," Multichannel News, June 8, 1998, at 8.

BellSouth picked Atlanta to become its second wireless market partly because of the "mosaic of technologies" the company already offers in the market, including mobile telephony and Internet access services.[13] Using programming by the Americast consortium, BellSouth offers Atlanta residents more than 160 digital channels of service. Its digital signals cover about a 30-mile radius in and around Atlanta, and are being configured to avoid any overlap with BellSouth's wireline cable properties in the Atlanta suburbs of Chamblee and DeKalb County.[14] BellSouth has recently predicted that its digital wireless systems "would capture a 30 percent to 35 percent share of the cable market in both cities within three to five years."[15]

In Florida, BellSouth completed its purchase of the wireless service owned by National Wireless Holdings' South Florida Television, which has the capability to provide wireless video service throughout Dade County as well as the southern portion of Broward County within its 35-mile radius.[16] MediaOne provides cable service to some 200,000 Dade County customers and 170,000 Broward County customers. The wireless service will establish a large footprint for BellSouth's competitive services and has the potential to overlay MediaOne's entire franchised area in Dade County. As previously mentioned, BellSouth also has a Title VI franchise for all of Dade County.

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13 "BellSouth MDS Offering Battles MediaOne in Atlanta," Video Competition Report, June 22, 1998, at p.10.

14 Id.

15 "Wireless Cable Ops Still Upbeat," Multichannel News, July 13, 1998, at 2.

16 CableFAX Daily, July 1, 1997.

BellSouth has further acquired wireless cable operations from American Telecasting, Inc. in six additional Florida markets: Jacksonville, Orlando, Daytona Beach, Ft. Myers, Lakeland, and Bradenton, as well as in Louisville, Kentucky.[17] MediaOne provides service to approximately 309,000 customers in Jacksonville and Ft. Myers. BellSouth also plans to compete with MediaOne using wireless technology in Daytona Beach, Jacksonville (including all of unincorporated St. Johns County) and Broward County, Florida by year end.[18]

In southern California, Pacific Bell Video Services ("PBVS"), a wholly-owned subsidiary of SBC Communications, has been operating a digital MMDS system to provide 150 channels of service to customers throughout the entire Los Angeles basin, including Orange County, an area of more than 5 million homes. The PBVS wireless service has secured customers in each of MediaOne's Greater Los Angeles franchise areas consisting of over 350,000 customers. Although PBVS refuses to disclose its subscriber numbers, MediaOne estimates that PBVS has nearly 30,000 digital MMDS customers. PBVS also operates an analog wireless cable system providing service to over 40,000 customers in Riverside County, which PBVS acquired from Cross Country Wireless in July, 1995.[19]

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17 . "Bell South to Buy Wireless Cable Markets from American Telecasting," Bell South News Release, March 19. 1997; "BellSouth Agrees to Buy Wireless Cable TV Services in Nine Southern Markets," Atlanta Journal-Constitution, Mar. 20, 1997.

18 Letter from Mr. John Hartman, Vice President, BellSouth Entertainment, to Ms. Jan Peters, President, MediaOne, Inc. dated July 16, 1998; "BellSouth MDS Offering Battles MediaOne in Atlanta," Video Competition Report, June 22, 1998, at p.10.

19 Pacific Telesis Proxy Statement, March 15, 1996, at F-4. MediaOne has had effective competition petitions with respect to PBVS on file with the FCC for Orange County (Costa Mesa and Tustin) and Riverside County (Corona, Pomona and Menifee) since September 17, 1997 and June 18, 1997,

3. Electric Utilities Are Competing With MediaOne Using Cable and OVS Systems.

MediaOne is facing competition from electric utilities or their affiliates for the provision of video services. MediaOne is facing cable and OVS competition from Residential Communications Network, Inc. ("RCN"). RCN has secured local approvals to offer cable service in the City of Boston and surrounding communities of Arlington, Brookline, Newton, Somerville, and Wakefield, and is seeking approvals to offer video service in more than 24 other local municipalities in the Boston Market.[20] In the meantime, RCN is using its OVS authority to build out its network and offer service where it lacks local franchises.[21] RCN's OVS service areas overlap with MediaOne's cable service areas in 20 communities.[22] RCN has entered into a joint venture with an unregulated subsidiary of Boston Edison, the local electrical utility, to provide phone, cable, and Internet services to 1.6 million Boston Edison customers as well as communities that are contiguous to the Boston Edison service territories.[23] This strategic alliance gave RCN access to Boston Edison's 200-mile advanced fiber-optic network, which covers large portions of Boston as well as nearly four dozen surrounding

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respectively. To date, the FCC has taken no action with respect to these petitions despite the fact that they are both unopposed.

[20] RCN Annual Report 1997; "RCN to Launch Multimillion Dollar Ad Campaign," Boston Herald, June 30, 1997, at 40.

[21] See Time Warner Cable v. RCN-BeCoCom, Memorandum Opinion and Order, DA 98-798 (rel. Apr. 28, 1998).

[22] Arlington, Burlington, Cambridge, Dedham, Hopkinton, Milton, Natick, Needham, Newton, Quincy, Sherborn, Stoneham, Waltham, Watertown, Wayland, Wellesley, Weston, Weymouth, Winchester, and Woburn, Massachusetts. Id. at ¶12 n.34.

[23] RCN Annual Report 1997.

communities. RCN is also seeking alliances with municipal light departments in the communities of Norwood, Wellesley, Braintree, Hingham, and Hull, Massachusetts, which are contiguous to Boston Edison's service territories.

RCN has expanded its Boston-area network rapidly. By the end of 1997, RCN's Boston backbone network had reached 9,347 fiber miles.[24] RCN's strategy is to deploy its networks in high density, high-usage neighborhoods. To this end, RCN has focused its efforts on the heavily populated Boston to Washington corridor, which represents 4% of the nation's geographical area but nearly 28% of its telecommunications market.[25] RCN is now turning its attention to the west coast and plans to focus its network construction on the San Francisco-to-San Diego corridor, which has similar characteristics to its Northeastern markets.[26]

4. DBS Is Providing Nationwide Video Competition To MediaOne.

In addition to competition from the local entities described above, MediaOne faces vigorous video competition from national DBS providers. As noted earlier, the number of direct broadcast satellite ("DBS") subscribers has reached about 7.3 million, and continues to grow at a record breaking pace. Satellite subscribership is expected to reach 10 million by the end of 1998.[27] Industry leader DirecTV has been averaging 30 percent higher monthly subscriber growth in 1998 than in 1997 and has "no reason to

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24 Id.

25 Id.

26 "RCN Seeks Calif. OK as OVS and CLEC," Multichannel News, June 8, 1998.

27 CableFAX Daily, July 27, 1998, at p.4.

think that this sales growth is going to slow down."[28] Indeed, at a recent convention, the President of the Satellite Broadcasting and Communication Association proclaimed that the "satellite television industry has grown so rapidly that a DBS dish is sold every 20 seconds" in the United States.[29]

This phenomenal growth rate can be partially attributed to the regulatory advantages which DBS operators enjoy over cable operators. Unlike DBS, cable operators such as MediaOne are unable to advertise a single price for service even across contiguous franchise areas, not to mention across the country, because of locally based rate regulation, local franchise obligations such as public, educational and governmental ("PEG") access support, local franchise fees, and taxes all of which impact the prices a cable operator may charge it customers. Similarly, MediaOne is unable to package or even align its channel line-ups in the same manner as DBS companies due to the restrictions imposed upon cable operators by rate regulation and must-carry requirements.

The success of DBS can also attributed to its programming flexibility. DBS operators are able to offer customers exclusive programming, such as packages of NBA, NHL, and NFL games that are extremely attractive to sports fans, and can offer stripped down channel line-ups to multiple dwelling units ("MDUs") because they are unrestricted by must-carry, PEG and leased-access carriage obligations. DBS' large channel capacity and lack of mandatory carriage requirements further allows it to carry niche services

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[28] "DBS Sales Heat Up in June," Multichannel News, July 20, 1998, at 54.

[29] CableFAX Daily, July 24, 1998, at 2.

which are unfeasible for cable operators.[30] DBS customers can even receive local broadcast signals using a new generation of off-air antennas that can seamlessly deliver high quality off-air broadcast signals directly to a DSS system with just a push of the customer's remote control.[31]

These significant regulatory advantages have allowed DBS providers to enter into marketing partnerships with other multichannel video providers. For instance, DirecTV has signed deals with MMDS operators given them the rights to sell DirecTV's DBS service to residential MDUs and single family homes in conjunction with the local signals provided by the MMDS operator.[32] Consequently, through an MMDS arrangement, DirecTV is providing video programming to the largest apartment community in the country – Gates Mills Towers, a 1,077 unit complex in Mayfield Heights, Ohio.[33] DirecTV and USSB have also signed marketing and distribution agreements with telephone companies such as GTE, Bell Atlantic, and SBC Communications.[34] These agreements give the telephone companies a proven and ubiquitous video product to bundle with their voice and data offerings in local markets where the telephone companies have universal name recognition and well-oiled marketing machines. The

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30 "DirecTV Readies Melting Pot of Nets," Multichannel News, July 20, 1998, at 6.

31 "YES YOU CAN! Enjoy Local Channels and DIRECTV® Too!," http://www.directv.com/misc/yesyoucan3.html.

32 "Heartland Signs MDU Deal With DirecTV," Multichannel News, Nov. 17, 1997; "DirecTV Signs More MDU Deals," Multichannel News, Oct. 13, 1997.

33 "DirecTV, Heartland Sign Landmark Deal," Multichannel News.

34 "DBS gets local help," Broadcasting & Cable, Mar. 9, 1998; "Bell Atlantic To Offer TV Service Via Satellite," Philadelphia Inquirer, March 3, 1998.

telephone companies reportedly receive a set fee for each new customer signed up and a percentage of revenue from each customer they bring in.[35]

5. MediaOne Is Facing Competition From SMATV Operators.

MediaOne competes with more than 30 SMATV providers in Georgia, a dozen SMATV providers in both Florida and California, at least six in Illinois, and five in New England. A number of these SMATV providers, such as Optel, Inc., Cable Plus, One Point Communications (an SBC Communications affiliate), and GE Rescom, have established a national presence and compete directly with MediaOne. Over the past year, the largest SMATV operator, OpTel, Inc. solidified its position in the MDU marketplace by closing on its acquisition of the third-largest operator, Interactive Cable Systems, Inc., and filed a registration statement for an initial public offering. OpTel now has over 200,000 cable subscribers, which is double what it had in 1996.[36]

SMATV operators generally do not "use" the public rights-of-way.[37] Consequently, SMATV operators primarily serve MDUs. Because SMATV operators' entire business is focused on MDUs, their presence makes the MDU market highly competitive. Like DBS, SMATV operators do not labor under any rate regulation, must-carry, customer service, or local franchising obligations, including franchise fees and universal service. This gives them tremendous competitive advantages in the MDU

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[35] Id.

[36] "OpTel's IPO Offers Look at Private-Cable Power," Multichannel News, June 15, 1998, at 54. OpTel also purchased Phonoscope, Inc. and Bay Area Cable in October, 1997. See Notice in Multichannel News, Nov. 17, 1997.

[37] 47 U.S.C. §522(7)(B) (private cable exemption); Guidry Cablevision v. City of Ballwin, No. 96-2037 (8th Cir. 1997) (SMATV cables crossing under a public street not a "use" of public right-of-way).

market as they may "cherry-pick" the most desirable properties, provide channel line-ups without unpopular PEG, leased access and must-carry signals, and offer landlords financial incentives to secure exclusive access to MDUs. Additionally, with the FCC's recent Entertainment Connections, Inc. ("ECI") ruling, SMATV operators who use common carrier video transport between service locations can now function exactly like a franchised cable operator without bearing any of the regulatory and franchise obligations under which franchised cable operators labor.[38]

The FCC's new rules governing the disposition of MDU wiring have only increased the current advantages of SMATV operators in the MDU marketplace by providing them access to wiring installed at the expense of incumbent operators.[39] MediaOne urges the Commission to apply its cable home wiring rules to all MVPDs to reduce any further regulatory disparity which creates false economies in the MDU marketplace. Likewise, given the competitiveness of the MDU market, any further rules promulgated by the Commission should be uniformly applied to all MVPDs.

B. MEDIAONE IS MEETING ITS COMPETITIVE CHALLENGES BY INVESTING IN INFRASTRUCTURE AND CREATING ADDED VALUE FOR ITS CUSTOMERS.

MediaOne believes that a long-term commitment to service, quality and value is essential to maintaining customer satisfaction and loyalty in a competitive market where

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[38] Entertainment Connections, Inc., Memorandum Opinion and Order, FCC 98-111 (rel. Jun. 30, 1998). Although the Commission sought to limit the effect of this ruling, industry analysts have predicted that SMATV operators will turn this loophole into a sinkhole. See "FCC Allows MDU Wire Interconnects Sans Franchise," Wireless/Private Cable Investor, June 30. 1998, at pp. 1-2.

[39] Cable Home Wiring, CS Docket No. 95-184 and MM Docket No. 92-260, Report and Order and Second Further Notice of Proposed Rulemaking, 13 FCC Rcd 3659 (1988). Of course, when MediaOne

consumers are well aware that they have video options from alternative providers. Consequently, MediaOne has invested heavily in upgrading its broadband networks to enhance network quality and reliability as well as to provide capacity for added video programming offerings and other new communications services. Specifically, by the end of 1997, MediaOne's capital expenditures reached $1.586 billion. This figure continues to grow as MediaOne seeks to upgrade or rebuild substantially all of its systems nationwide by the end of the year 2000.

As MediaOne's systems become upgraded or rebuilt, MediaOne is offering consumers various programming packages to satisfy a wide variety of subscriber needs. Programming choices span from the lowest cost "Lifeline tier," which includes local broadcast stations, local origination, and PEG access channels and is typically priced below $10 per month, to cable programming service tiers, migrated product tiers, new product tiers, premium service and pay-per-view offerings. MediaOne has added value to its cable programming service tiers, for example, by shifting popular channels, such as The Disney Channel and regional sports channels, from premium to cable programming service tiers.[40] In May, 1998, MediaOne introduced a digital cable offering in Detroit. This new service provides customers with the option to access 23 new multiplex premium channels and 40 digital Music Choice channels. Customers adding MediaOne digital service to their existing cable service now have access to more than 170 channels.

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loses access to its wiring, customers lose the ability to receive ancillary broadband capabilities, such as high speed Internet service, which generally are not provided by SMATV companies.

[40] See In the Matter of Comcast Cablevision of the South, Chamblee and De Kalb County, Georgia, DA 97-1209 (rel. Jun. 11, 1997) at ¶21 (recognizing movement of Disney Channel to expanded basic package in response to competition).

MediaOne has also expanded the rollout of its MediaOne Express high-speed-data offering to more of its service areas over the past year, and has merged with Time Warner's Road Runner service.[41] With investments from Microsoft Corp. and Compaq Computer Corp., MediaOne believes that the merged entity will speed consumer acceptance of cable Internet access and add further value to MediaOne's service offering in the eyes of consumers.

C. MEDIAONE'S PRICES FOR VIDEO PROGRAMMING CONTINUE TO BE COMPETITIVE GIVEN INFRASTRUCTURE INVESTMENTS AND COST INCREASES.

MediaOne's prices for video programming continue to be reasonable and competitive in light of the substantial investment it is making in system rebuilds, programming cost increases, and some of the additional public service obligations uniquely imposed on cable operators. In the NOI, the Commission noted that cable rates have risen faster than the national inflation rate and seeks information on the factors causing changes in cable rate levels.

1. MediaOne Continues To Deliver An Excellent Value.

MediaOne, like any other retail business, will normally reflect the wholesale costs of its product and delivery system in its price. And cable's costs have increased dramatically more than the rate of inflation. MediaOne's prices reflect the costs of infrastructure upgrades, programming service additions and license fees, and investment in innovative new technologies. These expenditures, however, result in a video offering

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[41] "Microsoft and Compaq Make Net-Access Bet," Wall Street Journal, Jun. 16, 1998, at A3; "Microsoft, Compaq Plunk $425M Into Road Runner, MediaOne," Multichannel News, Jun. 22, 1998, at 1.

that provides a solid value to our customers. Although prices have risen, cable subscribers have been treated to more programming choices with higher quality programming on those channels.[42] Significantly, cable operators have managed to keep prices competitive with other video providers despite the fact that cable operators are subject to public interest obligations that most other video providers do not share. Obligations such as PEG access channels and support, institutional networks, universal service, franchise fees, and other taxes make it more costly for cable operator than for MMDS, SMATV, or DBS providers to deliver a comparable package of service. These various obligations directly impact MediaOne's ability to remain price competitive.

2. MediaOne Has Invested More Than $400 Per Subscriber In System Rebuilds.

As noted earlier, MediaOne has invested heavily to upgrade or rebuild its networks to enable it to compete more effectively against the various video providers it faces in its markets, including BellSouth in Atlanta and Florida, RCN in Massachusetts, SBC in Los Angeles, and Ameritech throughout the Midwest. MediaOne has spent $1.586 billion in rebuilds and upgrades as of year end 1997. Looked at another way, the $2 to $3 increase in rates in 1997 was used to fund an investment of over $400 per subscriber. Obviously, the shareholders of MediaOne are bearing the majority of risk in this endeavor. And the construction continues at an accelerated rate not captured in the investment reported as of year end 1997.

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42 See "Cable TV rates rising again, but service and selection rising, too," The Fresno Bee, Dec. 26, 1997, a copy of which is attached hereto as Exhibit 1.

3. MediaOne Has Experienced A Dramatic Increase In Programming Costs.

The recent active auctioning of the rights to exhibit sports events on broadcast and cable television has resulted in significant increases in the licensing fees that cable operators must pay to carry sports programming. For MediaOne, sports programming costs grew to 19.75% of all programming costs in 1997 from 18.6% in 1996. This trend looks to further increase in 1998 and beyond.[43] When sports rights auctions result in higher license fees for sports carried by cable networks, and the cable networks then raise their compensation demands from MediaOne, the company is faced with a dilemma. MediaOne is committed to providing its customers with highly valued programming, and most of the sports rights auctions involved programming that is in that category. Moreover, MediaOne's channel line-up may be less attractive to certain customers without that programming. However, MediaOne is aware that a delicate balance must be maintained between carriage of programming valued by its customers and the cost of that programming. If MediaOne fails to maintain that equilibrium, our customers will look to alternative delivery sources for their video programming.

Although the increase in sports programming costs is perhaps the most dramatic, the issue of rising programming costs is endemic among all programming categories. The result has been upward pressure on MediaOne's prices and shrinking profit margins for the Company. Not only has MediaOne's cost of programming increased, but it represents a growing percentage of the revenues from regulated programming and of

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43 See, e.g., "Losses Predicted on NFL Deals," Los Angeles Times, Jan. 15, 1998, at D1; "Fox-ESPN Fight Over Sports Rights Raising Cable Rates," Los Angeles Times, Aug. 29, 1997, at D1.

revenues from all regulated activities (when equipment and installation is included). By way of comparison, MediaOne's cost of programming has grown from 15.3% of associated revenues in 1994 to 20.5% of the revenues from regulated programming in 1997. Taking into account all regulated revenues (including installation and equipment) as well as all additional sources of revenues (such as advertising commissions and marketing fees), the end result is that the cost of programming increased from 12.6% of revenue in 1994 to 16.6% in 1997.

D. MEDIAONE IS ENCOUNTERING NUMEROUS ROADBLOCKS IN ITS PROVISION OF TELEPHONE SERVICE OVER ITS CABLE SYSTEM.

The Commission's NOI seeks information on the extent to which cable operators are providing telephone service to compare video and other services offered through the various distribution technologies used to provide multichannel video programming.[44] The NOI specifically seeks a description of equipment and facilities used to deliver service, and whether multiple services are being provided over the same facilities.[45]

In addition to the $1.586 billion that MediaOne has spend to upgrade its cable plant over the past few years for video service, MediaOne has invested another $1.2 billion for a total investment of over $2.8 billion to deliver the full menu of products and services over broadband networks, such as telephony. These additional investment costs have not been reflected in cable rates and have been borne exclusively by MediaOne's shareholders. Given MediaOne's strategy of operating multi-use broadband networks, MediaOne looks at competition for video and voice customers as one integrated market.

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[44] NOI at ¶¶3, 7(f).

Unfortunately, while 13% of video customers receive their service from non-cable multichannel video programming distributors, only 1% of telephone customers receive their service from competitive local exchange carriers.

1. MediaOne Is Providing Cable Telephony Over Its HFC Network.

MediaOne's hybrid fiber/coax ("HFC") network is a local access transmission system that combines fiber optic and coaxial cable technologies in a physical star/ logical bus architecture. The HFC network simultaneously transports both analog and digital signals of all kinds, parallel in time, maintaining total format independence among the respective signals. In an HFC system, individual services are carried in different parts of the frequency spectrum, obviating mutual interference. This gives HFC the ability to transport multiple services on a single access network.

Cable telephony is a conventional circuit-switched telephone service transported over the HFC platform. Cable telephony devices at the ends of the HFC network convert signaling and voice signals to radio-frequency (RF) signals for transmission in a portion of the HFC frequency spectrum. The actual service is carried in digital form within the RF transmission link. Cable telephony has the ability to deliver service quality equal to or better than current state-of-the-art telephone networks because the service stays in digital form closer to customer telephone instruments.

MediaOne has launched retail local telephone offerings over its hybrid fiber/coaxial network infrastructure in two areas of the country. In its Atlanta, Georgia region, MediaOne began offering telephone services to the public in January, 1998. In

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[45] Id. at ¶7(f).

Southern California, MediaOne began offering telephone services to the public in April, 1998. MediaOne focuses on delivering these telephone services to residential customers. Although MediaOne plans to expand its telephony offering to other markets in the near future,[46] its efforts are being hindered by roadblocks erected by incumbent telephone companies.

2. MediaOne Is Encountering Errors, Delays, And Roadblocks From ILECs.

As a facilities-based provider of local telephone service, MediaOne Digital Telephone Services operates from a position of relative independence from the incumbent local exchange carrier ("ILEC"). Since MediaOne neither resells ILEC services nor purchases ILEC unbundled network elements in its broadband markets, MediaOne has a relatively short, but critical, list of essential ILEC services. Today, some MediaOne telecommunications companies purchase interconnection trunks, transport and termination, Interim Number Portability ("INP"), E-911, directory services listings, and collocation from the ILECs to provide local telephone service.[47]

Since MediaOne is just beginning to offer its retail telephone service to consumers, the process of transitioning customers from ILECs to MediaOne takes on heightened importance. Now is the time when customer perceptions are set and reputations made. Errors, delays, and roadblocks caused by an ILEC when consumers are switching their local service to MediaOne result in damage, perhaps permanent, to

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[46] "MediaOne launches phone service," The Boston Herald, July 22, 1998.

[47] Even with the introduction of Local Number Portability, MediaOne will still need to interconnect with ILECs.

MediaOne's reputation with affected customers. This damage amounts to a barrier to entry for MediaOne in particular, and a potentially fatal barrier to competition in the local loop in general.

For example, as a facilities-based CLEC, MediaOne is dependent on BellSouth for number portability to provide service in Atlanta, Georgia. MediaOne' experience matches that of other CLECs nationally – customers are reluctant to switch providers of local phone service if they cannot retain their phone number. Because permanent number portability was not available in Georgia when MediaOne launched its service, MediaOne had to rely on BellSouth to provide remote call forwarding ("RCF") as an interim solution for number portability. MediaOne has suffered quality of service problems with BellSouth's provision of RCF that impacts its ability to service customers in Georgia. Pursuant to its interconnection agreement, BellSouth has 48 hours to respond to an order for RCF with a Firm Order Commitment ("FOC") or a discrepancy. With a discrepancy, the 48 hour clock starts over when the order is resent.

MediaOne has experienced virtually continuous problems with BellSouth's response to its request for RCF. The process was so unreliable that MediaOne was forced to inform its customers that service could not be installed any sooner than seven days out. It is hard enough for a new entrant to convince customers to change their phone service from an incumbent provider with long established reputation and ubiquitous marketing. It becomes nearly impossible if the customer has to wait a week or longer to be switched over. Not surprisingly, MediaOne lost many potential customers due to this delay. In April, 1998, BellSouth implemented an electronic data interface ("EDI") for RCF which was supposed to remedy this intolerable delay. At first, BellSouth responded to

MediaOne's RCF orders with a FOC within 48 hours less than 50% of the time. Due to MediaOne's continued escalation of this matter within the ILEC, BellSouth currently is responding to MediaOne's RCF orders with a FOC within 48 hours about 75% of the time. The inability to provide timely installation of service to its MediaOne's customers continues to be a major impediment towards its ability to effectively compete with BellSouth.

BellSouth and Pacific Bell's implementation of INP has also been and continues to be problematic. For instance, MediaOne's customers have had their calls forwarded to incorrect telephone numbers. Customers have been left without dial tone when the ILECs failed to comply with MediaOne's request to delay INP orders. And customers have been without service when the ILECs did not release INP orders. It is not hard to imagine that when a customer switches over to a new entrant and then loses its dial tone, that customer will not hesitate to switch back to the original (incumbent) provider. Customers have no tolerance for a loss of dial tone. The result is that MediaOne not only loses a particular customer, but its reputation in the community is harmed, perhaps irreparably.

III. CONCLUSION

As evidenced by the number and variety of alternative service providers currently competing with MediaOne, there is robust competition in the multichannel video marketplace. MediaOne is facing heightened competition from a multitude of well-financed multichannel video programming distributors in every major geographical area in which it provides cable service. Non-cable video subscribership, particularly DBS, continues to grow at an unprecedented pace. MediaOne is meeting its competitive challenges by investing in infrastructure, creating added value for its customers, and offering telephony and data services over its facilities. To date, MediaOne's efforts to expand its retail local telephone offering have been hindered by roadblocks and potholes caused by ILECs. Nevertheless, MediaOne's early experience indicates that facilities-based CLECs can provide the true choice for consumers envisioned by the Telecommunications Act of 1996 once the local exchange markets are genuinely opened. For the reasons discussed above, the Commission should report to Congress that there is healthy competition in the multichannel video marketplace which is continuing to increase in magnitude throughout the United States.

Respectfully submitted,

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