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FEDERAL COMMUNICATIONS COMMISSION
OFFICE OF THE SECRETARY

Ms. Magalie Roman Salas
Secretary
The Portals, 445 Twelfth Street, S.W.
Washington, D.C. 20554

Re: Ex Parte Notice, CS Docket No. 96-85 (Cable Act Reform)

Dear Ms. Salas:

This letter provides notice that late yesterday Mike Hammer and the undersigned of Willkie Farr & Gallagher met with Susan Fox, Senior Legal Advisor to Chairman Kennard, on behalf of Tele-Communications, Inc. in connection with the above-captioned proceeding.

We urged the Commission to preclude local franchising authorities from "prohibit[ing], condition[ing], or restrict[ing] a cable system's use of any type of subscriber equipment or any transmission technology," pursuant to revised Section 624(e) of the Communications Act. We also recommended that for MDU predatory pricing cases, the Commission adopt a proxy for the below-cost element of the prima facie case, as well as a meeting competition defense. We gave Ms. Fox a copy of the attached talking points on the MDU pricing issue.

Please place a copy of this letter and the attachment in the docket of the above-captioned proceeding.

Kindly direct any inquiries about this matter to the undersigned. Thank you.

Sincerely,

Francis M. Buono

cc: Susan Fox

Attachment

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MDU PRICING

I. Federal Antitrust Standards Should Be Used In Reviewing Allegations Of Predatory Pricing.

- "Predatory price discrimination" is an anticompetitive activity which has previously been defined by both Congress and the Supreme Court under the Robinson-Patman Act. Given this well-established federal precedent, the use of the term "predatory" in section 301(b)(2) indicates Congress' intent to use these federal antitrust standards in the implementation of this provision.

- Reliance on federal antitrust standards will provide a national framework that will afford greater certainty than disparate state or local standards.

- It is also in line with well established Commission practice. Throughout its regulation of pricing behavior, the Commission has consistently defined "predatory pricing" in accordance with federal standards.

II. Proposed Elements Of A Prima Facie Case And Defense.

1. **Prima Facie Case -- Complainant Shows Below-Cost Pricing And Recoupment Possibility**. Under federal antitrust law, a plaintiff must show the following to make out a prima facie predatory pricing case: (1) the competitor's prices are below the competitor's costs; and (2) the competitor has a "reasonable prospect" or a "dangerous probability" of recouping any lost revenues after driving the complainant out of the market.[1] The Commission should require that a complainant in an MDU predatory pricing case show these two prima facie elements.

2. **Use Proxy For First Element Of Prima Facie Case -- Below-Cost Pricing Allegation**. To avoid needless complications and the significant costs and disclosure of confidential information associated with discovery of a defendant's costs, the Commission should adopt a proxy for the below-cost pricing element of the prima facie case. For example, Time Warner proposed that a complainant could satisfy the below-cost pricing element of the prima facie case where it shows that a cable operator's discount in the MDU, compared to the operator's retail residential rate in the franchise area, is "greater than the average industry cash flow margin as reported by the Commission."[2] This "cash flow margin" figure is set forth in each annual Video Competition Report. The industry cash flow margin is a reasonable surrogate for the

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1 See Brooke Group Ltd. v. Brown & Williamson Tobacco Corp., 509 U.S. 209, 222 (1993).

2 Time Warner Comments at 40.

amount that revenues exceed operating costs, and, therefore, any MDU discount less than this industry average cash flow margin can be assumed not to be below cost.

3. **Allow a Meeting Competition Defense**. If the complainant succeeds in making a prima facie case, the defendant would then be able to defend its price in the MDU by asserting that it was simply meeting the price offered by the competitor. This "meeting competition" defense would be a complete defense and, if established, would require dismissal of the complaint.[3]

   - Both Congress and the courts have recognized that a "meeting competition" defense is necessary to ensure that prohibitions against price discrimination foster, rather than hinder, competition. The Supreme Court has noted that the price discrimination prohibitions of the Robinson-Patman Act would be anti-competitive if a "meeting competition" defense were not allowed. Standard Oil, 340 U.S. 231, 249-250 (1951).

   - This defense is necessary if new section 623(d) is to have its intended effect of encouraging competition and lowering prices for cable service to MDU subscribers.

   - A "meeting competition" defense will also avoid needless controversies where the cable operator simply matches the price of a competitor. As such, it minimizes administrative burdens and conserves valuable resources of the Commission, cable operators, and alternative video distributors, consistent with the goals of the 1996 Act and the 1992 Cable Act.

4. **Defendant's Cost Showing**. If the defendant could not show it was meeting competition or assert any other defense to dismiss the complaint, it would have to produce information with which it could defend itself under conventional antitrust standards, including the requisite cost information to show that its pricing in the MDU is not below its costs.

5. **Discovery and Confidential Information**. The Commission should adopt the same Commission-controlled discovery procedures that are used, and which have worked well, in the program access context. It should also adopt rules providing for the confidential treatment of a cable operator's cost and pricing information, where such information must be submitted to defend against a predatory pricing claim.

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[3] See ex parte letter from Willkie Farr & Gallagher dated 12/30/96 in CS Docket No. 96-85, explaining that, under Supreme Court precedent, pricing designed to "meet competition," by definition, cannot be considered to be "predatory," regardless of whether or not the price is below the party's cost.