DOCKET FILE COPY ORIGINAL

RECEIVED & INSPECTED
JUN 19 2002
FCC - MAILROOM

Before the
Federal Communications Commission
Washington, D.C. 20554

In the Matter of	)	
	)	
Revisions to Cable Television Rate Regulations	)	MB Docket No. 02-144
	)	
Implementation of Sections of The Cable Television Consumer Protection and Competition Act of 1992: Rate Regulation	)	MM Docket No. 92-266
	)	
Implementation of Sections of The Cable Television Consumer Protection and Competition Act of 1992: Rate Regulation	)	MM Docket No. 93-215
	)	
Adoption of a Uniform Accounting System for the Provision of Regulated Cable Service	)	CS Docket No. 94-28
	)	
Cable Pricing Flexibility	)	CS Docket No. 96-157

NOTICE OF PROPOSED RULEMAKING AND ORDER

Adopted: June 13, 2002 **Released: June 19, 2002**

Comment Date: 60 days after publication in the Federal Register
Reply Comment Date: 90 days after publication in the Federal Register

By the Commission:

TABLE OF CONTENTS

Paragraph

I. BACKGROUND AND INTRODUCTION 1

II. ISSUES FOR COMMENT 6

A. Deletion or modification of the rules that address CPS tier rates 8

B. Rate adjustments when channels are added to or deleted from the BST 12
1. Calculating rate adjustments 12
2. "Single Tier" Systems 23

C. **Headend upgrades** 24

D. **Digital broadcast television rate adjustment issues** 25

E. **Initial regulated rates** 27

F. **Rate structures and uniform regional rates** 29

G. **Rates for commercial subscribers** 30

H. **Small system issues** 31

I. **Cost-of-service rate process** 34

J. **Abbreviated cost-of-cervice chowing on FCC Form 1235** 36

K. **Rates of interest** 38

L. **Unbundling** 40

M. **Refunds** 41

N. **Re-evaluation of the BST rate regulation process** 42
1. Recalibration of the "competitive differential" 42
2. Other approaches to BST rate regulation 43

O. **Equipment and inside wiring rate regulation** 44

P. **Recovery of lost revenues for equipment and installation due to subsequently reversed rate orders 50**

Q. **Charges for changes in service tiers** 51

R. **Effective competition showings** 52

S. **Procedures for Commission review of local rate decisions** 54

III. ORDER: INTERIM RATE ADJUSTMENTS FOR BST CHANNEL CHANGES 55

IV. ADMINISTRATIVE MATTERS 56

A. **Initial Regulatory Flexibility Analysis** 56
1. Need for, and Objectives of, the Proposed Rules 57
2. Legal Basis 61
3. Description and Estimate of the Number of Small Entities to Which the Proposed Rules Will Apply 62
4. Description of Projected Reporting, Recordkeeping and Other Compliance Requirements for Small Entities 66
5. Steps Taken to Minimize Significant Impact on Small Entities and Significant Alternatives Considered 68
6. Federal Rules Which Duplicate, Overlap, or Conflict with the Commission's Proposed Rules 75

B. Initial Paperwork Reduction Act of 1995 Analysis 76

C. Procedural Provisions 77

V. ORDERING CLAUSES 84

I. BACKGROUND AND INTRODUCTION

1. In this proceeding we seek comment on potential revisions to our cable television rate regulations in light of the March 1999 end of cable programming service tier rate regulation and the experience gained with our current regulations.

2. Section 623 of the Communications Act,[1] adopted as part of the Cable Television Consumer Protection and Competition Act of 1992,[2] governs the cable television rate regulation process. As adopted, section 623 provided for rate regulation of the basic service tier ("BST")[3] of cable service and for most cable customer premises equipment by local municipal franchise authorities.[4] Cable programming service tier (CPST) rate regulation would be undertaken by the Commission on a complaint basis.[5] Services offered on a per-channel or per-program charge basis were not subject to rate regulation. In communities where "effective competition" was found to exist there would be no rate regulation.[6] The Commission was charged with responsibility for adopting regulations to govern basic service tier, equipment, and CPST rates, and establishing procedures to govern appeals of local franchise authority rate decisions to the Commission. The Act instructs the Commission to establish regulations that "ensure that the rates for the basic service tier are reasonable[,]" and are "designed to achieve the goal of protecting subscribers ... from rates ... that exceed the rates that would be charged for the basic service

[1] 47 U.S.C. § 543.

[2] Pub. L. No. 102-385, 106 Stat. 1460 (1992).

[3] The basic service tier includes, at a minimum, the broadcast signals distributed by the cable operator (except superstations), along with any public, educational, or government access channels required by the local franchising authority. 47 U.S.C. § 543(b)(7); 47 C.F.R. § 76.901(a).

[4] Local franchising authorities have jurisdiction to regulate the cable operator's rates for the installation and lease of equipment used by subscribers to receive the basic service tier. 47 U.S.C. § 543(a)(2)(A), (b)(1), (b)(3)(A). The Commission has interpreted the scope of this authority to include all equipment in a subscriber's home, provided and maintained by the cable operator, that is used to receive the basic service tier, regardless of whether such equipment is additionally used for other services. 47 C.F.R. § 76.923(a)(1). The covered equipment includes converter boxes, remote control units, and inside wiring.

[5] The CPST is any video programming provided over a cable system, including installation or rental of equipment used for the receipt of such video programming, other than video programming carried on the basic tier or offered on a per channel or per program basis. 47 U.S.C. § 543(l)(2); 47 C.F.R. § 76.901(b).

[6] Effective competition is established in the franchise area if: (1) fewer than 30 percent of the households subscribe to the operator's service ("low penetration test"); (2) the cable operator and a competing provider each offer comparable video programming to at least 50% of the households and at least 15 percent of the households take service from multichannel video programming distributors ("MVPD") other than the largest one ("competing provider test"); (3) the franchising authority offers video programming as an MVPD to at least 50 percent of the households ("municipal provider test"); or (4) a local exchange carrier ("LEC") or an MVPD using LEC facilities offers comparable video programming directly to subscribers ("LEC test"). 47 U.S.C. § 543(l)(1); 47 C.F.R. § 76.905(b).

tier if such cable system were subject to effective competition."[7] In a series of proceedings undertaken pursuant to section 623, the Commission adopted the necessary rules and standards to govern the rate regulation process.[8]

[7] 47 U.S.C. § 543(b)(1).

[8] *See Implementation of Sections of the Cable Television Consumer Protection and Competition Act of 1992: Rate Regulation*, MM Docket No. 92-266, Report and Order and Further Notice of Proposed Rulemaking ("*Rate Order*"), 8 FCC Rcd 5631 (1993) (adopted regulatory structure); First Order on Reconsideration, Second Report and Order, and Third Notice of Proposed Rulemaking ("*First Reconsideration*"), 9 FCC Rcd. 1164 (1993) (affirmed benchmark/price cap approach to regulation, actual cost standard for leased equipment used for BST, procedural and jurisdictional issues including BST definition; determined that low penetration and municipal systems belonged in benchmark analysis); Third Report and Order, 8 FCC Rcd 8444 (1993) (required same ratemaking method for initial rates for all regulated tiers); Second Order on Reconsideration, Fourth Report and Order, and Fifth Notice of Proposed Rulemaking "(*Second Reconsideration*"), 9 FCC Rcd 4119 (1994) (recalculated the competitive differential, adjusted the price cap computation, provided administrative relief for small systems; adopted new "going forward" methodology based on a per-channel adjustment factor for capped rates); *Implementation of Sections of the Cable Television Consumer Protection and Competition Act of 1992: Rate Regulation,* MM Docket No. 92-266, *Buy-Through Prohibition,* MM Docket No. 92-262, Third Order on Reconsideration ("*Third Reconsideration*"), 9 FCC Rcd 4316 (1994) (addressed competition issues, tier buy-through prohibition, procedural and jurisdictional issues, generally applicable provisions, and equipment and installation issues); MM Docket No. 92-266, Fourth Order on Reconsideration, 9 FCC Rcd 5795 (1994) (permitted franchise fee and FCC regulatory fee pass-through without prior approval); MM Docket Nos. 93-215, 93-266 [*sic*], Fifth Order on Reconsideration and Further Notice of Proposed Rulemaking ("*Fifth Reconsideration*"), 9 FCC Rcd 5327 (1994) (administrative relief for small cable systems); MM Docket Nos. 92-266, 93-215, Sixth Order on Reconsideration, Fifth Report and Order, and Seventh Notice of Proposed Rulemaking ("*Going Forward Order*"), 10 FCC Rcd 1226 (1994) (revised rate adjustments for adding, deleting, or substituting channels); MM Docket No. 92-266, Seventh Order on Reconsideration ("*Seventh Reconsideration*"), 10 FCC Rcd 3225 (1995) (expanded use of small system headend upgrade incentive); MM Docket Nos. 92-266, 93-215, Eighth Order on Reconsideration ("*Eighth Reconsideration*"), 10 FCC Rcd 5179 (1995) (alternative rate adjustment agreements for small systems); MM Docket No. 92-266, Ninth Order on Reconsideration ("*Ninth Reconsideration*"), 10 FCC Rcd 5198 (1995) (inflation adjustments for systems receiving transition rate relief); MM Docket No. 92-266, Tenth Order on Reconsideration ("*Tenth Reconsideration*"), 10 FCC Rcd 6870 (1995) (reduced rate form reporting burden for transition systems); MM Docket Nos. 92-266, 93-215, Sixth Report and Order and Eleventh Order on Reconsideration ("*Small System Order*"), 10 FCC Rcd 7393 (1995) (defined small system and small cable companies; adopted simplified small system cost of service formula); MM Docket Nos. 92-266, 93-215, Twelfth Order on Reconsideration, 11 FCC Rcd 785 (1995) (eliminated home shopping offset); MM Docket No. 92-266, Thirteenth Order on Reconsideration ("*Thirteenth Reconsideration*"), 11 FCC Rcd 388 (1996) (adopted annual rate adjustment methodology); *Implementation of Sections of the Cable Television Consumer Protection and Competition Act of 1992: Rate Regulation*, MM Docket 92-266, *Cable Pricing Flexibility*, CS Docket 96-157, Memorandum Opinion and Order and Notice of Proposed Rulemaking, 11 FCC Rcd 9517 (1996) (required consistent ratemaking methodology for all regulated tiers; proposing cable pricing flexibility); MM Docket No. 92-266, 11 FCC Rcd 20206 (1996) (adopted rule changes per *Time Warner Entertainment Co. v. FCC*, 56 F.3d 151 (D.C. Cir. 1995)); MM Docket No. 92-266, Report and Order, 12 FCC Rcd 3445 (1997) (adopted low-price systems final rules); MM Docket Nos. 92-266, 93-215, Fourteenth Order on Reconsideration ("*Fourteenth Reconsideration*"), 12 FCC Rcd 15554 (1997) (denied reconsideration of *Small System Order*).

See also Implementation of Sections of the Cable Television Consumer Protection and Competition Act of 1992: Rate Regulation and Adoption of a Uniform Accounting System for Provision of Regulated Cable Service, MM Docket No. 93-215, CS Docket No. 94-28, Report and Order and Further Notice of Proposed Rulemaking ("*Cost Order*"), 9 FCC Rcd 4527 (1994) (interim cost rules); Second Report and Order, First Order on Reconsideration, and Further Notice of Proposed Rulemaking ("*Final Cost Order*"), 11 FCC Rcd 2220 (1996) (final cost rules); *Implementation of Sections of the Cable Television Consumer Protection and Competition Act of 1992 -- Rate Regulation*, CS Docket No. 95-174, Report and Order, 12 FCC Rcd 3425 (1997) (uniform rate methodology across multiple franchise areas).

3. The Telecommunications Act of 1996 amended section 623 to provide that cable programming service tier rates would no longer be subject to regulation after March 31, 1999.[9] Consequently, although the Commission has continued to address remaining complaints concerning earlier rates, CPST rates no longer are regulated.[10] In this proceeding we seek comment on rule changes that may be necessary or desirable in order to account for changes in the regulatory process resulting from the cessation of federal CPST rate regulation. In addition, we intend to refresh the record in or terminate other pending proceedings relating to the rate regulation process. We intend in this proceeding to focus on mechanical and procedural changes to the existing rules and forms that may be useful in order to make the existing basic tier and equipment rate rules more effective in the absence of CPS tier rate regulation. In addition, however, we solicit comment on the possibility of broader conceptual changes to the theory and mechanisms of basic tier and equipment rate regulation that might logically follow from the changed scope of regulation and intervening developments subsequent to the adoption of the initial rules.

4. The rate rules, when adopted, were primarily based on a benchmark and price cap approach to setting rates for regulated cable service. Under the benchmark approach, existing rates for cable service were compared to a benchmark that reflected the rates charged by cable systems subject to effective competition with the same number of subscribers and channels. Initial regulated rates were based on the higher of either the benchmark adjusted for changes in external costs through March 31, 1994, or the operator's rates in effect on September 30, 1992, reduced by the general differential between competitive and non-competitive systems and adjusted for certain intervening changes in inflation, external costs, and the number of regulated channels.[11] Forms and associated instructions were adopted for computing the benchmark comparisons and rate reductions and for unbundling equipment and installation costs from programming rates.[12] Once initial rates were determined, rates were governed on a going-forward basis by a price cap mechanism. The price cap permitted periodic adjustments for inflation, changes in the number of regulated channels, and changes in external costs generally beyond the operator's control, including programming costs, costs of franchise requirements, state and local taxes on cable service, and franchise fees. The rates determined by the competitive differential were expected to allow cable operators to cover their costs and obtain a reasonable profit, and operators could adjust those rates in the future for changes in external costs.[13] The Commission provided a cost-of-service option as a safety valve for cable operators unable to cover costs after applying the competitive differential through

[9] Telecommunications Act of 1996, Pub. L. No. 104-104 § 301(b)(1), 110 Stat. 115 (1996) (codified as 47 U.S.C. § 543(c)(4)) (subsection (c) "shall no longer apply to cable programming services offered after March 31, 1999").

[10] 47 C.F.R. § 76.950(b).

[11] *Second Reconsideration*, 9 FCC Rcd at 4166-68 ¶¶ 105 -110 *reconsidering Rate Order*, 8 FCC Rcd at 5770-74 ¶¶ 213-222. The competitive differential was initially found to be 10% but, on reconsideration, was found to be 17% with various other adjustments in the rules. *Rate Order* at 5644 ¶ 14, 6146 (Appendix E); *Second Reconsideration* at 4166 ¶ 105. Initially comparisons were based on per channel rates. *See* FCC Form 393, Determination of Maximum Initial Permitted Rates for Regulated Cable Programming Services and Equipment (Aug. 1993). On reconsideration, comparisons were based on per subscriber per tier revenues from regulated sources. *See* FCC Form 1200, Setting Maximum Initial Permitted Rates for Regulated Cable Services Pursuant to Rules Adopted February 22, 1994, "First-Time Filers Form" (May 1994).

[12] FCC 393 was replaced by FCC Form 1200.

[13] The Commission reasoned that its ratemaking approach was reasonable because a cable operator without market power would need to charge rates that would cover, for example, "the direct costs . . . of obtaining, transmitting, and otherwise providing signals," and "'the capital and operating costs of the cable system,'" which were among the factors specified in Communications Act § 623(b)(2)(C), (c)(2), 47 U.S.C. § 543(b)(2)(C), (c)(2). *Second Reconsideration*, 9 FCC Rcd at 4197 ¶ 163.

the benchmarking process.[14]

5. Although BST rates were subject to prior approval by local authorities and CPST rates were subject to adjustment and refunds on complaint to the Commission, the Commission carried out its substantive rate rule responsibilities by developing a common set of "tier-neutral" benchmarks and regulations so that the same methodology was to be used to set rates for the basic service tier and for cable programming service tiers.[15] The tier-neutral approach was designed to ensure that the rate regulations themselves did not create an incentive to place services in any particular rate-regulated tier. Cable system operators were thus able to determine whether to market a "fat basic" service with a large number of channels on the basic tier and a smaller optional CPS tier or, in the alternative, a "thin" lower cost basic tier with a larger optional CPS tier or tiers. The Commission subsequently created limited rate incentives for operators to add new programming services to the CPST or to single tier systems, but otherwise retained the tier-neutral approach to rate setting and required that the movement of channels between tiers of regulated services be revenue neutral.[16]

II. ISSUES FOR COMMENT

6. The primary focus of this proceeding is intended to be on improvements within this existing regulatory structure. Although the elimination of CPST rate regulation with the associated concept of a tier neutral regulatory process changes one of the predicates for the rules, this structure has come to be understood by both operators and local governments involved in the rate regulation process. There would be considerable regulatory cost involved in changing to an entirely new basic tier rate setting process. Thus, we intend to concentrate here on making improvements in the existing process rather than creating a new one. However, as discussed below, comments suggesting broader changes are also being solicited.

7. In this notice, we address deletion of rules pertaining to CPST rates, changes in the BST channel count, headend upgrades, digital broadcast television rate issues, determining the initial regulated rate when a system first comes under rate regulation, rate structure flexibility, rates for commercial subscribers, small system issues, the cost-of-service process, FCC Form 1235 issues, equipment and inside wiring rate regulation, other equipment rate issues, effective competition showings, and procedures for Commission review of local rate decisions. We additionally seek comment on recalibrating the competitive differential between rates of systems subjected to effective competition and noncompetitive systems and question whether there may be a different approach to establishing reasonable rates for the BST.

A. Deletion or modification of the rules that address CPS tier rates

8. The initial task in this proceeding is to separate out and eliminate all of those rules that pertain solely to the regulation of CPST rates, which are no longer relevant. Although this appears to be

[14] *Second Reconsideration,* 9 FCC Rcd at 4196 ¶ 162.

[15] *Rate Order*, 8 FCC Rcd at 5746, 5759-60, 5881-82, ¶¶ 171, 197, 396; *reconsideration denied on this issue*, *First Reconsideration*, 9 FCC Rcd at 1182-85 ¶¶ 31-36.

[16] The Commission permitted operators to add new services to the CPST or to systems with only a single programming tier at a special capped rate not otherwise available for channels added to the BST. *See* 47 C.F.R. § 76.922(g)((3); *Going Forward Order*, 10 FCC Rcd at 1248-55 ¶¶ 64-82. Channels added under this capped rate could not be moved from the CPST to the BST. 47 C.F.R. § 76.922(g)(5). Other channels could be moved between tiers on a revenue neutral basis. Small systems owned by small cable companies could additionally increase rates to recover the actual cost up to a specified amount of headend equipment needed to add up to seven channels to CPSTs and single tier systems. *Going Forward Order* at 1258-59 ¶¶ 91-94; 47 C.F.R. § 76.922(g)(7).

largely a ministerial task, we seek comment on what rules should be changed or eliminated. Are there, for example, linkages between the BST and CPST rules or forms that might not readily be recognized and that would need to be accounted for? Regardless of the rule changes made in this proceeding, the existing rules would continue to apply to all pending CPST matters.

9. We propose to delete the following rule sections or paragraphs: 76.901(d); 76.922(c)(4); 76.924(e)(1)(ii); 76.924(e)(2)(ii); 76.934(c)(2); 76.934(d); 76.934(h)(3)(iii); 76.934(h)(6); 76.934(h)(10); 76.950; 76.951; 76.953; 76.954; 76.955; 76.956; 76.957; 76.960; 76.961; 76.962; 76.963(b); 76.980(b), (d)-(f); 76.985 (FCC Form 329 and Instructions); 76.986; 76.987; 76.1402; 76.1605; and 76.1606. Other rules continue to be applicable to BST rate making but should be updated or amended to eliminate references to CPST or to reflect the end of CPST rate regulation. These rule sections or paragraphs are: 76.922(a); 76.922(b)(5); 76.922(b)(7); 76.922(e)(2)(iii)(C); 76.922(f)(4); 76.922(f)(8); 76.922(g); 76.922(i)(1), (2); 76.922(k); 76.924(a); 76.924(e)(1)(iii); 76.933(e); 76.933(g)(5); 76.934(c)(3); 76.934(e); 76.934(f); 76.934(g)(1); 76.934(g)(2) (retaining the last sentence); 76.934(h)(2)(ii)(A); 76.934(h)(4)(i), (v); 76.934(h)(8)(ii); 76.963(a); 76.990(a); 76.990(b)(3); 76.1800. We seek comment on these proposed changes and on whether the sunset of CPST rate regulation should be reflected by changes to other rules.

10. Other rules should be eliminated as obsolete. These rule sections or paragraphs are: 76.922(b)(6)(ii); 76.922(e)(3)(ii); 76.922(e)(4); and 76.934(h)(8)(ii)(last sentence). We seek comment on these changes and on whether additional rules have become obsolete and should be removed.

11. We also propose to modify or eliminate the rate forms and rate form instructions consistent with changes made to our rules in this proceeding. The forms used for rate regulation are FCC Forms 1200, 1205, 1210, 1220, 1230, 1235, and 1240.[17] We seek comment on changes needed to rate forms and instructions to reflect the end of CPST rate regulation. The Commission's rules contain references to FCC Forms 1215 and 1225.[18] The Commission advised the Office of Management and Budget that it would no longer support use of these forms, and dropped these forms from its information collection budget effective April 30, 1997. Absent a showing of need for reinstatement of these forms, we propose to eliminate references to these forms from the rules.[19]

B. Rate adjustments when channels are added to or deleted from the BST

1. Calculating rate adjustments

12. We next address issues that arise when channels are added to or deleted from a tier or moved from one tier to another.[20] When the Commission first addressed adding and deleting channels from regulated tiers of service in March 1994, it allowed operators to adjust the "residual" component of

[17] The Commission's rules also refer to FCC Form 1211. This form is not in use and references will be deleted from the Commission's rules. *See* 47 C.F.R. §§ 76.922, 76.934.

[18] FCC Form 1215, Instructions for FCC Form 1215: A La Carte Channel Offerings (May 1994); FCC Form 1225, Cost of Service Filing for Regulated Cable Services for Small Systems (Apr. 1994).

[19] *See* 47 C.F.R. §§ 76.922(b)(6), 76.934(g).

[20] Section 623(b)(7)(B) contains the following specific reference to rate increases associated with the addition of channels to the basic tier: "A cable operator may add additional video programming signals or services to the basic service tier. Any such additional signals or services provided on the basic service tier shall be provided to subscribers at rates determined under the regulations prescribed by the Commission under this subsection." 47 U.S.C. § 543(b)(7)(B).

the tier charge by a specified per channel adjustment set forth in a "mark-up" table in the rules.[21] The "residual" was the tier charge less external costs and could be roughly analogized to the costs of providing and maintaining the network and offering the service. The amount of the adjustment varied with the number of regulated channels on the system as a whole, decreasing as the number of channels increased and increasing as the number of channels decreased.[22] This adjustment was intended to incorporate the efficiencies and economies of scale reflected in the benchmark rates. The Commission additionally allowed operators to recover their external costs and to mark-up new programming expenses by 7.5%. Operators were required to reduce rates for decreases in programming expenses plus an additional 7.5%.[23]

13. In November 1994, when the Commission revisited the rate adjustment rule for changes in the number of regulated channels in the *Going Forward Order*, it retained the mark-up table and 7.5% mark-up on programming costs for channels added to the BST in section 76.922(g)(2),[24] and provided an optional alternative channel adjustment methodology, the "caps" methodology in section 76.922(g)(3), [25] for channels added to the CPST or to systems with only a single programming tier. This caps methodology was available through 1997 as an incentive for operators to add channels to their CPST. Under this methodology a fixed increase per channel (generally $0.20 plus an additional limited amount to reflect license fees) could be added for a limited number of channels.

14. At that time, the Commission also specified how operators should adjust rates when deleting channels or moving channels between regulated tiers.[26] Operators dropping a channel were to reflect the net reduction in external costs in the tier rate and also to reduce the tier rate by the residual associated with the channel.[27] When shifting a channel between regulated tiers, operators were to shift the residual and programming cost associated with the channel. The residual was to be shifted on a revenue neutral basis by taking into account the different numbers of subscribers on the tiers involved. Operators substituting channels on a tier did not take a per channel adjustment but were required to reflect net changes in external costs in their rates. These provisions were codified in section 76.922(g)(4)-(6) of the Commission's rules. [28]

15. Section 76.922(g)(8) provides that "[p]aragraph (g) of this section shall cease to be effective on January 1, 1998 unless renewed by the Commission."[29] The intent of this sunset language has been the subject of some debate. Cable operators have questioned whether the Commission meant to

[21] *Second Reconsideration*, 9 FCC Rcd at 4243-44 ¶¶ 247-48; *see* 47 C.F.R. § 76.922(e) (1994).

[22] *Id.* at 4239-45 ¶¶ 242-49.

[23] *Id.* at 4242-43 ¶ 246. The amount was set below what the Commission determined to be a reasonable rate of return on investment in plant for regulated services, but above a minimal level. The Commission stated its intention to monitor the amount and revise it later if appropriate. *Id.* n.345.

[24] 47 C.F.R. § 76.922(g)(2); *see Going Forward Order*, 10 FCC Rcd at 1248-49 ¶ 65.

[25] 47 C.F.R. § 76.922(g)(3); *see Going Forward Order* at 1248-55 ¶¶ 64-83.

[26] *See Going Forward Order* at 1256-57 ¶¶ 84-86.

[27] For channels other than those added by the "caps" method, operators would divide the tier residual by the number of channels on the tier. Neither "caps" channels nor any "caps" adjustments would be included in the channel count or tier residual when computing the per-channel residual. 47 C.F.R. § 76.922(g)(4). The residual for a "caps" channel was the "caps" adjustment associated with that channel. Rates would be adjusted for a deleted "caps" channel based on that channel's "caps" residual.

[28] 47 C.F.R. § 76.922(g)(4)-(6).

[29] 47 C.F.R. § 76.922(g)(8).

preclude use of the mark-up table in paragraph (g)(2) when adding new channels to the system or preclude adjusting a tier's residual when deleting channels or moving channels between tiers pursuant to paragraphs (g)(4) and (g)(5), respectively. If paragraph (g)(8) is read to encompass all of paragraph (g), rather than only those provisions in paragraph (g) relating to incentives for adding channels, rates would be adjusted when channels are added to or deleted from the BST only for changes in external costs, including the 7.5% mark-up for programming costs associated with the affected channels, as provided by section 76.922(f).[30] However, FCC Forms 1210 and 1240,[31] the forms for calculating rate adjustments using the quarterly or annual rate adjustments methodologies, respectively, were not changed and continued in use. Section 76.922(h) provides that "[p]ermitted charges for a tier shall be determined in accordance with forms and associated instructions established by the Commission."[32]

16. In reviewing complaints about rates for CPST services provided through March 31, 1999, the end of CPST rate regulation, the Commission has accepted operators' rate calculations on Commission rate forms that included residual adjustments for channel deletions and channel movements between tiers of service subject to regulation, because subscribers benefited from the reduction in rates when the residual associated with a deleted channel was removed from the rates, and moving the residual with a shifted channel was revenue neutral to the operator and had little, if any, impact on the combined rate for all regulated tiers. The Commission has also issued stays of local rate orders that disallowed comparable BST rate adjustments for channels shifted to the BST before March 31, 1999.[33] Commission staff have been advised informally that operator and franchising authority practices with respect to channel deletions and channel movements have varied considerably both before and after March 31, 1999. Some operators have deleted or moved channels from the BST using the rate form to calculate adjustments to the tier residual as well as to external costs; others have adjusted rates only for the external costs associated with the deleted or moved channel. Some franchising authorities have accepted residual adjustments for channel deletions or channel movements from BST to CPST but may not have allowed residual adjustments for channels moved from the CPST to the BST or added to the BST. In some franchise areas, inconsistent approaches may have been used from year to year.

17. The policy objective in terms of channel additions or deletions was to provide the system operator with an appropriate return of its investment in the underlying facilities and programming services and to make sure that system subscribers were only paying for the services they received. The rules also sought to reflect the fact that the unit cost of a channel declines as the total channel capacity of a system increases. In an environment in which both BST and CPST rates were subject to regulation, the policy objective underlying the rules relating to channel shifts between tiers was simply to make the immediate consequences of any move of channels between tiers revenue neutral to the system operator. That is, the rules were designed to avoid a situation where the process created an incentive to move channels between tiers.

18. To address the applicability of our policy objectives in light of the sunset of CPST rate regulation, we seek comment on the following possibilities as to how the rules should be revised or interpreted. One possibility would be to continue to adjust BST rates for changes in the number of BST channels by adding or subtracting the specific "external" costs associated with the channel additions and deletions and the associated 7.5% mark-up adjustment provided in section 76.922(f). Our concern is that

[30] 47 C.F.R. § 76.922(f).

[31] FCC Form 1210, Updating Maximum Permitted Rates for Regulated Cable Services (May 1995); FCC Form 1240, Updating Maximum Permitted Rates for Regulated Cable Services (July 1996).

[32] 47 C.F.R. § 76.922(h).

[33] *See TCI TKR of Georgia, Inc.*, 15 FCC Rcd 4451 (CSB 2000) (Moultrie, GA); *TCI Cablevision of Dallas, Inc.*, 14 FCC Rcd 9252 (CSB 1999) (Farmers Branch, TX).

applying this methodology to channels deleted or moved from the BST, without further adjustments, will have only a minimal impact on the BST rate. When a large number of BST channels are removed from the tier, subscribers could receive a substantial reduction in BST service without an equally substantial reduction in the BST rate.

19. Another possible approach on which we seek comment would be to adjust rates further for changes in the number of channels by adding or subtracting the "per-channel adjustment factor" from the table in section 76.922(g)(2) of the rules,[34] but identifying the specific amount of adjustment not by reference to the number of "regulated channels" but by reference to the current number of channels that would be subject to regulation if CPST rate regulation had not ended. Continuing to use the per-channel adjustment factors from the chart would not be appropriate without this change because the chart was derived from a study based on data from both BST and CPST channels combined and the chart reflects the declining price of channels as total channel capacity increases. The chart also does not take into consideration any diversion of spectrum from analog programming tiers to digital services. The chart is based on the economies of scale reflected in the benchmark rates that formed the basis for the Commission's first rule for adjusting capped rates for the addition, deletion, or movement of channels. We are concerned that this approach, like the external cost approach, will have only a minimal impact on BST rates when channels are deleted.

20. Alternatively, we seek comment on whether rate adjustments for changes in the number of channels on the BST should include some other adjustment to the tier residual and whether the type of adjustment should depend on whether channels are added to or deleted from the BST. Paragraph (g) provided that cable systems could add channels to the BST by adjusting for external cost changes, including the 7.5% markup, and using the chart in paragraph (g)(2) to reflect the incremental change to the total tier residual from the added channel or channels, but were to adjust rates for dropped channels based on the pro rata share of the tier residual for the dropped channel or channels in addition to external cost and markup adjustments. Cable systems dropping channels that had been added using the "caps" incentives would adjust rates based on the actual per channel adjustment taken when the channel was added to the tier.[35] Should this approach be reinstated or should something similar be adopted? Alternatively, if some adjustment to the residual is appropriate when channels are added to the BST, should an adjustment be made other than a per-channel adjustment like that in the paragraph (g)(2) chart? If some other residual adjustment is appropriate, how should that adjustment be determined?

21. We also seek comment as to whether the movement of channels to the BST from previously regulated programming tiers is relevant in determining the BST rate adjustments associated with those channels. Paragraph (g) provided that systems moving channels between regulated tiers would move the external costs and residual value with the channel on a revenue neutral basis. Systems moving previously unregulated channels, such as premium channels, would not move any residual value to the BST. Channels added to the CPST pursuant to the caps incentives could not be moved to the BST. In light of the end of CPST rate regulation, can a residual for CPST channels be computed when a channel is moved to the BST without inflating the BST rate or relying on old records? We are concerned that computing the residual for a now unregulated CPST channel as a pro rata share of the CPST tier rate would permit a system operator to retain an unregulated revenue stream for any CPST channel moved to the BST, which is contrary to the underlying statutory premise that controls over basic tier rates remain desirable. It would also be inconsistent with the treatment of other unregulated channels that are moved to

[34] This is consistent with the approach taken in the Fourth Report and Order. *Second Reconsideration*, 9 FCC Rcd at 4243-45.

[35] Although the caps incentive was primarily for CTST, single tier systems were able to take advantage of the caps incentive when adding new channels. *See* 47 C.F.R. § 76.922(g)(3).

the BST.

22. Should we, instead, establish new BST per-channel values through new benchmarks based on an updated comparison of BST rates charged by competitive and non-competitive systems? If we do so, should we look only at cable system rates, or should we also consider the rates of alternative providers, such as DBS? Could a simple formula be developed? Should the operator's base rate be recalibrated using new benchmarks or should new per-channel values be applied only to channels added to and deleted from the BST after this rulemaking? Or should we consider adjusting tier rates for changes in the number of channels based on rates at competitive systems with comparable market and channel characteristics? How would comparability be evaluated? We also seek comment on whether we should allow channels added to the CPST pursuant to the caps methodology to be moved to the BST.

2. "Single Tier" Systems

23. The Commission's rules currently provide that cable operators using the annual rate adjustment methodology may make an additional rate adjustment to reflect channel additions if the operator offers only a BST and does not offer a CPS tier.[36] Should this option be retained for "single tier" systems? In determining whether a cable operator offers a single tier or multiple tiers of service, should digital service tiers be considered?

C. Headend upgrades

24. We plan to modify section 76.922(g)(7) to reflect the sunset of the opportunity for single tier small systems to make headend upgrade adjustments. Paragraph (g)(7) was added to our rules as an incentive for adding channels to the CPST and to single tier systems through 1997. Small systems could recover the additional headend costs incurred for adding up to seven new channels and could continue to depreciate these costs for the useful life of the equipment. By its own terms, the incentive in paragraph (g)(7) expired, and we see no need to reinstate it. Operators who previously adjusted rates pursuant to paragraph (g)(7), however, may continue to recover undepreciated costs for the useful life of the equipment as provided by that rule and calculated on FCC Form 1210 Module B or FCC Form 1240 Worksheet 6.

D. Digital broadcast television rate adjustment issues

25. The Commission in its *DTV Must Carry First Report and Order* discussed issues associated with the carriage of a broadcaster's digital television signal on cable systems.[37] This *Report and Order* also amended section 76.922 of the Commission's rules to allow recovery of headend equipment costs necessary for the carriage of DTV signals as an external cost in paragraph 76.922(f)(1)(vii) and also allowed cable operators to recover costs of improvements necessary for carriage of digital signals through the network upgrade surcharge pursuant to paragraph (j)(1).[38] So that operators cannot recover more than once for the same cost, we propose to clarify that operators may use either method for adjusting rates, but not both, and we seek comment on this proposal.

26. In the *Further Notice of Proposed Rulemaking* accompanying the *DTV Must Carry First Report and Order*, the Commission proposed to permit BST rate adjustments separate from the upgrade surcharge adjustment addressed above to reflect the addition of channels of digital broadcast

[36] 47 C.F.R. § 76. 922(e)(2)(iii)(C).

[37] *Carriage of Digital Television Broadcast Signals,* CS Docket No. 98-120, First Report and Order and Further Notice of Proposed Rulemaking ("*DTV Must Carry First Report and Order*"), 16 FCC Rcd 2598 (2001).

[38] *Id.* at 2646-47 ¶¶ 109-110; 47 C.F.R. § 76.922(f)(1)(vii), (j)(1).

programming to the BST.[39] Specifically, the Commission proposed to allow cable operators adding digital broadcast signals to their channel line-ups to increase rates for each 6 MHz of capacity devoted to such carriage and solicited comment on the proper adjustment methodology. The Commission was concerned that cable operators have sufficient incentives to add digital television signals, particularly during the transition from analog to digital service, that subscribers should bear a fair share of the costs of providing service on the tier carrying digital signals relative to the system's overall capacity, and that subscriber rates be reasonable. In light of the broader questions being posed in this proceeding, we ask commenters to update the record with comments in this proceeding regarding rate adjustments for carrying digital broadcast services on a rate regulated BST.

E. Initial regulated rates

27. We also seek comment on how initial rate levels should be determined for systems first becoming subject to regulation. Under the current rules, the initial regulated rate, if the system was in operation in 1992, would be calculated using rate and subscribership data from 1992 and 1994 and external cost data from 1994 and adjusted to a current permissible rate level using the price caps methodology. As time passes, however, it becomes increasingly likely that the data necessary for this calculation will be unavailable and that the competitive differential computed from 1992 rate data is not reflective of the competitive differential today. Should we consider alternatives to this process? One option would be to eliminate franchising authority review of the operator's entire rate structure and, instead, limit review to the operator's most recent rate increase or its next rate increase after the franchising authority becomes certified to regulate rates. With respect to CPST rates, the Commission determined after rate regulation had been in effect for about two years that an operator's entire rate structure should not be subject to regulatory review when a complaint was filed.[40] It found that its previous policy of reviewing the entire CPST rate structure at that point created an uncertain business environment for affected cable operators and could discourage the investment necessary for upgrading networks and adding new services. We seek comment as to whether similar concerns are applicable to BST rate regulation and whether this approach is consistent with the statutory directive in section 623(b)(1) that regulations be designed to protect subscribers from BST rates that exceed rates that would be charged if the system were subject to effective competition. Another option for finding a current permissible rate would be to impute a rate from another regulated system with as nearly comparable characteristics as possible. We seek comment on this option, including how comparability should be evaluated and how disputes should be resolved under this option. If the system had been found to have been subject to effective competition in the past, another option would be to use the last "competitive" rate as the starting point for regulation with the price caps methodology followed thereafter. We also seek comment as to whether there are other ways to determine initial regulated rates when unregulated systems are brought under rate regulation. If the approach in the current rules is no longer required, is there any reason to retain the methods for determining the permitted rate for a tier on May 15, 1994, as set forth paragraph 76.922(b) of the Commission's rules and referred to in the last five sentences of paragraph 76.922(d)(2)?[41] Can other rules or paragraphs also be eliminated if the current approach is no longer required?

28. If the Commission were to retain the current approach to establishing initial regulated rates, can the Commission continue to use the current Form 1200? Form 1200 applies the competitive differential to the operator's total revenues from sources that were subject to regulation when the form

[39] *DTV Must Carry Report and Order* at 2656-57 ¶¶ 133-134.

[40] *Thirteenth Reconsideration*, 11 FCC Rcd at 450-52 ¶¶ 161-64.

[41] 47 C.F.R. § 76.922(b), (d)(2). The methods include the full reduction rate, the March 31, 1994, benchmark rate, transition rates, low-price systems, and streamlined rate reductions.

was developed, including the CPST. We seek comment as to whether the end of CPST rate regulation requires any revision to Form 1200 when that form is used as the first step in determining the current maximum permitted BST rate.

F. Rate structures and uniform regional rates

29. We have explored in the past in Dockets 95-174 and 96-157 techniques of permitting greater rate structure flexibility. In the first of these proceedings some rule changes were adopted to facilitate operators having rates that could be uniform on a regional basis.[42] In the second of these proceedings, comment was sought on techniques allowing operators, on a revenue neutral basis, to adjust basic and CPST prices on a more flexible basis when both tiers were subject to rate regulation.[43] This second proceeding appears to have been by-passed by the sunset of CPST tier rate regulation. We seek comment on whether this is correct and updated comments on whether there are other changes in the rules that might be useful in order to create greater flexibility in rate structures or more uniform regional rates while continuing to maintain rules designed to keep BST rates reasonable.

G. Rates for commercial subscribers

30. In its *Fifth Notice of Proposed Rulemaking* in MM Docket No. 92-266, the Commission sought comment on issues relating to the establishment of commercial rates.[44] Although comments were received in response to this *Notice,* the issues raised remain unresolved. The earlier *Notice* and the comments received in response to it generally explored three basic questions. First, to what extent was section 623 of the Communications Act intended to apply to commercial rates? Section 623(a)(2)(A) provides that rates charged by an operator for basic service "shall be subject to regulation."[45] Second, how should commercial rates be defined in the cable context? And third, because commercial subscribers may have greater access to competitive sources of supply, are market forces sufficient to ensure that rates are reasonable in the absence of direct regulation? We invite interested parties to update the record on these or related issues regarding commercial rates.

H. Small system issues

31. The Commission has previously addressed rate regulation issues that are specific to operators of small systems.[46] As the competitive landscape changes, we continue to believe that it is

---

[42] *Implementation of Sections of the Cable Television Consumer Protection and Competition Act of 1992 -- Rate Regulation, Uniform Rate Setting Methodology*, CS Docket No. 95-174, Notice of Proposed Rulemaking, 11 FCC Rcd 3791 (1995); Report and Order, 12 FCC Rcd 3425 (1997); 47 C.F.R. § 76.922(n).

[43] *Implementation of Sections of the Cable Television Consumer Protection and Competition Act of 1992, Rate Regulation,* MM Docket No. 92-266, *Cable Pricing Flexibility*, CS Docket No. 96-157, Memorandum Opinion and Order and Notice of Proposed Rulemaking, 11 FCC 2d 9517 (1996) (docket remains open).

[44] *Second Reconsideration*, 9 FCC Rcd at 4248-49 ¶ 257.

[45] 47 U.S.C. § 543(a)(2)(A).

[46] *See Rate Order*, 8 FCC Rcd at 5921-24 ¶¶ 462-65 (franchising authorities could accept rate certifications; rate formula reflected substantive relief); *Second Reconsideration*, 9 FCC Rcd at 4220-29 ¶¶ 206-21 (streamlined rate reduction for initial regulated rates; equipment averaging); *Fifth Reconsideration*, 9 FCC Rcd 5327 (administrative relief); *Going Forward Order*, 10 FCC Rcd at 1258-59 ¶¶ 87-94 (small system headend upgrade incentive); *Seventh Reconsideration*, 10 FCC Rcd 3225 (small system headend upgrade incentive allowed in addition to other rate-setting methodologies); *Eighth Reconsideration,* 10 FCC Rcd 5179 (alternative rate regulation agreements between small systems and franchising authorities); *Ninth Reconsideration*, 10 FCC Rcd 5198 (inflation adjustments for small systems receiving transition rate relief); *Tenth Reconsideration*, 10 FCC Rcd 6870 (reduced reporting burden for small systems with transition rates); *Small System Order*, 10 FCC Rcd 7393 (defined small system and small

(continued....)

important to recognize the unique challenges facing small operators of small systems and to make sure that the regulation process does not impede the ability of these systems to raise capital and position themselves to respond to the challenges resulting from competition. Smaller multiple system operators have been described as holding "small-town, rural properties that lack the heft to be upgraded efficiently and, hence, have been ravaged by DirecTV and EchoStar."[47]

32. Recognizing the continuing difficulties faced by operators of smaller systems, we seek comment on any changes in the rate rules that might address the problems associated with the simultaneous growth in competition and need for additional investment to upgrade facilities. We seek comment as to whether changes proposed in this notice of proposed rulemaking, such as elimination of consideration of the CPST from our rules and rate forms, will have an untoward effect on small systems. We also seek comment on whether the presumptively reasonable per channel rate in section 76.934(h)(5) of our rules should be reexamined if CPST channels, expenses, and rate base are no longer included on FCC Form 1230.[48]

33. The Commission has asked for comment about the process for setting initial regulated rates *supra* in section II.E. Section 76.922(b)(5) of the Commission's rules allows small systems owned by small cable companies to use streamlined rate reductions for setting initial regulated rates.[49] We seek comment on whether small systems have need for streamlined rate reductions in light of the availability of small system rate relief in section 76.934 of the Commission's rules, including the small system cost-of-service methodology in section 76.934(h) and FCC Form 1230.

I. Cost-of-service rate process

34. Another rate issue concerns the alternative "cost-of-service" rate setting process. This is a very information and labor intensive mechanism for establishing rates. It was adopted as a safety valve mechanism to take care of particularly high cost systems that might not receive a constitutionally adequate rate of return under the benchmark system. The Commission adopted interim cost rules to permit operators to recover operating expenses and a fair return on investment for regulated services, while protecting subscribers from unreasonable rates,[50] and finalized the rules with adjustments in the *Final Cost Order*.[51] The Commission addressed issues concerning the rate base, including used and useful plant, intangible assets, start-up losses, and tangible assets. It also addressed issues concerning a presumptive rate of return, depreciation, taxes, cost allocation, accounting requirements, affiliate transactions, and hardship relief. At the same time, it issued a further notice of proposed rulemaking to explore an optional alternative to the presumptive unitary rate of return for cost of service filings. This further notice as well as petitions for reconsideration of the *Final Cost Order* remain pending.[52]

(...continued from previous page)
cable companies; adopted simplified small system cost of service formula); *Fourteenth Reconsideration*, 12 FCC Rcd 15554 (clarified presumption of reasonableness).

[47] "Meager Mergers, Unless AT&T's In," *Broadcasting and Cable*, February 19, 2001.

[48] 47 C.F.R. § 76.934(h)(5).

[49] 47 C.F.R. § 76.922(b)(5).

[50] *Cost Order*, 9 FCC Rcd 4527.

[51] 11 FCC Rcd 2220; *see* 47 C.F.R. §§ 76.922(i), 76.924. Petitions for reconsideration are pending, and an appeal of the adopted rules has been filed in *Comcast Cable Communications, Inc. v. FCC* (D.C. Cir. Case No. 96-1148). This case has been held in abeyance.

[52] *See* Jones Intercable, Inc. and Benchmark Communications, Inc., Petition for Reconsideration (filed Apr. 8, 1996) (addressing the straight channel allocator for allocating the cost of commonly used plant, the treatment of
(continued....)

35. With the demise of CPST regulation, it seems possible that the cost-of-service process is no longer needed as an alternative for BST regulation. We seek comment on this question as well as what further actions should be taken in the pending "COS" docket in light of the end of CPST rate regulation. We also seek comment on any impact these questions regarding cost-of-service rules for BST rates will have on determinations of equipment and installation rates pursuant to section 76.923 of the Commission's rules and FCC Form 1205,[53] and on determinations of rate increases for network upgrade surcharges pursuant to section 76.922(j) of our rules and FCC Form 1235.[54] Both incorporate cost-of-service components and section 76.924 cost allocation categories.[55]

J. Abbreviated cost-of-service showing on FCC Form 1235

36. We seek comment about the abbreviated cost-of-service showing permitted for significant network upgrades. This streamlined approach allows cable operators to recover network upgrade costs through a surcharge on regulated rates without having to develop and examine all the costs associated with their systems. Before the end of CPST rate regulation, operators allocated the upgrade costs to the BST, the CPST, and other services, usually based on the system channel capacity devoted to each service,[56] but could elect to recover all the costs associated with regulated services through a surcharge only on the CPST.[57] We seek comment as to whether the abbreviated cost-of-service option continues to meet a need. When the option was adopted, a substantial portion of the services offered over a cable system were subject to rate regulation. The Commission was concerned that benchmark/price cap rates might not provide sufficient revenue to attract capital for upgrades in some cases and that the cost-of-service alternative was unduly burdensome. In light of the breadth of unregulated services that can now be delivered over cable systems, including CPST, we seek comment on whether we should continue to allow operators to file abbreviated cost-of-service showings. Even if the option is eliminated for most cable systems, should the option continue to be available for systems that meet the definition of "small system" under the Commission's rules?

37. If we retain the abbreviated cost-of-service option for the BST, we propose to modify the form used for determining the maximum permitted network upgrade surcharge, FCC Form 1235, to remove the requirement that cost assignments to the CPST and a CPST revenue requirement be shown. With the end of CPST rate regulation, there is no need for separately showing CPST information. We also propose to modify FCC Form 1235 so that rate base recoveries will be limited to an operator's average upgrade investment over the life of the upgrade rather than its total investment over the life of the

---

(...continued from previous page)
unactivated channels, and distributions by non-subchapter C corporations; seeking clarification that adjustments for depreciation expense also be made to accumulated depreciation; and advocating application of a First Amendment intermediate scrutiny test to the rate-setting process); Petition by the Southern New England Telephone Company for Partial Reconsideration of the Second Report and Order (filed Feb. 26, 1996) (addressing affiliate transactions).

[53] 47 C.F.R. § 76.923; FCC Form 1205, Determining Regulated Equipment and Installation Costs, "Equipment Form" (June 1996).

[54] 47 C.F.R. § 76.922(j); FCC Form 1235, Abbreviated Cost of Service Filing For Cable Network Upgrades (Feb. 1996).

[55] *See* 47 C.F.R. § 76.924.

[56] *See* FCC Form 1235, Worksheets A, B (cost assignments and allocations; allocation key); FCC Form 1235, Instructions for Completion of Abbreviated Cost of Service Filing for Cable Network Upgrades ("FCC Form 1235 Instructions"), at 8-12 (Instructions for Worksheets A, B); *Final Cost Order*, 11 FCC Rcd at 2270 ¶ 123 ("in most cases, a straight channel ratio would be a reasonable approach to the allocation of plant costs").

[57] *See* FCC Form 1235, Part III (Allocation of Upgrade Revenue Requirement to Basic and Cable Programming Service Tiers); FCC Form 1235 Instructions at 7-8 (Instructions for Part III).

upgrade. Although the rate form currently permits operators to earn a rate of return on their total upgrade investment throughout the life of the upgrade, operators are also allowed to recover depreciation expenses annually. As a result, operators have been able to continue recovering a rate of return on investment that has already been recovered through depreciation. We seek comment on these proposals and also on whether other adjustments to the abbreviated cost-of-service showing are needed.

K. Rates of interest

38. Operators using the annual rate adjustment methodology calculated on FCC Form 1240 must correct for over- and underestimations of projected costs, with interest at 11.25%. We seek comment as to whether we should revise the rate of interest in section 76.922(e)(3)(i) and the instructions for Form 1240, Module H, Lines H4 and H8, and what an appropriate rate of interest should be.[58] Should it be fixed in the rules and rate form calculation or tied to some kind of indicator? If the latter, what should the indicator be? If the rate of interest in section 76.922(e)(3)(i) is revised, should that revised rate of interest be used for the interest on franchise fee refunds owed by the franchising authority to the cable operator pursuant to section 76.942(f)?[59] The interest rate currently specified in section 76.942(f) is 11.25%.

39. Section 76.942(e) currently provides that refunds for subscriber rate overcharges shall be "computed at applicable rates published by the Internal Revenue Service for tax refunds and additional tax payments."[60] Should the rule specify which rate should be used or whether the higher (or lower) of the two rates is to be used?

L. Unbundling

40. Operators setting initial regulated rates were required to unbundle equipment costs from programming rates. In the *Third Reconsideration*, the Commission expressed concern about evasions of rate regulation, such as charging for services previously provided without extra charge unless the value of that service, as reflected in new charges, "was removed from the base rate number when calculating the reduction in rates necessary to establish reasonable [programming service] rates."[61] Questions have been raised about the continued applicability or the appropriate response to this Commission concern. We request comment on this matter.

M. Refunds

41. Section 76.942 of the Commission's rules addresses refunds of previously paid rates in excess of maximum permitted rates.[62] We seek comment on whether and, if so, how this rule should be updated.

N. Re-evaluation of the BST rate regulation process

1. Recalibration of the "competitive differential"

42. The foregoing discussion has addressed adjustments to our rate rules based on the

[58] *See* 47 C.F.R. § 76.922(e)(3)(i); Instructions for FCC Form 1240, Annual Updating of Maximum Permitted Rates for Regulated Cable Services, "Annual Update Form" (July 1996), at 20, 21, Lines H4, H8.

[59] 47 C.F.R. § 76.942(f).

[60] 47 C.F.R. § 76.942(e).

[61] *Third Reconsideration,* 9 FCC Rcd at 4365 ¶ 135.

[62] 47 C.F.R. § 76.942.

assumption that the benchmark/price cap process we have adopted should continue. We seek comment as to whether a more fundamental change to our rate regulations should be enacted, for example, by recalibrating the "competitive differential" between monopoly systems (those subject to regulation) and competitive systems (those not subject to regulation because of the presence of effective competition) focusing specifically on basic tier service. The initial process of attempting to calculate the competitive differential was based on 1992 data for a relatively small sample of competitive systems and did not focus on basic tier service separate from CPST service. Would there now be significant value in attempting to recalibrate the whole process through a new rate comparison? Would it be possible to find appropriate samples, and how should the resulting differential be used in the resulting rate setting process? Should we consider data from all four types of systems reflected in the statutory effective competition test or focus on particular types of systems?[63] Should we take upgrades into account as a separate factor? This task could conceivably be accomplished (although with some considerable effort) by expanding the annual price survey process.[64]

2. Other approaches to BST rate regulation

43. We also seek comment as to whether there is another method for regulating BST rates that will ensure reasonable rates for basic service through a simplified regulatory process.[65] For any alternatives proposed, commenters should discuss how the alternative would be implemented. Commenters should also address the regulatory costs to cable operators and franchising authorities from implementing a proposed alternative, and how the Commission would review the reasonableness of a franchising authority's rate action. If an alternative is adopted, should it replace the traditional approach to rate regulation or be available as an alternative to traditional rate regulation?

O. Equipment and inside wiring rate regulation

44. Associated with basic service tier rate regulation is the regulation of certain charges for equipment that is used with the provision of basic service. There are three matters here on which we seek comment. The first relates to the definition of the type of equipment that is subject to regulation; the second, to whether it is possible, or may become possible in the future, to rely on market forces to ensure that the rates involved are kept at a reasonable level; the third, to the showing on the rate form.

45. With respect to the first point, there is some tension in the Communications Act as to what equipment is subject to regulation by local authorities along with basic tier service. The Act, including in particular sections 623(b)(3) and 623(l)(2), seems to suggest that some equipment might be specifically associated with the basic tier[66] and some with the CPST or with other unregulated service

---

[63] *See supra* note 6.

[64] *See* 47 U.S.C. § 543(g) (Commission is to require the annual filing of "such financial information as may be needed for purposes of administering and enforcing this section"); *id.* § 543(k) (Commission is to report annually on average rates for BST, other cable programming, and equipment of systems found to be subject to effective competition and systems not found to be subject to effective competition); 47 C.F.R. § 76.1800 Note 2.

[65] *See* H.R. CONF. REP. NO. 862, 102d Cong., 2d Sess. 62 (1992), expressing Congress' intent "to give the Commission the authority to choose the best method of ensuring reasonable rates for the basic service tier and to encourage the Commission to simplify the regulatory process."

[66] 47 U.S.C. § 543(b)(3), which relates to the establishment of basic tier rate regulation states:

> The regulations prescribed by the Commission under this subsection shall include standards to establish, on the basis of actual cost, the price or rate for--
>
> (A) installation and lease of the equipment used by subscribers to receive the basic service tier, including a converter box and a remote control unit and, if requested by the subscriber, such

(continued....)

offerings.[67] The Act, however, did not make clear specifically how to connect a particular type of equipment with a particular service tier. As a practical matter, because there is a statutory requirement that all subscribers receive basic tier service, virtually all equipment used for the receipt of video service has been regarded as associated with the basic tier of service.[68] The definitional tension involved was acknowledged when the Commission adopted its initial rules.[69] At that time, however, the Commission felt obliged to give an "expansive reading"[70] to the basic tier definition even though it resulted in virtually no equipment coming within the CPST tier equipment definition. The Commission suggested at the time that this was a matter requiring further review.[71]

46. Since that time there have been two changes that warrant a new a look at this issue. First, there has been the introduction of tiers of digital video service that involve the use of a digital set-top box, the functions and cost of which are largely associated with non-basic service offerings. And second, section 629 of the Communications Act was adopted as part of the Telecommunications Act of 1996.[72] This provision, entitled "Competitive Availability of Navigation Devices," is intended to create a competitive market for equipment used to access cable and other MVPD services.

47. In light of these changes, we seek comment on whether the categorization of equipment should be reconsidered. In particular, would it be appropriate to associate digital equipment or other equipment that involves investments very largely used to receive CPST or other unregulated services with the non-regulated tiers for rate regulation purposes? If it is appropriate, should this association be discretionary or mandatory for the cable operator?

48. Alternatively, we seek comment on whether a process should be established so that when a competitive market for equipment or wiring can be demonstrated to exist, governmental rate setting should cease and the presence of competitive alternatives allowed to ensure that the rates in question meet the statutory "actual cost" standard.[73] We seek comment on whether this would be consistent with existing precedent.[74] We also seek comment on whether other changes in the equipment rate regulation

---

(...continued from previous page)

> addressable converter box or other equipment as is required to access programming described in paragraph (8)[tier buy-through provision]; and
>
> (B) installation and monthly use of connections for additional television receivers.

[67] Section 623(l)(2) states:

> The term "cable programming service" means any video programming provided over a cable system, regardless of service tier, <u>including installation or rental of equipment used for the receipt of such video programming,</u> other than (A) video programming carried on the basic service tier, and (B) video programming offered on a per channel or per program basis. (Emphasis added).

[68] *See* 47 U.S.C. § 543(b)(7)(A); 47 C.F.R. § 76.923(a).

[69] *Rate Order*, 8 FCC Rcd at 5802 ¶ 276.

[70] *Id.* at 5806-07 ¶ 283. *See also id.* at 5800 ¶ 273 ("We further conclude that Congress intended these actual cost regulations to cover all installations and equipment used by subscribers to receive the basic service tier in systems not subject to effective competition, even if the installation or equipment is also used for other cable services.").

[71] *Id.* at 5805-06 ¶ 282.

[72] 47 U.S.C. § 549.

[73] Remote control units, for example, have previously been argued to be widely and competitively available. *See Rate Order*, 8 FCC Rcd at 5802-03 ¶ 277.

[74] The Commission found it unnecessary to regulate the rates for "new product" CPS tiers directly based on a conclusion that rates for such tiers would otherwise be protected against unreasonable increase. *Going Forward* (continued....)

rules might be used to assist in the creation of a more competitive market for equipment in a manner consistent with section 629. Operators might, it has been suggested, avoid regulation of a type of equipment by certifying that a particular type of equipment is available for sale or lease from third party sources and that subscribers have been advised of that fact.[75] In this regard we note that the equipment rate regulation process may interfere with the development of such a market.[76] Would or should substitution of marketplace regulation for direct regulation of equipment rates affect the regulation of rates for installing or maintaining the affected equipment and charges for customer-initiated changes in equipment?[77]

49. We also seek comment on whether FCC Form 1205 can be simplified in any way to ease the burden of regulation on both cable operators and franchising authorities. The Communications Act provides that cable operators can aggregate costs into broad categories and at the level of the operator's choice,[78] subject to the requirement that Commission regulations include standards to establish equipment and installation rates on the basis of actual cost.[79] FCC Form 1205, designed to implement these requirements, calculates rates on a cost-of-service basis and must be filed annually.[80] Once an operator has established equipment rates based on its costs, is there a less burdensome way to adjust equipment or installation rates that would be consistent with the statutory standard? Can any information used in setting rates be standardized based on industry-wide information? If so, how would that process work?

P. Recovery of lost revenues for equipment and installation due to subsequently reversed rate orders

50. A cable operator's permitted rates for equipment and installation are computed on FCC Form 1205 and submitted for franchising authority review in advance of the intended implementation date. If a franchising authority disallows any or all of the proposed rate increase and the local rate order is reversed on appeal to the Commission, the cable operator may be unable to recoup revenues lost or refunds paid pursuant to the erroneous rate order. This creates an incentive for the operator to disregard the rate order or seek a stay of the rate order from the Commission. To address this problem, should we allow cable operators to recover the amount of revenues lost or excess refunds paid due to local rate orders subsequently reversed by the Commission through an entry on Form 1205, perhaps as an "other"

(...continued from previous page)
Order, 10 FCC Rcd at 1234-39 ¶¶ 22-37, *review denied sub nom. Adelphia Communications Corp. v. FCC*, 88 F.3d 1250 (D.C. Cir. 1996). The Cable Services Bureau found the offering of an inside wire maintenance service plan covering both cable television and telephone wiring not to be subject to regulation based, at least in part, on the availability of competitive providers of this service. *Request for Clarification of Rate Regulatory Rules: Inside Wire Maintenance,* 16 FCC Rcd 2198 (2001).

[75] *Rate Order*, 8 FCC Rcd at 5802-03 ¶ 277.

[76] *See, e.g.*, CS Docket No. 97-80, Letter from Radio Shack Corporation and Circuit City Stores, Inc. to Chairman Michael K. Powell, FCC (Apr. 16, 2001); CS Docket No. 97-80, Letter from Neal M. Goldberg, NCTA, to Commissioner Susan Ness, FCC (May 16, 2001). Section 629 contains a direction that equipment charges not be subsidized by charges for any programming services. Concerns have been raised relating to both the limits on the rate of return that regulated equipment providers are entitled to receive and the distortions in that market created by section 623(a)(7) and the associated rules, which specifically permit the aggregation of low cost and high cost devices for rate setting purposes. *See* 47 U.S.C. § 543(a)(7); 47 C.F.R. § 76.923(c)(1).

[77] *See* 47 C.F.R. §§ 76.923, 76.980(c).

[78] 47 U.S.C. § 543(a)(7).

[79] 47 U.S.C. § 543(b)(3).

[80] *See* 47 § 76.923(n).

expense on Form 1205, Schedule B? Our concern is that, when franchising authorities unreasonably limit rates, they deny operators the cost recovery determined to be permissible under the Commission's rules and rate forms and contemplated by section 623(b)(3). We do not propose to allow operators voluntarily setting rates below the permitted rate to recover the shortfall. We seek comment on this proposal.

Q. Charges for changes in service tiers

51. Charges for changes in service tiers initiated by the subscriber have been limited to actual costs by section 76.980 of the Commission's rules.[81] We seek comment on the effect of the end of CPST rate regulation on regulation of rates for service tier changes.

R. Effective competition showings

52. Another area where it has been informally suggested that our rate regulation process might be improved relates to the procedures used to demonstrate the presence of effective competition. Pursuant to section 623, rate regulation in a community ends when effective competition is present.[82] In the absence of a demonstration to the contrary, cable systems are presumed not to be subject to effective competition.[83] The cable operator bears the burden of rebutting the presumption that such effective competition does not exist and so must provide evidence sufficient to demonstrate that effective competition is present in the franchise area.[84]

53. The Commission's *Eighth Competition Report* states that DBS penetration now exceeds 20% of television households in 30 states and 30% in five states.[85] The growth and development in DBS services has suggested to some that the effective competition determination process should be expedited, for example, by altering the burden of proof in areas of high DBS penetration so that community-by-community decisions might not always be needed. Thus, we seek comment on whether there are techniques consistent with the Communications Act to improve and expedite effective competition showings and review as competition, particularly from satellite service, becomes more prevalent.

S. Procedures for Commission review of local rate decisions

54. Finally, we seek comment on whether there are procedural aspects of the Commission's review of local rate decisions that might be improved. In particular, should the deference already given to these local rate decisions be increased so that the Commission would intervene only when there were significant deviations from the established rules?

III. ORDER: INTERIM RATE ADJUSTMENTS FOR BST CHANNEL CHANGES

55. In light of the confusion created by section 76.922(g)(8) of the Commission's rules and the intent expressed in the *Going Forward Order* that there be some mechanism for dealing with channel changes if the incentives in paragraph (g) were not renewed,[86] we clarify how channel changes should be

[81] 47 C.F.R. § 76.980.

[82] *See supra* note 6.

[83] See 47 C.F.R. § 76.906.

[84] 47 C.F.R. § 76.907(b).

[85] *See Annual Assessment of the Status of Competition in the Market for the Delivery of Video Programming*, CS Docket No. 01-129, Eighth Annual Report, 17 FCC Rcd 1244, 1273 ¶ 58 (2002) (citing Satellite Broadcasting and Communications Ass'n Comments at 3-4 and App. A).

[86] *See* 47 C.F.R. § 76.922(g); *Going Forward Order*, 10 FCC Rcd at 1260 ¶ 98.

handled pending action on this notice of proposed rulemaking. We base this clarification on the provisions in paragraph (g) and Forms 1210 and 1240 for the BST, which are understood by cable operators and franchising authorities. We also take into consideration the sunset of CPST rate regulation. Franchising authorities reviewing rates should accept rate adjustments for channels added to the BST using the per channel adjustment factor in section 76.922(g)(2), based on the number of channels that would have been subject to regulation if CPST rate regulation had not ended. Franchising authorities should also accept and may require rate adjustments for channel deletions and substitutions consistent with section 76.922(g)(4) and (g)(6), respectively.[87] The calculations should be done using FCC Forms 1210 and 1240. We will review appeals of local rate orders consistent with this approach. In reviewing appeals of local rate orders concerning rate adjustments for the movement of channels between tiers of regulated service, we will find reasonable orders that are consistent with section 76.922(g)(5) and the Commission's rate forms for BST channels and also for CPST channels moved on or before March 31, 1999, the sunset of CPST rate regulation, provided that the rate adjustments are computed from CPST rates that were subject to rate regulation.[88] The provisions in section 76.922(f), (g) of the Commission's rules concerning external costs, including the permitted 7.5% mark-up on programming cost increases, continue to apply. This clarification is consistent with Commission rate forms, which have remained in effect since their adoption, and with the Commission's handling of rate complaints and stays of local rate appeals. Without this clarification, subscribers may experience a decrease or change in BST service without a corresponding adjustment to their rates. The clarification with respect to the movement of channels between tiers maintains the balance between regulated revenue sources, which has been a consistent part of our rate regulations, for the period that the CPST was subject to rate regulation. Because of our concern about determining the CPST residual from unregulated rates, we will not find franchising authority orders unreasonable for disallowing the movement of residual for channels moved from the CPST to the BST after the sunset of CPST rate regulation. However, franchising authorities that have accepted a residual movement from the CPST to the BST either in orders or by inaction within the period for reviewing a Form 1240 should not change that determination in the true-up process. Our intent with these interim guidelines is to create some stability in the rate-making process pending resolution of this proceeding, not to overturn rate adjustments previously accepted based on a good faith interpretation of our rules and rate forms.

IV. ADMINISTRATIVE MATTERS

A. Initial Regulatory Flexibility Analysis

56. As required by the Regulatory Flexibility Act of 1980, as amended ("RFA"),[89] the Commission has prepared this present Initial Regulatory Flexibility Analysis ("IRFA") of the possible significant economic impact on a substantial number of small entities by the policies and rules proposed in this Notice of Proposed Rulemaking ("NPRM"). Written public comments are requested on this IRFA. Comments must be identified as responses to the IRFA and must be filed by the deadlines for comments provided in paragraph 77 of the item. The Commission will send a copy of the NPRM, including this

[87] Briefly, when an operator deletes a channel pursuant to 47 C.F.R. § 76.922(g)(4), the operator reduces the rate to reflect the net reduction in external costs and the residual associated with the dropped channel. For channels added pursuant to the caps method, the residual is the actual per channel adjustment taken for that channel when it was added to the tier. When an operator substitutes a channel pursuant to 47 C.F.R. § 76.922(g)(6), its rate must reflect the net difference in programming costs associated with the substitution.

[88] 47 C.F.R. § 76.922(g)(5) provides for the revenue-neutral movement of residual associated with a channel when the channel is moved between rate regulated tiers of service.

[89] *See* 5 U.S.C. § 603. The RFA, *see* 5 U.S.C. § 601 – 612, has been amended by the Small Business Regulatory Enforcement Fairness Act of 1996 (SBREFA), Pub. L. No. 104-121, Title II, 110 Stat. 857 (1996).

IRFA, to the Chief Counsel for Advocacy of the Small Business Administration ("SBA").[90] In addition, the NPRM and IRFA (or summaries thereof) will be published in the Federal Register.[91]

1. Need for, and Objectives of, the Proposed Rules

57. The Commission developed rules and forms for the regulation of cable television rates when both the basic service tier ("BST") and the cable programming service tiers ("CPST") were subject to rate regulation. The Commission proposes to update these regulations and rate forms. Updating is needed so that the rules and rate forms will reflect the end of CPST rate regulation pursuant to the Telecommunications Act of 1996.[92] Updating is also needed because the Commission's rule for adjusting rates for changes in the number of channels on the BST has sunset, and cable operators and franchising authorities need guidance about how to adjust rates when the number of BST channels changes.[93] Updating would be needed for rules and rate forms available specifically to small cable systems owned by small cable operators as well as for rules and rate forms used by large systems.

58. The Commission also proposes changes in the regulation of both BST and equipment rates with the objective of improving the existing regulatory structure for all cable systems. For small cable systems owned by small cable operators, the Commission proposes to consider rule changes with the additional objectives of: (1) ensuring that the regulatory process does not impede the ability of small systems to raise capital and respond to competitive challenges, and (2) avoiding an untoward effect on small systems from other changes being considered for the rate rules generally. As discussed in paragraph 67, the Commission also proposes to discontinue the streamlined rate reduction ratemaking method that may no longer be useful for small systems in order to eliminate unneeded requirements.

59. For cable systems in general, including small cable systems, the Commission proposes changes to its rules and rate forms with the objectives of: resolving whether the rates charged to commercial subscribers are regulated rates;[94] eliminating some of the regulatory burdens associated with equipment and inside wiring rates;[95] and reducing the regulatory burden associated with showings that a cable system is no longer subject to rate regulation.[96] The Commission also proposes changes that would streamline the setting of initial regulated rates for previously unregulated systems.[97] This streamlining would be available to small systems not choosing to use one of the special small system ratemaking options.[98]

---

[90] *See* 5 U.S.C. § 603(a).

[91] *Id.*

[92] This is codified as Communications Act §623(c)4), 47 U.S.C. § 543(c)(4).

[93] 47 C.F.R. § 76.922(g)(8).

[94] *See supra* section II.G.

[95] *See supra* section II.O.

[96] *See supra* section II.R.

[97] *See supra* section II.E.

[98] The Commission also proposes rule changes or clarifications that are most likely to be applicable only to cable systems that do not use one of the small cable ratemaking options described *infra* in paragraph 67. These proposed changes and objectives include: providing more flexibility in setting regional rates (*supra* section II.F); clarifying the handling of services provided without an extra charge when initial regulated rates were set, often referred to as "unbundling" (*supra* section II.L); and assessing the continued need for optional cost-of-service and abbreviated cost-of-service ratemaking methodologies (*supra* sections II.I and II.J). Because these proposals are not likely to affect small cable systems, there is no need to consider alternatives to these proposals.

60. In addition, the Commission proposes broader changes to the regulatory process with the objective of ensuring reasonable BST rates through a simplified regulatory process. Change could be accomplished by recalibrating the competitive differential that forms the basis for determining regulated rates or by another alternative proposed by commenters.[99]

2. Legal Basis

61. The authority for the action proposed in this rulemaking is contained in sections 1, 2(a), 3, 4(i), 4(j), 303(r), 601(3), 602, and 623 of the Communications Act of 1934, as amended, 47 U.S.C. §§ 151, 152(a), 153, 154(i), 154(j), 303(r), 521, 522, and 543.

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

62. The RFA directs agencies to provide a description of, and where feasible, an estimate of the number of small entities that may be affected by the proposed rules, if adopted.[100] The RFA generally defines the term "small entity" as having the same meaning as the terms "small business," "small organization," and "small governmental jurisdiction."[101] In addition, the term "small business" has the same meaning as the term "small business concern" under the Small Business Act.[102] 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 SBA.[103]

63. The SBA has developed a small business size standard for cable and other program distribution, which includes all such companies generating $11 million or less in revenue annually.[104] This category includes, among others, cable operators, closed circuit television services, direct broadcast satellite services, multipoint distribution services, open video systems, satellite master antenna television systems, and subscription television services. According to the Census Bureau data from 1992, there were 1,788 total cable and other pay television services and 1,423 had less than $11 million in revenue.[105] We address cable operators below to provide a more precise estimate of the affected small entities. We do not believe that the other pay television services would be affected by the proposals in this notice of proposed rulemaking.

64. *Cable Systems*. The Commission has developed its own small business size standard for

[99] *See supra* section II.N.

[100] 5 U.S.C. § 603(b)(3).

[101] *Id.* § 601(6).

[102] *Id.* § 601(3) (incorporating by reference the definition of "small business concern" in the Small Business Act, 15 U.S.C. § 632). 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 Small Business Administration 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."

[103] 15 U.S.C. § 632.

[104] 13 C.F.R. § 121.201, North American Industry Classification System ("NAICS") codes 513210 and 513220.

[105] *See U.S. Department of Commerce, Bureau of the Census, 1992 Economic Census Industry and Enterprise Receipts Size Report,* Table 2D (U.S. Bureau of the Census data under contract to the Office of Advocacy of the U.S. Small Business Administration). These data have been updated for 1997, but without the small business breakout. *See* Summary, 1997 Economic Census, Subject Series: Information, at 24 (issued April 2001). By 1997, the census total for firms in this category had increased to 4,185. *Id.*

a small cable operator for the purposes of rate regulation. Under the Commission's rules, a "small cable company" is one serving fewer than 400,000 subscribers nationwide.[106] Based on our most recent information, we estimate that there were 1,439 cable operators that qualified as small cable companies at the end of 1995.[107] 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 operators. Consequently, we estimate that there are fewer than 1,439 small cable companies that may be affected by the proposed rules. A "small system" under the Commission's rules, is one serving "15,000 or fewer subscribers. The service area of a small system shall be determined by the number of subscribers that are served by the system's principal headend, including any other headends or microwave receive sites that are technically integrated to the principal headend."[108]

65. The Communications Act of 1934, as amended, also contains a size standard for a "small cable operator," which is "a cable operator that, directly or through an affiliate, serves in the aggregate fewer than one 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."[109] The Commission has determined that there are 67,700,000 subscribers in the United States.[110] Therefore, an operator serving fewer than 677,000 subscribers shall be 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.[111] Based on available data, we estimate that the number of cable operators serving 677,000 subscribers or less totals approximately 1,450.[112] We do not request or collect information on whether cable operators are affiliated with entities whose gross annual revenues exceed $250,000,000,[113] and therefore are unable to estimate accurately the number of cable system operators that would qualify as small cable operators under the definition in the Communications Act.

4. Description of Projected Reporting, Recordkeeping and Other Compliance Requirements for Small Entities

66. Cable operators whose basic service tier rates are regulated must justify their basic service tier and associated equipment and installation rates using Commission rate forms.[114] When

[106] 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. *See Small System Order*, 10 FCC Rcd at 7408-7409 ¶¶ 28-30.

[107] Paul Kagan Assocs., Inc., Cable TV Investor, Feb. 29, 1996 (based on figures for Dec. 30, 1995).

[108] 47 C.F.R. § 76.901(c).

[109] 47 U.S.C. § 543(m)(2).

[110] *See FCC Announces New Subscriber Count for the Definition of Small Cable Operator,* 16 FCC Rcd 2225 (2001).

[111] 47 C.F.R. § 76.1403(b).

[112] *See* 16 FCC Rcd 2225.

[113] We do receive such information on a case-by-case basis only if a cable operator appeals a local franchise authority's finding that the operator does not qualify as a small cable operator pursuant to section 76.901(f) of the Commission's rules. See 47 C.F.R. § 76.990(b).

[114] *See* FCC Forms 1200, 1205, 1210, 1220, 1230, 1235, and 1240. The Commission's rules also reference FCC Forms 1211, 1215, and 1225. As noted *supra* note 17, Form 1211 is not in use and references will be deleted from the Commission's rules. As noted *supra* para. 11, the Commission advised the Office of Management and Budget that it would no longer support use of FCC Forms 1215 and 1225, and dropped these forms from its information collection budget effective April 30, 1997. The Commission proposes to drop references to these forms from its rules.

changes to the rate rules are determined, rate forms will be modified accordingly. Elimination of information regarding the CPST is anticipated, because CPST is no longer subject to rate regulation. One of the affected forms would be FCC Form 1230 used for small system cost-of-service showings.[115] Entities using FCC Form 1230 have previously aggregated data for CPST and BST. If CPST data is no longer included, they would bear the burden of excluding CPST data from the data included on the rate form. In addition, the presumptively reasonable rate in section 76.934(h) of the Commission's rules may change to reflect the elimination of CPST data from the relevant data on FCC Form 1230.[116] No other increase in the regulatory burden on small systems is expected to result from this proceeding.

67. The Commission's rules currently offer regulatory options to small systems owned by small cable operators that are less burdensome than the regulations applicable to larger cable systems and operators. One is the small system cost-of-service option discussed above in paragraph 66. Another option, the streamlined rate reduction for systems first becoming subject to rate regulation,[117] could be eliminated pursuant to proposals in the NPRM.[118] Easing the regulatory burden of establishing initial regulated rates as proposed in the NPRM would provide a reason for finding this option unnecessary,[119] and FCC Form 1230 described in paragraph 66 will continue to be available. Two more small system options, certifying with the franchising authority's consent that rates comply with the Commission's rate rules and entering into an alternative rate regulation agreement with the franchising authority,[120] would not be affected by this proceeding.

5. Steps Taken to Minimize Significant Impact on Small Entities and Significant Alternatives Considered

68. The RFA requires an agency to describe any significant, specifically small business, alternatives that it has considered in reaching its proposed approach, which may include the following four alternatives (among others): "(1) the establishment of differing compliance or reporting requirements or timetables that take into account the resources available to small entities; (2) the clarification, consolidation, or simplification of compliance and reporting requirements under the rule for such small entities; (3) the use of performance rather than design standards; and (4) an exemption from coverage of the rule, or any part thereof, for such small entities."[121]

69. As noted in paragraphs 57, 58, and 59, the Commission will consider potential revisions to cable television rate regulations in order to conform the rules to the sunset of CPST rate regulation and to improve the existing regulatory structure. Alternatively, the Commission will consider broader changes, as noted in paragraph 60.[122]

---

[115] *See* 47 C.F.R. § 76.934(h); FCC Form 1230, Establishing Maximum Permitted Rates for Regulated Cable Services on Small Cable Systems (Aug. 1995).

[116] *See supra* paragraph 32.

[117] *See* 47 C.F.R. § 76.922(b)(5).

[118] *See supra* para. 33. *See* also *supra* n.114 regarding dropping FCC Form 1225 from the Commission's rules. Form 1225 is a more burdensome way to establish regulated rates using cost-of-service methodology than FCC Form 1230.

[119] *See supra* section II.E.

[120] *See* 47 C.F.R. § 76.934(b), (g).

[121] 5 U.S.C. § 603(c)(1) – (c)(4).

[122] *See supra* section II.N.

70. The Commission's rules currently give small systems owned by small cable companies options for establishing their regulated BST rates that are less burdensome than the ratemaking methods used by large entities.[123] The Commission will consider amending the rule addressing one of the options, small system cost of service showings, to reflect the end of CPST rate regulation, and making conforming changes to its FCC Form 1230, which is used for establishing permitted rates on small systems.[124] Except at noted in paragraph 66, these changes should not increase the regulatory burden small systems face as a result of rate regulation, but eliminating CPST-associated costs and expenses from the rate base could have an impact on the resulting BST per channel rate. We do not have a basis for determining what that impact will be. An alternative is to consider changes in the rate rules that might address continuing difficulties faced by operators of small systems, such as the problems associated with the simultaneous growth in competition and the need for additional investment to upgrade facilities.[125]

71. Small systems owned by small cable companies can choose to adjust their regulated rates using the price cap methodology included in the Commission's rules.[126] The rule governing changes in the number of channels has sunset and is under review in the NPRM.[127] The approach ultimately adopted in this proceeding could require revisions to the Commission's rate forms.[128] While we do not anticipate that rule changes will result in an increase in the burden of computing rate adjustments on rate forms, the approach adopted in the rulemaking proceeding could affect the maximum permitted rate computed on the rate forms, particularly for systems moving a large number of channels from or to the BST. The Commission does not have a basis for determining what that impact will be. A corollary issue is the appropriate adjustment to rates for adding or removing digital television broadcast signals from the BST.[129]

72. The Commission also has under consideration a less burdensome way to set initial regulated rates than currently provided in the rules when a previously unregulated system first becomes subject to rate regulation.[130] Options include limiting the period addressed in the rate review and looking to the rates of comparable systems. These changes would apply to large systems, but any changes made by the Commission would be available to small systems. Small systems owned by small cable companies currently have ratemaking options available that are less burdensome than the ratemaking process for other systems. These are the FCC Form 1230 option, the certification option available with the consent of the franchising authority, and the negotiated rate option, which are described in paragraph 67.[131] These options would continue to be available to small systems. The Commission will consider whether there is a continued need for the streamlined rate reduction method that is available only to small systems setting initial regulated rates.[132]

---

[123] *See* 47 C.F.R. §§ 76.901(c), (e), (f), 76.922(b)(5), 76.934. *See also* FCC Form 1230.

[124] *See supra* paras. 9, 11, proposing to amend section 76.934 of the Commission's Rules and FCC Form 1230.

[125] *See supra* section II.H. Comment is sought on this topic.

[126] *See* 47 C.F.R. §§ 76.922(d), (e), 76.934(h)(8).

[127] *See supra* section II.B.

[128] *See* FCC Form 1210, Updating Maximum Permitted Rates for Regulated Cable Services (May 1995); FCC Form 1240, Updating Maximum Permitted Rates for Regulated Cable Services (July 1996).

[129] *See supra* section II.D.

[130] *See supra* section II.E.

[131] *See* 47 C.F.R. § 76.934.

[132] *See supra para. 67.*

73. With respect to equipment rates, the Commission has three matters under consideration: the definition of equipment that is subject to regulation; whether reliance can be placed on competitive forces to ensure reasonable rates; and the rate form used primarily by large cable companies.[133] Because small cable systems owned by small cable companies have the option of using the small cable cost of service ratemaking methodology on FCC Form 1230, the regulatory burden of equipment rate regulation is currently less than that experienced by large cable systems. The regulatory approaches addressed in the NPRM with respect to equipment look toward easing the regulatory burden on cable operators generally and, if adopted, should not result in increased burdens on small cable systems.

74. Finally, the Commission is considering the showing needed to establish effective competition.[134] Only cable systems that are not subject to effective competition are subject to rate regulation by franchising authorities. Small systems would benefit from any efficiencies in demonstrating effective competition.

6. Federal Rules Which Duplicate, Overlap, or Conflict with the Commission's Proposed Rules

75. None.

B. Initial Paperwork Reduction Act of 1995 Analysis

76. This NPRM contains a modified information collection. The Commission, as part of its continuing effort to reduce paperwork burdens, invites the general public and the Office of Management and Budget ("OMB") to take this opportunity to comment on the information collections contained in this NPRM, as required by the Paperwork Reduction Act of 1995, Public Law 104-13. Public and agency comments are due at the same time as other comments on this NPRM; OMB notification of action is due 60 days from date of publication of this NPRM in the Federal Register. Comments should address: (a) 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; (b) the accuracy of the Commission's burden estimates; (c) ways to enhance the quality, utility, and clarity of the information collected; and (d) ways to minimize the burden of the collection of information on the respondents, including the use of automated collection techniques or other forms of information technology.

C. Procedural Provisions

77. *Comments and Reply Comments.* Pursuant to Sections 1.415 and 1.419 of the Commission's rules, 47 C.F.R. §§ 1.415, 1.419, interested parties may file comments on or before 60 days after publication in the *Federal Register*, and reply comments on or before 90 days after publication in the *Federal Register*. Comments may be filed using the Commission's Electronic Comment Filing System (ECFS) or by filing paper copies. *See Electronic Filing of Documents in Rulemaking Proceedings*, 63 Fed. Reg. 24121 (1998).

78. Comments filed through the ECFS can be sent as an electronic file via the Internet to <http://www.fcc.gov/e-file/ecfs.html>. Generally, only one copy of an electronic submission must be filed. Although multiple docket numbers appear in the caption of this proceeding, commenters should transmit one electronic copy of the comments only to MB Docket No. 02-144, Revisions to Cable Television Rate Regulations. In completing the transmittal screen, commenters should include their full name, U.S. Postal Service mailing address, and the applicable docket or rulemaking number. Parties may

[133] *See supra* section II.O.

[134] *See supra* section II.R.

also submit an electronic comment by Internet e-mail. To get filing instructions for e-mail comments, commenters should send an e-mail to ecfs@fcc.gov, and should include the following words in the body of the message, "get form <your e-mail address>." A sample form and directions will be sent in reply. Parties who choose to file by paper must file an original and four copies of each filing. Although more than one docket number appears in the caption of this proceeding, commenters should submit copies only to MB Docket No. 02-144, Revisions to Cable Television Rate Regulations. Filings can be sent by hand or messenger delivery, by commercial overnight courier, or by first-class or overnight U.S. Postal Service mail (although we continue to experience delays in receiving U.S. Postal Service mail). The Commission's contractor, Vistronix, Inc., will receive hand-delivered or messenger-delivered paper filings for the Commission's Secretary at 236 Massachusetts Avenue, N.E., Suite 110, Washington, D.C. 20002. The filing hours at this location are 8:00 a.m. to 7:00 p.m. All hand deliveries must be held together with rubber bands or fasteners. Any envelopes must be disposed of before entering the building. Commercial overnight mail (other than U.S. Postal Service Express Mail and Priority Mail) must be sent to 9300 East Hampton Drive, Capitol Heights, MD 20743. U.S. Postal Service first-class mail, Express Mail, and Priority Mail should be addressed to 445 12th Street, SW, Washington, D.C. 20554. All filings must be addressed to the Commission's Secretary, Marlene H. Dortch, Office of the Secretary, Federal Communications Commission. One copy of each filing also must be filed with Qualex International, Portals II, 445 12th Street, SW, Room CY-B402, Washington, DC, 20554. In addition, parties must also send four (4) copies of each paper filing to Wanda Hardy, Media Bureau, 445 12th Street, SW, Room3-A862, Washington, DC 20554. Parties filing electronically must send one electronic copy via e-mail to whardy@fcc.gov.

79. The full text of this document is available for public inspection and copying during regular business hours at the FCC Reference Information Center, Portals II, 445 12th Street, SW, Room CY-A257, Washington, DC 20554. This document may also be purchased from the Commission's duplicating contractor, Qualex International, Portals II, 445 12th Street, SW, Room CY-B402, Washington, DC 20554, telephone 202-863-2893, facsimile 202-863-2898, or via e-mail qualexint@aol.com.

80. Comments and reply comments will be available for public inspection and copying during regular business hours in the FCC Reference Information Center, 445 12th Street, SW, CY-A257, Washington, DC 20554. Persons with disabilities who need assistance in the FCC Reference Center may contact Bill Cline at (202) 418-0270, (202) 418-7365 TTY, or bcline@fcc.gov. Comments and reply comments also will be available electronically at the Commission's Disabilities Issues Task Force web site: www.fcc.gov/dtf, and also from the Commission's Electronic Comment Filing System. Comments and reply comments are available electronically in ASCII text, Word 97, and Adobe Acrobat. Copies of filings in this proceeding may also be purchased from Qualex International, Portals II, 445 12th Street, SW, Room, CY-B402, Washington, DC, 20554, telephone (202) 863-2893, facsimile (202) 863-2898, or via email qualexint@aol.com.

81. This document is available in alternative formats (computer diskette, large print, audio cassette, and Braille). Persons who need documents in such formats may contact Brian Millin at (202) 418-7426, TTY (202) 418-7365, or send an email to access@fcc.gov.

82. The media contact for this proceeding is Margo Domon Davenport at (202) 418- 2949. The Media Bureau contacts for this proceeding are John Norton at (202) 418-7037 or jnorton@fcc.gov, or Wanda Hardy at (202) 418-2129 or whardy@fcc.gov, or TTY at (202) 418-7365 or (888) 835-5322.

83. *Ex Parte Rules.* 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 Commission's rules.[135] 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 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.[136] Additional rules pertaining to oral and written presentations are set forth in section 1.1206(b) of the Commission's rules. Finally, one copy of each disclosure filing also must be filed with other offices, as follows: (1) Qualex International, Portals II, 445 12th Street, SW, Room CY-B402, Washington, DC, 20554; (2) John Norton, Media Bureau, 445 12th Street, SW, Room 4-C764, Washington, DC, 20554; (3)Wanda Hardy, Media Bureau, 445 12th Street, SW, Room 3-A862, Washington, DC, 20554.

V. ORDERING CLAUSES

84. Accordingly, IT IS ORDERED that, pursuant to the authority contained in sections 1, 2(a), 3, 4(i), 4(j), 303(r), 601(3), 602, and 623 of the Communications Act of 1934, as amended, 47 U.S.C. §§ 151, 152(a), 153, 154(i), 154(j), 303(r), 521, 522, 543, the Notice of Proposed Rulemaking IS ADOPTED.

85. IT IS FURTHER ORDERED that the clarification about how channel changes should be handled pending action on this Notice of Proposed Rulemaking, as described *supra* in section III, paragraph 55, IS ADOPTED.

86. IT IS FURTHER ORDERED that the Commission's Consumer and Governmental Affairs Bureau, Reference Information Center, shall send a copy of this Notice, including the Initial Regulatory Flexibility Analysis, to the Chief Counsel for Advocacy of the Small Business Administration.

FEDERAL COMMUNICATIONS COMMISSION

Marlene H. Dortch

Marlene H. Dortch
Secretary

[135] 47 C.F.R. § 1.1206(b).

[136] *See id.* § 1.1206(b)(2).