Charter
COMMUNICATIONS
A WIRED WORLD COMPANY

Neil Smit
President & CEO

February 12, 2007

Marlene H. Dortch
Secretary
Federal Communications Commission
445 12th St., S.W.
Washington, DC 20554

Re: *Charter Communications, Inc. Request for Waiver of 47 C.F.R. § 76.1204(a)(1)*, CSR-7049-Z; CS Docket No. 97-80

Dear Ms. Dortch:

Charter Communications, Inc. submits the following additional information concerning its July 14, 2006 request for a limited waiver of the integration ban for low-end set-top boxes ("Request"). In its Request for Waiver and Reply Comments in support thereof, Charter demonstrated that, compared to other large MVPDs, the digital transition will cost Charter much more per subscriber, yet Charter has far fewer financial resources available to fund it. Charter explained:

> To be able to offer non-integrated, limited-functionality set-top boxes, Charter would have to bear the enormous capital costs of the integration ban up front. Whatever the capabilities of larger cable operators, Charter simply does not have adequate financial resources to undertake this expense for all of its new devices.[1]

The purpose of this letter is to provide additional information to supplement the record evidence regarding Charter's financial situation and the impact of the integration ban on Charter's digital transition.

Charter estimates that, if the waiver is granted, it will deploy approximately 240,000-280,000 low-end set-tops per year and 300,000-350,000 "high-end" set-top boxes (such as HD and DVR boxes). Charter estimates that the application of the integration ban to all of its leased set-top boxes would cost it approximately $100 million between mid-2007 and the end of 2009. Even though the low-cost boxes covered by this waiver represent only 40-45% of the new set-tops, they represent more than half of the cost of the integration ban because the price increase

[1] Request for Waiver at 15 (citing "Charting A New Course," MULTICHANNEL NEWS, Jun. 19, 2006, and "Charter, Hurt By Satellite TV, Posts Wider Loss," WALL STREET JOURNAL, Mar. 2, 2005).

for low-cost devices is disproportionately high.[2] Therefore, Charter estimates that grant of the requested waiver would save it, and its customers, more than $50 million.

These are funds that are essential for Charter to move forward with its digital transition in concert with the DTV transition scheduled for February 2009. Charter has more than $20 billion in outstanding debt obligations,[3] almost 11 times its annualized EBITDA.[4] This leverage ratio is more than three times higher than Comcast and Time Warner and at least 50% more than the leverage borne by most large public MSOs, according to publicly available information.[5] In addition, Charter has experienced a negative free cash flow in each of the past five years.[6] Free cash flow is an important economic metric that indicates a company's ability to fund new capital projects such as broadband infrastructure investment or digital simulcast. Its most recent annual report filed with the U.S. Securities and Exchange Commission explains that:

> We have a history of net losses. Further, we expect to continue to report net losses for the foreseeable future. Our net losses are primarily attributable to insufficient revenue to cover the combination of operating costs and interest cost we incur on our debt ....[7]

As a result, in the first risk factor provided to investors in that report, Charter warned that:

> We may not generate (or, in general, have available to the applicable obligor) sufficient cash flow or access to additional external liquidity sources to fund our capital expenditures, ongoing operations and debt obligations, including our payment obligations under the original notes and the new notes, which could have a material adverse effect on you as holders of the original notes and the new notes.... If we are unable to generate sufficient cash flow or access additional external liquidity sources, we may not be able to service and repay our debt,

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[2] This data is based upon actual price information that Charter has obtained from its suppliers. Higher-end devices already possess more of the requirements that are needed to support CableCARDs.

[3] *See* Exhibit 3 hereto, Charter Communications, Inc. Form 10-Q for the Quarter Ending September 30, 2006, at 5 (showing long-term debt of $18.799 billion and current liabilities of $1.36 billion, offset by $85 million cash), available at http://phx.corporate-ir.net/phoenix.zhtml?c=112298&p=irol-SECText&TEXT=aHR0cDovL2NjYm4uMTBrd2l6YXJkLmNvbS94bWwvZmlsaW5nLnhtbD9yZXBvPXRlbmsma XBhZ2U9NDQ1NDYyNiZhdHRhY2g9T04=. A large portion of these debts was incurred in making investments to upgrade outdated cable systems that Charter acquired from other operators in the 1990s. *See* Charter Reply Comments at 17.

[4] *See id.* at 6 (for nine months ending 9-30-06, showing revenues of $4.09B; annualized EBITDA is revenue less $1.83B operating expenses less $860M administrative expenses, extrapolated to twelve months).

[5] *See* Exhibit 2 hereto.

[6] *See* Exhibit 4 hereto, also available at http://media.corporate-ir.net/media_files/irol/11/112298/proforma_103106.pdf (summarizing public data showing negative free cash flow in every quarter of 2005 and the first three quarters of 2006); *see* Exhibit 5 hereto, 2005 Annual Report at 166 (showing negative free cash flow in 2005 and 2004); *see* Exhibit 6 hereto 2003 Annual Report at 4 (showing negative free cash flow in 2003 and 2002).

[7] *See* Exhibit 7 hereto, Charter Communications Holdings, LLC Form 10-K for the Year 2005, at 1, available at http://library.corporate-ir.net/library/11/112/112298/items/207833/CHTR_AR05.pdf.

operate our business, respond to competitive challenges or fund our other liquidity and capital needs.[8]

Charter therefore has far fewer financial resources than many operators to dedicate to its digital transition above and beyond the amount that would be spent complying with the integration ban.

The Commission has determined that the advancement of a cable operator's digital transition may justify a waiver of the integration ban for certain low-cost devices, "particularly when considered in the context of the Commission's goal in the *2005 Deferral Order* of promoting the digital transition and in light of its potential to further the objectives of Section 706 of the Telecommunications Act of 1996."[9] As an operator of many small, widely-dispersed systems, Charter's financial constraints are especially relevant because the digital transition will cost Charter far more per subscriber than it will for more consolidated MSOs. Charter is a decentralized, highly scattered collection of local systems that were purchased from smaller, often rural operators across the country located in 31 different states.[10] Charter has 3379 franchises, more than four and one-half times as many as Cox, which has a comparable number of subscribers. Other large operators with more concentrated services areas have fewer headends per subscriber and have backbone networks that enable a more cost-efficient delivery of digital services. Charter, on the other hand, does not have a national backbone interconnecting its systems. Charter must therefore spend significantly more per subscriber to launch digital simulcast in many of its markets because of higher distribution costs and because the fixed per-headend costs must be recouped from smaller, more localized bases of customers.

Under Sections 1.3 and 76.7 and of the Commission's rules, the Commission should consider these individualized circumstances in making its determination of whether application of the integration ban to Charter's low-cost devices would produce more incremental benefit for consumers than harm.[11] Given the individualized circumstances discussed above, Charter respectfully submits that grant of the requested waiver would provide a critical boost to Charter's digital transition, whose benefit to consumers outweighs any perceived incremental cost from the exemption of a minority of Charter's set-top boxes from the integration ban.

Very truly yours,

Neil Smit
CEO & President

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[8] *Id.* at 22.

[9] *Bend Cable Communications, LLC d/b/a BendBroadband Request for Waiver of Section 76.1204(a)(1) of the Commission's Rules*, CSR-7057-Z, Memorandum Opinion and Order, DA 07-47, ¶ 21 (rel. Jan. 10, 2007).

[10] *See* Exhibit 1 (map of Charter's service areas).

[11] *See WAIT Radio v. FCC*, 418 F.2d 1153, 1157 (D.C. Cir. 1969) ("The Commission is charged with administration in the 'public interest.' That an agency may discharge its responsibilities by promulgating rules of general application which, in the overall perspective, establish the 'public interest' for a broad range of situations, does not relieve it of an obligation to seek out the 'public interest' in particular, individualized cases.").