

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

FCC 95-397

In the Matter of)
)
 Implementation of Sections of) MM Docket No. 92-266
 the Cable Television Consumer)
 Protection and Competition)
 Act of 1992: Rate Regulation)

THIRTEENTH ORDER ON RECONSIDERATION

Adopted: September 15, 1995

Released: September 22, 1995

By the Commission: Commissioner Chong issuing a statement:

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I. INTRODUCTION

1. The Cable Television Consumer Protection and Competition Act of 1992 ("the 1992 Cable Act") required the Commission to prescribe rate regulations that protect subscribers from having to pay unreasonable rates by ensuring that basic service tier ("BST") and cable programming service tier ("CPST") rate levels do not exceed rates that would be charged in the presence of effective competition.¹ The 1992 Cable Act directed the Commission to "seek to reduce administrative burdens on subscribers, cable operators, franchising authorities and the Commission" in meeting this mandate.²

2. Pursuant to the 1992 Cable Act's rate regulation requirements, we designed a system of rate regulation that ensures subscribers pay reasonable rates for regulated cable services. Our rules for establishing initial rates employ a benchmark formula in lieu of using the cost-of-service methodology that is traditionally applied to public utilities. We developed the benchmark formula because the significant administrative and compliance costs of cost-of-service regulation would impose heavy burdens on regulators and regulated companies.

3. Moreover, as required by the 1992 Cable Act, the benchmark system protects subscribers by ensuring that an operator's regulated rates do not exceed what the operator would charge if it faced effective competition.³ Under our rules, we required most regulated cable operators to either reduce their regulated rates to a level that represented their September 30, 1992 regulated revenues reduced by a 17% "competitive differential" (adjusted for annual inflation increases, changes in external costs and changes in the number

¹ Cable Television Consumer Protection and Competition Act ("1992 Cable Act"), Pub. L. No. 102-385, 106 Stat. 1460 (1992), Sections 623(b), (c) of the Communications Act of 1934, as amended ("Communications Act"), 47 U.S.C. § 543(b), (c). In this order, we modify our rules in light of petitions for reconsideration filed in response to our Second Order on Reconsideration, Fourth Report and Order, and Fifth Notice of Proposed Rulemaking, MM Docket No. 92-266, FCC 94-28, 9 FCC Rcd 4119 (1994) ("*Second Reconsideration Order*"); Third Order on Reconsideration, MM Docket Nos. 92-262 and 92-266, FCC 94-40, 9 FCC Rcd 4316 (1994) ("*Third Reconsideration Order*"); and Fourth Order on Reconsideration, MM Docket No. 92-266, FCC 94-254, 9 FCC Rcd 5795 (1994) ("*Fourth Reconsideration Order*"). We also reconsider, in response to the petitions for reconsideration and on our own motion, certain decisions made in the *Fourth Report and Order* in this docket. The Commission retains jurisdiction to modify on its own motion an order from which reconsideration is sought. See 47 U.S.C. § 405; 47 C.F.R. § 1.108; see also *Central Florida Enterprises v. FCC*, 598 F. 2d 37, 48 n.51 (D.C. Cir. 1978).

² Communications Act, § 623(b)(2)(A).

³ *Id.* at § 623(b)(1).

of programming channels) or submit a cost-of-service showing supporting higher rates.⁴ The 17% "competitive differential" represented the average difference that the Commission determined existed between the rates of competitive and noncompetitive systems.⁵

4. We also adopted a price cap approach to govern how operators can adjust their rates on a going forward basis following the establishment of initial rates. Under the price cap approach, operators adjust their rates annually for inflation and may reflect changes in external costs and changes in the number of regulated channels up to four times per year. Operators make these rate adjustments by filing an FCC Form 1210 pursuant to a streamlined rate review process.

5. Based on information we have secured from operators, we have concluded that we should further streamline the rate review process in ways that will benefit subscribers, cable operators, local franchising authorities, and the Commission. The current process allows, and to some degree encourages, operators to file for multiple rate adjustments during each year. This process can be costly for operators because they must file Form 1210s and provide subscribers with 30 days' advance written notice each time they file for a rate adjustment. In addition, multiple rate adjustments in one year could create subscriber confusion. Multiple rate adjustments also impose administrative burdens on regulatory authorities because they must review each proposed rate adjustment.

6. We have found that under the current rate framework, some operators are delayed when attempting to recover their costs because they are not permitted to file for recovery of external cost increases and additions of new channels until the quarter after costs are incurred or channel changes are made. Operators may experience further delay while regulatory authorities review the proposed adjustments. Further, operators are never able to recover costs between the date they are incurred and the date a rate adjustment is permitted. Also, under the so-called "use or lose" provision of the current rules, operators must file for rate increases that reflect cost increases within one year of the date they first incur those additional costs, or else lose the ability to pass through those costs.

7. In order to address these concerns, we are adopting on our own motion a new optional rate adjustment methodology where cable operators will be permitted to make only annual rate changes to their BSTs and CPSTs. Operators that elect to use this new methodology will adjust their rates once per year to reflect reasonably certain and reasonably quantifiable changes in external costs, inflation, and the number of regulated channels that are projected for the 12 months following the rate change. Because operators will be permitted to estimate cost changes that will occur in the 12 months following the rate filing, we expect that this methodology will limit delays in recovering costs that operators may

⁴ See *Second Reconsideration Order*, 9 FCC Rcd at 4124.

⁵ *Id.*

experience under the current system. Any incurred cost that is not projected may be accrued with interest and added to rates at a later time. If actual and projected costs are different during the rate year, a "true up" mechanism is available to correct estimated costs with actual cost changes. The "true up" requires operators to decrease their rates or alternatively, permits them to increase their rates to make adjustments for over- or under- estimations of these cost changes. Operators would not lose the right to make a rate increase at a later date if they choose not to implement a rate adjustment at the beginning of the next rate year. Finally, in order that operators not feel compelled to make rate filings or increase rates when they otherwise would not, we will eliminate the "use or lose" requirement for operators that elect this methodology.

8. We believe that operators will benefit from this system because it will alleviate the difficulty of delays for rate adjustments that they now experience and will permit them to utilize annual rate adjustments without the loss of revenues they now incur as a result of the current methodology. Subscriber confusion will be alleviated because rate adjustments will take place once per year. Moreover, subscribers will be protected by this system because if an operator overestimates its permitted rate increase as a result of its projections, the operator would be required to rectify the error with interest when it makes its rate adjustment at the beginning of the next rate year. Finally, franchising authorities and the Commission will benefit from this methodology because they will not be required to review more than one rate adjustment per year.⁶

9. We are also requiring operators that elect the annual rate adjustment methodology to file BST rate adjustment requests 90 days prior to the effective date of the proposed changes. Operators may implement rate changes as proposed in their filings 90 days after they file unless the franchising authority rejects the proposed rate as unreasonable. If the franchising authority has not issued a rate decision and the operator makes a rate adjustment after the 90-day period has expired, the franchising authority may order a prospective rate reduction and refunds at a later time, where appropriate. The franchising authority need not issue an accounting order to preserve its right to issue its rate order after the 90-day review period. However, if an operator inquires as to whether the franchising authority intends to issue a rate order after the 90-day review period, the franchising authority must notify the operator of its intent in this regard within 15 days of the operator's request or lose its ability to order a refund or a prospective rate reduction. If a proposed rate goes into effect before the franchising authority issues its rate order, the franchising authority will have 12 months from the date the operator filed for the rate adjustment to issue its rate order. In the event that the franchising authority does not act within this time, it may not at a later date order a refund or a prospective rate reduction with respect to the rate

⁶ Some operators may prefer the quarterly system because they are already familiar with it, or because they are unable or unwilling to gather the information they would need to project costs in advance. For this reason we will retain the quarterly system, and will provide the annual system as an optional alternative.

filing.

10. An operator that has a CPST complaint pending against it or has been ordered by the Commission to reduce its CPST rates, and that elects the annual rate adjustment option, must propose the annual rate adjustment at least 30 days prior to the effective date of the rate change. The Commission can deny an increase before the end of the 30-day period, but if the Commission does not act within 30 days, the operator may implement the rate increase as proposed on the Form 1240. The increase would go into effect, subject to a prospective rate reduction and refund, where appropriate, which the Commission may order at a later time.

11. Although operators that elect the annual rate adjustment option generally will not be permitted to make more than one rate adjustment per year, we will permit operators to make rate adjustments for the addition of channels to BSTs that the operator is required by federal or local law to carry, i.e., new must-carry, local origination, public, educational and governmental access and leased access channels. Franchising authorities will have 60 days to review these increases prior to their going into effect. The proposed rate adjustment will go into effect 60 days after filing unless the franchising authority finds that the adjustment would be unreasonable. We also will allow operators to make one additional rate adjustment during the year to reflect channel additions to CPSTs, and to BSTs where the operator offers only one regulated tier. Operators may make this additional rate adjustment reflecting channel additions to CPSTs at any time during the year. Subject to the existing going forward rules, which affect the amount by which an operator can increase its rates, operators will have no limit on the number of channels they may add when they make this rate adjustment during the year.

12. Operators that elect the annual rate adjustment system must file for rate adjustments for equipment and installations on Form 1205 on the same date that they file for their other rate adjustments on Form 1240.⁷ Therefore, for operators that elect to use the annual rate adjustment methodology, we are changing the current rule which requires operators to file 60 days after the close of their fiscal year.⁸ In addition, we will continue to require operators to base their proposed annual customer equipment and installations rate adjustments on past costs because we believe that it would be far more difficult to project reasonably certain and reasonably quantifiable changes in equipment and installation costs. We also will require that when an operator introduces a new type of equipment, the operator must file for a rate adjustment no later than 60 days before the date the operator intends to

⁷ If an operator's BST is subject to regulation and the operator elects not to file a Form 1240 during a given year, the operator must continue to file its Form 1205 on an annual basis. FCC Form 1205, Instructions for Determining Costs of Regulated Cable Equipment and Installation at 2.

⁸ *Id.*

charge subscribers for the new type of equipment. The proposed rate would go into effect at the end of this 60-day period unless the franchising authority rejects the proposed rate as unreasonable or the franchising authority finds that the operator has submitted an incomplete filing.

13. Operators that do not elect to use the annual rate adjustment system may continue to use the existing system which allows operators to make rate adjustments up to once per calendar year quarter. With respect to the current quarterly rate adjustment system, this order affirms our decision in the *Fourth Reconsideration Order* to allow operators to pass through changes in franchise fees and Commission regulatory fees within 30 days of filing for a rate adjustment reflecting these costs unless the franchising authority finds that these rate adjustments are unreasonable before 30-day period has expired.

14. This Order will also simplify the rate review process by eliminating our current practice of reviewing the entire CPST rate after receiving a CPST complaint. On the effective date of these rules, this system of rate regulation, commonly referred to as "all rates in play," will be eliminated for CPSTs that have not been subject to a rate complaint. Following that date, CPST rate complaints will require a Commission determination whether the amount of the rate increase complained about is reasonable.

15. In addition, we clarify that for purposes of adjusting rates to reflect increases in franchise requirement costs, operators are entitled to pass through any increases in costs that are specifically required by franchise agreements, provided that the recovery of costs may not encompass costs the operator would incur in the absence of the franchise requirement. Consistent with this goal, operators are permitted to pass through to subscribers (a) cost increases associated with technical standards and customer service standards that exceed federal requirements; (b) cost increases attributable to satisfying franchise requirements to support public, educational and governmental access; (c) increases in the costs of providing institutional networks, video services, voice transmissions and data services to or from governmental institutions and educational institutions, including private schools; and (d) cost increases associated with a franchise requirement that an operator remove cable from utility poles and place the same cable underground.

16. Further, the Order affirms the Commission's decision to permit operators to advertise rates for regulated cable services regionally using a single tier rate plus a franchise fee. The order also permits franchising authorities to determine the method by which franchise fee overpayments are returned to cable operators. However, franchising authorities must return overpayments within a reasonable period of time.

II. ANNUAL RATE ADJUSTMENTS FOR BASIC SERVICES AND CABLE PROGRAMMING SERVICES

A. Background

1. Jurisdiction Over BSTs and CPSTs

17. Under the 1992 Cable Act, cable rate regulation is undertaken jointly by the Commission and by state and local governments. For purposes of allocating regulatory responsibility over the rates for services offered by cable system operators, the 1992 Cable Act divides regulated cable services into two categories.

18. The first category is the BST which includes, at a minimum, the local broadcast signals distributed by the cable operator and any public, educational, and governmental access channels.⁹ Cable operators have the discretion to include other services in the BST. Regulation of rates for BSTs is the responsibility of certified state and local governments, pursuant to standards and procedures established by the Commission.¹⁰ The Commission serves as the forum for appeals to review local rate decisions.¹¹ Under certain circumstances, the Commission will directly regulate BST rates.¹²

19. The second category is the CPST, which includes all video programming distributed over the system that is not on the BST and for which the operator does not charge on a per channel or per program basis.¹³ Under the 1992 Cable Act, CPSTs are subject to regulation by the Commission only if the Commission receives a complaint from a subscriber or local regulatory authority regarding an operator's CPST rate.¹⁴ The following subsections describe our current rules regarding the setting of initial rates, the regulatory review process under the price cap system, and permitted adjustments under the price cap.

2. Setting Initial Rates

a. Regulatory Review Process for Initial Rates

20. The 1992 Cable Act permits a franchising authority to regulate its BST only if it certifies in writing to the Commission that (a) its rate regulations will be consistent with the standards prescribed by the Commission; (b) it has the legal authority to adopt, and the personnel to administer, rate regulations; and (c) its procedural rules provide an opportunity

⁹ 47 C.F.R. § 76.901(a). Unless otherwise stated, all references to Commission rules are to rules in effect as of the date of this Order, and not to rule changes made in this Order.

¹⁰ Communications Act, § 623(a)(2)(A).

¹¹ 47 C.F.R. § 76.944(a).

¹² 47 C.F.R. § 76.913.

¹³ Communications Act, § 623(l)(2).

¹⁴ Communications Act, § 623(c)(3).

for the consideration of views of interested parties.¹⁵ A franchising authority becomes certified to regulate BSTs 30 days after filing for certification unless the Commission denies certification because the franchising authority has not met one of the criteria.¹⁶ Once a franchising authority has been certified and has adopted rules, it must notify the cable operator that these requirements have been met and that the franchising authority intends to regulate the rates for the BST and the customer premises equipment used to receive the BST.¹⁷ The operator is then required to justify its existing BST rate by filing FCC Form 1200, Form 1220, or Form 1225 with the franchising authority.

21. The franchising authority reviews the operator's justification for initial BST rates through a two step process. Under the first step, if a franchising authority approves the operator's existing rate within 30 days of the filing, the increase will go into effect 30 days after the filing.¹⁸ Under the second step, if a franchising authority is unable to determine whether the BST rate is reasonable within the initial 30 day period, the franchising authority may issue a tolling order so that it may review the rate justification for an additional 90 days.¹⁹ If no action is taken within this 90 day period, the franchising authority may preserve its right to issue a subsequent refund order by issuing a written accounting order before the end of the 90 day period, which directs the operator to keep accurate accounts of all amounts received by reason of the proposed rate and on whose behalf such amounts are paid.²⁰ The refund period is limited to a maximum of one year.

22. The 1992 Cable Act provides that the Commission will regulate rates of CPSTs only in response to complaints.²¹ Under the 1992 Cable Act, parties had 180 days from the effective date of the Commission rules to file a complaint about CPST rates that existed as of the effective date of the Act.²² Complainants must use the complaint form

¹⁵ 47 C.F.R. § 76.910.

¹⁶ *Id.*

¹⁷ *Id.*

¹⁸ See *Report and Order and Further Notice of Proposed Rulemaking ("Rate Order")*, MM Docket No. 92-266, FCC 93-177, 8 FCC Rcd 5631, 5709 (1993); see also 47 C.F.R. § 76.933(a).

¹⁹ Franchising authorities can toll the effective date of a proposed rate adjustment for 150 days to evaluate cost-of-service showings. *Rate Order*, 8 FCC Rcd at 5709.

²⁰ *Id.*

²¹ Communications Act, § 623(c)(1).

²² *Id.*

adopted by the Commission and serve a copy on the cable operator and franchising authority.²³ The operator must respond to a complaint within 30 days of its service.²⁴ If the Commission finds that the operator's rates are unreasonable, the operator is required to make a prospective rate reduction and may have to make refunds to subscribers.²⁵ The refund period runs from the date the operator implements a prospective rate reduction pursuant to a Commission order and extends back to the date the complaint was filed with the Commission.²⁶

b. Standard for Establishing Initial Rates on BSTs and CPSTs

23. In the *Rate Order*, we developed a benchmark formula for the purpose of establishing initial rates for BSTs and CPSTs.²⁷ Companies electing to justify rates under the benchmark approach were required to use a formula established to calculate an applicable benchmark -- an estimate of the rate that a cable system with similar characteristics, but subject to effective competition, would charge.²⁸ Cable systems whose rates exceeded the applicable benchmark were required to reduce their rates either to the benchmark or by 10%, whichever reduction was less.²⁹ The 10% "competitive differential" represented the average difference that the Commission determined existed between the rates of competitive and noncompetitive systems.³⁰ In the *Second Reconsideration Order*, we refined the econometric model, recalculated the competitive differential, and concluded that a competitive differential of 17% more accurately estimated the difference between cable rates in competitive and noncompetitive markets.³¹ For those cases in which the benchmark approach may not

²³ 47 C.F.R. § 76.956.

²⁴ 47 C.F.R. § 76.956(a).

²⁵ 47 C.F.R. §§ 76.960, 76.961.

²⁶ 47 C.F.R. § 76.961(b).

²⁷ *Rate Order*, 8 FCC Rcd 5770.

²⁸ *Id.*

²⁹ *Id.* at 5772.

³⁰ *Id.* at 5770.

³¹ *Second Reconsideration Order*, 9 FCC Rcd at 4124. We granted two classes of cable systems transition relief by not requiring them to implement the full 17% reduction rate, pending a review of their prices and costs. The first category of systems that were provided with transition relief is systems owned by "small operators," defined as operators serving 15,000 or fewer subscribers and not affiliated with a larger operator. *Id.* at 4167-68, 4172-

produce fully compensatory rates. operators were given the option of establishing rates based on costs pursuant to individual cost-of-service showings.³²

3. Rate Adjustments Under the Price Cap System

a. Basic Service Tier

24. Where a franchising authority has been certified, a cable operator in a franchise area that is not subject to effective competition as defined in the 1992 Cable Act may not increase its BST rates without approval from the franchising authority. If such an operator proposes a rate increase to its BST and the franchising authority determines that the proposed rate increase is reasonable, the increase goes into effect 30 days after FCC Form 1210 is filed.³³ If the franchising authority is unable to determine whether the proposed rate adjustment is reasonable within the initial 30 day period, the franchising authority may toll the effective date of the rate adjustment for an additional 90 days.³⁴ Franchising authorities can take this additional time to solicit further information, to review the proposed rates, and to consider the views of interested parties.³⁵ If no action is taken within this 90 day period, the proposed rate goes into effect.³⁶ In order to preserve its ability to order a refund, the franchising authority must issue a written order at the end of the tolling period directing the operator to keep accurate accounts of all amounts received by reason of the proposed rate.³⁷ However, the refund period begins on the date the rate increase is implemented and ends on either the date that the operator implements a prospective rate reduction ordered by the franchising authority or one year after the rate increase, whichever period is shorter.³⁸

75. The second category of systems that were provided with transition relief is systems that charge relatively low prices for regulated services. *Id.* at 4168-69, 4176-78.

³² *Rate Order*, 8 FCC Rcd at 5794-95.

³³ *See Rate Order*, 8 FCC Rcd at 5709-10; *see also* 47 C.F.R. § 76.933(a).

³⁴ Franchising authorities can toll the effective date of a proposed rate adjustment for 150 days to evaluate cost-of-service showings. *Rate Order*, 8 FCC Rcd at 5709.

³⁵ *Id.*

³⁶ *Id.*

³⁷ 47 C.F.R. § 76.933(c).

³⁸ 47 C.F.R. § 76.942(c).

Franchising authorities may order prospective rate reductions at any time.³⁹

25. If an operator fails to complete its rate justification form or to include supporting information called for by the form, the franchising authority may order the cable operator to file the required information.⁴⁰ While the franchising authority is waiting to receive this information from the cable operator, the deadline for the franchising authority to rule on the reasonableness of the proposed rates is tolled.⁴¹ Once the operator has made its filing complete, the time for determining the reasonableness of the rate by the franchising authority will recommence.⁴²

b. Cable Programming Service Tier

26. Section 3(c) of the 1992 Cable Act requires that, upon the receipt of a specific complaint regarding a CPST rate, the Commission is to ensure that such rates are not unreasonable.⁴³ We review CPST rate changes when a complaint is filed with the Commission within 45 days from the date the subscriber receives a bill from the cable operator reflecting the rate change.⁴⁴ The cable operator is required to respond to a CPST complaint within 30 days of the date that it is served with the complaint.⁴⁵ As a part of its review of rate increase complaints, the Commission reviews the amount of the rate increase and the operator's existing rates as of the effective date of the rules.

27. If an operator seeks to make a rate adjustment to a CPST due to an increase in external costs and the Commission has found the rate unlawful and ordered the operator to reduce CPST rates during the past year, the operator must receive approval from the Commission before the rate can go into effect.⁴⁶ A cable operator with pending CPST complaints but no adverse Commission decision in a franchise area must inform the Commission of any CPST rate changes in that franchise area by filing FCC Form 1210, but

³⁹ 47 C.F.R. § 76.933(c).

⁴⁰ *Third Reconsideration Order*, 9 FCC Rcd at 4348.

⁴¹ *Id.*

⁴² *Id.* at 4348 n.52.

⁴³ Communications Act, § 623(c).

⁴⁴ 47 C.F.R. § 76.953(b).

⁴⁵ 47 C.F.R. § 76.956.

⁴⁶ 47 C.F.R. § 76.960.

the rate change may go into effect without prior approval.⁴⁷ If the rate change goes into effect without prior approval, the Commission may order a prospective rate reduction and refund if it later determines the rate is unreasonable.⁴⁸ The refund liability period would begin on the date the Commission receives a valid complaint and end on the date the operator implements a rate decrease pursuant to a Commission order.⁴⁹

4. Price Cap Adjustment Mechanism

28. Under the Commission's price cap rules, once initial rates are established, operators are permitted to adjust their rates for inflation, changes in external costs, and changes in the number of regulated channels.⁵⁰ Operators adjust their rates on an annual basis to reflect inflation.⁵¹ They are permitted to adjust their rates on a calendar year quarterly basis to reflect changes in certain categories of external costs, and in the number of regulated channels.⁵² Cable operators seeking to adjust regulated rates to reflect these changes must support the proposed rate on FCC Form 1210,⁵³ and file the form with the appropriate regulatory authority. The changes in external costs reflected on FCC Form 1210 are based upon costs which were actually incurred, and operators may not file to recover these costs until the quarter after such costs were incurred.⁵⁴

29. Under our rules, operators are permitted to adjust their BST and CPST rates annually for inflation by tracking the external cost component of their permitted charge and

⁴⁷ *Id.*

⁴⁸ 47 C.F.R. § 76.933(c).

⁴⁹ 47 C.F.R. § 76.961(b).

⁵⁰ *Rate Order*, 8 FCC Rcd at 5776; *Second Reconsideration Order*, 9 FCC Rcd at 4202-04.

⁵¹ *Second Reconsideration Order*, 9 FCC Rcd at 4203.

⁵² First Order on Reconsideration, Second Report and Order, and Third Notice of Proposed Rulemaking in MM Docket No. 92-266, 9 FCC Rcd 1164, 1235 (*"First Reconsideration Order"*) (1993).

⁵³ FCC Form 1210, Updating Maximum Permitted Rates for Regulated Cable Service (May 1994). See also 47 C.F.R. §§ 76.922(d), 76.933. Cable operators need not use FCC Form 1210 when merely demonstrating the calculation of rate increases on account of franchise or Commission regulatory fees. *Fourth Reconsideration Order*, 9 FCC Rcd at 5796 n.13, 5797.

⁵⁴ 47 C.F.R. § 76.922(d)(3)(iii).

adjusting the remaining charge, referred to as the residual component, for inflation.⁵⁵ The inflation adjustment is based on changes in the Gross National Product Price Index (GNP-PI) as published by the Bureau of Economic Analysis of the United States Department of Commerce.⁵⁶ The annual inflation adjustment is based on inflation occurring between June 30 of the previous year and June 30 of the year in which the inflation adjustment is made. The adjustment may not be made until after September 30, and can be implemented any time before August 31 of the next calendar year.⁵⁷

30. Operators may increase rates to reflect increases in external costs to the extent that such increases exceed inflation. External costs include retransmission consent fees, other programming costs, copyright fees, cable specific taxes, Commission regulatory fees, franchise fees, and franchise requirement costs.⁵⁸

31. When cable operators seek to make rate adjustments due to changes in external costs, they may not file for rate adjustments more frequently than once per calendar year quarter.⁵⁹ Operators are not permitted to file for a proposed rate adjustment reflecting these changes before the first day of the quarter following the quarter in which the change in external costs occurred.⁶⁰ If an operator incurs an external cost increase in January, for example, the operator may not file FCC Form 1210 until April 1.

32. Any time an operator files for an increase in external costs or its annual

⁵⁵ 47 C.F.R. § 76.922(d).

⁵⁶ The Bureau of Economic Analysis (BEA) produces two fixed weight indexes that measure inflation in the overall economy. The GNP-PI measures inflation in the gross national product. The Gross Domestic Product fixed weight price index (GDP-PI), which BEA began producing recently, measures inflation in the domestic national product. The GNP-PI is an appropriate measure of inflation that the Commission currently allows telephone companies to use for inflation adjustment in annual price cap filings. U.S. Department of Commerce, Bureau of Economic Analysis, Survey of Current Business: August 1991.

⁵⁷ 47 C.F.R. § 76.922(d)(2).

⁵⁸ 47 C.F.R. § 76.922(d)(3)(iv). In the *Fourth Reconsideration Order* we permitted operators to pass through two types of external costs, franchise fees and Commission regulatory fees, within 30 days of filing for rate increases reflecting such fees unless the franchising authority determines that the rate adjustment is unreasonable before 30 days has expired. See Section III, *infra*; see also 47 C.F.R. § 76.933(e).

⁵⁹ 47 C.F.R. § 76.922(d)(3)(i).

⁶⁰ 47 C.F.R. § 76.922(d)(3)(iii).

inflation adjustment, it must also identify any decreases in external costs that have occurred over the same period.⁶¹ In addition, all regulated operators must adjust their rates annually to reflect any net decreases in external costs that have not previously been accounted for in rates.⁶² Moreover, if a regulated operator is going to adjust its rates to reflect increases in external costs, the operator has one year from the date the cost is incurred to make the rate adjustment or lose the right to ever adjust rates for those external costs.⁶³

33. Operators may adjust their rates quarterly to reflect increases in the number of regulated channels.⁶⁴ Operators may file FCC Form 1210 no earlier than the first day of the quarter following the quarter in which the channel change occurred.⁶⁵ When an operator reduces the number of regulated channels on a tier, the operator must adjust the tier charge to reflect this change in the next calendar quarter.⁶⁶

34. In making these rate adjustments for channel changes, operators must use either the channel adjustment methodology provided for under the initial rules⁶⁷ or the alternative per channel adjustment methodology adopted pursuant to our new going forward rules.⁶⁸ The initial per channel adjustment methodology must be used for adding channels to

⁶¹ 47 C.F.R. § 76.922(d).

⁶² *Id.*

⁶³ 47 C.F.R. § 76.922(d)(3).

⁶⁴ *Id.*

⁶⁵ *Id.*

⁶⁶ *Id.*

⁶⁷ The Commission's initial per channel adjustment methodology permits operators to increase rates by a per channel amount when channels are added to BSTs and CPSTs, with the per channel amount decreasing as the number of channels on a system increases. These rules also permit operators to pass through the costs of obtaining programming plus a 7.5% mark-up on new programming costs. See 47 C.F.R. § 76.922(d)-(e).

⁶⁸ Sixth Order on Reconsideration, Fifth Report and Order, and Seventh Notice of Proposed Rulemaking ("*Sixth Reconsideration Order*") in MM Docket No. 92-266, 10 FCC Rcd 1226 (1994). Operators electing to use the new rules are allowed to take a per channel mark-up of up to 20 cents for each channel added to CPSTs. *Id.* Under this alternative, operators may make rate adjustments at any time during the three-year period beginning on January 1, 1995. *Id.* They may not make per channel adjustments to monthly rates totalling more than \$1.20 per subscriber over the first two years of the three-year period for new channels added on CPSTs or by more than \$1.40 plus licensing fees over the full three-year

BSTs except for single tier systems. Operators may choose between the initial channel adjustment methodology and the alternative methodology for channels added to CPSTs and single tier systems between May 15, 1994 and December 31, 1997. They must make this election the first time they adjust rates after December 31, 1994 to reflect a channel addition that occurred on or after May 15, 1994 and must use the elected methodology for all channel adjustments through December 31, 1997.

5. Equipment and Installation

35. The 1992 Cable Act requires cable operators to charge rates based on actual costs for installation and lease of subscriber equipment.⁶⁹ Regulated equipment includes all of the equipment located in the subscriber's home, including converter boxes, remote control units, connections for additional television receivers, and other cable wiring used to obtain basic services.⁷⁰ Cable operators must unbundle charges for equipment, installation, and additional outlets from the BST rate.⁷¹ They also must use a specific methodology for determining the actual cost of each piece of equipment and installation.⁷² Under this methodology, the cable operator must establish an equipment basket to which it assigns the direct costs of service installation, additional outlets and leasing and repairing equipment.⁷³ In the equipment basket, the cable operator must allocate the system's joint and common costs that service installation, leasing, and equipment repair share with other activities (but not general system overhead), plus a reasonable profit.⁷⁴ Cable operators must complete and file with the franchising authority an FCC Form 1205 for several different purposes. First, they must file Form 1205 with the franchising authority for the purpose of setting initial rates

period. *Id.* Operators may make the 20 cents per channel adjustment in the third year only for channels added in that year. *Id.* Operators electing to use the per channel adjustment in the new rules may not take the 7.5% mark-up on programming cost increases for channels added after May 14, 1994. *Id.* Between January 1, 1995 and December 31, 1996, operators may use any portion of the \$1.20 per channel adjustment to recover license fees. *Id.* In addition, operators may recover an additional amount of not more than 30 cents per subscriber per month for license fees associated with adding new channels during this two year period. *Id.*

⁶⁹ 1992 Cable Act, § 3(b)(3); Communications Act, § 623(b)(3).

⁷⁰ 47 C.F.R. § 76.923(a).

⁷¹ 47 C.F.R. § 76.923(b).

⁷² 47 C.F.R. § 76.923(d)-(m).

⁷³ 47 C.F.R. § 76.923(c).

⁷⁴ *Id.*

under either the benchmark system or through a cost-of-service showing.⁷⁵ Second, all operators must file Form 1205 with their franchising authorities once every year within 60 days of the end their fiscal year.⁷⁶ Finally, operators must file Form 1205 with the franchising authority 30 days before they seek to adjust their equipment rates.⁷⁷

B. Contentions

1. Quarterly Rate Adjustment System

36. In its Petition for Reconsideration of the *Fourth Reconsideration Order*, TKR Cable Company ("TKR") criticizes the quarterly rate adjustment system because it believes that operators will never recover that portion of the increases in external costs that are incurred between the date the additional external costs begin accumulating and the date the new rate takes effect. TKR argues that the denial of a portion of their external costs deprives TKR of its property without due compensation, and implicates takings considerations under the Fifth and Fourteenth Amendments to the U.S. Constitution.⁷⁸ Moreover, TKR contends that permitting subscribers to pay "lower" rates, or rates not based on TKR's current actual costs of providing service, grants subscribers an undeserved benefit.⁷⁹

37. According to TKR, Section 76.933(b) of our rules is inconsistent with the language of the *Rate Order* concerning franchising authority review of external cost showings. TKR notes that while in the *Rate Order* the Commission determined that franchising authorities may toll the effective date of rate adjustments as necessary in certain complex cases, Section 76.922(b) permits franchising authorities to issue a tolling order in cases "where it cannot be determined, based on the material submitted, whether the

⁷⁵ 47 C.F.R. § 76.922(b)(6).

⁷⁶ In a letter released March 1, 1995, the Cable Services Bureau granted operators a waiver permitting them to file 30 days after the 60 day period, provided that they notify the appropriate regulatory authority that strict compliance with the 60 day requirement is not feasible. Letter from Meredith Jones, Chief, Cable Services Bureau to Eric Breisach, Howard and Howard, DA 95-381 (Mar. 1, 1995).

⁷⁷ FCC Form 1205, Determining Costs of Regulated Cable Equipment and Installation.

⁷⁸ TKR Petition for Reconsideration at 14 (citing *Duquesne Light Co. v. Barash*, 488 U.S. 299, 308 (1989)).

⁷⁹ *Id.* at 15 (citing *Papago Tribal Util. Auth. v. FERC*, 628 F.2d 235, 240-41 (D.C. Cir., cert. denied, 449 U.S. 1061 (1980)).

operator's rates are reasonable."⁸⁰ TKR and the Cable Telecommunications Association, Inc. ("CATA") argue that franchising authorities should not be permitted to issue a tolling order when they examine external cost showings because external cost showings do not offer complex cases.⁸¹ CATA further asserts that no room for judgment exists in a cable operator's calculation of external cost pass throughs. CATA states, for example, that the costs of franchise requirements should be apparent to the franchising authority to the same degree as are franchise fees, and permitted rate increases resulting from channel additions which are pre-determined under the Commission's going forward rules.⁸² TKR asserts that its interpretation is supported by the *Rate Order* because it describes the increases reflecting external costs as "automatic adjustments."⁸³

38. In addition, TKR asserts that franchising authorities arbitrarily take advantage of the tolling mechanism, often failing to even begin reviewing external cost showings within the initial 30 day period.⁸⁴ CATA asserts that franchising authorities have political incentives to delay all rate increases no matter how justified, and that this delay unfairly and arbitrarily

⁸⁰ *Id.* at 3 (citing *Rate Order*, 8 FCC Rcd at 5710).

⁸¹ *Id.*; CATA Comments at 3-4 (citing *Rate Order*, 8 FCC Rcd at 5710).

⁸² CATA Comments at 6 (citing 47 C.F.R. §§ 76.922(d)(3)(x) - (e)(7)); see also *Sixth Reconsideration Order*, 10 FCC Rcd at 1248-57.

⁸³ TKR Petition for Reconsideration at 4.

⁸⁴ *Id.* at 6. TKR references a letter it submitted to the Cable Services Bureau in which it accuses the State of New Jersey Board of Public Utilities' Office of Cable Television (BPU/OCT) of "arbitrarily, and without sufficient cause" tolling the effectiveness of proposed rates demonstrated on TKR's FCC Form 1210 showing submitted in June 1994. TKR argued that the BPU/OCT wrongly refused to rely on statements contained in a letter issued by the Cable Services Bureau concerning the addition of the program service *The fX Channel*. These statements encouraged local authorities to act upon rate increase showings promptly, and to endeavor to approve the new rates, where at all possible, within 30 days. Letter from Mark J. Palchick, Esq., Counsel for TKR Cable Company to Gregory J. Vogt, Esq., Deputy Chief, Cable Services Bureau, at 3 (October 19, 1994) (citing *In re The fX Channel* at 3 (Cable Services Bureau, April 22, 1994)). The BPU/OCT responded that it tolled TKR's proposed rates after determining that it was not possible to properly review TKR's rates within the 30 day time period based on the data provided by TKR, and that it would not be in the best interest of TKR's subscribers to approve a rate increase pursuant to Form 1210 before the BPU/OCT could review and approve TKR's Form 1200, on which TKR supported its initial rates. Letter from Deborah T. Poritz, Esq., Attorney General, State of New Jersey to Gregory J. Vogt, Esq., Deputy Chief, Cable Services Bureau, at 1 (November 10, 1994).

denies operators their ability to recover legitimate costs.⁸⁵ TKR states that tolling can lead to a delay of its recovery of external costs for up to eight months. TKR notes, for example, that if an operator incurs an external cost in the first month of a quarter, it must wait nearly three months to file its FCC Form 1210 because it is not permitted to file until the quarter after a cost is incurred. In addition, after the operator files, the franchising authority has an initial 30 days to review the filing and can subsequently toll the effective date of the rate adjustment for an additional 90 days. Finally, TKR states that after the operator has received approval for the rate adjustment, it must provide subscribers with 30 days advance written notice before it can implement the new rate.⁸⁶ United Video argues that the Commission's regulations governing operators' recovery of additional programming costs resulting from the addition of new program services unfairly force operators to wait as long as three months before beginning to recover those new costs in subscriber rates.⁸⁷ The National Cable Satellite Corporation, Inc. ("C-SPAN") believes that because of the delays in recovering costs, the current tolling provisions reduce operators' incentives to launch new cable programming services.⁸⁸

39. TKR also requests that we permit cable operators to collect the cumulative amount of all categories of external costs on the same conditions as Commission regulatory fees, namely, in 12 equal monthly installments during the year after that in which the cost increases were incurred.

40. TKR, supported by CATA and Howard & Howard, urges the Commission to permit cable operators to pass through all external costs without the prior regulatory approval of franchising authorities. TKR argues that operators should be permitted to pass through all external costs automatically upon 30 days' prior notice to subscribers and the franchising authority. Under TKR's proposal, franchising authorities would be permitted to toll the review of proposed rates for 90 days without suspending their effectiveness and later to order refunds for rates found to be calculated incorrectly. CATA believes that tolling is unnecessary because franchising authorities need only determine that a few lines on FCC Form 1210 have been properly completed and calculated in order to approve the new rate.⁸⁹

41. CATA urges the Commission to prohibit franchising authorities from denying a proposed rate increase even during the initial 30 day period for review, stating that refunds fully protect subscribers. Without this provision, CATA asserts, franchising authorities will

⁸⁵ CATA Comments at 8.

⁸⁶ TKR Petition for Reconsideration at 6-7.

⁸⁷ See Petition for Reconsideration, filed by United Video (May 16, 1994).

⁸⁸ C-SPAN Comments at 1-2.

⁸⁹ CATA Comments at 2-3.

"automatically" deny the proposed rates during the initial 30 days, thereby forcing the operator to appeal to the Commission for a final decision.⁹⁰ CATA and Howard & Howard believe the current rate adjustment process can result in an operator filing multiple FCC Form 1210s, and results in excess work for both industry and regulators.⁹¹ Howard & Howard also believes the current procedure causes problems because cable operators do not know when rate adjustments will go into effect.⁹² Howard & Howard contends that customers would benefit under its proposals because they prefer less frequent rate increases.⁹³

42. Further, Howard & Howard and Cole, Raywid & Braverman ("Cole Raywid") ask that the Commission change its current practice of requiring operators to adjust their rates within one year of the date they incur their costs. They contend that this requirement forces cable operators to raise rates sooner and more frequently than they would if they could wait without permanently forfeiting the increase, and is therefore contrary to the intent of the 1992 Cable Act.⁹⁴ Cole, Raywid also believes that allowing cable operators to avoid repeated rate adjustments will avoid confusion on the part of subscribers and franchising authorities, and will alleviate the real costs of printing and mailing subscriber notices and fielding subscribers' phone inquiries.⁹⁵

43. Howard & Howard suggests allowing operators to use a target date for implementing rate adjustments, and if that date is missed, a compensating adjustment would be carried over to the next filing.⁹⁶ Howard & Howard predicts that the amount of this compensating adjustment would be minimal. According to Howard & Howard, this proposal

⁹⁰ *Id.* at 6-7. CATA argues that the Commission need not amend its rules to prohibit franchising authorities from tolling external cost-based rate adjustments. Rather, CATA contends that the Commission merely needs to clarify that statements in the *Rate Order* describing such cost adjustments as "automatic," "simple," and "presumed reasonable," indicate the Commission's genuine intent that an operator's external cost showing should be automatically approved by the franchising authority, and not tolled unless the franchising authority reasonably requires additional information from the operator for its review of the showing. *Id.* at 3-4 (citing *Rate Order*, 8 FCC Rcd at 5720).

⁹¹ *Id.* at 8; Howard & Howard at 4.

⁹² Howard & Howard at 5.

⁹³ *Id.*

⁹⁴ *Id.* at 6; Letter to Meredith Jones, Chief, Cable Service Bureau, from Paul Glist of Cole, Raywid & Braverman, at 1 ((Mar. 15, 1995) ("Cole, Raywid Letter").

⁹⁵ Cole, Raywid Letter at 2.

⁹⁶ Howard & Howard at 5.

would alleviate the industry's uncertainty with respect to routine rate adjustments and it would help operators consolidate their rate increases into one per year.⁹⁷

44. Finally, Howard & Howard contends that the timing for filing FCC Form 1205 is not concurrent with the year end or first quarter rate increases preferred by operators.⁹⁸ It asks that the Commission recommend a remedy to the timing problem.

45. The National Association of Telecommunications Officers and Advisors ("NATOA") and the City of New York (collectively, the "Local Governments") argue that TKR's petition for reconsideration is not properly before the Commission because TKR does not seek Commission reconsideration of any decisions reached in the *Fourth Reconsideration Order*. The Local Governments argue that because TKR asks the Commission to permit cable operators to automatically pass through all categories of external cost increases without the prior approval of franchising authorities, this request actually requires reconsideration of Commission rules governing the time periods for a franchising authority's review of a proposed rate increase and our rules setting forth the procedures for filing FCC Form 1210,⁹⁹ which were adopted in the *Rate Order* and the *Second Reconsideration Order*.¹⁰⁰ They argue, therefore, that TKR's petition for reconsideration must be denied because the deadlines for seeking reconsideration of the issues addressed by these Commission decisions have long passed.¹⁰¹

46. In addition, the Local Governments oppose the substance and impact of TKR's proposal. They note that the *Rate Order* clearly states that the "franchising authority may toll the effective date of the proposed rates."¹⁰² They argue that nothing in Section 76.933(b) of our rules, or any other section of our rules, supports TKR's assertion that the Commission intended to limit the period for franchising authority review of external cost showings to only 30 days. Local Governments then state that the proper allocation and calculation of external costs is far from clear in many jurisdictions. They argue that franchising authorities would find it very difficult to render decisions within 30 days because cable operators typically fail

⁹⁷ *Id.* at 4.

⁹⁸ *Id.* at 6.

⁹⁹ 47 C.F.R. §§ 76.933(a) - (c), 76.922(d) - (d)(3)(iii).

¹⁰⁰ *See Rate Order*, 8 FCC Rcd 5631; *Second Reconsideration Order*, 9 FCC Rcd 4119.

¹⁰¹ Local Governments Opposition at 2-3. *See also* 47 C.F.R. § 1.429(d) (requiring petitions for reconsideration to be filed within 30 days of the date of public notice of a Commission action). Local Governments suggest that TKR alternatively may file a petition for rulemaking.

¹⁰² Local Governments Opposition at 4 (*citing Rate Order*, 8 FCC Rcd at 5709-10).

to submit all the information required for the authority's review concurrent with the FCC Form 1210, and, in many cases take an unreasonable amount of time to respond to a franchising authority's request for such information. The Local Governments argue that TKR's approach would allow operators simply to adjust rates as they see fit, and, because the rates would already be in effect, would completely eliminate operators' incentives to submit timely data required by franchising authorities for their review of external cost showings. The Local Governments reiterate that all rate increases should be subject to the same review and approval process because, from the subscriber's point of view, no difference exists between an overcharge based on external costs and one for basic cable service.¹⁰³

47. The Local Governments also urge the Commission to deny TKR's recommendation that operators be permitted to recover for the accrual of external costs between the date they are incurred and the date a rate adjustment is approved. They state that cable operators can alleviate their concerns over being denied recovery of a portion of their external costs by taking a few simple actions. First, the Local Governments state that the review period for rate justifications could be reduced if cable operators would submit a properly completed FCC Form 1210, accompanied by all supplemental information called for by the form, and respond promptly to requests for such information from franchising authorities where the information was not provided with the form. Second, the Local Governments recommend that operators ensure that any budgetary increases, new investments, or other new increased expenditures sufficiently coincide with the FCC Form 1210 approval process before taking on such financial obligations. Third, the Local Governments state that operators should gather all the data justifying their external cost increases before submitting the FCC Form 1210. Fourth, Local Governments suggest that cable operators can better plan their annual budgets by, for example, taking into account when programming contracts will expire.¹⁰⁴

2. Annual Rate Adjustment Option

48. The parties in this proceeding generally agree that operators should be encouraged to reduce the number of rate filings.¹⁰⁵ TKR proposes, for example, a mechanism for operators seeking to recover the aggregate amount of increases in external

¹⁰³ *Id.* at 5-8.

¹⁰⁴ Local Governments Opposition at 8-9.

¹⁰⁵ *See, e.g.*, Letter to Gregory J. Vogt, Deputy Chief, Cable Services Bureau from James A. Hatcher, Vice President, Legal & Regulatory Affairs at Cox Communications, Inc. (Mar. 30, 1995) ("Cox Letter"); Letter to William Caton from Eric E. Breisach at 4 (Feb. 27, 1995) ("Howard & Howard Letter"); Ex Parte presentation from William E. Cook, Jr., National Association of Telecommunications Officers and Advisors at 1 (May 23, 1995) ("NATOA Letter").

costs that were previously incurred.¹⁰⁶ The aggregate amount could be recovered in 12 equal monthly installments during the year following the year in which the additional costs were incurred by the operator, in the same manner as that prescribed for the Commission regulatory fees.¹⁰⁷ TKR states that this could permit operators to increase subscriber rates no more than annually, thereby greatly reducing the administrative burden on both regulators and industry. TKR asserts that subscribers would be fully protected by this approach because franchising authorities have the ability to order refunds for rates that are calculated incorrectly or exceed reasonable levels.¹⁰⁸

49. Cox Communications, Inc. ("Cox") also suggests a methodology designed to encourage operators to make annual rather than quarterly filings. It contends that cable operators incur substantial external costs during the franchising authorities' period of review. Cox argues that the review period, when combined with the requirement to give customers 30 days prior written notice of any rate changes, creates an unreasonably long regulatory lag between the date a rate increase is deemed necessary and the date the increase actually goes into effect.¹⁰⁹ According to Cox, cable operators are currently unable to recover the substantial external costs they incur during the lag time.¹¹⁰ As a remedy, Cox suggests an annual rate change option, through which cable operators would have the option of filing rate increases once per year.¹¹¹ Cox argues that such a policy would avoid customer dissatisfaction by reducing the number of rate increases, and would reduce the administrative burden for both operators and the regulatory authorities. Cox contends that the current policy encourages numerous rate increases because of the "use or lose" provisions, whereby an operator must file for an increase within a certain time, or else lose its ability to file for the increase. In addition, the current rules require that the operator must immediately anticipate the need for a rate increase and file for such an increase, or lose its ability to recoup the revenue for the time it delayed the rate increase.¹¹²

50. Cox asserts that its proposal would limit the number of rate changes operators could take without losing the chance to recover costs and would give operators incentives to add new programming without delay. The annual filing would request an increase in rates

¹⁰⁶ TKR Petition for Reconsideration at 8-9.

¹⁰⁷ *Id.* at 9.

¹⁰⁸ *Id.*

¹⁰⁹ Cox Letter at 1.

¹¹⁰ *Id.*

¹¹¹ *Id.* at 3.

¹¹² *Id.* at 2.

based upon external costs incurred over the preceding year, plus interest and prospective known and verifiable costs such as programming, user fees and cable-related taxes. Cox's proposal would also enable cable operators to project their inflation by using the officially published data for the preceding 12 months rather than the final GNP-PI. Equipment rates would still be based on costs from the preceding year, but could be determined using the preceding 12-month period rather than the operator's preceding fiscal year.¹¹³ Additionally, Cox proposes that an operator be permitted to carry over to the following year any portion of its rate increase it deems inadvisable to implement immediately.¹¹⁴ Cox further argues that such a mechanism should allow for the addition of must-carry stations and other government mandated channel additions when they occur, rather than annually.¹¹⁵ In examining a rate justification under this methodology, franchising authorities would have 60 days to review rate filings, and would be given no extensions and no opportunity to request accounting orders.¹¹⁶ Cox believes this procedure would allow cable operators to implement approved rate increases in a more timely fashion and would expedite the appeals process for rate increases that are denied. Cox suggests the rate increases would go into effect 105 days after filing, after allowing 45 days to implement the 30 day customer notice requirement.¹¹⁷

51. NATOA also supports a system that would encourage operators to limit themselves to annual rate adjustments.¹¹⁸ NATOA recommends that each operator's annual filing date be set jointly by the franchising authority and the cable operator.¹¹⁹ NATOA suggests that the filing date be based on the operator's budget year, program contract year, the franchising authority's fiscal year or some "other appropriate base."¹²⁰ Under this model, NATOA argues, the rate review process will be faster and franchising authorities can approve rates before the budget year begins.¹²¹

52. NATOA asserts that, under the once a year rate review model, operators could

¹¹³ *Id.* at 3.

¹¹⁴ *Id.*

¹¹⁵ *Id.* at 3-4.

¹¹⁶ *Id.* at 2.

¹¹⁷ *Id.*

¹¹⁸ NATOA Letter at 1.

¹¹⁹ *Id.*

¹²⁰ *Id.*

¹²¹ *Id.*

set rates prospectively based on actual and verifiable increases in external costs that will take place in the coming year.¹²² NATOA states that at the end of each year, it may be appropriate for operators to "true up" the cost increases they projected at the beginning of the year and adjust their rates accordingly.¹²³ NATOA argues that if it is determined that an operator overcharged its subscribers, subscribers should receive refunds with the same interest that operators would receive if it was determined that the operator undercharged its subscribers.¹²⁴ NATOA also argues that all program cost decreases must be factored into the true up.¹²⁵

53. In addition, NATOA states that if the Commission adopts an annual methodology, there should be at least a one or two quarter moratorium on rate adjustments so that franchising authorities can complete current and pending rate cases.¹²⁶ Alternatively, NATOA suggests that franchising authorities be permitted to look at pending cases under the new rules so that rates may be examined both retrospectively and prospectively.¹²⁷

54. In addition, NATOA states that franchising authorities would be better able to review rate justifications if they receive clear guidelines for review.¹²⁸ NATOA further asks that refund liability for BSTs extend for more than one year.¹²⁹ It argues that franchising authorities should be granted adequate time to review rate filings, and that the rules should take into account the fact that franchising authorities' governments do not always meet or remain in session within the Commission's mandated review periods.¹³⁰ NATOA also asks that we adopt rules to ensure that operators promptly supply relevant information.¹³¹ NATOA argues that cable operators should be penalized, rather than rewarded as they are

¹²² *Id.* at 2.

¹²³ *Id.* at 3.

¹²⁴ *Id.*

¹²⁵ *Id.*

¹²⁶ *Id.* at 1.

¹²⁷ *Id.*

¹²⁸ *Id.*

¹²⁹ *Id.* at 2.

¹³⁰ *Id.* at 1-2.

¹³¹ *Id.* at 2.

under the present rules, for non-compliance with franchising authority deadlines.¹³²

C. Discussion

55. We believe that the current price cap adjustment system generally protects subscribers from unreasonable rates. Nevertheless, with the benefit of more than one year of experience with the current system, we have found that there are some disadvantages to the current price cap adjustment mechanism. One of our concerns about the current system is that operators file for multiple rate adjustments each year because they realize cost increases throughout the year and are unable to adjust their rates to recover these costs until after these costs are incurred. We believe that this process can be costly and inefficient because operators must file a Form 1210 and provide subscribers with 30 days' advance written notice each time they file for a rate adjustment. In addition, we are concerned that multiple rate adjustments in one year can cause confusion among subscribers. Furthermore, each rate adjustment imposes an administrative burden on regulatory authorities who must review the adjustment.

56. We also are concerned about the delays that operators may experience in recovering their costs under the current rate adjustment system. Because operators incur costs before they can file for rate adjustments and they often experience delays in being able to implement rate adjustments after they have filed for them, they never recover costs that are incurred as a result of these delays.

57. Moreover, the current rate adjustment system provides that if an operator waits more than 12 months to make rate adjustments reflecting increases in external costs and the number of regulated channels, the operator loses the ability to recover for these cost increases.¹³³ In addition, operators are required to make their annual inflation adjustment during an eleven month period or lose the ability to make that inflation adjustment. Although we adopted these rules to ensure that subscribers do not experience rate shock in cases where an operator delays implementing large numbers of rate increases, we are concerned that the "use or lose" mechanisms may result in some cable operators charging higher rates before they would otherwise elect to adjust their rates.

1. Annual Rate Adjustment System

58. In order to address these concerns, on our own motion¹³⁴ we are adopting a

¹³² *Id.*

¹³³ 47 C.F.R. § 76.922(d)(3)(1).

¹³⁴ We have received a number of Petitions for Reconsideration concerning the pass through of external costs. While the methodology we adopt is not specifically contained in those petitions, the record supports much of our annual rate adjustment system.

new optional rate adjustment methodology that encourages cable operators to make only annual rate changes to their BSTs and CPSTs. Following the approval of the new Form 1240 by the Office of Management and Budget, operators may choose between the existing quarterly rate adjustment system and a new annual rate adjustment system. Operators that elect to use the new methodology would adjust their rates once a year to reflect changes in external costs, inflation, and the number of regulated channels that they expect to occur during the 12 months following the rate change. Because operators will be permitted to project changes that will occur in the 12 months following the rate filing, we expect that this methodology will limit delays that operators experience under the current system. Any cost that is not projected may be accrued and added to rates, with 11.25% interest,¹³⁵ when the operator makes its next filing. Moreover, at the end of the rate year, operators "true up" their projected changes to correct for differences between actual and projected costs during the rate year. Operators would not lose the right to make rate increases at a later date if they choose not to implement a rate change at the beginning of the next rate year. Moreover, if an operator overestimates its permitted rate as a result of its projections, the operator would be required to correct this overestimation, with interest, when it makes its next rate adjustment at the beginning of the next rate year.

59. We believe that this annual rate adjustment option will benefit subscribers, cable operators, franchising authorities, and the Commission. Annual rate modifications would limit subscriber confusion and frustration, for example, because subscribers would not have to contend with numerous rate adjustments during a given year. An annual adjustment makes good business sense for cable operators because it would allow them to file for a rate increase and provide notice to subscribers of such rate increases once a year. Regulatory authorities benefit from an annual rate adjustment system because it will minimize the number of rate adjustments they have to review each year.

60. Moreover, the annual filing option addresses concerns raised by some cable operators that under the current system they can experience delays in recovering costs.¹³⁶ Under the quarterly system, the operator will begin recovering these costs prospectively once the rate is approved, but will never recover the costs incurred during a period in which adjustments to its rates to reflect cost changes were delayed. However, operators that elect the annual system will face minimal delays in recovering their costs because they are permitted to adjust their rates to reflect reasonably certain and reasonably quantifiable changes that will occur up to 12 months after the rate adjustment will take effect. Moreover, even in cases where there are delays in cost recovery, the operator will be made whole because it will be permitted to recover for the accrual of unrecovered costs plus 11.25% interest between the date costs are incurred and the date the rate adjustment is made.

¹³⁵ See Section C(3), *infra*.

¹³⁶ See notes 83 & 84, *supra*.

61. Subscribers are protected by this system because if an operator overestimates its permitted rate as a result of its projections, the operator would be required to account for this overestimation plus 11.25% interest when it makes its next rate adjustment at the beginning of the next rate year.

62. On our own motion,¹³⁷ we are also eliminating the "use or lose" mechanism for inflation, increases in external costs and increases in the number of channels for operators that elect the annual rate adjustment method.¹³⁸ As a result, operators will not have to file more frequently than they would otherwise in order to recover costs they have incurred. In addition, subscribers will, in many cases, receive the benefit of having rate increases delayed.

63. The annual option applies to all rate changes: inflation, changes in external costs, changes in the number of regulated channels, and changes in equipment and installation costs. Under this option, an operator would file an FCC Form 1240 once a year for the purpose of making rate adjustments to reflect changes in external costs, inflation, and the number of regulated channels on a tier. On the same date that it files an FCC Form 1240, the operator also would file an FCC Form 1205 for the purpose of adjusting rates for regulated equipment and installations.

64. Operators may choose the annual filing date, but they must notify the franchising authority of their proposed date prior to their filing. Franchising authorities or their designees may reject the annual filing date chosen by the operator for good cause. For example, where a City Council must approve the rate adjustments at issue, if the review period the operator chooses coincides with a City Council recess, the franchising authority would be justified in rejecting the operator's chosen filing date. A franchising authority may not reject an operator's filing date, however, for the purpose of delaying an operator's ability to make rate adjustments. If the franchising authority finds good cause to reject the proposed filing date, the franchising authority and the operator should work together in an effort to reach a mutually acceptable date. If no agreement can be reached, the franchising authority may set the filing date up to 60 days later. In addition, operators that elect annual rate adjustments may change their filing dates from year-to-year, but at least twelve months must

¹³⁷ See note 1, *supra*.

¹³⁸ The elimination of "use or lose" for operators that use the annual rate adjustment system takes effect on the release date of this *Order*. Costs that have been incurred as of the release date of this *Order*, but which were first incurred less than one year before the release date of this *Order*, will not be lost if an operator's next filing uses the annual rate adjustment method. If an operator's next filing uses a Form 1210, the "use or lose" requirement remains for that operator, but would not apply to subsequently incurred costs should the operator's subsequent filing use the annual method.

pass before the operator can implement its next annual adjustment.¹³⁹

65. Operators must use the annual or quarterly methodology for both BSTs and CPSTs.¹⁴⁰ This requirement makes BST and CPST cost assumptions on an equivalent basis and ensures that subscribers receive the full benefit of the annual rate adjustment methodology, i.e., a minimal number of rate adjustments.

66. Although we do not expect that operators will want to switch between the annual rate adjustment option and the quarterly option, our new rules will permit switching, provided they meet certain conditions. Whenever an operator switches from the current quarterly system to the annual system, the operator may not file a Form 1240 earlier than 90 days after the operator proposed its last rate adjustment on a Form 1210.¹⁴¹ This will give regulatory authorities a reasonable period of time to complete their review of an operator's previous rate increase request before it begins reviewing an annual rate adjustment request. Similarly, when an operator changes from the annual system to the quarterly system, the operator may not return to a quarterly adjustment using a Form 1210 until a full quarter after it has filed a true up of its annual rate on a Form 1240 for the preceding period.¹⁴² This will ensure that operators do not file a Form 1210 until after the initial regulatory review period for the true up on the Form 1240 has expired. It will also prevent operators from being able to double recover for changes in their expenses because the rate period under the annual

¹³⁹ This provision does not alter the requirement that net cost decreases must be implemented at least every twelve months.

¹⁴⁰ Such a requirement is consistent with our earlier decision requiring operators to elect either the cost-of-service or benchmark method for initial BST and CPST rate filings. *Third Report and Order*, MM Docket No. 92-266, FCC 93-519, 8 FCC Rcd 8444 (1993).

¹⁴¹ Operators may begin filing for rate adjustments under the annual option (subject to our rules) as soon as the new Form 1240 is approved by the Office of Management and Budget.

¹⁴² When returning to the quarterly adjustment method from the annual method, the operator should still file its FCC Form 1205 on an annual basis. However, the operator cannot file its final true up until 15 months after the operator filed its most recent FCC Form 1240. The true up will cover a 15-month period, the last three months from the previous projection and the 12 months of the just completed rate year. Because of the extra period for review, operators that switch from a Form 1240 to a Form 1210 need not file for decreases in costs until the end of that 15-month period. This is a limited exception to the requirement that they file within 12 months of such decreases. See note 139, *supra*.

system and the quarterly system will not coincide.¹⁴³

67. The Commission will review this new annual rate adjustment option prior to December 31, 1998 to determine whether the new option is producing the expected benefits and whether the quarterly system should be eliminated and replaced with the annual rate adjustment system.

2. Projecting Changes in External Costs, Inflation, and Number of Regulated Channels

68. An operator that elects the annual option will be permitted to adjust its rates to reflect changes in its costs that are projected in the 12 months after its rate change is scheduled to go into effect. An operator's annual filing on a Form 1240 may include projections of changes in external costs, inflation, and the number of regulated channels that are expected in the 12 months following the date the operator files for the rate adjustment.¹⁴⁴ Projected rate adjustments must be based upon reasonably certain and reasonably quantifiable changes in external costs, inflation, and the number of regulated channels. In accordance with Sections 76.937(a) and 76.956(b) of the Commission's rules, operators have the burden of proving that projected changes in external costs, inflation or the number of regulated channels are reasonably certain and reasonably quantifiable.¹⁴⁵ The total amount of expenses the operator is entitled to recover between the date the rate change is expected to occur and the date of the next annual rate increase must be calculated by dividing the amount into 12 equal monthly installments and converted into a per subscriber amount.

¹⁴³ Any operator that cannot meet these conditions can file for a waiver of these filing limitations. A waiver will be granted only for good cause and upon a showing that double recovery is absent. Moreover, an operator may file a cost-of-service showing after two years from the date initial rates have been approved. *Report and Order and Further Notice of Proposed Rulemaking*, MM Docket No. 93-215, 9 FCC Rcd 4527, 4541 (1994) ("*Cost-of-Service Order*").

¹⁴⁴ In an operator's first annual filing, the operator will be permitted to recover for the accrual of costs associated with increases in external costs and changes in the number of regulated channels that occur between the date of the operator's last Form 1210 filing and the date the operator implements its rate adjustment pursuant to its Form 1210. If there is a net decrease in such costs during this period, the operator's rate adjustment on its Form 1240 must reflect the accrual of such cost decreases from the date the decreases occur through the date of the rate adjustment.

¹⁴⁵ Section 76.937 of the Commission's rules provide that a cable operator has the burden of proving that its existing or proposed rates for basic service and associated equipment comply with 47 U.S.C. § 543 and §§ 76.922 and 76.923. Section 76.956(b) provides that "[t]he burden shall be on the cable operator to prove that the [cable programming] service rate or equipment charge in question is not unreasonable."

69. We believe that operators will benefit from this system because it will minimize the delays they experience in recovering their costs under the existing rate adjustment system. Under the current rate adjustment system, operators must wait until the quarter after costs are incurred to file for a rate adjustment. As a result, operators begin recovering these costs prospectively once the rates are approved, but never recover the costs during the quarter when first incurred. In contrast, operators that elect the annual system will face minimal delays in recovering their costs because they are permitted to adjust their rates to reflect projected increases that will occur up to 12 months after the rate adjustment will take effect.

70. At the same time, subscribers will be protected from paying unreasonable rates because operators must demonstrate that their projections are reasonably certain and reasonably quantifiable. We agree with Cox that subscribers would also benefit under this approach because it would give operators incentives to add new programming without delay. Moreover, as explained more fully below, if an operator overestimates its permitted rate as a result of its projections, the operator would be required to correct this overestimation, with interest, when it makes its next rate adjustment at the beginning of the next rate year.

71. Under the annual system, operators may adjust for inflation at the beginning of each year for the coming year using the most recent 12 month estimate of the GNP-PI made available by the Commission. We believe that the previous year's inflation will serve as a fair proxy to the upcoming year's inflation. The Commission will issue a public notice in September of each year indicating the GNP-PI figure, based on inflation for the July 1 through June 30 year.

72. Operators may recover reasonably certain and reasonably quantifiable changes expected in external costs during the twelve months to which the rate filing applies. We believe that most external costs can and should be projected because this will minimize the need to permit operators to recover accrued costs plus interest. Accordingly, filings for the following categories of external costs are presumed to be reasonably certain and reasonably quantifiable: copyright fees, retransmission consent fees, other programming costs, Commission regulatory fees, and cable specific taxes.¹⁴⁶ As explained below, it is neither necessary nor appropriate to project the rate impact of increases in franchise fees. Moreover, we will not presume, as a matter of course, that franchise requirement costs are reasonably certain and reasonably quantifiable, although they may be projected to the extent the operator demonstrates that they are reasonably certain and reasonably quantifiable.

73. Projected changes in programming costs, which generally are program licensing fees and retransmission consent fees, are reasonably certain and reasonably quantifiable to the extent that programmers and operators have agreed in advance to the

¹⁴⁶ This presumption does not eliminate an operator's duty to respond to reasonable requests for information in support of its rate filings. See 47 C.F.R. § 76.937(a).

amount of programming cost changes and the date the cost changes will take effect.¹⁴⁷ We find that the appropriate regulatory authority should also be able to verify projected copyright fees because cable operators pay these fees to the U.S. Copyright Office on the basis of operators' gross receipts and distant signal equivalents.¹⁴⁸ We believe most operators should be able to project the number of broadcast signals and the amount of gross receipts 12 months in advance.

74. In addition, we find that increases in Commission regulatory fees should normally be reasonably certain and reasonably quantifiable after the Commission adopts fee changes. We expect that increases in Commission regulatory fees will be reasonably certain and reasonably quantifiable because in adopting any change to the fees, the Commission will prescribe a specific change to be assessed and to take effect on a specific date.

75. Further, we expect that changes in cable specific taxes will normally be reasonably certain and reasonably quantifiable. We believe that if a state or local government imposes a cable specific tax change, it normally will be reasonably certain and reasonably quantifiable because we would expect that the tax change would be set at a specific amount to take effect on a specific date.

76. We will not presume that changes in franchise requirement costs are reasonably certain and reasonably quantifiable. Certain changes in franchise requirement costs may not be reasonably certain and reasonably quantifiable because determining the types of costs and implementation dates can be more difficult than with other types of external costs. Even determining what qualifies as a franchise requirement cost may, in some cases, be difficult. For example, if a franchising authority adopts customer service standards that exceed the Commission's customer service standards, the operator will be permitted to pass-through the cost of implementing these standards only to the extent that the costs exceed the costs of implementing the Commission standards. We believe that it may be difficult, in some cases, to determine the difference between the cost of implementing the Commission's standards and the franchising authority's standards. Nevertheless, to the extent that operators demonstrate that such franchise requirement costs are reasonably certain and reasonably quantifiable, such costs may be projected.

77. In addition, we find that, given the way franchise fees are collected from subscribers, it would be neither necessary nor appropriate to project the rate impact of increases in franchise fees on FCC Form 1240. It is not possible to project the rate impact

¹⁴⁷ Letter from Meredith J. Jones, Chief, Cable Services Bureau, to Wesley Heppler and Paul Glist, of Cole, Raywid & Braverman, DA 95-1175 (May 26, 1995).

¹⁴⁸ See U.S. Copyright Office Form SA3, Statement of Account for Secondary Transmissions by Cable Systems. Copyright fees for carriage of local signals are accounted for on the basis of the operator's gross receipts.

of an increase in franchise fees on particular subscribers because franchise fees are normally collected from cable subscribers by assessing a fixed percentage of their total bill, at the time they receive their bill. Therefore, the amount of franchise fees collected will differ among subscribers, depending upon the total bill of a particular subscriber. Accordingly, an operator using the annual rate adjustment system may use the same methodology as with the quarterly rate adjustment system,¹⁴⁹ i.e. it may pass through franchise fees to its subscribers within 30 days of filing for an increase unless the franchising authority finds that the rate adjustment is unreasonable before 30 days has expired or requires additional information due to an incomplete rate filing.¹⁵⁰ If the franchising authority does not issue a rate decision within this 30 day period, the proposed rate will go into effect, subject to subsequent refund orders. Alternatively, if the effective date of an increase in franchise fees is the same as that for the annual rate increase, the operator may file the franchise fee adjustment concurrent with the rate increase. We encourage such an approach to minimize subscriber confusion and to reduce the franchising authority's administrative burden.

78. Finally, operators are permitted to adjust their rates to reflect reasonably certain and reasonably quantifiable changes expected in the number of regulated channels on a tier. An operator may know when changes in the number of channels on a regulated tier will take place. We believe operators should be able to make these projections just as they can with external cost changes.

3. True-up and Accrual for Changes Not Projected

79. In many cases, we expect that operators' projections will not exactly reflect the actual changes in external costs, inflation, and the number of regulated channels. For example, differences may result from estimations that were not exact, or from changes in the date an operator incurs the additional costs. Similarly, an operator's projections may not include certain changes in external costs and the number of regulated channels. Therefore, as part of the annual rate change, a "true up" mechanism is available to correct projected cost changes with actual cost changes.¹⁵¹ The true up requires operators to decrease their

¹⁴⁹ See Section III.A, *infra*.

¹⁵⁰ The operator may give notice to subscribers of an increase in franchise fees concurrent with its filing with the franchising authority. 47 C.F.R. §§ 76.932, 76.964.

¹⁵¹ Because the true-up will examine what costs were actually incurred, it can only examine costs as of the date the Form 1240 is filed. As a result, and because the Form 1240 must be filed at least 90 days before the proposed increase is scheduled to take effect, *see* Section C(6), *infra*, and the projections are made for the year beginning with the proposed implementation date, the period applicable for the true up will not exactly coincide with the previous year's projections. For example, if an operator files annually on October 1 for rates to take effect on January 1, the true up will cover the period from the previous October through September, but the projections will apply to the period January to December.

rates or permits them to increase their rates to adjust for over- or under- estimations of these cost changes. To the extent that there is an underestimation of these cost changes, future rates may be increased to permit recovery of the accrued costs plus interest between the date the costs are incurred and the date the operator is entitled to make its next rate adjustment.¹⁵² To the extent that there is an overestimation of these cost changes, future rates must be reduced to reflect the accrued amount of the overcharge plus interest.

80. Moreover, operators will be able to recover excess accrued costs with interest to the extent that the projected costs did not cover the increases that actually took place.¹⁵³ In the operator's next filing, the operator is entitled to recover these excess costs plus interest between the date the costs are incurred and the date the operator is entitled to make its next annual rate adjustment. Because we have already determined that 11.25% is presumptively the cable operator's cost of capital,¹⁵⁴ we find that the interest rate presumptively should be 11.25%. If the operator elects not to recover these accrued costs with interest on the date the operator is entitled to make its annual rate adjustment, the interest will cease to accrue as of the date the operator is entitled to make the annual rate adjustment, but the operator will not lose its ability to recover such costs and interest. Although interest will cease to accrue, operators will be permitted to recover for the accrual of costs between the date such costs are incurred and the date the operator actually implements the rate adjustment to recover for such costs. This policy will give operators the flexibility to delay rate increases without losing the opportunity to recover interest on costs that accrued due to circumstances beyond their control. At the same time, this policy ensures that where an operator makes a business decision to delay a rate increase, subscribers are not required to pay for the cost of the delay.

81. We are adopting this true up mechanism because we find that it will allow operators to elect the annual rate adjustment system without incurring financial harm due to inaccurate projections. Although operators electing this option will limit themselves to annual rate adjustments, the true up will provide them with the opportunity to recover for all costs associated with changes in external costs, inflation and the number of regulated channels. To the extent that there are any delays in making rate adjustments, the true up will minimize the operator's lost revenues because the operator will be permitted to recover for these costs.

¹⁵² For ease of administration, FCC Form 1240 calculates interest for purposes of the true up by assuming the additional costs are incurred at the mid-point of the true-up period.

¹⁵³ Operators that use the annual methodology in their next filing after the release date of this Order may accrue costs and interest incurred since July 1, 1995, in that filing. Operators that file a Form 1210 in their next filing after the release date of this Order, and elect to use Form 1240 in a subsequent filing, may accrue costs and interest incurred since the end of the last quarter to which a Form 1210 applies.

¹⁵⁴ *Cost of Service Order*, 9 FCC Rcd at 4633-35.

82. By the same token, the true up will allow many subscribers to realize the benefit of only one rate increase per year without ultimately being overcharged for regulated services. Although in some cases an operator may make an annual rate increase that reflects projected cost changes that are greater than what actually occur in practice, when operators adjust their rates pursuant to the true up in the next year, the operator will reduce its rates on a prospective basis and the overcharges plus interest will be returned to subscribers in the form of reduced rates in twelve equal monthly installments. Further, because the result of operators being able to recover more of their costs sooner is that operators will be more likely to invest in services of interest to subscribers, and do so earlier, subscribers will benefit from the true-up mechanism.

4. Channel Additions

83. Generally, operators that elect the annual rate adjustment option will not be permitted to make more than one rate adjustment per year. However, we recognize that customer and market demands for channel line-ups may change during the course of a year. As a result, operators might want to add programming during the year that they could not reasonably have projected at the time of their annual filing. Although operators may accrue these costs and reflect them in the following year's filing, we are concerned that operators may be reluctant to add new channels until they can raise rates, particularly because new programming costs can be substantial.

84. Consequently, operators may make rate adjustments for the addition of required channels to BSTs that the operator is required by federal or local law to carry, i.e., must-carry, local origination, public, educational and governmental access and leased access channels. The parties agree that when an operator is required to add channels after its annual rate adjustment, the operator should be able to pass through the costs of such channels immediately, even if this occurs outside of the annual filing cycle.¹⁵⁵ Since there would be no programming costs associated with these channel additions, adjustments will be limited to the non-external costs adjustment associated with channel additions. Franchising authorities will have 60 days to review these increases prior to their going into effect. The proposed rate adjustment will go into effect 60 days after filing unless the franchising authority finds that the adjustment would be unreasonable. Should the operator elect not to pass through the costs immediately, it may accrue the costs of the additional channels plus interest, as described in Section II(C)(3) above.

85. Further, because we have a longstanding policy to encourage new programming beyond channel additions that are required by law, we will allow operators to make one additional rate adjustment during the year to reflect channel additions to CPSTs, or to BSTs where the operator offers only one regulated tier. Operators may make this additional rate adjustment reflecting channel additions to CPSTs at any time during the year.

¹⁵⁵ See, e.g., Cox Letter at 3; NATOA Letter at 2.

Subject to the existing going forward rules, which affect the amount by which an operator can increase its rates, operators will have no limit on the number of channels they may add when they make this rate adjustment during the year. Should the operator elect not to pass through the costs immediately, it may accrue the costs of the additional channels plus interest, as described in Section II(C)(3) above. We encourage operators to put channel adjustments in their annual filings especially where their channel addition filing would be close in time to the annual filing. The regulatory review period for an increase under the mid-year channel addition is the same as under the annual adjustment for CPST.

86. We recognize, as we did in the *Sixth Reconsideration Order*, that allowing recovery for unlimited mid-year channel additions to CPSTs, and not to BSTs (except systems with only one regulated tier) may create greater incentives to add channels to CPSTs than to BSTs.¹⁵⁶ We believe that preserving rate stability on the BST, which carries broadcast signals and which every subscriber must purchase in order to receive other programming services, is sufficient reason to limit the applicability of this rule to CPSTs.¹⁵⁷ Moreover, we are concerned that, if we allowed operators to add an unlimited number of channels to BSTs, it would increase the complexity of the regulatory task faced by franchising authorities.¹⁵⁸ For these reasons, we limit application of the new rules to CPSTs and to those BSTs that are offered by operators with only a single regulated tier. Franchising authorities that receive mid-year channel addition filings from single-tier operators have 60 days to review these filings.

5. Treatment of Equipment and Installation

87. Operators that elect the annual rate adjustment system must file for rate adjustments for equipment and installations on Form 1205 on the same date that they file for their other rate adjustments on Form 1240.¹⁵⁹ Therefore, for operators that elect to use the annual rate adjustment methodology, we are changing the current rule which requires operators to file Form 1205 60 days after the close of their fiscal year.¹⁶⁰ Both forms must be filed with franchising authorities 90 days before the rate adjustment is scheduled to go

¹⁵⁶ 10 FCC Rcd at 1250-51.

¹⁵⁷ *Id.*

¹⁵⁸ *Id.* at 1251. In addition, NATOA has stated that it opposes permitting operators make unlimited channel additions to BSTs. NATOA Letter at 2-3.

¹⁵⁹ If an operator's BST is subject to regulation and the operator elects not to file a Form 1240 during a given year, the operator must continue to file its Form 1205 on an annual basis. FCC Form 1205, Instructions for Determining Costs of Regulated Cable Equipment and Installation at 2.

¹⁶⁰ *Id.*

into effect so that operators propose to implement all rate adjustments on the same date. We also find that requiring the filing of both forms on the same date would ease the administrative burdens on franchising authorities. This modifies the current requirement that operators file their Form 1205 no more than annually to the extent necessary when the operator changes to the annual system.

88. In addition, we will continue to require operators to base their proposed annual customer equipment and installations rate adjustments on past costs. However, in order to provide operators with flexibility to set their annual filing dates, we will allow an alternative to the present requirement that operators must set their rates using data from the last fiscal year.¹⁶¹ Specifically, if an operator that elects the annual rate change option chooses a filing date that does not coincide with the end of its fiscal year, the operator may use either data from the 12 months preceding the filing or data from its most recent fiscal year. We are providing operators with the flexibility to choose between these options because we recognize that an operator's equipment costs may change significantly between the close of the fiscal year and the date the operator files its Form 1205. Moreover, where operators face an unusual change in operations that would not be reflected in either methodology, we will continue to permit them to use a representative month for the purpose of calculating equipment rates, provided that franchising authorities agree to this arrangement.¹⁶²

89. We believe that it would be far more difficult to project changes in equipment and installation costs because the variables involved with the calculation of customer equipment and installation rates are more numerous than are the variables in projecting external costs, inflation, and channel additions. In determining equipment rates, for example, it is necessary to determine the total maintenance costs and/or service hours, the total number of units that have been brought into service, the gross book value of the equipment, the accumulated depreciation of the equipment, the deferred tax balance associated with the equipment, the grossed up rate of return on the equipment, and the depreciation expense. This is far more complicated and uncertain than projecting inflation, channel additions, and increases in external costs. Moreover, installation costs are set by determining an hourly service charge which is based on calculating (a) the total capital costs for vehicles, tools and facilities used for maintenance of equipment, (b) annual operating expenses associated with vehicles, tools and facilities used for maintaining equipment, (c) a percentage of the total capital costs and operating expenses for equipment and installations, and (d) the total labor hours for maintenance and installation of customer equipment and services. In light of the large number of complicated variables that enter into calculating equipment and installation costs, we will not permit operators to project these costs. We believe that verifying these projected costs would impose a substantial administrative burden on franchising authorities that exceeds the benefit to operators associated with projecting

¹⁶¹ *First Reconsideration Order*, 9 FCC Rcd at 1200.

¹⁶² *See First Reconsideration Order*, 9 FCC Rcd at 1200.

equipment costs.

90. Moreover, under existing rules, operators set their equipment and installation rates on an annual basis using the preceding fiscal year. We continue to believe, as we found in the *Third Reconsideration Order*, that setting rates using costs not projected permits operators to recover their full cost of equipment.¹⁶³ For those cases where operators face an unusual change in operations that would not be reflected in the previous year's annual data, the *First Reconsideration Order* stated that operators are permitted to use a representative month for the purpose of calculating equipment rates, provided that franchising authorities agree to this arrangement.¹⁶⁴

91. Finally, we clarify how an operator should set its initial rates for new types of equipment.¹⁶⁵ We have previously stated that when an operator introduces a new type of equipment, the operator may set a rate for that equipment at the time it is introduced.¹⁶⁶ Until now, however, we have not provided a methodology. Accordingly, no earlier than 60 days before the date the new type of equipment is scheduled to be introduced to subscribers, the operator will be permitted to file for a rate adjustment on a Form 1205. The proposed rate would go into effect at the end of this 60-day period unless the franchising authority rejects the proposed rate as unreasonable or the franchising authority finds that the operator has submitted an incomplete filing. In setting rates for new types of equipment, operators would complete the relevant portion of Schedule C and the relevant step of the Worksheet for Calculating Permitted Equipment and Installation Charges of a Form 1205. Moreover, where applicable, the operator would use figures from the most recent Form 1205 for the information not specifically related to the new equipment, e.g., the Hourly Service Charge. In calculating the annual maintenance and service hours for the new equipment, the operator should base its entry on the average annual expected time required to maintain the unit, i.e., expected service hours required over the life of the equipment unit being introduced divided by the equipment unit's expected life.

6. Regulatory Review Period for Annual Rate Changes

a. Basic Service Tier

92. Operators that elect the annual rate adjustment methodology must file BST rate change requests at least 90 days prior to the date they plan to implement the proposed

¹⁶³ *Third Reconsideration Order*, 9 FCC Rcd 4372.

¹⁶⁴ *First Reconsideration Order*, 9 FCC Rcd at 1200.

¹⁶⁵ This approach is not limited to operators that elect the annual filing, but applies to all operators that file Form 1205.

¹⁶⁶ *First Reconsideration Order*, 9 FCC Rcd at 1199.

changes.¹⁶⁷ Operators may implement rate changes as they have proposed in their filings 90 days after they file unless the franchising authority rejects the proposed rate as unreasonable. If the franchising authority has not issued a rate decision and the operator makes a rate adjustment after the 90-day period has expired, the franchising authority may order a prospective rate reduction and refunds at a later time, where appropriate. The franchising authority need not issue an accounting order to preserve its right to require a refund after the 90-day review period. However, if at the end of the 90-day review period an operator inquires as to whether the franchising authority is continuing to review the operator's filing, the franchising authority or its designee must respond to the operator within 15 days of receiving the inquiry. Failure to reply in the requisite amount of time will result in the franchising authority losing its ability to issue refunds or to order prospective rate reductions. In its response, the franchising authority must indicate whether it is continuing to review the operator's filing. If a proposed rate goes into effect before the franchising authority issues its rate order, the franchising authority will have 12 months from the date the operator filed for the rate adjustment to issue its rate order.¹⁶⁸ In the event that the franchising authority does not act within the 12-month period, it may not at a later date order a refund or a prospective rate reduction with respect to the rate filing. We set this time constraint on franchising authorities because we believe that one year should provide ample time for review, and because operators need to have certainty with respect to their liability for refunds and whether their rates will be permitted to remain in effect.

93. We believe that a 90-day regulatory review period strikes a good balance among the interests of subscribers, franchising authorities and cable operators. If operators were required to file any more than 90 days before a rate adjustment is scheduled to take effect, they would encounter much greater difficulty in projecting their costs accurately. On the other hand, if operators were permitted to file less than 90 days before a rate adjustment is scheduled to take effect, franchising authorities may not have enough time to review a complete rate filing because the franchising authority must simultaneously determine whether an operator has (a) justified projected inflation, changes in external costs, and changes in the number of regulated channels; (b) accurately estimated any undercharges or overcharges in its true up of the previous year; and (c) accurately determined its actual costs for customer equipment and installations in its annual Form 1205 filing. Without ample time to review operators' rate filings, franchising authorities may be unable to ensure that subscribers are paying reasonable rates for BSTs. This 90-day review period will also help operators

¹⁶⁷ Such requests would include FCC Forms 1205 and 1240, and may include Form 1215. An operator may file more than 90 days in advance of its implementation date, but the franchising authority still has a 90-day review period. This option will allow an operator to implement a price change after it knows how the franchising authority has acted on its proposal.

¹⁶⁸ Our current price cap rules contain no limits on the amount of time franchising authorities can take to issue rate decisions. See 47 C.F.R. § 76.933(c).

develop their business plans because it provides them with certainty as to when rate changes will become effective.

94. If there is a material change in an operator's circumstances during the 90-day review period and the change affects the operator's rate change filing, the operator may file an amendment to its Form 1240. Such an amendment must be filed, however, before the end of the 90-day review period. If the operator files such an amendment to its filing, the franchising authority will have at least 30 days to review the filing. Therefore, if the amendment is filed more than 60 days after the operator made its initial filing, the operator's proposed rate change may not go into effect any earlier than 30 days after the filing of its amendment. However, if the operator files its amended application on or prior to the sixtieth day of the 90-day review period, the operator may implement its proposed rate adjustment, as modified by the amendment, 90 days after its initial filing.

95. Consistent with our current rule,¹⁶⁹ proposed rates do not take effect at the end of the 90-day period if the franchising authority concludes that the operator has submitted a facially incomplete filing. We maintain the current rule because we recognize that a franchising authority lacks sufficient information to act on a rate justification that is facially incomplete, and because the franchising authority's period to review a complete filing should not be limited as the result of the operator's failure to provide the information required on the form. Facially incomplete filings are those filings which do not have all the information required by the form. They are to be distinguished from other filings which contain all of the required information, but about which franchising authorities seek clarifying or substantiating information. Under this limited exception, the franchising authority or its designee must notify the operator of the incomplete filing within 45 days of the date the filing is made. While the franchising authority is waiting for this information, the franchising authority's deadline for issuing a decision, the date on which rates may go into effect if no decision is issued, and the period for which refunds are payable, will be tolled.

96. At the time an operator files its rates with the franchising authority, the operator may give customers notice of the proposed rate changes.¹⁷⁰ Such notice should state that the proposed rate change is subject to approval by the franchising authority. If the operator is only permitted a smaller increase than was provided for in the notice, the operator must provide an explanation to subscribers on the bill in which the rate adjustment is implemented. If the operator is not permitted to implement any of the rate increase that was provided for in the notice, the operator must provide an explanation to subscribers

¹⁶⁹ 47 C.F.R. § 76.937(e).

¹⁷⁰ If an operator plans to implement a rate adjustment 90 days after the operator submits its filing for a rate adjustment, the operator is required to provide subscribers with advance written notice of the proposed rate increase no later than 30 days before the end of the 90-day review period. See 47 C.F.R. §§ 76.309(b)(3)(i)(B), 76.964(b).

within 60 days of the date of the franchising authority's decision.¹⁷¹ Additional advance notice is only required in the unlikely event that the rate exceeds the previously noticed rate.

97. We reject Cox's proposal that we allow contested rate increases to go into effect subject to refund liability pending the outcome of an expedited appeal to the Commission.¹⁷² We find that it would be inappropriate for the Commission to allow operators to implement BST rate increases in cases where the operator has appealed a franchising authority decision that found the rates to be unreasonable because the Commission only conducts an appellate review of franchising authority decisions regarding BST rates and does not set the rate on appeal. In fact, the Commission will reverse a franchising authority's decision only if it determines that the franchising authority acted unreasonably in applying the Commission's rules in rendering its local rate order.¹⁷³ If the Commission reverses a franchising authority's decision, it will not substitute its own decision but instead will remand the issue to the franchising authority with instructions to resolve the case consistent with the Commission's decision on appeal.¹⁷⁴

98. However, if a franchising authority finds that the rate set by the operator on its Form 1240 is unreasonable and the operator appeals the decision to the Commission, the operator will recover any lost revenues if the Commission ultimately determines that the franchising authority unreasonably denied the operator's proposed rate adjustment. The operator will be permitted to recover all lost revenues with interest between the date of the franchising authority's decision and the date the operator is permitted to make the rate adjustment as a part of the true up in its next annual rate filing.¹⁷⁵ We allow the operator to make this recovery because we believe it is appropriate to place the operator in the position in which it would have been had the franchising authority approved the operator's reasonable rate adjustment proposal.

b. Cable Programming Services Tiers

99. Section 76.960 of the Commission's rules provides that if the Commission has ordered an operator to make a prospective rate reduction for a CPST, the rate reduction will

¹⁷¹ Consistent with our customer service standards, of which the notice requirement is a part, this Order does not preempt notice requirements imposed by state and local law. 47 C.F.R. §§ 76.309(b)(3-4), .309(c)(3)(B)(i); *see also Report & Order*, MM Docket No. 92-263, FCC 93-145, 8 FCC Rcd 2892, 2895-96 (1993).

¹⁷² Cox Letter at 2.

¹⁷³ *Rate Order*, 8 FCC Rcd at 5732; *Third Reconsideration Order*, 9 FCC Rcd at 4346.

¹⁷⁴ *Id.*

¹⁷⁵ *See* Section II(C)(3), *supra*.

be binding on the operator for one year, unless the Commission specifies otherwise.¹⁷⁶ Accordingly, operators that have been required to reduce their CPST rates have not been permitted to increase their rates under our price cap rules for one year without prior Commission approval.

100. We will eliminate this requirement for operators that elect to use the annual rate adjustment system. Operators that have been ordered to make a rate reduction within one year of filing for an increase under the annual system may implement their annual rate adjustment without prior Commission approval. They will be required to file a Form 1240 proposing an annual rate adjustment for their CPST rate adjustments 30 days before the operator plans to implement the rate change. The Commission can deny the increase before the end of 30 day-period, but if the Commission does not act within 30 days, the operator may implement the rate increase as proposed on the Form 1240. The increase would go into effect, subject to a prospective rate reduction and refund, where appropriate, which may be ordered at a later time.

101. Operators that elect the annual rate adjustment system and have CPST complaints pending also must propose the annual rate adjustment by filing an FCC Form 1240 with the Commission at least 30 days prior to the date the operator plans to implement the rate change.¹⁷⁷ The Commission can deny the increase before the end of 30 day-period, but if the Commission does not act within 30 days, the operator may implement the rate increase as proposed on the Form 1240. The increase would go into effect, subject to a prospective rate reduction and refunds, where appropriate, which may be ordered at a later time.

102. An operator that has a CPST complaint pending or has been ordered by the Commission to reduce its CPST rates within the past year may amend its rate change filing after the 30-day review period has commenced, if there is a material change in an operator's circumstances that affects the operator's proposed rate change. Such an amendment must be filed, however, before the end of the 30-day review period.

103. Where both an operator's BST and CPSTs are subject to rate regulation and the operator is filing for annual adjustments to both tiers, the operator must file for these rate adjustments so that they are scheduled to go into effect on the same date. That is, the 90-day review period for the BST adjustment must coincide with the 30-day review period for the CPST adjustment so that both rate adjustments may be implemented on the same subscriber bills. While we are not requiring operators to actually implement the rate adjustments on the same date, we believe that this policy will encourage operators to make rate changes to their

¹⁷⁶ 47 C.F.R. § 76.960.

¹⁷⁷ 47 C.F.R. § 76.958. An operator may of course file its Form 1240 with the Commission at the same time that it files with its franchising authority.

BSTs and CPSTs on the same date once per year, which will reduce customer confusion associated with multiple rate increases.¹⁷⁸

104. The operator may give the required notice to subscribers¹⁷⁹ concurrently with its filing with the Commission.¹⁸⁰ If the Commission acts on the rate application before it goes into effect and the operator is only permitted a smaller increase than was provided for in the notice, the operator must provide an explanation to subscribers on the bill in which the rate adjustment is implemented. If the operator is not permitted to implement any of the rate increase that was provided for in the notice, the operator must provide an explanation to subscribers within 60 days of the date of the Commission's decision.¹⁸¹ Additional advance notice is only required in the unlikely event that the rate exceeds the previously noticed rate.

7. Treatment of External Costs Under the Quarterly Rate Adjustment System

105. In light of our decision to adopt this annual rate adjustment option, we will not alter the existing quarterly rate adjustment system. We find that it is not necessary to eliminate regulatory lag under the quarterly system because if operators believe that regulatory lag under the quarterly system prevents them from recovering all of their costs, they can use the annual option. Moreover, we reject suggestions by TKR and CATA that we allow operators to pass through changes in external costs under the existing quarterly system within 30 days of an operator's filing for such a rate adjustment. We reject this recommendation because we are not convinced that, in all cases, the 30-day period will provide franchising authorities with the time to conduct a proper review of the reasonableness of these external costs.

106. As an initial matter we find that TKR's request that the Commission permit operators to pass through all external costs without prior regulatory approval is an issue that

¹⁷⁸ Operators with CPST complaints pending or that have been ordered by the Commission to reduce their CPST rates must implement net cost decreases by the anniversary date of the annual adjustment period.

¹⁷⁹ 47 C.F.R. §§ 76.309(b)(3)(i)(B) and 76.964(b).

¹⁸⁰ Operators should notify subscribers about rate changes for the BST, CPSTs, and equipment at the same time, in order to avoid subscriber confusion resulting from giving multiple notices.

¹⁸¹ Consistent with our customer service standards, of which the notice requirement is a part, this Order does not preempt notice requirements imposed by state and local law. 47 C.F.R. §§ 76.309(b)(3-4), .309(c)(3)(B)(i); *see also Report & Order*, MM Docket No. 92-263, FCC 93-145, 8 FCC Rcd 2892, 2895-96 (1993).

is properly before us on reconsideration of the *Fourth Reconsideration Order*. In the *Fourth Reconsideration Order*, we permitted cable operators to pass through two categories of external costs without prior regulatory approval: franchise fees and Commission regulatory fees. Because TKR is seeking to extend this treatment to all categories of external costs, we find that TKR is raising issues that were addressed in the *Fourth Reconsideration Order*.¹⁸²

107. Although, under the quarterly rate adjustment system, we previously decided to permit operators to adjust their rates to reflect changes in franchise fees and Commission regulatory fees within 30 days of filing for recovery of such costs because we found that franchising authorities should be able to easily complete their review of the reasonableness of these costs within 30 days,¹⁸³ we find that TKR and CATA have failed to demonstrate that 30 days will always provide franchising authorities with sufficient time to review the reasonableness of a cable operator's filing concerning other categories of external costs. We believe that unlike franchise fees, determining the reasonableness of other categories of external costs, particularly retransmission consent fees, programming costs, and franchise requirement costs, can be somewhat complicated. In determining the reasonableness of the cost of franchise requirements, for example, the franchising authority's determination as to the amount of a franchise requirement cost may, in some cases, be a difficult question which may take a franchising authority longer than 30 days to resolve. If a franchising authority adopts customer service and technical standards that exceed such requirements under our rules, operators are permitted to pass through the cost of these standards, to the extent that they exceed the requirements under our rules. Because it may be difficult in some cases to determine the incremental cost of the local standards that exceed the requirements under our rules, franchising authorities may reasonably need more time to make this determination. Franchising authorities also may require additional time, in some cases, to review retransmission consent fees and other programming cost increases because the franchising authority may have to review additional information in order to verify the costs claimed on the operator's FCC Form 1210.

III. TREATMENT OF FRANCHISE FEES AND COMMISSION REGULATORY

¹⁸² Even if this issue was not properly before the Commission on reconsideration, the Commission has the authority to decide this issue on our own motion. See note 1, *supra*.

¹⁸³ We found that the franchising authority's review of the pass through of franchise fees and regulatory fees should entail minimal administrative burdens because the amount of these fees can be easily verified. For example, Commission regulatory fees can be easily calculated because each cable system operator is assessed \$370 per 1,000 subscribers for the fee and franchise fees most often can be determined by computing a fixed percentage of the operator's gross annual revenues.

FEES UNDER QUARTERLY RATE ADJUSTMENT OPTION

108. As stated above, operators that do not elect the annual rate adjustment option may continue to adjust their rates on a calendar year quarterly basis to reflect changes in certain categories of external costs, and the number of regulated channels. Cable operators seeking to adjust regulated rates to reflect these changes must support the proposed rate on FCC Form 1210,¹⁸⁴ and file the form with the appropriate regulatory authority. In the *Fourth Reconsideration Order*, we extended external cost treatment to Commission regulatory fees and modified external cost treatment of franchise fees. This section addresses petitions for reconsideration that were filed in response to the *Fourth Reconsideration Order*.

A. Franchise Fees

1. *Fourth Reconsideration Order*

109. In the *Fourth Reconsideration Order* we permitted operators to pass through franchise fees as external costs in 30 days unless the franchising authority determines that the rate adjustment is unreasonable before 30 days has expired.¹⁸⁵ In making this decision, we found that because franchise fees are set by the franchising authority, which generally is aware of and sensitive to the fees' impact on subscribers, prior regulatory review of the franchise fee appears less necessary from a consumer protection standpoint than it is for other categories of external costs. Under this approach, the new rate automatically takes effect following a franchising authority's 30-day review period.¹⁸⁶ However, we preserved a cable operator's obligations to provide subscribers and franchising authorities with 30 days' prior notice of any rate changes,¹⁸⁷ and to supply the franchising authority with information justifying the calculation of the new rate.¹⁸⁸ We also presumed a franchising authority's right to order a prospective rate reduction, a refund, or both, in accordance with our rules in cases where the franchising authority allowed a rate to go into effect, but later found the rate to be

¹⁸⁴ FCC Form 1210: Updating Maximum Permitted Rates for Regulated Cable Service (May 1994). See also 47 C.F.R. §§ 76.922(d), 76.933. Cable operators need not use FCC Form 1210 when merely demonstrating the calculation of rate increases on account of franchise or Commission regulatory fees. *Fourth Reconsideration Order*, 9 FCC Rcd at 5796 n.13, 5797.

¹⁸⁵ *Fourth Reconsideration Order*, 9 FCC Rcd at 5796; see also 47 C.F.R. § 76.933(e).

¹⁸⁶ 47 C.F.R. § 76.933(e).

¹⁸⁷ 47 C.F.R. § 76.964(b).

¹⁸⁸ *Fourth Reconsideration Order*, 9 FCC Rcd at 5796 n.12.

unlawful.¹⁸⁹

2. Contentions

110. The Local Governments dispute our assumption that prior review of subscriber rate increases due to increased franchise fees is less necessary because the franchising authority usually sets the fees. They assert that the amount of an operator's costs that may be properly allocated to franchise fees is far from clear in many jurisdictions, particularly with respect to the amount attributed to franchise fees on subscribers' bills. For example, they argue that cable operators often attempt to treat costs associated with the provision of public, educational or governmental ("PEG") access channels as franchise fees. The Local Governments argue that our decisions in the *Fourth Reconsideration Order* will permit cable operators to exploit these disagreements with franchising authorities by simply passing through the alleged franchise fee increases without prior regulatory review or approval. They contend that, although subscribers ultimately may be protected by refunds for rate increases later deemed unreasonable, it is unfair to force subscribers to suffer higher rates while the franchising authority reviews the new rates. Finally, the Local Governments contend that subscriber rate increases on account of franchise fees should be subject to prior regulatory review just like increases in the rate for the BST because, from a subscriber's viewpoint, no difference exists between an overcharge due to improper franchise fees and an overcharge associated with some other type of external cost.¹⁹⁰

111. The National Cable Television Association ("NCTA"), on the other hand, urges the Commission to refrain from modifying our decision permitting the automatic pass through of franchise fees. NCTA disputes the Local Governments' claim that cable operators will abuse disagreements with franchising authorities pursuant to this revised rule. NCTA notes that franchising authorities will continue to receive 30 days' prior notice of the proposed rate increase and argues that this period should be sufficient for their review of franchise fee-based rate increases in all but the most unusual cases. Finally, NCTA argues that the refund mechanism adequately protects subscribers from harm if the rate increase is later found to be based on incorrect data calculations.¹⁹¹

3. Discussion

112. We affirm our decision to permit operators that file rate adjustments under the quarterly system to pass through franchise fees within 30 days of filing unless the franchising authority finds that the rate adjustment is unreasonable before 30 days has expired. If the

¹⁸⁹ *Id.* at 5796 n.18 (describing requirements under 47 C.F.R. § 76.933(a) - (c)). See also 47 C.F.R. §§ 76.942, 76.945.

¹⁹⁰ Local Governments Petition for Reconsideration at 2-5.

¹⁹¹ NCTA Opposition at 2-3.

franchising authority does not issue a rate decision within this 30 day period, the proposed rate will go into effect, subject to subsequent refund orders.¹⁹² In order to issue a refund order, the franchising authority must issue a written order at the end of the 30 day period directing the operator to keep an accurate account of all amounts received by reason of the proposed rate and on whose behalf such amounts are paid.¹⁹³

113. We do not believe this rule presents a serious risk of harm to subscribers because, contrary to the assertions of Local Governments, we believe franchising authorities normally should be able to complete their review of rate adjustments reflecting the pass through of franchise fees within 30 days of an operator's filing. In most cases, the franchising authority's review of the franchise fee pass through generally should entail minimal administrative burdens since the franchising authority is intimately familiar with how the fee is assessed. Because the operator pays the franchise fee to the franchising authority, there should not be any dispute over the amount of franchise fees that were actually paid to the franchising authority. Further, the franchise fee is generally easily determined by computing a fixed percentage of the operator's gross annual revenues or some other easily ascertainable amount. We find that franchising authorities can easily determine how the pass through of such fees should be reflected in a BST rate adjustment because the entire cost of franchise fees is directly assigned to the BST.¹⁹⁴ Finally, to the extent franchise fees are miscalculated, we believe that our approach fully protects subscribers' interests in paying reasonable rates because franchise fee increases are subject to refunds.

114. As with all other rate adjustment filings, if an operator files for a rate adjustment to reflect an increase in franchise fees and fails to complete its rate justification form or to include supporting information called for by the form, the franchising authority may order the cable operator to file supplemental information.¹⁹⁵ While the franchising authority is waiting to receive this information from the cable operator, the deadline for the franchising authority to rule on the reasonableness of the proposed rates is tolled.¹⁹⁶ Once the supplemental information has been filed with the franchising authority, the time for determining the reasonableness of the rate by the franchising authority will recommence.¹⁹⁷ We believe that this requirement is essential if franchising authorities are going to have the minimum information necessary to complete a review of an operator's rate adjustment

¹⁹² *Id.*

¹⁹³ *Id.*

¹⁹⁴ *See* FCC Form 1210, Module B.

¹⁹⁵ *See Third Reconsideration Order*, 9 FCC Rcd at 4348.

¹⁹⁶ *Id.*

¹⁹⁷ *Id.* at 4348 n.52.

request within 30 days of the filing.

B. Commission Regulatory Fees

1. *Fourth Reconsideration Order*

115. In the *Fourth Reconsideration Order* we also determined that Commission annual regulatory fees¹⁹⁸ imposed under Section 9 of the Communications Act of 1934 should be passed through as external costs as provided under our price cap rules governing cable service regulation.¹⁹⁹ We further determined that cable operators may adjust rates to reflect the annual regulatory fees on the same conditions as franchise fees, namely, without the prior approval of franchising authorities, but subject to potential refund liability.²⁰⁰ Finally, we stated that, on a going-forward basis, operators may recover the regulatory fees in 12 equal monthly installments from subscribers during the fiscal year following the fiscal year during which the payment was imposed. We recognized that a cable operator may not collect the fees from subscribers until after the operator has paid the fees to the Commission; however, we prohibited operators from assessing interest on the amounts charged to the subscribers to avoid the substantial administrative burdens required for such calculations.²⁰¹

2. Contentions

116. The Local Governments urge the Commission to reverse our decision according external cost treatment to the Commission cable service regulatory fees because the fees will not represent a significant burden to cable operators. They note that the Commission declined to accord external treatment to Cable Television Antenna Relay Service ("CARS") license application fees assessed on cable operators because these fees, which are assessed on a flat fee basis of \$220 per license, are viewed as insignificant by most

¹⁹⁸ *Fourth Reconsideration Order*, 9 FCC Rcd at 5797; 47 C.F.R. § 76.922(d)(3)(iv)(F). The Commission is required to collect cable system regulatory fees of \$370 per 1,000 subscribers from cable television systems on an annual basis. See Public Notice: Cable Television System Regulatory Fees (June 20, 1994); see also 47 C.F.R. § 159 (imposing the fees). The purpose of requiring cable systems to pay regulatory fees to the Commission is to permit the Commission to recover the annual cost of its various regulatory activities.

¹⁹⁹ *Fourth Reconsideration Order*, 9 FCC Rcd at 5797.

²⁰⁰ *Id.*

²⁰¹ *Id.*

operators.²⁰²

117. The Local Governments also oppose the Commission's assignment of the Commission regulatory fees to the BST for purposes of cable operators' recovery of the fees from subscribers. They argue that this approach is regressive in that it unfairly burdens basic-only subscribers who, the Local Governments allege, often are elderly, low-income subscribers or those who cannot otherwise receive over-the-air local broadcast stations due to signal interference from mountains, buildings, and other structures. The Local Governments contend that assignment of the fees to the BST forces basic-only subscribers to pay a disproportionate share of the fees, and therefore contradicts Section 543(b)(1) of the Communications Act, which requires the Commission to ensure that subscribers pay only "reasonable" rates for regulated cable service.²⁰³ NCTA opposes the Local Governments' request, stating that the law imposing the regulatory fees is not based on an individual's level of service; rather, the law requires payment on a per subscriber basis. Therefore, assignment of the fees to the BST is appropriate because every subscriber must receive the BST.²⁰⁴

3. Discussion

118. We affirm our decision to permit operators to pass through Commission annual regulatory fees as external costs. As we stated in the *Fourth Reconsideration Order*, Commission annual regulatory fees should be afforded external cost treatment because they are exceptional, newly imposed, governmentally assessed fees that are easily measurable and beyond the control of operators.²⁰⁵ We disagree with NATOA's argument that Commission regulatory fees are like CARS fees in that they do not impose a significant financial burden on cable operators. We find that Commission regulatory fees can reach significant levels because they are assessed on a per subscriber basis, as opposed to CARS fees, which are assessed on a flat fee basis of \$220 per license and which comprise only a small expense for most cable systems.

119. In addition, with respect to operators that elect to file rate adjustments under the quarterly system, we affirm our decision to permit operators to adjust rates on account of

²⁰² Local Governments Petition for Reconsideration at 8 (*citing Fourth Reconsideration Order*, 9 FCC Rcd at 5797 n.35).

²⁰³ *Id.* at 6-7 (*citing* 47 U.S.C. § 543(b)(1)).

²⁰⁴ NCTA Opposition at 6-7.

²⁰⁵ *Fourth Reconsideration Order*, 9 FCC Rcd at 5797.

changes in Commission regulatory fees within 30 days of filing.²⁰⁶ We do not believe this rule presents a serious risk of harm to consumers because we believe franchising authorities normally should be able to complete their review of rate adjustments reflecting the pass through of Commission annual regulatory fees within 30 days of an operator's filing. In most cases, the franchising authority's review of the franchise fee pass through should entail minimal administrative burdens because the amount of any rate adjustment reflecting an increase should be easy to determine since it is fixed on a per subscriber basis. To the extent Commission annual regulatory fees are miscalculated, we believe that our approach fully protects subscribers' interests in paying reasonable rates because fee increases are subject to refunds.

120. We also affirm our decision to require operators to assign the Commission's annual regulatory fee directly to the BST. As we noted in the *Fourth Reconsideration Order*, the fee is intended to reimburse the Commission for its costs of regulating cable service, including oversight of basic cable service and other regulatory activities. We continue to believe that direct assignment to the BST is the most equitable means of permitting cable systems to pass through regulatory fees to subscribers because cable system annual regulatory fees are assessed on a per subscriber basis and all subscribers receive the BST. If we were to allocate these costs among the tiers, some subscribers would pay more than others even though the cost is imposed on the cable operator evenly per subscriber.²⁰⁷ Moreover, the administrative burdens associated with calculating and assigning fees among the BST and CPSTs weigh against such an assignment.²⁰⁸

IV. EXTERNAL COST TREATMENT OF FRANCHISE REQUIREMENTS

A. Background

121. The 1992 Cable Act specifically identifies franchise-imposed costs as being relevant to the determination of whether cable rates for basic service are reasonable. In prescribing regulations governing basic rates of regulated operators, Section 623(b)(2)(C) of the Communications Act directs the Commission to take into account, among other factors, "any amount required, in accordance with paragraph (4), to satisfy franchise requirements to support public, educational, or governmental channels or the use of such channels or any

²⁰⁶ Operators that elect the new annual rate filing methodology incorporate changes in Commission regulatory fees into their annual filings. See Section II(C)(2).

²⁰⁷ *Id.*

²⁰⁸ *Id.*

other services required under the franchise. . . ."²⁰⁹ As for our duty to identify such costs "in accordance with paragraph 4 [of Section 623(B)]," that section provides:

The regulations prescribed by the Commission under this subsection shall include standards to identify costs attributable to satisfying franchise requirements to support public, educational, or governmental channels or the use of such channels or any other services required under the franchise.²¹⁰

122. In the *Rate Order*, we determined that external costs include franchise imposed costs, i.e., the "costs of satisfying franchise requirements, including costs of satisfying franchise requirements for local, public, educational, and governmental access channels."²¹¹ We explained that these costs "are largely beyond the control of the cable operator, and should be passed on to subscribers without a cost-of-service showing."²¹²

123. In response to petitions for reconsideration of the *Rate Order* seeking clarification of what constitute franchise-imposed costs, we noted that our rule essentially incorporated the language of the 1992 Cable Act, and stated that we should decide to include or exclude costs in a way that will produce equitable results for both operators and subscribers. We thus determined that only increases specifically required in the franchise documents should be accorded external treatment. This includes the costs of meeting local technical and customer service standards. We stated that this approach would permit franchising authorities and cable operators to work cooperatively to establish the costs of meeting franchise requirements that would be accorded external treatment.²¹³

124. In the *Second Reconsideration Order*, we adopted the existing methodology for calculating rate adjustments based on external costs, but we did not deem it necessary to provide any further guidance as to what constitutes a franchise imposed cost.²¹⁴ However,

²⁰⁹ Section 623(b)(2)(C)(vi) of the Communications Act, as amended, 47 U.S.C. § 543(b)(2)(C)(vi).

²¹⁰ Section 623(b)(4) of the Communications Act, as amended, 47 U.S.C. § 543(b)(4). Although the legislative history discusses the provision as it applies to PEG services, it does not address the meaning of "other services required under the franchise." See H. Rep. 628, 102d Cong., 2d Sess. 84 (1992).

²¹¹ *Rate Order*, 9 FCC Rcd at 5790.

²¹² *Id.*

²¹³ *First Reconsideration Order*, 9 FCC Rcd at 1220 (footnotes omitted).

²¹⁴ *Second Reconsideration Order*, 9 FCC Rcd at 4200-04.

comments supporting and opposing petitions for reconsideration of the *Second Reconsideration Order* reveal differences of opinion as to this subject.

B. Contentions

125. NATOA, in its Petition for Reconsideration of the *Second Reconsideration Order and Third Reconsideration Order*, urges us to clarify what is meant by "[c]osts of complying with franchise requirements," as that term is used in Section 76.922(d)(3)(iv)(B) of our rules.²¹⁵ NATOA also seeks clarification as to the precise manner in which cable operators may pass through these costs. NATOA states that addressing this issue could "minimize disputes between a franchising authority or the Commission and a cable operator, and [could] prevent unwarranted surcharges on regulated rates." For example, NATOA argues that a provision in a franchise agreement that the cable system be operated "in a safe and reasonable manner" can lead to disputes if the operator, citing this provision, attempts to pass through as external costs the expenses related to routine system maintenance necessary to operate the system "in a safe and reasonable manner." Likewise, NATOA claims that a cable operator might extend its trunk line in order to reach more subscribers and increase its profits, but then claim the cost of the line extension as an external cost eligible for pass through treatment because its franchise requires the operator to provide service to any person requesting service in any area where it is "feasible" for the company to provide service.²¹⁶

126. In sum, NATOA argues that it would be inconsistent with the goals of the 1992 Cable Act to permit a cable operator to pass through costs that the operator would have incurred "to maintain a first-class competitive business" even in the absence of any franchise requirements.²¹⁷ As described in its petition for reconsideration of the *Rate Order*, NATOA again suggests that franchise-related costs accorded external treatment should include only new or additional direct monetary costs which are specifically enumerated by a stated dollar amount in a franchise agreement to satisfy franchise requirements imposed by the franchising authority, or specifically attributable to a specific new or additional franchise requirement imposed by the franchising authority. However, such costs should not include normal types of business costs other companies incur in doing business with a jurisdiction, the costs of keeping pace with current technological developments in the cable industry, or the costs of remaining competitive in the marketplace.²¹⁸

127. NCTA disputes NATOA's suggestion as overly narrow and inconsistent with

²¹⁵ NATOA Petition for Reconsideration at 4.

²¹⁶ *Id.* at 4-5.

²¹⁷ *Id.* at 6.

²¹⁸ *Id.* at 6.

our previous analysis of franchise-imposed costs.²¹⁹ NCTA claims that further clarification of our analysis of this issue, as described in the *First Reconsideration Order*, is unnecessary, stating that "[W]hat is and should remain relevant to a determination of whether certain costs are external is whether the services are specifically required in a franchise and whether the costs for providing those services have increased."²²⁰

128. Viacom International Inc. ("Viacom") argues that NATOA's proposal runs counter to our goal, as stated in the *First Reconsideration Order*, that franchising authorities and cable operators work cooperatively to assess the costs and benefits of various franchise requirements.²²¹ According to Viacom, there is no justification for the distinction drawn by NATOA between franchise imposed costs to which the parties assign a specific dollar amount and other such costs for which no such dollar amount is assigned.²²² Viacom also argues that by embracing only "new or additional" costs and burdens, the NATOA proposal appears, allegedly without justification, to apply only to franchise agreements made after enactment of the 1992 Cable Act.²²³

129. Howard & Howard stated that if the Commission is going to clarify what is meant by franchise requirement costs, it should ensure that the clarification defines franchise requirement costs as including a number of different costs that are required by franchise agreements. First, Howard & Howard stated that increases in costs associated with requirements that an operator wire private educational institutions should be included as external cost pass throughs. In addition, it stated that the Commission should clarify that the cost increases related to providing any type of cable services to any public facility or institution should receive external cost treatment. Also, Howard & Howard recommended that if a franchise required an operator to remove aerial facilities and place them underground, the operator should be permitted to pass through such relocation costs to subscribers.²²⁴

130. In reply comments, GTE Service Corporation ("GTE") agrees with NATOA that clarification of this issue is necessary to ensure cable operators do not attempt to claim as external "any cost that may be remotely associated with the requirements that local

²¹⁹ NCTA Opposition at 2-4.

²²⁰ *Id.*

²²¹ Viacom Opposition at 6, quoting *First Reconsideration Order*, 9 FCC Rcd at 1220.

²²² *Id.*

²²³ *Id.*

²²⁴ Howard & Howard at 2-3.

franchise authorities may impose."²²⁵

131. The parties also disagree as to the timing of the pass through of franchise-imposed costs, however they are defined. NATOA argues that the operator should be required to spread such costs evenly throughout the franchise term to prevent the operator "from overestimating increases in such costs in any quarter it files the FCC Form 1210" ²²⁶ NCTA responds that a cable operator should be entitled to recover its costs immediately if the franchise requires the operator to incur those costs all at once.²²⁷

C. Discussion

132. On reconsideration, we believe that operators should be permitted to include increases in franchise requirement costs that the operator would not have incurred in the absence of the franchise requirement. Such increases include both new requirements that the franchising authority imposes and increases in the cost of complying with existing requirements. Our current rules permit external cost treatment for increases in the cost of satisfying franchise requirements for (a) PEG access channels, (b) public, educational, and governmental access programming, and (c) customer service standards and technical standards that exceed federal requirements. In our view, such increased costs would not have been incurred in the absence of a franchise agreement because we believe that the operator would not have chosen to provide such services.

133. We believe that operators also should be permitted to pass through increases in the costs of institutional networks and the provision of video services, voice transmissions and data transmissions to or from governmental institutions and educational institutions, including private schools, to the extent such services are required by the franchise agreement. We believe that such costs should be afforded external cost treatment because we believe that operators generally would not provide such services in the absence of a franchising requirement. Because such costs are largely beyond the control of the cable operator, we believe they should be passed on to subscribers without a cost-of-service showing.

134. In addition, under certain circumstances, we will permit operators to pass through to subscribers the cost of meeting franchise requirements that they remove aerial facilities and place them underground. However, the external cost pass through should be limited to cases where the operator has been required to actually remove cable from utility poles and place the same cable underground. We do not believe that external cost treatment should be afforded in cases where the franchise agreement requires the operator to place new

²²⁵ GTE Reply Comments at 4.

²²⁶ NATOA Comments at 6.

²²⁷ NCTA Opposition at 4.

cable facilities underground because we believe that this is a cost associated with a rebuild or an upgrade of the cable system and we have determined that we will not permit external cost treatment of upgrades or rebuilds.²²⁸ Moreover, costs associated with placing cable underground in these circumstances are costs that the operator could have incurred in absence of the franchise requirement as a result of the upgrade or rebuild.

135. We believe that increased costs resulting from normal maintenance or from a simple expansion of service within the franchise area should not be subject to external treatment. An operator may not pass through the costs associated with expanding the reach of its cable system even if such expansion is contained in the franchise documents. Accordingly, we reject NCTA's suggestion that external cost treatment should be imposed as long as the service is "specifically required" in the franchise agreement. Such a formulation of the rule could encompass costs that the cable operator could have incurred even in the absence of a specific franchise requirement²²⁹ or would be obligated to incur under pre-existing federal standards.²³⁰ We reject NATOA's suggestion to allow only obligations enumerated in a franchise agreement by a specific dollar amount as unduly complicating franchise negotiations. This would require parties to specify the costs of providing certain services or facilities where such costs may not be certain when the contract is negotiated.

136. As for the timing of the pass throughs of these costs, the operator will be required to amortize the cost of franchise imposed capital expenditures over the useful life of the items. We find such treatment appropriate because current subscribers should not be required to pay all costs associated with a service that will benefit future ratepayers as well. Consistent with interim rules governing cost-of-service showings, we find that operators will be permitted to recover an 11.25% rate of return on this investment.

²²⁸ *Rate Order*, 8 FCC Rcd at 5791-92 n.608; *First Reconsideration Order*, 9 FCC Rcd at 1216; *Second Reconsideration Order*, 9 FCC Rcd at 4240-41 n.340. Operators are permitted to recover the costs of significant upgrades to their systems with a streamlined cost-of-service showing. *Cost of Service Order*, 9 FCC Rcd at 4674-76.

²²⁹ For example, a cable system that chooses to offer service in a portion of a franchise area that is not required under the franchise agreement could not pass through the costs of that simple expansion as an external cost related to franchise requirements.

²³⁰ In its petition for reconsideration, the Public Interest Petitioners urge that we permit operators to pass through network upgrade costs, even if the franchise did not require it to perform the upgrade. Public Interest Petitioners Petition for Reconsideration at 15; see also A & E Comments at 19. We will not reconsider this issue at this time, however, because we previously rejected arguments in favor of external cost treatment for network upgrades in both the *Rate Order* and the *Second Reconsideration Order*. In the *Second Reconsideration Order*, we stated that "we will not establish, or further consider in this proceeding external cost treatment for upgrades generally, or for upgrades required by local franchising authorities." *Second Reconsideration Order*, 9 FCC Rcd at 4241 n.340.

V. ADVERTISING OF RATES

A. Background

137. Section 622(c) of the Communications Act provides that cable operators may separately identify each of the following charges on their bills to subscribers: (a) the amount assessed as a franchise fee (as well as the identity of the franchising authority); (b) the amount of the bill assessed to satisfy any franchise agreement imposed on the operator for costs related to PEG channels; and (c) the amount attributable to any charges a governmental authority imposes on the transaction between the operator and the subscriber.²³¹ In the *Rate Order*, we determined that, although operators are permitted to itemize these charges on subscribers' bills, operators are not permitted to separately bill subscribers for such charges.²³² We stated that any bill itemized pursuant to Section 622(c) may require only one payment for the operator's services on the part of a consumer, the total for which must include all fees and costs itemized pursuant to Section 622(c).²³³

138. Consistent with this approach, the *Rate Order* also prohibited cable operators from advertising a rate for cable service that did not include the costs that were itemized pursuant to Section 622(c) of the Communications Act.²³⁴ The Commission reasoned that if operators were not required to advertise the total rate, including itemized costs, it would result in needless confusion for subscribers.²³⁵

²³¹ Section 622(c) of the Communications Act, as amended, 47 U.S.C. § 542(c).

²³² *Rate Order*, 8 FCC Rcd at 5971-5972. We stated that, if we permitted operators to require subscribers to remit separate payments for the items listed in Section 622(c), it would impose an unnecessary burden on subscribers. We also said that listing such charges "below the line" would confuse subscribers as to what is part of their bills. *Id.*

²³³ *Id.* This requirement is consistent with the House Report which states that:

The cable operator shall not identify cost itemized pursuant to section [622(c)] as separate costs over and beyond the amount the cable operator charges a subscriber for cable service. The Committee intends that such costs shall be included as a part of the total amount a cable operator charges a cable subscriber for cable service.

House Report at 86.

²³⁴ *Rate Order*, 8 FCC Rcd at 5972 n.1415.

²³⁵ *Id.*

139. In the *Third Reconsideration Order*, we made an exception to this requirement for cable systems that cover multiple franchise areas and have different franchise fees, different franchise requirement costs, different channel line-ups, or slightly different rate structures. We determined that such systems should be permitted some flexibility in designing region-wide advertising that will reasonably advise potential subscribers of the total rate for cable service. We decided that where a cable system covers multiple franchise areas, the operator may advertise a range of fees or a "fee plus" rate that takes account of variations in the itemized costs throughout the franchise area. We said that under these circumstances, an operator need not indicate the total rate for each individual franchise area. An operator's advertisement might declare, for example, "that basic service is \$14.00 per month plus a franchise fee of \$0.28 to \$0.70, depending on location, or that it is \$14.28 to \$14.70, depending on the location."²³⁶

B. Contentions

140. Local Governments seek reconsideration of our decision to adopt the "fee plus" approach for systems serving multiple franchise areas.²³⁷ Local Governments assert that the fee plus approach violates the intent of Section 622(c) of the Communications Act and is inconsistent with the Commission's subscriber bill itemization rules because it permits operators to advertise by separating the rate for cable service from the franchise fee cost.²³⁸ Local Governments state that they do not question the appropriateness of permitting operators to advertise a range of rates, provided that each rate in the range includes the franchise fee.²³⁹

141. Local Governments argue that the "fee plus" approach would violate the intent of the 1992 Cable Act because the legislative history demonstrates that "it was not the intent of Congress to allow operators to add franchise fees or other Section 622(c) charges to subscribers' bills in addition to regular charges for cable service."²⁴⁰ Local Governments also assert that the "fee plus" approach is inconsistent with the Commission determination in the *Rate Order* that "any bill itemized pursuant to Section 622(c) may require only one payment for the operator's services on the part of a consumer, the total of which must include all fees and costs itemized pursuant to Section 622(c)."²⁴¹

²³⁶ *Third Reconsideration Order*, 9 FCC Rcd at 4368 n.99.

²³⁷ NATOA Petition for Reconsideration at 7-13.

²³⁸ *Id.* at 7.

²³⁹ *Id.* at 7-8.

²⁴⁰ *Id.* at 8-9.

²⁴¹ *Id.* at 10, quoting *Rate Order*, 8 FCC Rcd at 5971-5972.

142. Local Governments also complain that the Commission's "fee plus" example suggests that the Commission misunderstands the amount on which franchising authorities may assess franchise fees pursuant to Section 622(b) of the Communications Act. Local Governments assert that in the example, the Commission effectively treats the franchise fee as a tax on top of the basic rate and that this would give franchising authorities less than they would be entitled to under Section 622(b) of the Communications Act.²⁴²

143. The City of Detroit supports Local Governments' petitions because it believes that the "fee plus" approach will allow operators to advertise their rates in violation of the intent of Section 622(b) of the Communications Act and would suggest that cable operators can itemize their franchise fees in a manner that would deprive franchising authorities of the full 5% of gross annual revenues.²⁴³

144. In response, NCTA argues that the Commission's "fee plus" approach would not confuse potential subscribers about what amount they would have to pay cable operators for their total monthly bill. NCTA states that Local Governments' objection to the "fee plus" approach appears to be "a continuation of their effort to keep cable subscribers in the dark as to what portion of their bill is attributable to the fees paid to the local franchising authority."²⁴⁴

145. Time Warner Entertainment Company ("Time Warner") argues that the subscriber bill itemization requirements in Section 622(c) of the Communications Act do not attempt to control the format or the content of a cable operator's advertisement. According to Time Warner, the purpose of Section 622(c) is to prevent cable operators from separately billing customers for franchise and other governmentally imposed fees. As long as customers are only required to remit one periodic payment for cable service, Time Warner states, cable operators are free to advertise governmental fees separately. Time Warner also argues that advertising is protected commercial speech under the First Amendment and that neither Congress nor the Commission has the authority to regulate the advertiser's freedom of speech under these circumstances. Time Warner also argues that if cable operators were required to advertise separate rate schedules for each community based solely on differences in the franchise fee, system-wide advertising would be virtually impossible and consumer confusion would result.²⁴⁵

C. Discussion

²⁴² *Id.* at 10-12.

²⁴³ Response of City of Detroit at 2-4.

²⁴⁴ NCTA Comments at 4-6.

²⁴⁵ Time Warner Opposition at 3-6.

146. On reconsideration, we continue to believe that cable system operators covering multiple franchise areas that have different franchise fees, franchise costs, channel line-ups, or rate structures should be permitted to use the "fee plus" approach when they advertise their rates. We find that the "fee plus" approach provides operators that cover multiple franchise areas the flexibility to efficiently advertise their services to consumers. We disagree with Local Governments' assertion that the "fee plus" approach violates Section 622(c) of the Communications Act. Section 622(c) permits operators to itemize certain fees imposed by franchise and governmental authorities. While operators are allowed to itemize certain fees on a subscribers bill, Congress intended that cable operators only be permitted to require one payment from subscribers for services. We find that because the "fee plus" approach only addresses how an operator serving multiple franchise areas may advertise services, it is not related to the operator's billing practices and does not, therefore, violate the intent of Section 622(c). Moreover, we believe that the "fee plus" approach is consistent with the spirit of the subscriber bill itemization requirements in Section 622(c) of the 1992 Cable Act and Section 76.985 of the Commission's rules because it permits operators to inform consumers of the amount of franchise fees without confusing them as to the total cost of cable service.

147. We believe that operators should be permitted to advertise their rates using either of the methods described above because both methods of advertising reasonably informs potential subscribers of the true price of cable service. This approach is consistent with the Commission's goal of enhancing industry's flexibility in making business and marketing decisions wherever reasonably possible. Therefore, we affirm our decision to allow cable systems that cover multiple franchise areas to advertise a range of fees or a "fee plus" rate that take account of variations in the itemized costs throughout the franchise area.

148. Although Local Governments' are concerned that the "fee plus" approach may result in a reduction in the amount of franchise fees that franchising authorities may assess, we decline to address this matter in this Order. The Cable Services Bureau has issued a decision regarding the proper assessment of franchise fees,²⁴⁶ and is currently reviewing a number of petitions for reconsideration filed in response to that decision.²⁴⁷

²⁴⁶ United Artists Cable of Baltimore, DA 95-737 (Apr. 6, 1995).

²⁴⁷ See, e.g., Petition for Reconsideration of the City of Baltimore, Maryland, NATOA, the National League of Cities, and the City of New York, New York (May 8, 1995); Petition for Reconsideration of the City of Dallas, Texas, the City of Dubuque, Iowa, the City of Indianapolis, Indiana, the City of Laredo, Texas, Montgomery County, Maryland, the Miami Valley Cable Council, Ohio, the City of St. Louis, Missouri, and the City of Tallahassee, Florida (May 8, 1995). See also Public Notice, *Commission Applies "Permit but Disclose" Ex Parte Rules to Reconsideration of United Artists Cable of Baltimore*, DA 95-1366 (June 19, 1995).

VI. FRANCHISE FEE REFUNDS

A. Background

149. Section 622(b) of the Communications Act provides that a cable operator's franchise fees for any 12-month period shall not exceed 5% of the operator's gross annual revenues. In the *Third Reconsideration Order*, we found that when an operator is required to refund subscribers for overcharges, the franchise fee must be reduced because the refund caused a reduction in the operator's gross annual revenues. We found that where a refund has been ordered, franchising authorities must return to the cable operator the amount of a franchise fee that has been overpaid as a result of the reduction in the operator's gross annual revenues. We stated that the franchise fee overcharge may be returned to the operator by either deducting the amount from future franchise fee payments or by having the franchising authority return it in an immediate lump sum payment.²⁴⁸

B. Contentions

150. NATOA seeks clarification as to whether the franchising authority or the cable operator has the discretion to determine whether franchise fee overpayments will be returned to the operator by an immediate lump sum payment or by deducting the amount from the cable operator's future franchise fee payments. NATOA argues that the Commission should permit franchising authorities to choose the method of returning the overpayment because a private entity should not be permitted to order a governmental entity to take certain actions. In addition, NATOA argues that in determining how franchise fee overpayments are refunded to cable operators, franchising authorities should receive the same discretion that operators have in determining how to implement refunds to subscribers. NATOA states that because operators have the discretion to implement a refund to subscribers by check or as a credit to a customer's bill, franchising authorities should have the discretion to determine whether to refund franchise fee overcharges or to offset overcharges against future franchise fee payments.²⁴⁹

151. In response, NCTA argues that it is the federal government and not a private entity that has established the rules governing the return of overcharges. NCTA states that, once operators have given full refunds or credits to subscribers, it is only fair that operators have the choice of immediately obtaining an up-front, lump payment for the franchise fee overcharge.²⁵⁰

C. Discussion

²⁴⁸ *Third Reconsideration Order*, 9 FCC Rcd at 4354.

²⁴⁹ NATOA Petition/Comments at 14-16.

²⁵⁰ NCTA Comments at 8.

152. On reconsideration, we find that franchising authorities may determine whether a franchise fee overpayment is to be returned to the cable operator in one lump sum payment or by offsetting the overcharges against future franchise fee payments, provided that the overcharges are returned to the operator within a reasonable period of time. We recognize that in most instances, the operator holds franchise fees on behalf of the franchising authority for lump sum payment at the end of an agreed upon period. In those situations, the operator should offset the overpayments against the franchise fees it then holds. In the rare instances where the overpayments are very large, the franchising authority has the discretion to determine a reasonable repayment period plus interest. Because we have already determined that 11.25% is presumptively the cable operator's cost of capital,²⁵¹ we find that the interest rate presumptively should be 11.25%.

153. We agree with NATOA that franchising authorities should have the discretion to determine the means by which overpayments are to be returned to cable operators because it would be inappropriate to permit cable operators to dictate how the franchising authority should recompense operators. Moreover, in certain cases, the franchise fee overpayment may have been spent before it has been determined that an overpayment has been made and the franchising authority may not have the funds to immediately return the overpayment. However, we also believe that operators are entitled to receive interest on any franchise fee overpayments if franchising authorities delay returning overpayments to operators and that, in any case, operators should have overpayments returned within a reasonable period of time. We find that the meaning of "reasonable period of time" is dependent upon the amount of the overcharge and the relationship it bears to a franchising authority's budget. That is, the larger the absolute amount of the overpayment and the larger its amount in relation to a franchising authority's budget, the longer the franchising authority may need either to credit the operator for future franchise fee payments or to make a lump sum payment to the operator. We believe that this approach balances the franchising authority's need to have discretion in determining the means by which overcharges are returned with the operator's need to have such overcharges returned within a reasonable period of time.

VII. REGULATORY REVIEW OF EXISTING RATES

A. Background

154. Section 623(c) of the 1992 Cable Act requires that, upon the receipt of specific complaints regarding a CPST, the Commission must ensure that such rates are not unreasonable.²⁵² Under our rules, we review CPST complaints in the event that a cable operator increases its rates for CPS, provided that such complaints make a minimum

²⁵¹ *Cost-of-Service Order*, 9 FCC Rcd at 4633-4635.

²⁵² 1992 Cable Act § 3(c), 106 Stat. at 1468-69.

showing²⁵³ and are filed with the Commission within 45 days of the date the subscriber receives a bill from the cable operator reflecting the rate increase.²⁵⁴

155. The 1992 Cable Act provided an exception to the general rule that complaints may be filed only against a CPST rate increase. The exception permitted subscribers and franchising authorities to file complaints regarding CPST rates that existed as of the effective date of our rules within 180 days following the implementation of the initial rate regulations on September 1, 1993. Following the expiration of this initial 180 day period on February 28, 1994, complainants were not permitted to challenge rates that were in effect on September 1, 1993.²⁵⁵ Complaints filed after February 28, 1994 were valid only if a cable operator raised its rate and the complainant filed within 45 days from the date the subscriber received a bill.

156. In the *Rate Order*, we determined that for complaints filed no later than February 28, 1994, the operator's refund liability would equal the difference between the disputed rate and the rate determined by the Commission to be not unreasonable under either the benchmark formula or pursuant to a cost-of-service proceeding. We stated that when an operator's initial rate as of September 1, 1993 was not challenged within the 180 day period, i.e., by February 28, 1994, the operator would not face refund liability for its existing rate. Instead, upon the Commission's receipt of a valid complaint filed within 45 days of a rate increase, the refund would be limited to the difference between an operator's disputed rates and its unchallenged rates in existence as of the effective date of our rules.²⁵⁶

157. However, in footnote 907 of the *Rate Order*, we stated that this exception does not apply to prospective rate reductions. We stated that:

[I]f we conclude that an operator's subsequent rate increase is unreasonable (but its existing rate as of the effective date of our rules was not challenged), we will employ our standard procedures for designating a reasonable rate that the cable operator must charge on a prospective basis. Because of the prospective nature of this remedy, Section 623(c)(3) does not preclude designation of a reasonable, prospective rate below the cable operator's existing rate as of the effective date of our rules.²⁵⁷

²⁵³ 47 C.F.R. § 76.954 (1993).

²⁵⁴ 47 C.F.R. § 76.953(b) (1993).

²⁵⁵ Communications Act, § 623(c)(3); 47 U.S.C. § 543(c)(3).

²⁵⁶ *Rate Order*, 8 FCC Rcd at 5866.

²⁵⁷ 8 FCC Rcd 5866 n.907. Moreover, the Cable Services Bureau clarified that for CPST complaints filed after February 28, 1994, "the Commission will consider the total rate and not just the most recent rate increase." See News Release, Min. No. 4173 (rel).

B. Contentions

158. On reconsideration, Public Interest Petitioners (Dr. Everett Parker and Mr. Henry Geller, Esq.) and United Video argue that the Commission's rules improperly permit rate changes to trigger challenges to an operator's entire rate in violation of the 1992 Cable Act.²⁵⁸ They and other petitioners also argue that the current complaint process deters operators from adding new programming since rate increases may lead to a subscriber rate complaint which would subject the operator to a review of the entire CPST rate.²⁵⁹

159. Public Interest Petitioners also argue that the complaint process violates the 1992 Cable Act and legislative history since the reexamination of the entire rate for CPSTs would nullify the time limits imposed by Congress.²⁶⁰ Public Interest Petitioners and United Video recommend establishing a complaint process that reviews only the increase in CPST rates and not the entire rates.²⁶¹

160. NATOA asserts that the Commission has correctly interpreted the statute, noting that Section 623(c)(3) of the Communications, which established the window for challenging existing rates, does not limit the Commission's authority to establish rules that permit a regulatory review of the overall reasonableness of rates in the context of a rate increase.²⁶²

C. Discussion

161. On our own motion,²⁶³ we have decided to end regulatory review of the

February 9, 1994).

²⁵⁸ Public Interest Petitioners Petition at 13; United Video Petition at 9.

²⁵⁹ United Video Petition for reconsideration at 9; Public Interest Petitioners Petition for Reconsideration at 12-13; Providence Journal Response to Fifth NPRM at 19; Viacom Comments on Fifth NPRM at 18; Court TV Comments at 9, 16; Discovery Comments at 10-11; NCTA Comments on Fifth NPRM at 10.

²⁶⁰ Public Interest Petitioners Petition for Reconsideration at 13.

²⁶¹ *Id.*; United Video Petition at 9.

²⁶² NATOA Opposition to Petitions for Reconsideration at 7-8.

²⁶³ Although Public Interest Petitioners filed in response to the *Second Reconsideration Order*, this matter was not addressed there. Thus, we act on our own motion rather than respond to its Petition. See note 1, *supra*.

operator's entire rate structure when we receive future CPST rate complaints.²⁶⁴ Operators that have never been subject to CPST rate regulation will not face Commission review of their entire rate structure if a complaint is filed after the effective date of these rules. Complaints filed after the effective date of these rules on subsequent CPST rate changes must be filed with the Commission within 45 days of the date subscribers receive a bill reflecting the operator's next CPST rate increase, and will result in Commission review of only the amount of the rate increase complained about.

162. Although Commission review will be so limited, in order to meet its burden of showing that its CPST rates are not unreasonable,²⁶⁵ the operator nevertheless may have to provide the Commission with details about its previous increases where no earlier filing provides those details. For example, an operator that attempts to use the new Going Forward method for channel additions²⁶⁶ in its current filing may need to demonstrate that its current increase, in conjunction with its previous rate increases, does not exceed the operator's cap. As another example, if no complaint was filed for the operator's relevant earlier rate adjustments, an operator that adjusts its rates using the annual rate adjustment method²⁶⁷ should provide the projections on which the operator's previous rates were based so that the Commission can review the operator's true up in its current filing.

163. We are eliminating review of an operator's entire rate structure because we find that continuing this policy creates an uncertain business environment for cable operators that have not had their CPSTs subject to rate regulation. We are concerned about this because an uncertain business environment may generally discourage investment, without which operators may lack the resources to upgrade their networks, add new programming services, and provide new innovative services.

164. We find that, if no rate complaint is filed prior to the effective date of these rules, the operator's initial CPST rates under regulation are not unreasonable. In our view, subscribers and franchising authorities have had ample opportunity to file a complaint that would result in Commission review of operators' entire rate structure. It has been nearly two years since subscribers and franchising authorities first had the opportunity to complain about their CPST rates. Since September 1, 1993, subscribers had an initial 180 day period to complain about initial CPST rates. If they missed the opportunity to complain during this initial 180 day period, they could have complained about any subsequent rate increase and that would have triggered a review of the operator's entire rate structure. We believe that if

²⁶⁴ In resolving a complaint pending on the effective date of these rules, we will review an operator's entire rate structure in addition to any rate increases.

²⁶⁵ 47 C.F.R. § 76.956(b).

²⁶⁶ 47 C.F.R. § 76.922(e)(3).

²⁶⁷ See Section II, *supra*.

subscribers and the franchising authority have not filed a CPST rate complaint, it indicates a level of satisfaction with their current rates that would not exist if they believed CPST rates were unreasonable. We also believe that the Commission can fulfill its responsibility to ensure that CPST rates are not unreasonable when only reviewing rate changes.

VIII. REGULATORY FLEXIBILITY ACT ANALYSIS

A. Final Analysis for the Thirteenth Reconsideration Order

165. Pursuant to the Regulatory Flexibility Act of 1980, 5 U.S.C. §§ 601-612, the Commission's final analysis with respect to the *Thirteenth Order on Reconsideration* is as follows:

166. Need and purpose of this action. The Commission, in compliance with § 3 of the Cable Television Consumer Protection and Competition Act of 1992, 47 U.S.C. § 543 (1992), pertaining to rate regulation, adopts revised rules and procedures intended to ensure that cable services are offered at reasonable rates with minimum regulatory and administrative burdens on cable entities.

167. Summary of issues raised by the public in response to the Initial Regulatory Flexibility Analysis. There were no comments submitted in response to the Initial Regulatory Flexibility Analysis. The Chief Counsel for Advocacy of the United States Small Business Administration (SBA) filed comments in the original rulemaking order. The Commission addressed the concerns raised by the Office of Advocacy in the *Rate Order*. The SBA also filed reply comments in response to the *Fifth Notice*. The Commission addressed those comments in the Fifth Report and Order.

168. Significant alternatives considered and rejected. Petitioners representing cable interests and franchising authorities submitted several alternatives aimed at minimizing administrative burdens. In this proceeding, the Commission has attempted to accommodate the concerns expressed by these parties. For example, the revised rules permitting the expedited pass through of certain external costs are designed to reduce administrative burdens on industry. In addition, the revised rules permitting operators to recover the full portion of previously incurred increases in external costs are designed to maintain and enhance incentives for cable operators to achieve efficiency cost savings and reduce administrative burdens on both industry and regulators. Finally, the *Order* further reduces burdens by clarifying rules concerning the advertising of rates, the refunds of franchise fees, and the costs related to franchise requirements.

IX. PAPERWORK REDUCTION ACT

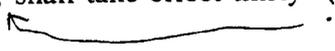
169. The requirements adopted herein have been analyzed with respect to the Paperwork Reduction Act of 1980 and found to impose a new or modified information

collection requirement on the public. Implementation of any new or modified requirement will be subject to approval by the Office of Management and Budget as prescribed by the Act.

X. ORDERING CLAUSES

170. Accordingly, IT IS ORDERED that, pursuant to Sections 4(i), 4(j), 303 (r), 612, 622(c) and 623 of the Communications Act of 1934, as amended, 47 U.S.C. §§ 154(i), 154(j), 303(r), 532, 542(c) and 543, the rules, requirements and policies discussed in this Thirteenth Order on Reconsideration, ARE ADOPTED and Part 76 of the Commission's rules, 47 C.F.R. Part 76, IS AMENDED as set forth below.

171. IT IS FURTHER ORDERED that the Secretary shall send a copy of this Report and Order to the Chief Counsel for Advocacy of the Small Business Administration in accordance with paragraph 603(a) of the Regulatory Flexibility Act. Pub. L. No. 96-354, 94 Stat. 1164, 5 U.S.C. §§ 601 *et seq.* (1981).

172. IT IS FURTHER ORDERED that the requirements and regulations established in this decision shall become effective thirty (30) days after publication in the Federal Register, except that the new reporting requirements in Section __, shall take effect thirty (30) days after approval by the Office of Management and Budget. 

FEDERAL COMMUNICATIONS COMMISSION

William F. Caton
Acting Secretary

**SEPARATE STATEMENT OF
COMMISSIONER RACHELLE B. CHONG**

Re: Implementation of Sections of the Cable Television Consumer Protection and Competition Act of 1992: Rate Regulation (MM Docket No. 92-266), Thirteenth Order on Reconsideration

Under the Commission's existing cable rate regulation rules, cable operators often seek to implement multiple rate adjustments within the same year. This frequent rate churn causes confusion and frustration for subscribers, and increases costs and administrative burdens for cable operators and regulators. The new rules adopted in this Order on Reconsideration are designed to address these concerns by encouraging cable operators to seek rate changes less frequently, on an annual basis. Minimizing the number of rate adjustments within a particular twelve month period should benefit consumers, cable operators, local franchising authorities and the FCC. I therefore support this decision, even though of necessity it adds another layer to the Commission's already abundant cable rate regulation rules.

As I have noted previously, regulation of cable television rates "is a complex, burdensome and resource-intensive proposition for cable operators, local franchising authorities and the Commission."¹ Cable rate regulation is pervasive and, in some instances, may be overly intrusive. It involves detailed intervention by the government in a myriad of pricing and marketing decisions by private businesses, as this reconsideration order amply illustrates. I eagerly await the day when the rise of competition and the discipline of market forces enables cable rate regulation to go the way of the dinosaurs -- so that the FCC is not called upon to issue orders like this one. In the meantime, the Commission should seek ways to reduce the substantial burdens associated with cable rate regulation, consistent with existing law.

¹ *Video Dialtone Reconsideration Order*, 10 FCC Rcd 244, 399 (1994) (Separate Statement of Commissioner Rachelle B. Chong).