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Rate regulation and the Cable Television Consumer Protection and Competition Act of 1992

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In October, 1992, Congress responded to consumer complaints about their cable rates and services by passing the Cable Television Consumer Protection and Competition Act of 1992. The numerous provisions of the new act were the subject of two, day-long workshops held in Portland and Orono last fall that were targeted to municipal officials. The workshops were jointly sponsored by the Margaret Chase Smith Center for Public Policy, the Maine Municipal Association and the Community Television Network of Portland. The following articles were excerpted from those presentations in an effort to both communicate and explain the important changes wrought by the new cable act. In the first article, Lisa Gelb and Frederick Ellrod offer an overview of the recent changes effecting cable rate regulation. Portland attorney Barbara Krause follows with a discussion of the new consumer protection and consumer services provisions of the 1992 Cable Act. Finally, Portland attorney George Burns describes two of his experiences with local cable franchise renewals.

Cable rate regulation provisions

by Lisa S. Gelb and Frederick E. Ellrod III

Background

Until 1984, there was no federal legislation that specifically was directed at regulation of cable television. Rate regulation was governed by state and local law. Cable operators claimed that this local regulation was unduly restrictive, and inhibited the natural growth of the industry. In 1984, partly in response to the cable industry's complaints, Congress passed the Cable Communications Policy Act of 1984. That act set guidelines for many aspects of cable franchising.

The 1984 Act, as implemented by the Federal Communications Commission (FCC), resulted in rate deregulation in nearly every community. However, most communities were (and are) served by only a single operator: Cable is, in effect, a local monopoly, and few subscribers had a choice of service providers. The result was poor service and high rates.

In an effort to cure the abuses cable companies were able to perpetrate due to their monopoly power, Congress passed the Cable Television Consumer Protection and Competition Act of 1992. This Act was intended to stimulate competition in multichannel video services, but, in the absence of competition, to reduce prices to the levels that would prevail if cable operators did face competition.

In April, 1993, the FCC adopted rules governing cable rate regulation. According to the FCC, those rules would reduce rates by ten percent, on average, and would lower rates for as many as seventy-five percent of all cable subscribers throughout the country. The FCC estimated that its rules would lead to \$1 billion in rate reductions.

The new rules took effect on September 1, 1993. Many communities took immediate action to regulate rates, and these communities are now beginning to receive rate information from their local cable companies. However, as of this writing, it does not appear that most subscribers have actually seen reductions in their monthly bills. On the contrary, many have actually seen rate increases. The impact of the FCC's rules remains uncertain.

What can be regulated

Under the new federal law, rates can be regulated only if the franchise area is not subject to "effective competition." The 1992 Cable Act deems effective competition to exist where (1) the cable operator provides service to fewer than thirty percent of the households in the area to which it has offered service; (2) one or more alternative providers (such as another cable company) offer service to at least fifty percent of area households, and at least fifteen percent of area households take service from the nondominant cable provider; or (3) the franchising authority operates a cable system that offers service to at least fifty percent of area households. Unless one of these three conditions exists, the operator is subject to rate regulation. Since none of these "effective competition" tests are satisfied in most communities, most cable operators are now subject to rate regulation.

Under the 1992 Cable Act, basic and non-basic services and related equipment are subject to regulation, except where the programming is offered on a per-channel or per-program basis, as with HBO or a pay-per-view sporting event. Per-channel and per-program offerings are not subject to rate regulation. The basic service tier generally includes television broadcast signals and public, educational and governmental ("PEG") channels. The operator may also include other programming on the basic tier if it chooses to do so.

The non-basic tiers, referred to as "cable programming service" in the 1992 Act but often called "expanded basic," include any programming offered on a tier other than the basic tier. An operator may offer more than one basic tier. It may also offer services individually, on an "à la carte" basis, and such non-tier services are not subject to regulation. For this reason, many operators have recently taken key channels out of existing tiers and begun to offer them both as a separate package and on an à la carte basis. Operators argue that those services are not subject to regulation because they are offered on a per channel basis. However, they have set the prices in such a way that subscribers are unlikely to choose the individual services rather than the entire package. The FCC is currently investigating whether such tactics may constitute an evasion of the rate regulation rules.

Who can regulate

The 1992 law act sets up a two-level regulatory regime. Basic rates can be regulated by the franchising authority (in Maine, this is generally the municipality), or in some instances by the FCC. Expanded basic rates may be regulated by the FCC, but only if a franchising authority or an individual subscriber takes action by filing a complaint form with the FCC.

Initiating rate regulation

There is no deadline for initiating basic rate regulation. However, there may be some advantage to beginning to regulate promptly. In April, 1993, the FCC ordered a freeze on rates for regulated

services. During the freeze, average subscriber bills for regulated services may not increase, although prices and tiers may be adjusted in such a way as not to affect average subscriber bills. The rate freeze is now scheduled to expire on February 15. After the freeze ends, cable operators may raise rates in communities that have not already begun regulation. Delay may reduce the amount of allowable refunds, depending on how the FCC's rules affect rates in a particular community. Thus, while a franchising authority that begins to regulate after February 15 may order refunds for overcharges, the amount of refunds may be reduced as a result of the delay.

In addition, a franchising authority may order refunds only back to September 1, 1993 (when rate regulation began) or for up to one year, whichever is less. Therefore, subscribers in communities that delay regulation until after September 1, 1994 may lose out on potential refunds.

Some operators have urged franchising authorities not to initiate regulation at all, but to instead enter into a private rate agreement with the operator. The FCC seems to have concluded that agreements not to regulate are invalid and unenforceable. Thus, a community wishing to afford local subscribers maximum rate protection should avoid rate agreements and instead set rates by conforming to the FCC's rules.

Basic rate regulation

Basic rates will not be regulated unless the franchising authority files a certification form (Form 328) with the FCC. Form 328 is a one-page, relatively straightforward form seeking certification from the FCC to regulate basic rates. The franchising authority certifies that it has the legal authority and resources to regulate basic rates, and that the franchise area does not face effective competition. The FCC presumes that effective competition does not exist, and the franchising authority may so certify as long as it does not have any evidence or reason to believe that the operator faces effective competition.

If a franchising authority cannot handle rate regulation, it may ask the FCC to regulate basic rates on behalf of the community. For example, if the franchising authority does not have the financial resources necessary to regulate, it may ask the FCC to step in. In that case, however, the FCC requires the franchising authority to show why it cannot use franchise fees to cover the costs of regulation. In general, the FCC appears reluctant to assume authority over basic rates, and views local governments as the primary regulators in that area.

If the franchising authority does not hear from the FCC after filing Form 328, the certification is deemed granted after 30 days have passed from the date the form was filed. The franchising authority then has 130 days to adopt regulations, consistent with FCC rules, that will govern rate regulation proceedings. If there is a problem with Form 328, (for example, it was not filled out correctly), the FCC will so notify the franchising authority and provide it with an opportunity to correct the filing.

The most significant task for the franchising authority in initiating basic regulations is adopting local rules to govern basic rate regulation proceedings. State and local requirements (such as public notice requirements) must be taken into account in adopting these regulations. Federal law also sets out several requirements. For example, the regulations may provide an opportunity to consider the views of interested parties, whether by public hearing or through written comments. The regulations should also include provisions governing disclosure of any confidential

information the operator may provide. In addition, the federal regulations set out specific timing requirements that need to be followed.

Once the franchising authority is certified and has adopted its regulations, it must notify the operator that it is subject to basic rate regulation. Basic rate regulation is considered to begin on the date such notice is given.

After the franchising authority has notified the operator that it will regulate basic rates, the operator has 30 days to file FCC Form 393 and to justify its rate under the FCC's rate regulations. An operator has the option of supporting its rates in either of two ways. Under the "benchmark method," the operator merely submits a completed Form 393, which is designed to show whether or not the operator's rates are below the ceilings the FCC has established based on the national average of rates in allegedly competitive systems. On the other hand, if the operator wants to charge a rate higher than that allowed under the benchmark system, the operator can elect to use the "cost of service" method. Under this method, the operator must justify its rates on the basis of its costs plus a reasonable profit on its investment. The FCC plans to issue detailed rules for evaluating a cost of service showing, but had not done so as of December 1, 1993. Until those rules are issued, cost of service filings must be reviewed under general utility ratemaking standards.

The franchising authority does not have the right, according to the FCC, to require a cost of service showing. However, if the operator does submit a cost of service showing, the franchising authority (or the FCC, if it is the regulatory body) can examine the evidence presented and set an appropriate rate, even if it is below the benchmark.

After the operator has filed its Form 393, the franchising authority has 30 days to act. It may approve the rate proposed by the operator, establish a different rate, or issue an order stating that it needs additional time to review the rate. In most cases, the franchising authority will issue a written order explaining the reasons for its decision.

If the franchising authority has issued an order seeking more time to review the rates, it must issue a second order within 90 days after the first order (or within 150 days, if the operator has presented a cost of service showing). If at the end of that period the franchising authority still needs additional time to determine whether the rates are unreasonable, it must notify the operator that the rate may go into effect, subject to refund, and that the operator must keep records enabling it to issue refunds to subscribers once the final rate decision is made.

Expanded basic rate regulation

A specific form, Form 329, is used by franchising authorities and subscribers to complain about rates that are other than basic tier rates. This completed form is sent to the FCC, and a copy is sent to the cable company that is the subject of the complaint. The FCC will take no action unless it receives a Form 329. If a subscriber files a Form 329, he or she must also send a copy of the complaint to the franchising authority. Subscribers may also call the franchising authority for assistance in filling out the form.

The FCC began to accept these forms on September 1, 1993. Any complaints regarding rates in effect on that date must be filed by February 28, 1994. For subsequent rate increases, the

subscriber has 45 days after receiving a bill that contains the rate increase in which to file a complaint. Because there is a 30-day advance notice requirement for any such rate changes, subscribers should have a total of 75 days after they are notified of a rate increase in which to file a complaint.

Once the complaint is filed, the burden is on the operator to justify its rates by submitting Form 393, the same form used to justify basic rates. As with basic rates, the operator must either show that the rate is reasonable according to the benchmark method, or establish that its costs justify a rate above the benchmark. The operator has 30 days to respond after a subscriber or franchising authority sends a copy of Form 329 to the operator. There is no specific time within which the FCC has to issue its decision. But refunds will date back to the date a valid rate complaint was filed; thus, delay in filing a rate complaint will result in lost refunds for expanded basic.

Future rate regulation

Once the initial rate has been set by the process just described, rates may only increase by the amount of inflation (based on the GNP Price Index) and by the amount to which certain "external costs" have increased above the rate of inflation. The external costs recognized by the FCC are (1) programming costs; (2) retransmission consent fees charged by broadcasters, after the first year; (3) franchise fees; and (4) other franchise requirements. At present, system upgrades and similar capital costs are not considered to be external costs. However, the FCC is currently reconsidering that determination. In general, after rate regulation has begun, these external costs may be added onto the rate the operator can charge, to the extent that the increase in external costs exceeds the rate of inflation. However, the operator also must take into account any decreases in external costs, which will decrease the allowable rate the operator can charge.

Conclusions

We have presented an overview of the regulatory scheme established by Congress and the FCC under the Cable Act of 1992. The real impact of the new federal regulatory scheme on subscriber rates is not yet clear. Thus, it is impossible at this point to determine whether the effort and expense of rate regulation outweighs the benefit to subscribers. Moreover, both costs and benefits are likely to vary from one community to the next. In addition, the FCC's rules are a work-in-progress. Further rulemakings and legal challenges to the FCC's rules are pending. What is clear in the early days of this regulatory scheme is that cable rates are of great concern to the public and that the ball is in the franchising authority's court to take action to keep rates as reasonable as possible.

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