

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

In the Matter of	)	
	)	
TELE-MEDIA COMPANY	)	
of NORTH CAROLINA	)	CSB-A-0159
	)	
Appeal of Local Rate Order of	)	
Alamance County, North Carolina CUID NC0386	)	
	)	
	)	

**MEMORANDUM OPINION AND ORDER**

**Adopted: February 23, 2000**

**Released: February 25, 2000**

By the Deputy Chief, Cable Services Bureau:

**I. INTRODUCTION**

1. Tele-Media of North Carolina, operator of the cable system serving Alamance County, North Carolina, (“Tele-Media”) filed an appeal of the local rate order adopted by the Board of Commissioners of Alamance County, North Carolina, (the “Board”) on May 1, 1995.<sup>1</sup> The Board filed an opposition to the appeal.<sup>2</sup> The cable operator supplemented its appeal, seeking treatment as a small cable operator.

**II. BACKGROUND**

2. Under the Commission’s rules, rate orders issued by local franchising authorities may be appealed to the Commission.<sup>3</sup> In ruling on an appeal of a local rate order, the Commission will not conduct a *de novo* review, but will sustain the franchising authority’s decision provided there is a reasonable basis for that decision, and will reverse a franchising authority’s decision only if the franchising authority unreasonably applied the Commission’s rules in its local rate order.<sup>4</sup> If the Commission reverses a franchising authority’s decision, it will not substitute its own decision but will

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<sup>1</sup>Petition for Review of Local Rate Order and Request for a Stay of the Rate Order of Tele-Media Company of North Carolina (June 7, 1995). Because of our action herein, the request for stay included in the appeal is dismissed as moot.

<sup>2</sup> Opposition to Petition for Review and to Request for Stay of the Local Rate Order, Alamance County, North Carolina (June 28, 1995).

<sup>3</sup> 47 C.F.R. § 76.944.

<sup>4</sup> See *Implementation of Sections of the Cable Television Consumer Protection and Competition Act of 1992, Rate Regulation*, 8 FCC Rcd 5631, 5731 (1993) (“*Rate Order*”); See also *Implementation of Sections of the Cable Television Consumer Protection and Competition Act of 1992, Rate Regulation, Third Order on Reconsideration*, 9 FCC Rcd 4316, 4346 (1994) (“*Third Reconsideration*”).

remand the issue to the franchising authority with instructions to resolve the case consistent with the Commission decision on appeal.<sup>5</sup>

3. An operator seeking to justify its existing or proposed rates for the basic service tier, equipment, or installation bears the burden of demonstrating that the rates conform with our rules.<sup>6</sup> In determining whether the operator's rates conform with our rules, a franchising authority may direct the operator to provide supporting information.<sup>7</sup> After reviewing an operator's rate forms and any other additional information submitted, the franchising authority may approve the operator's rates or issue a written decision explaining why the operator's rates are not reasonable.<sup>8</sup> If the franchising authority determines that the operator's rates exceed the maximum permitted rate as determined by the Commission's rules, it may prescribe a rate different from the proposed rate or order refunds, provided that it explains why the operator's rate or rates are unreasonable and any prescribed rate is reasonable.

4. Cable operators may justify their basic service tier ("BST") rates using either the benchmark methodology established in the *Rate Order* or a cost-of-service showing based on the cable operator's actual cost and revenue data.<sup>9</sup> When a cable operator elects to make a cost-of-service showing, the Commission's rules permit local authorities to prescribe any rate that is justified by the cost showing, including a rate lower than the benchmark or operator's current rate level.<sup>10</sup> The Commission adopted interim cost-of-service rules effective May 15, 1994 and final cost-of-service rules effective March 9, 1996.<sup>11</sup> Operators with cases pending under the interim rules when the final cost rules became effective could elect to have their cases decided under the final rules. Cases already decided by a final decision of a franchising authority when the final cost rules became effective are to be reviewed in accordance with the rules in effect when the decision was made.

5. The significant administrative and compliance costs associated with cost-of-service regulation impose heavy burdens on regulators and regulated entities.<sup>12</sup> To offer small cable companies administrative relief from rate regulation, the Commission amended the definition of small cable companies and small cable systems and introduced a simplified form of small system relief in *the Small*

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<sup>5</sup> *Rate Order*, 8 FCC Rcd at 5732.

<sup>6</sup> 47 C.F.R. § 76.937(a).

<sup>7</sup> See *Rate Order* at 5718-19; *Third Reconsideration*, 9 FCC Rcd at 4348.

<sup>8</sup> 47 C.F.R. § 76.936; see *Ultracom of Marple, Inc.*, 10 FCC Rcd 6640, 6641-42 (CSB 1995).

<sup>9</sup> *Rate Order* at 5755 para. 187; *Implementation of Sections of the Cable Television Consumer Protection and Competition Act of 1992: Rate Regulation, Second Report and Order, First Order on Reconsideration, and Further Notice of Proposed Rulemaking*, 11 FCC Rcd 2220, 2223-24 (1996) ("*Final Cost Order*").

<sup>10</sup> *Rate Order* at 5800 para. 272.

<sup>11</sup> *Implementation of Sections of the Cable Television Consumer Protection and Competition Act of 1992: Rate Regulation, Report and Order and Further Notice of Proposed Rulemaking*, 9 FCC Rcd 4527 ("*Cost Order*") (interim rules); *Final Cost Order*, 11 FCC Rcd 2220 (final rules).

<sup>12</sup> See *Rate Order* at 5755-56.

*System Order*.<sup>13</sup> Cable systems serving 15,000 or fewer subscribers, and owned by a company having 400,000 or fewer subscribers, may elect to use the new small cable system rate mechanism in lieu of other Commission rate processes.<sup>14</sup> In adopting these definitions, the Commission took particular note of Congressional intent to ease the regulatory burdens imposed on small cable systems, franchising authorities, and the Commission by rate regulation while protecting cable subscribers from unreasonable rates and enhancing small cable systems' ability to attract capital and achieve the goals set by Congress in the Statement of Policy contained in the Cable Act of 1992.<sup>15</sup>

6. The *Small System Order* stated that in order to qualify for the modified form of relief, systems and companies must meet the modified size standards as of either the effective date of that order or on the date thereafter when a request for relief under those revised provisions is filed.<sup>16</sup> Franchising authorities were directed to permit systems to use the small system cost-of-service approach in any proceeding that was pending when the *Small Systems Order* was released, using data that was accurate when the rates were charged. To make the small system cost-of-service showing in a pending case, the system was required to show that it met the new definitions of a small system owned by a small cable company when the *Small Systems Order* was released and when the disputed rates were in effect.<sup>17</sup> Further, in the interest of administrative finality, the *Small System Order* stated that the revised form of regulation would not affect the validity of a final rate decision made by a franchising authority before the release date of that item. If such a decision is appealed to the Commission, the decision is to be reviewed in accordance with the rules in effect at the time the rates were charged and the decision was made.<sup>18</sup>

### III. DISCUSSION

7. Tele-Media's system serves 1869 subscribers in Alamance County, North Carolina, and 1433 subscribers in Mebane, North Carolina. It is affiliated with a larger Tele-Media organization which provides cable services to approximately 300,000 subscribers in the United States by means of a family of companies under common management that does not involve any parent company.<sup>19</sup> In response to a Board notification of intent to regulate its cable service rates, Tele-Media filed a series of Commission cable rate regulation forms with the Board, including an FCC Form 1220 submitted on April 12, 1995 in support of its BST rates under the Commission's cost of service regulations.<sup>20</sup> The Board accepted a revised Form 1220 on April 17, 1995 and adopted the rate order that is the subject of Tele-Media's appeal

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<sup>13</sup> *Implementation of Sections of the Cable Television Consumer Protection and Competition Act of 1992: Rate Regulation, Sixth Report and Order and Eleventh Order on Reconsideration*, 10 FCC Rcd 7393 (1995) ("*Small System Order*").

<sup>14</sup> Operators attempting to justify their rates through small system relief use FCC Form 1230.

<sup>15</sup> See *Small System Order*, 10 FCC Rcd at 7406-7412.

<sup>16</sup> See *id.* at 7413.

<sup>17</sup> *Id.* at 7428 para. 74.

<sup>18</sup> See *id.* at 7428.

<sup>19</sup> Tele-Media Petition, at 3.

<sup>20</sup> Tele-Media had separately entered into a settlement agreement with respect to its rates for service in Mebane, North Carolina.

on May 1, 1995. These Forms 1220 sought approval of a \$14.54 BST rate in place of the \$13.14 rate then in effect. The Board's rate order made certain adjustments to cost of service data submitted with the Forms 1220 described below, prescribed a \$9.09 BST rate, and ordered refunds dating back to a year from the date of the order.

8. Complaints regarding Tele-Media's rates for its cable programming services tier ("CPST") in Alamance County, Mebane and four other communities were considered in *Tele-Media Company of North Carolina*, 11 FCC Rcd 13196 (CSB 1996) (the "*CPST Order*").<sup>21</sup> The *CPST Order* granted a Tele-Media request for small system relief under the *Small System Order*. The *CPST Order* also reviewed FCC Form 1230s Tele-Media filed with the Commission on December 15, 1995, seeking to justify its CPST rates through the simplified small system cost of service procedures under the *Small System Order*. Based on a review of Tele-Media's FCC Form 1230 filings, the *CPST Order* denied the pending CPST complaints, found that Tele-Media's CPST actual rates per channel in the referenced franchise areas did not exceed its per subscriber, per channel monthly programming costs, that the Maximum Permitted Rates did not exceed \$1.24, and concluded, therefore, that Tele-Media's CPST rates were not unreasonable.

9. Tele-Media's appeal asserts that the Board's rate order erred by disallowing claimed start-up period losses and intangible assets in the computation of the revenue requirement, by an inappropriate application of the Commission's prescribed 11.25% rate of return in place of Tele-Media's claimed average 12.34% cost of outstanding debt, and by failing to allow management fees Tele-Media paid to an affiliated company. Tele-Media also claims that a fair cost of service proceeding was denied because the Board inadequately considered Tele-Media's rebuttals of the presumptions that are integral to the Commission's cost of service cable rate regulations. The Board disallowed start-up period losses and intangible assets and adjusted the rate of return figure largely by application of presumptions and limitations adopted in the *Cost Order* as an integral part of the cost of service regulatory scheme. The Board defended against Tele-Media's attack on the rate order largely by defending its application of these presumptions and restrictions. However, the Commission noted in the *Small System Order* that the presumptions and restrictions applied by the Board in this proceeding should not be applied to cable systems fitting within the small cable system definitions adopted in that order. In particular, the Commission stated that the presumption that it is unreasonable to include in the rate base start-up costs that exceed the first two years of operating expenses will not apply, nor will intangibles such as acquisition costs be presumptively excluded from the net rate base. The Commission also stated that at minimum the permitted rate of return for small cable systems shall be equal to the operator's actual cost of debt as set forth in loan agreements with third parties.<sup>22</sup> A strong presumption of reasonableness will apply where an operator seeks to establish rates no higher than \$1.24 per channel.

10. Tele-Media fits within the definition of a small cable system as defined in the *Small System Order*. As noted earlier, the system serves approximately 3302 subscribers, 1869 of which are in Alamance County, and the entire Tele-Media organization provides cable service under common management to approximately 300,000 subscribers. Indeed, as noted earlier, the *CPST Order* determined that Tele-Media fitted within the 15,000 system subscriber - 400,000 total company subscriber limits adopted in the *Small System Order*. Thus, Tele-Media represents a prime

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<sup>21</sup>On June 9, 1998, Tele-Media filed a Supplement to Basic Service Tier Rate Appeal calling attention to the *CPST Order*.

<sup>22</sup>See *Small System Order*, 10 FCC Rcd at 7422-7423.

example of a small cable system contemplated for relief by the *Small System Order* from excessive cost of service regulatory burdens.

11. In its Supplement, Tele-Media argues that the *CPST Order*, which granted Tele-Media relief for the CPST tier pursuant to the *Small System Order*, should resolve the issues here. The local rate order preceded the *Small System Order*, however, and we are required by the *Small System Order* to review it in accordance with the rules in effect at the time the rates were charged and the decision was made. Nevertheless, if the local rate order must be remanded to the franchising authority, the local rate order should no longer be considered a “final rate decision” within the meaning of paragraph 74 of the *Small System Order*, and the operator should be able to avail itself of the relief provided in that order if it otherwise meets the criteria for doing so. Allowing small cable operators to avail themselves of the relief provided in the *Small System Order* on reconsideration of remanded local rate orders is fully consistent with the Congressional goals referenced in that order.

12. Turning to the merits of the Board’s rate order under review here, we find it necessary to address only Tele-Media’s contentions concerning the disallowance of certain intangible assets in the computation of the revenue requirement, which alone is sufficient to require a remand of the Board’s rate order. The Board disallowed amounts claimed on Line 12 of Tele-Media’s Form 1220 for Organizational and Franchise Costs, on the grounds that the cable operator failed to provide a satisfactory response to an information request for justification of these claimed amounts. The Board disregarded Tele-Media’s explanation that the amounts represented legitimate business assets purchased in arms-length transactions - namely, part of the purchase price paid for the cable system. The Board argues here that Tele-Media made no effort to establish how it obtained the figures nor explained how the figures may be distinguished from goodwill, which it translates to excess acquisition costs, and therefore failed to meet its burden of justifying the inclusion of the figures in the regulated rate base.

13. The Commission determined in the *Cost Order* that a cable operator should not expect to recover monopolistic profits represented by excess acquisition costs through its ratebase. However, intangibles Tele-Media included as franchise acquisition costs are subject to only a presumption that they will be excluded from the ratebase. We have previously concluded that a local franchising authority should use the asset valuation approach followed in *Telemedia Company of Western Connecticut ("Telemedia")*<sup>23</sup> and *Falcon Cablevision*.<sup>24</sup> The *Telemedia* and *Falcon Cablevision* approach achieves a fair balance between the operator's interests for reasonable recovery of investment and the local franchising authority's interest in setting reasonable cable rates. Since the facts presented in this appeal are substantially similar to those prior cost-of-service cases, the County should have used such valuation approach here.<sup>25</sup> In both *Telemedia* and *Falcon Cablevision*, we found the local franchising authority's

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<sup>23</sup>11 FCC Rcd 3161 (CSB 1996).

<sup>24</sup>11 FCC Rcd 10511 (CSB 1996).

<sup>25</sup>See *Falcon Cable Systems*, 13 FCC Rcd 4425, 4432 (CSB (1998), for a detailed discussion of that valuation approach which we need not repeat here. The operators in *Telemedia* and *Falcon Cablevision*, as did Tele-Media, acquired their systems prior to adoption of rate regulations. Thus, under the *Cost Order*, the acquisition price is presumed to include expectations of monopoly profits. The *Small System Order* determined that such presumption does not apply in the case of small cable systems. See *Small System Order*, 10 FCC Rcd at 7422.

The Board improperly disallowed all amounts listed in Line 12, including that for the BST and the CPST. The Board has no jurisdiction over CPST rates, and this disallowance of the gross amount from the revenue (continued....)

rejection of intangibles to be unreasonable under the interim cost-of-service rules. Constrained as we are by the *Small System Order* to apply precedent established under the *Cost Order* to this “final rate decision” of the Board, we have reached a similar conclusion here and find the Board’s rate order unreasonable and remand it for further consideration.

14. On remand we direct the Board to provide Tele-Media with an opportunity to support its BST and regulated equipment and installation rates for the period covered by the Form 1220 in issue here by means of Form 1230 and the modified cost of service rate regulations adopted in the *Small System Order*. If Tele-Media avails itself of this opportunity, the Board’s review must adhere to the provisions of the *Small System Order*.

15. There remains only the issue of Tele-Media’s assertion that the Board improperly disallowed management fees paid to an affiliated management company. Tele-Media’s petition will be denied with respect to this issue. In the *Cost Order*, the Commission promulgated rules for valuing transaction between cable operators and affiliated companies. Those rules require that affiliated transaction be valued at the “prevailing company price,” if the provider has sold the same kind of asset or services to a substantial number of third parties at a generally available price. If similar transactions with third parties have not occurred, then the lower of cost or fair market value must be used with respect to assets and the services provider’s costs must be used with respect to the provision of services.<sup>26</sup> The Commission revisited and reaffirmed the appropriateness of these rules in the *Final Cost Order*.<sup>27</sup> We agree with the Board that Tele-Media failed to provide any information tending to establish that the fees paid to the affiliated management company satisfy the requirements of the Commission’s affiliated transaction rules for valuing any management services that may be related to those fees.

#### IV. ORDERING CLAUSES

16. For the foregoing reasons, **IT IS ORDERED**, pursuant to authority delegated by Section 0.321 of the Commission's rules, that the Petition for Review of the local rate order of the County of Alamance, North Carolina (CSB-A-0386), filed by Tele-Media Company of North Carolina on June 7, 1995 **IS GRANTED IN PART AND DENIED IN PART** as indicated in this Memorandum Opinion and Order, and the Resolution Regarding Regulation of Rates Charged for Basic Cable Service and Related Equipment adopted by the County of Alamance, North Carolina, on May 1, 1995 **IS REMANDED** for further consideration consistent with this Memorandum Opinion and Order.

17. **IT IS FURTHER ORDERED** that Tele-Media Company of North Carolina’s request for stay **IS DISMISSED**.

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requirement for BST rates is therefore unreasonable and sufficient reason of itself for remand of the Board’s rate order.

<sup>26</sup>See *Cost Order*, 9 FCC Rcd at 4658-68.

<sup>27</sup>See *Final Cost Order*, 11 FCC Rcd 2220, 2277-79 (1996).

18. **IT IS FURTHER ORDERED** that the County of Alamance shall not enforce the remanded Resolution pending further action by the County on these matters.

FEDERAL COMMUNICATIONS COMMISSION

William H. Johnson  
Deputy Chief, Cable Services Bureau