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

In the matter of	)	
	)	
TCI of Pennsylvania, Inc.	)	
	)	
Appeal of Local Rate Order of the City of Pittsburgh, Pennsylvania	)	File No. CSB-A-0438
	)	

MEMORANDUM OPINION AND ORDER

Adopted: May 21, 2004 **Released: May 26, 2004**

By the Deputy Chief, Policy Division, Media Bureau:

I. INTRODUCTION

1. TCI of Pennsylvania, Inc. ("TCI"), the franchised cable operator serving the City of Pittsburgh ("City"), Pennsylvania has appealed a local rate order adopted by the City on May 30, 1997 ("order"),[1] which rejected proposed basic service tier ("BST") and equipment rates as unreasonable. The City rejected TCI's Form 1240 for BST rates because TCI used an unapproved starting Maximum Permitted Rate ("MPR"), failed to provide proper or complete documentation for reported programming cost increases, and inserted a line item surcharge for the federal regulatory fee paid to the Commission. The City also rejected TCI's Form 1205 for equipment and installation rates because TCI failed to justify the cost allocation factor used to calculate hourly service charges ("HSC"), used a five year depreciation schedule for converters, and sought recovery of unfunded deferred taxes. TCI also claims that the order was deficient because the City did not provide revised versions of the rate forms to TCI. The City filed an opposition to the appeal to which TCI replied. TCI also filed a request for emergency stay of the City's rate order, which the City opposed. TCI's stay request is rendered moot by this order and is dismissed. Based upon our review of the record, we grant in part and deny in part TCI's appeal.

II. BACKGROUND

2. The Communications Act provides that, where effective competition is absent, cable rates for the BST are subject to regulation by franchising authorities.[2] Rates for the BST should not exceed rates that would be charged by systems facing effective competition, as determined in accordance with Commission regulations for setting rates.[3]

3. Rate orders issued by franchising authorities may be appealed to the Commission pursuant to Commission rules.[4] In ruling on appeals of local rate orders, the Commission will not

[1] Identified locally as Resolution No. 280.

[2] 47 U.S.C. § 543(a)(2).

[3] 47 U.S.C. § 543(b)(1); 47 C.F.R. § 76.922.

[4] 47 U.S.C. § 543(b)(5)(B); 47 C.F.R. § 76.944.

conduct a *de novo* review, but instead will sustain the franchising authority's decision as long as a reasonable basis for that decision exists.[5] The Commission will reverse a franchising authority's rate decision only if it determines that the franchising authority acted unreasonably in applying the Commission's rules. 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.

4. An operator that wants to increase its BST rate has the burden of demonstrating that the increase is in conformance with the Commission's rules.[6] In determining whether the operator's rates conform with our rules, a franchising authority may direct the operator to provide supporting information.[7] After reviewing an operator's rate forms and any other additional information submitted, the franchising authority may approve the operator's rate increases or issue a written decision explaining why the operator's rates are not reasonable.[8] If the franchising authority determines that the operator's proposed rates exceed the MPR as determined by the Commission's rules, it may prescribe a rate different from the proposed rate and order refunds, provided that it explains why the operator's rate or rates are unreasonable and the prescribed rate is reasonable.[9]

5. On March 1, 1997, TCI filed FCC Forms 1240 and 1205 with the City. On April 14, 1997, the City sent TCI an extensive Letter of Inquiry ("LOI") requesting clarification and additional information regarding the filed forms. TCI delivered a written reply to the LOI on April 24, 1997. On May 30, 1997, the City issued its order denying the proposed rate increases.

III. DISCUSSION

A. Form 1240

1. Starting MPR

6. TCI entered the 1996 Form 1240 MPR of $11.0029 on Line A1 of the 1997 Form 1240 as the starting MPR even though the City had rejected it in its 1996 rate order ("1996 order").[10] The 1996 order rejected TCI's proposed MPR and approved a MPR of $10.23. The City's current order concluded that TCI's starting MPR on Line A1 of the 1997 Form 1240 should have been the $10.23 MPR approved by the City in the 1996 order.

7. TCI states that it appealed the City's 1996 order rejecting its $10.23 MPR and requested a stay to prevent the City's 1996 order from becoming effective.[11] TCI argues that had it used the City approved MPR instead of its 1996 Form 1240 MPR, it "would lack the legal and economic ability to assess customers a surcharge in the future to recover 'lost revenue' that was not even claimed in this

[5] Implementation of Sections of the Cable Television Consumer Protection and Competition Act, Report and Order and Further Notice of Proposed Rulemaking, 8 FCC Rcd 5631 (1993) ("*Rate Order*"); Third Reconsideration Order, 9 FCC Rcd 4316, 4346 (1994).

[6] 47 C.F.R. § 76.937(a).

[7] *Rate Order* at 5718.

[8] 47 C.F.R. § 76.936; *see* Ultracom of Marple Inc., 10 FCC Rcd 6640, 6641-42 (1995).

[9] *See* Century Cable of Southern California, 11 FCC Rcd 501 (1995); TCI of Iowa, Inc., 13 FCC Rcd 12020 (1998).

[10] Appeal at 6-7.

[11] *Id.*

year's filing."[12]

8. In opposition, the City asserts that the instructions for the Form 1240, Module A, Line A1, advise the operator to "enter the maximum rate which you are currently permitted to charge for regulated programming services according to Commission regulations."[13] The City argues that under section 76.933(g)[14] of the Commission's regulations, operators must obtain prior approval for rate increases and a proposed rate may go into effect only if the franchising authority expressly approves it or fails to act within the requisite period. The City asserts that the only time that an operator can use a starting rate that varies from the one approved by the franchising authority is when the Commission has stayed the franchising authority's decision. But in this instance, the City's order was not stayed and remained valid and in effect.

9. In this case, the rate TCI was "permitted to charge" when TCI filed its 1997 Form 1240 was the $10.23 MPR established by the City in its 1996 order[15] which reviewed the 1996 Form 1240. Although TCI appealed the City's earlier order, the order was not stayed by the Commission.[16] In *Mickelson Media, Inc., d/b/a Adelphia Cable Communications*,[17] we stated that absent a stay, operators are expected to comply with valid rate orders when issued. Neither TCI's appeal of the order nor its request for a stay renders the order unenforceable. While TCI will not realize revenue represented by the difference between the rates approved by the City and the rates TCI had originally proposed, TCI will be able to recover costs ultimately approved after remand of its appeal through the true-up and accrued cost procedures. We deny TCI's appeal with respect to the starting rate MPR. The correct MPR for purposes of filling in Line A1 of the Form 1240 is the MPR the operator is currently permitted to charge.[18]

2. Affiliated/Non-Affiliated Programming

10. TCI's 1997 Form 1240 filing sought a rate increase based on increased costs for six programming services: Faith and Values ("F&V"), Pittsburgh Cable News Channel ("PCNC"), Mind Extension University ("MEU"), WTBS, Sneak, and Prevue Guide ("Prevue"). F&V and PCNC are purchased from affiliated programmers. The City rejected all of the claimed cost increases. TCI challenges the City's rejection of its Form 1240 programming costs for all six programming services. TCI alleges that it provided all BST programming service information, including adequate documentation of the relevant portions of the F&V and PCNC contracts that set forth the programming rates. TCI further asserts that the programming rates are final rates and it does not receive any offsetting rebates from either F&V or PCNC. TCI also alleges that it provided the proper documentation for MEU, although the contracting cable party is not identified, and for F&V and WTBS even though the contracts identified Satellite Services, Inc. ("SSI") rather than TCI as the contracting purchaser. TCI states that SSI is a wholly-owned subsidiary of TCI, which contracts with and pays national programming vendors for all TCI systems, and these facts were explained last year in the rate

[12] *Id.* at 7.

[13] Opposition at 5.

[14] 47 U.S.C. § 76.933(g).

[15] The rate order was issued in the form of a letter dated May 30, 1996 from Deborah S. Miskovich, Superintendent, Bureau of Cable Communications, City of Pittsburgh, to Shawn M. McGorry, General Manager, TCI of Pennsylvania, Inc.

[16] *See* TCI of Pennsylvania, Inc. ("TCI of Pennsylvania"), 19 FCC Rcd 312 (2004).

[17] 15 FCC Rcd 13311, 13314 (2000).

[18] Falcon First, Inc., 15 FCC Rcd 6209, 6210 (2000). *See also* Form 1240, Instructions at 12, "Instructions for FCC Form 1240 Annual Updating of Maximum Permitted Rates for Regulated Cable Services.

making process. Finally, TCI also disputes the City's claim that its supporting documentation -- monthly invoices -- for Sneak and Prevue was insufficient because there were no contract agreements.

11. In opposition, the City asserts that TCI did not establish the showing required by section 76.922(f)(6) of the Commission's rules for external costs.[19] The City alleges that TCI failed to satisfy its burden by not furnishing information specifying how much F&V and PCNC charge non-TCI affiliated operators, and whether the price charged to TCI for each channel is the prevailing price of the program supplier or the fair market value. The City argues that TCI had two opportunities, the initial filing and the LOI response, to submit proper information, but failed to satisfy its burden of proof by failing to provide the correct information initially, and then subsequently failing to fully respond to the LOI. The City asserts that portion's of TCI's supporting documentation was so substantially redacted that the City concluded that relevant information to the analysis may have been concealed.[20] For instance, the City alleges that it could not determine whether TCI received any quality discounts or rebates and the terms of payments. The City also alleges that the information for F&V and WTBS was incomplete because the contract agreements reflected SSI as the contracting party rather than TCI. The City argues that TCI is required by section 76.939 of the Commission's rules to comply with its information request and is prohibited from submitting information that omits relevant material information.[21] Finally, the City argues that it relied upon the best information available to it at the time the order was issued and objects to TCI's attempt to submit information on appeal that the City requested and that was readily available to TCI before the City rendered its order. Notwithstanding the fact that the requested price increases are small, the City argues that it was unable to determine whether the rates on which the programming increases are based have been artificially inflated.

12. We will first address the issues raised with respect to the affiliated programming provided by F&V and PCNC, and then address those issues raised with respect to the non-affiliated programming of MEU, WTBS, Sneak, and Prevue.

a. Affiliated Programming

13. TCI cited cost increases for F&V and PCNC to justify its rate increases in its Form 1240. Section 76.922(f)(6) of the Commission's rules provides that an operator may adjust its rates to reflect increases in the costs of affiliated programming, provided that the programming rates charged to the operator by the affiliated programmer reflect either (1) the prevailing company prices offered by the programmer to unaffiliated entities or (2) the fair market value of the programming.[22] TCI's original filing failed to so indicate. Because TCI failed to submit the relevant information on F&V and PCNC, the City requested the information through an LOI. The LOI requested that TCI provide information concerning the programming prices charged by F&V and PCNC to TCI and to unaffiliated cable operators so that the City could determine whether TCI satisfied the requirements of section 76.922(f)(6). TCI responded by providing the amount of the increases for F&V and PCNC and relevant portions of the F&V and PCNC contracts in support of its costs. The documents were heavily redacted to protect confidential information. TCI did not indicate whether the price increases reflected the prevailing company price offered to unaffiliated programmers or the fair market price. TCI did indicate that "with respect to the information that you requested from other cable operators, TCI-P does not keep information regarding other cable operators, including the services that are carried on their respective systems."[23] TCI claimed that information provided by it to the City in connection with the submission of

[19] 47 C.F.R. § 76.922(f)(6).

[20] Opposition at 13.

[21] *Id*. at 12-13; 47 C.F.R. § 76.939.

[22] 47 C.F.R. § 76.922(f)(6).

[23] See LOI Response to Request and Exhibits 3-1 and 3-2.

the 1996 Form 1240 was responsive to the LOI regarding the 1997 Form 1240. The City reviewed the F&V and PCNC contracts, but concluded that the non-redacted portions did not contain enough information to allow the City to determine either the prevailing prices offered to unaffiliated entities or the fair market value of the programming.[24]

14. We addressed this same issue in TCI's appeal of the City's 1996 order in *TCI of Pennsylvania.*[25] As we indicated in *TCI of Pennsylvania,* the burden is on TCI to prove that its existing or proposed rates for the BST comply with the requisite laws and regulations.[26] The City is not required to obtain the necessary information from sources other than TCI. TCI had ample notice and opportunity to supply the City with responsive information before the City's record-closing date. Furthermore, TCI is obligated to provide any information that is reasonably necessary to support its proposed rates, including proprietary or confidential information if requested by the local franchising authority as long as the operator is provided a justification for the information requested.[27] Because TCI failed to provide information necessary for the City to complete its evaluation of the programming costs TCI seeks to recover pursuant to section 76.922(f)(6), we find that TCI failed to meet its burden of proof with respect to its claimed programming costs for F&V and PCNC.[28] We deny TCI's appeal with respect to the affiliated programming cost justifications provided for F&V and PCNC.

b. Non-affiliated Programming

1. True Up Period

MEU

15. TCI claimed $201,841.36 in True-Up Period programming costs for MEU, Sneak, and Prevue. A "true-up" adjustment is an adjustment or correction of projected cost increases estimated in the prior year's Form 1240. The City rejected the MEU programming costs in the true-up adjustment because the contract that TCI provided "fails to identify the parties to the business arrangements reflected or even any relevance to the applicant in the captioned matter."[29] The City questioned whether the contract provided applied to the Pittsburgh system. TCI does not specifically address the MEU contract excerpt in its appeal. After the City had adopted, but not yet completed, its rate order, TCI, on its own initiative, supplied invoice documentation that shows TCI as the payor of the MEU programming costs.[30] TCI does not explain why it did not provide this information when it responded to the LOI. TCI dismisses as unreasonable the City's presumption that TCI might submit a contract between MEU and another operator.

16. The City's concern with TCI's omission is rational since TCI did not explain in its LOI response why the name of the purchasing party was redacted. The identity of the purchaser here is not a matter to be accorded confidential treatment since the purchasing party is presumed to be the cable operator whose rates are at issue. TCI's invoice submission, which was submitted after the close of the

[24] Appeal Attachment A, Superintendent's Recommended Decision at 2.

[25] 19 FCC Rcd 312, 315-316.

[26] 19 FCC Rcd at 316. *See also*, 47 C.F.R. § 76.937.

[27] 19 FCC Rcd at 316. *See also*, 47 C.F.R. § 76.938.

[28] *See* 47 C.F.R. § 76.922(f)(6).

[29] Appeal Attachment A, Superintendent's Recommended Decision at 3.

[30] See Appeal Attachment D, Letter from Sharon M. McCarthy, Director of Business Operations, TCI of Pennsylvania, Inc., to Deborah S. Miskovich, Director, City of Pittsburgh Department of General Services dated May 9, 1997.

record, shows TCI as the purchasing party and confirms that it was the purchaser of services. There is a presumption that the information provided by a cable operator in written statements and in response to inquiries from local franchising authorities is truthful.[31] The City could have asked TCI to explain why the name of the purchaser was redacted and could have asked TCI to clarify that it was the purchaser. But it appears to have done neither. While TCI should not have redacted its own identity in the document, the City should not have summarily rejected the programming costs indicated thereon. We conclude that the City acted unreasonably. We grant TCI's appeal with respect to the MEU programming costs.

Sneak and Prevue

17. The City rejected TCI's costs for Sneak and Prevue just as it had the year before because TCI failed to provide copies of its programming contracts. The LOI requested copies of programming contracts and TCI's LOI response did not explain that TCI had no written contracts with Sneak or Prevue. The sheet listing Sneak and Prevue costs indicates that the contractual basis is "Flat Fee/Invoiced."[32] TCI explains in its appeal petition that there are no contract agreements for Sneak or Prevue and that, for each month of service, TCI pays a flat fee equal to the amount shown on the invoices it provided to the City. As we concluded in *TCI of Pennsylvania*,[33] TCI adequately established its costs by providing the monthly invoices which serve as documentary evidence of TCI's programming costs for Sneak and Prevue. We reject the City's conclusion that because there are no written contracts, the City will recognize no costs. We conclude that the City acted unreasonably. We grant TCI's appeal with respect to the Sneak and Prevue programming costs.

2. Projected Period

MEU

18. TCI estimated $416,500.20 in programming costs for MEU and WTBS for the projected period. The Commission's rules provide that an operator may adjust its annual rates based on projected period costs to reflect inflation and changes in external costs and the number of regulated channels that are projected for the subsequent 12 months following the date of the operator's scheduled rate adjustment.[34] The Commission's rules provide that "in order that rates be adjusted for projections in external costs, the operator must demonstrate that such projections are reasonably certain and reasonably quantifiable."[35] The City determined that TCI did not adequately justify its programming cost increases because the MEU contract excerpt TCI provided redacted the identity of the purchasing party and did not include costs for 1998, part of which falls within the projected period. The cost entry for 1998 is relevant to the question of whether TCI supported its projected cost increases TCI includes in its rates. As we stated above with respect to the true-up period, TCI should not have redacted its identity and its costs for 1998. But the City should not have summarily rejected all of TCI's costs. Clearly some costs were incurred. We grant the appeal with respect to MEU projected costs. In addition, on remand, TCI should provide to the City the necessary information for that part of the 1998 calendar year that falls within the projected period.

WTBS

[31] 47 C.F.R. § 76.939.

[32] Appeal Exhibit 4-4.

[33] 19 FCC Rcd at 318.

[34] 47 C.F.R. § 76.922(e)(2).

[35] 47 C.F.R. § 76.922(e)(2)(ii)(A).

19. The City rejected the WTBS programming costs in the projected adjustment because the contract that TCI provided shows SSI as the contracting party and did not explain its connection to SSI in the record below. TCI argues that at this stage in the regulatory process, the City knows its relationship with SSI because it was explained in TCI's appeal of the 1996 Form 1240. In *TCI of Pennsylvania*, we concluded that the City should not have rejected TCI's programming costs on the ground that SSI was identified as the contracting party rather than TCI.[36] In this instance, the City does have actual knowledge of the relationship between SSI and TCI from the 1996 rate proceeding. TCI provided credible evidence that it did incur programming costs. We find that the City's exclusion of these costs was unreasonable and grant the appeal with respect to WTBS costs.

Sneak and Prevue

20. The City rejected the projected costs for Sneak and Prevue because TCI based its justification on invoices for a one month period in 1996. As we discussed previously with regard to MEU's projected costs, rates may be adjusted for projections in external costs provided that, the operator can demonstrate that such projections are "reasonably certain and reasonably quantifiable."[37] In addition, as we stated above with respect to the true-up period, TCI had no written contracts with Sneak and Prevue and the monthly invoices are sufficient evidentiary information to establish TCI's costs. Also, in this case, the projected costs for Sneak and Prevue programming are equal to the incurred costs for that programming as set forth in the one-month invoices. These costs, therefore, appear to be reasonably certain and reasonably quantifiable. The City's rejection of these costs was unreasonable. We grant the appeal with respect to the Sneak and Prevue projected costs.

3. Federal Regulatory Fee

21. The City rejected TCI's recovery of the Commission's regulatory fee after concluding that TCI had improperly added the fee to the total subscriber bill, which allegedly resulted in a double recovery. On appeal, TCI argues that there is no double recovery because TCI deducted the regulatory fee from the BST rate prior to separately itemizing the fee on customer bills. Thus, the amount billed customers as a separately itemized regulatory fee entry is matched by a subtraction from the rate identified on the bill for the BST. TCI maintains that it is permitted to itemize and collect the regulatory fee as an addition to the total charges for BST service. TCI states that the BST rate and the regulatory fee did not exceed the City-prescribed MPR during the relevant period.[38]

22. In opposition, the City argues that under section 76.985[39] of the Commission's rules, the maximum monthly charge per subscriber for BST programming is the total of a permitted per channel charge multiplied by the number of channels on the BST, plus a charge for franchise fees.[40] The City asserts that a cable operator is not allowed to add any additional amounts to this total. Moreover, Form 1240, Worksheet 7, Line 708, provides a mechanism for passing through the regulatory fee to subscribers as part of the form calculations. The City states that TCI filed an Amended 1996 Form 1240 dated March 1, 1996, which proposed an operator selected rate ("OSR") of $10.19, but subsequently submitted a cover letter dated April 29, 1996, which proposed an OSR of $10.15.[41] The City therefore assumed that the letter rather than the 1996 Amended Form 1240 represented the correct OSR since it

[36] 19 FCC Rcd 312, 317 (2004).

[37] *Supra* para. 18; *See also*, 47 C.F.R. § 76.922(e)(2)(ii)(A).

[38] Appeal at 7; Reply at 4-5.

[39] 47 C.F.R. § 76.985.

[40] Opposition at 9.

[41] *Id*. at 9-10.

was the most recent communication. Under the City's interpretation of section 76.985, TCI could not add the regulatory fee to the OSR.[42]

23. In reply, TCI argues that the City has changed its position from accusing TCI of double-collecting the regulatory fee in the order to arguing on appeal that TCI charged an OSR of $10.19, which included $.04 for the regulatory fee instead of the OSR of $10.15. TCI asserts that the City's confusion about the OSR does not change the fact that TCI was entitled to collect a total of $10.19 from its BST customers. TCI states that the City's 1996 order concluded that TCI's MPR was $10.23 and that its $10.15 BST rate was acceptable because it was less than the City approved MPR.[43] TCI argues that the combined BST rate and the regulatory fee is only $10.19, which is still $.04 below the MPR set by the City. Accordingly, the City has no basis to object to the $10.19 charge since it is obligated to accept any rate up to the MPR of $10.23.

24. Our rules allow cable operators to separately itemize the Commission's regulatory fee on subscriber bills, provided that the charge identified on the subscriber bill as the total charge for cable service includes all such itemized fees and costs.[44] The subscriber bills TCI has attached to its appeal and the subscriber bill the City attaches to its opposition show a proper itemization of the regulatory fee. A total charge is shown below all of the itemized charges and the total shown includes all of the itemized charges, and the sum of the itemized charges for BST service and the regulatory fee do not exceed the MPR during the period at issue in the rate order.[45] We grant TCI's appeal on this issue.

B. Form 1205

25. TCI appeals the City's rejection of: 1) the cost allocation factor used to calculate its HSC and various equipment and installation charges; 2) TCI's five year depreciation schedule for converters; and 3) recovery of unfunded deferred taxes. The City concluded that TCI failed to 1) support the cost allocation factor used to calculate its HSC; 2) support a five year depreciation schedule for converters; and 3) explain how amortization of deferred tax is a proper expense on an accrual basis.

1. Hourly Service Charge

26. The City's order rejected TCI's entry of 47.03% as the cost allocation factor for the HSC and replaced it with the 33.44% figure from TCI's 1996 Form 1205 after concluding that TCI did not adequately explain how it arrived at the 47.03% figure used on the Form 1205, "Worksheet for Calculating Permitted Equipment and Installation Charges ("HSC Worksheet"), Step A, Line 4: Customer Equipment and Installation Percentage.[46]

27. TCI argues that the shift in the cost allocation factor from 33.44% in its 1996 local filing to 47.03% in its 1997 national aggregated filing is attributable to a wide array of factors, including both

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[42] Id. at 10-11.

[43] Reply at 4.

[44] 47 C.F.R. § 76.985(b); 47 C.F.R. § 76.985(a)(3).

[45] After the order was issued, however, TCI began charging subscribers a rate in excess of the MPR prescribed in the order. *See* Appeal Attachment F (subscriber bill dated June 6, 1997). Before the order was issued, TCI billed BST subscribers at a rate that was less than the MPR. During this period, TCI billed subscribers $10.15 for BST service. TCI added to that amount a regulatory fee of $.04, as well as charges for other services, equipment, taxes, and franchise fee. The sum of the BST charge and the regulatory fee was $10.19. The MPR was $10.23, as prescribed by the City in its 1996 order. Appeal at 7, n.7; Appeal Attachment F (sample bills); Reply at 4; Opposition Exhibit 10 (sample bill).

[46] Appeal Attachment C at 2-3.

the national aggregation process and an increase in costly customer-related activities. TCI states that the City cannot reject TCI's figures simply because they represent a shift from the previous year and states further that such a shift is expected in the initial switch to nationally aggregated figures.[47] TCI provided the City with its Statistical Analysis Report explaining how it derived its national equipment basket based on a careful study of 40 scientifically selected systems. TCI argues that the City offers no criticism of that report, nor did it seek any additional support. TCI separately tallies its total installation and maintenance costs and its customer installation and maintenance costs and only then does it derive the percentage entry by comparing the two existing tallies.

28. In opposition, the City argues that TCI's explanation was inadequate and it was forced to rely upon the best information then available to it, which was the 1996 cost allocation factor.[48] The City states that TCI has admitted its failure to follow the step-by-step approach required by the Form 1205.[49] The City states that TCI's Statistical Analysis Report is irrelevant because the report primarily addresses issues found at Step A of the Worksheet for Calculating Permitted Equipment and Installation Charges and does not address TCI's failure to use the "step-by-step" approach required by the Form 1205.[50]

29. In reply, TCI argues that it used the same methodology in compiling the previous year's entry, which the City accepted. Moreover, there is nothing improper with TCI's method of calculating the HSC.[51]

30. Sections 76.923(c)(1) and (3) of our rules provide that a cable operator may aggregate equipment and installation costs on a franchise, system, regional, or company level.[52] In addition, when submitting its equipment and installation costs based on average charges, the cable operator must provide a general description of the averaging methodology employed and a justification that its averaging methodology produces reasonable rates.[53] In *TCI of Richardson, Inc.*, we stated that the magnitude of an increase may be a reason to closely examine supporting information, but the magnitude of the rate increase alone is not determinative of its reasonableness.[54] We further stated that local franchising authorities could reasonably require clarifying or substantiating information.[55]

31. TCI's Form 1205 did not inform the City that TCI used actual costs in Step A, Line 5, instead of estimated costs derived from the cost allocation factor. In its response to the City's LOI, however, TCI clarified that it used actual costs in Step A, Line 5, and it provided a copy of its statistical analysis in support of the reported costs. TCI should have notified the City that additional information was available. The City dismissed the cost information TCI did provide as irrelevant to its evaluation of TCI's HSC. The City's rejection and recalculation of the HSC seems to be premised on the view that an operator should not be permitted to use actual costs in Step A, Line 5, to derive the HSC. This premise is incorrect.[56] The City

[47] *Id.* at 8.

[48] Opposition at 20-21.

[49] *Id.* at 22.

[50] *Id.*

[51] Reply at 5.

[52] In the Matter of Time Warner Cable, 18 FCC Rcd 738, 742 (2003).

[53] *Id.*; *See also* 47 C.F.R. § 76.923 (c) (1) and (3).

[54] 14 FCC Rcd 11,700, 11710 (1999), *Petition for Reconsideration granted in part and denied in part.*

[55] *Id*. at 11709.

[56] Time Warner Cable, 18 FCC Rcd 738, 742 (2003).

must accept TCI's HSC calculation if it finds that the evidentiary support for the costs and other data used to derive the HSC is adequate. Because the City did not give due consideration to the adequacy of TCI's support for the costs reported at Step A, Line 5, we remand this issue to the City so that it can evaluate TCI's cost support and seek any additional information it deems necessary.[57]

2. Depreciation

32. Another issue raised by TCI involves Schedule C of Form 1205, which is used to compute annually the cost-based permitted charges for leased customer premises equipment offered in connection with regulated service. The current provision for depreciation (Line J) is one of the factors used to compute the costs. The City rejected TCI's five-year depreciation schedule for converters and recalculated TCI's converter rates using a ten-year depreciation schedule.[58] The City had concluded that the useful life of converters is ten years.[59] In support of its finding, the City cited our decision in *Media General Cable of Fredericksburg ("Media General*"),[60] where we rejected an operator's change from a 10-year depreciation schedule for converters to a 30-year depreciation schedule.

33. TCI argues that the City erroneously changed the depreciation schedule for converters from five years to ten years, just as it did in the 1996 rate order. TCI asserts that five years is the useful life used company-wide to depreciate converters, both before and after equipment rates became subject to regulation. The five-year depreciation is used in TCI's general ledger and audited financial statements. Thus, the five year depreciation figure is consistent with Commission regulations. TCI claims that the City's treatment of converter depreciation is in direct conflict with the Commission's recent ruling in *Tele-Media Company of Western Connecticut*.[61] In *Tele-Media*, the Commission overruled a local franchising authority order that rejected the operator's proposed five year depreciable life in favor of seven years. The Commission concluded that the operator's depreciation life was within the ranges of standard industry practice and should have been considered reasonable by the local franchising authority.

34. Form 1205 requires operators to use "financial data from the company's general ledger and subsidiary records maintained in accordance with generally accepted accounting principles" ("GAAP").[62] GAAP does not prescribe useful lives for specific assets but instead provides guidelines for determining useful life.[63] As we concluded in *TCI of Pennsylvania*,[64] the City erred in relying on our ruling in *Media General* to reject TCI's converter rates. Our finding in *Media General* does not mean that a converter depreciation schedule of less than ten years is inappropriate. We merely concluded that ten years, at that time, reasonably approximated the industry-standard useful life of converters, and that 30 years did not. We did not, however, consider the reasonableness of depreciation schedules shorter than ten years. Subsequent to *Media General*, we did consider a depreciation schedule of less than ten

[57] Id.

[58] Order at 4.

[59] *Id.*

[60] 10 FCC Rcd 9390 (1995).

[61] 11 FCC Rcd 3161, 3163-3164 (1996).

[62] Form 1205 Instructions at 3, "General Instructions."

[63] See Implementation of Sections of the Cable Television Consumer Protection and Competition Act of 1992: Rate Regulation and Adoption of a Uniform Accounting System for Provision of Regulated Cable Service, MM Docket No. 93-215 and CS Docket No. 94-28, Second Report and Order, First Order on Reconsideration, and Further Notice of Proposed Rulemaking ("Second Report and Order"), 11 FCC Rcd 2220, 2259 (1996).

[64] 19 FCC Rcd 312, 322-323 (2004).

years and held that the franchising authority erred when it rejected the operator's five-year depreciation schedule for converters in favor of a seven-year depreciation schedule.[65] We conclude that the City's rejection of TCI's depreciation schedule for converters does not comport with Commission rules and therefore is unreasonable. We grant TCI's appeal on the depreciation period.

3. Unfunded Deferred Taxes

35. In computing its rates for converters on Schedule C, TCI included in Line J, "Depreciation Expense," an amount representing the amortization of "unfunded deferred taxes."[66] The City rejected this entry on the grounds that Commission rules do not permit operators to claim such an expense. TCI asserts that the City's action was unreasonable because the Commission has recognized that operators are entitled to recover unfunded deferred taxes. For the reasons explained below, we find that the City interpreted Commission rules correctly and acted reasonably in rejecting TCI's unfunded deferred tax expense.

36. Form 1205 requires an operator to reduce its ratebase by the amount of any deferred taxes it accrues from the accelerated depreciation of equipment.[67] Deferred income taxes represent the tax benefit enjoyed by regulated entities that depreciate rate base assets on an accelerated basis for tax purposes, but that establish rates based on the regulatory presumption that rate base assets are depreciated on a straight-line basis. Straight-line depreciation results in a longer depreciation schedule than does an accelerated depreciation method. When rates are calculated using straight-line depreciation, the presumed tax liability for regulatory purposes exceeds the actual tax liability that results from the operator's use of accelerated depreciation for tax purposes.[68] Eventually, the operator's use of a shorter depreciation schedule for tax purposes than for regulatory purposes will have the reverse effect, and the operator's actual tax liability will exceed the tax liability that would result from the longer depreciation schedule used for regulatory purposes. The initial "savings" that results from the use of a shorter depreciation schedule for tax purposes than for regulatory purposes is referred to as deferred taxes because the tax liability is deferred to a later date. Cable rates are calculated as if the operator were subject to the tax liability that would result from the use of a straight-line depreciation schedule. As a result, the operator using straight-line asset depreciation for regulatory purposes and accelerated depreciation for tax purposes receives revenues from subscribers today for tax liability it will not incur until a later date. In the early years, this discrepancy in depreciation methodologies will result in an over-collection of revenues the operator needs to pay its current tax liability. These excess revenues are viewed as subscriber-provided funds, which are available to the operator at no cost to fund the future payment of its deferred taxes.[69] The Form 1205 addresses the over-recovery of revenues by requiring

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[65] *See* Tele-Media Company of Western Connecticut, 11 FCC Rcd 3161, 3163-64 (1996) (rejecting the local franchising authority's alternative depreciation schedule because it did not consider industry practices before developing its depreciation schedule), *petition for reconsideration dismissed*, 13 FCC Rcd 17,756 (1998).

[66] The Form 1205 does not include a line for unfunded deferred taxes.

[67] *See* Implementation of Sections of the Cable Television Consumer Protection and Competition Act of 1992: Rate Regulation and Adoption of a Uniform Accounting System for Provision of Regulated Cable Service, Second Report and Order, First Order on Reconsideration, and Further Notice of Proposed Rulemaking ("COS Order"), 11 FCC Rcd 2220, 2248 (1996); FCC Form 1205 Instructions for Determining Costs of Regulated Cable Equipment and Installation, p.7, Line D (June 1996) ("Form 1205 Instructions").

[68] This is because accelerated depreciation, as compared to the straight-line method, produces a higher expense amount to offset against revenues, which reduces the operator's tax liability.

[69] The operator does not pay interest to subscribers to obtain and use the funds. In later years, when the deferred tax effect has been reversed and actual tax liability exceeds regulatory tax liability, rates calculated using the regulatory depreciation schedule will not be sufficient to fund the tax liability that results from a shorter depreciation schedule for tax purposes.

operators to deduct deferred tax balances from the equipment rate base.[70] As a result, rates are reduced by an amount equal to the deferred taxes multiplied by the rate of return on rate base. We have explained this aspect of the Form 1205 previously:

> The requirement to reduce the rate base by [the deferred tax balance] is premised on the assumption that the operator has included the tax expense in its rates even though the amount was not payable to taxing authorities. In these instances, since the operator has use of these "no cost funds" provided by the ratepayer, an adjustment is made to the rate base for an appropriate reduction to the revenue requirement.[71]

37. TCI claims that its existing deferred tax balance is "unfunded" because prior to the effective date of rate regulation it did not calculate its rates to recover any excess revenues to fund the future payment of deferred taxes; rather, it collected from subscribers only the amount it needed to pay then-current actual tax liability. TCI's so-called unfunded deferred tax balance represents the difference between TCI's actual tax liability prior to regulation, which it recovered from subscribers, and TCI's hypothetical regulatory tax liability during the same period, which it did not seek to recover from subscribers. According to TCI, the Commission assumed when it designed the Form 393, which operators used to establish initial regulated programming and equipment rates, that all operators had already included deferred taxes in rates before they became subject to rate regulation. TCI argues that because it did not include deferred taxes in calculating rates prior to regulation, it was penalized by the Form 393 requirement that it deduct deferred taxes from its rate base.[72] TCI states that the Commission later determined that this aspect of the Form 393 was incorrect and attempted to remedy its error.[73] Asserting that the Commission's remedy was inadequate, TCI now seeks to redress the alleged injury by amortizing its so-called unfunded deferred tax balance over a period of years by treating a portion of the balance as an expense on its Form 1205.[74]

38. TCI has made the same argument in other rate appeals, and we have rejected it.[75] TCI is correct that the Commission modified its initial approach to deferred taxes. Initially, the Commission required operators to reduce the regulated rate base by the total deferred taxes associated with the rate base investment. Subsequently, we modified this rule to require the reduction of the rate base by deferred taxes accrued only since the date the operator became subject to rate regulation.[76] Stating that the deduction we initially required was "premised on the regulatory presumption that rates reflect the operator's use of straight-line depreciation," we concluded that the presumption was not valid in the absence of rate regulation.[77] Accordingly, we modified our approach to require operators to deduct deferred taxes from rate base only to the extent the deferred taxes were accrued after the operator became subject to rate regulation.[78] Under the modified approach, we have permitted operators to

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[70] *See Second Report and Order, 11 FCC Rcd at 2248.*

[71] TCI TKR of Houston, Inc., 11 FCC Rcd 20929, 20932 (1996), *petition for reconsideration denied,* 13 FCC Rcd 13801(1998), *application for review dismissed* ("TKR of Houston"), 14 FCC Rcd 21472 (1999). *See also TCI Cablevision of St. Louis, Inc.*, 12 FCC Rcd 15287, 15295 (1997), *petition for reconsideration dismissed* ("TCI of St. Louis"), 14 FCC Rcd 15241 (1999).

[72] Appeal at 14-15.

[73] *Id.* at 14.

[74] *Id.* at 15.

[75] TCI of St. Louis, Inc., 12 FCC Rcd at 15294-95; TCI TKR of Houston, 11 FCC Rcd at 20931-32.

[76] *See Final Cost Order*, 11 FCC Rcd at 2247-48.

[77] *Id.* at 2248.

[78] *Id.*

deduct their pre-regulation deferred tax balance from their current deferred tax balance before they deduct deferred taxes from rate base.[79] This results in a smaller deduction to rate base and, correspondingly, a larger overall return amount.

39. The City applied our rules correctly when it rejected TCI's attempt to recover deferred taxes as an amortized expense. Our rules do not provide the remedy TCI seeks, and the local rate appeal process is not the proper vehicle for TCI to seek modification of our rules. TCI could have submitted a Form 1205 using the Commission-approved methodology. At the same time TCI could have asked the City to consider its alternative methodology. The burden was on TCI, not the City, to calculate rates based on the approved methodology. TCI chose not to meet its burden, even though it was aware that the Commission had previously rejected its approach. Even if TCI had prepared its Form 1205 using the Commission-approved methodology and had proferred its amortization approach as an alternative, the City could have reasonably rejected TCI's proposal. TCI offers no factual support for its claim that prior to regulation it collected from subscribers only the amount needed to pay its then-current tax liability. Moreover, TCI's depreciation practices and rate design methods prior to regulation were matters entirely within TCI's discretion. The Commission's prescribed deferred tax treatment addresses TCI's concern that the Form 393 required it to subtract its deferred tax balance from rate base: TCI and other operators are no longer required to do so. Subscribers should not now pay a penalty, through TCI's treatment of its unfunded deferred tax balance as an expense, simply because TCI used accounting and rate design methods prior to regulation that TCI now wishes to reverse. TCI's appeal of this issue is denied.

C. Written Decision

40. Finally, TCI claims that the City failed to issue a "written decision" as required by the Commission's rules because it did not provide TCI with revised versions of TCI's Form 1240 and Form 1205 showing how the City derived the approved rates.[80] TCI claims it has been unable to replicate the City's prescribed rates, although TCI neither identifies nor quantifies the discrepancies it has encountered.[81]

41. Commission rules require that a local franchising authority reviewing an operator's rate filing issue a written decision that apprises the operator of the reasons for the franchising authority's actions.[82] The franchising authority's decision must be publicly available and, if the operator's rates are not approved, the decision must provide a sufficient basis for the authority's rulings to inform the operator of the reasons the rate was disapproved so the operator may determine whether to appeal the decision.[83] We have held that franchising authorities are not required to prepare revised rate forms or provide the revised forms to operators.[84] Here, the City's rate order consisted of a three-page City Council Resolution finding the filed rates unreasonable and specifying the approved rates, as well as two Recommended Decisions, one applicable to the Form 1240 and another applicable to the Form 1205. The Resolution adopts and incorporates the Recommended Decisions. Each Recommended Decision describes the action taken and the basis for such action with respect to specific aspects of TCI's filings.

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[79] TCI of St. Louis, 12 FCC Rcd at 15295-96; TKR of Houston, 11 FCC Rcd at 20932.

[80] Appeal at 3 n.5 (citing 47 C.F.R. § 76.936).

[81] The City does not respond to TCI's allegation. We note, however, that TCI presented the allegation in a footnote and did not develop its argument anywhere in its Appeal.

[82] Rate Order, 8 FCC Rcd at 5723-24.

[83] Falcon Telecable, DA 98-213, *mimeo.* at para. 12 (1998).

[84] Meredith/New Heritage Strategic Partners, L.P., 10 FCC Rcd 13406, 13410-11 (1995); Time Warner Cable of New York City and Queens Inner Unity Cable Systems, 10 FCC Rcd 5161, 5163 (1995), *petition for review dismissed*, 14 FCC Rcd 4514 (1999); Century Cable of So. California, 10 FCC Rcd 4402, 4405 (1995).

Based on the level of detail in the Recommended Decisions and in TCI's Appeal, we conclude that TCI knew and understood the reasons for the City's rejection of its rates. Accordingly, we find that the City's order meets the Commission's "written decision" standard.

IV. ORDERING CLAUSES

42. Accordingly, **IT IS ORDERED** that the Appeal of the Local Rate Order filed by TCI of Pennsylvania on June 30, 1997, **IS GRANTED IN PART AND DENIED IN PART** and the local rate order of the City of Pittsburgh, Pennsylvania **IS REMANDED** for further consideration consistent with this Memorandum Opinion and Order.

43. **IT IS FURTHER ORDERED** that TCI of Pennsylvania's stay request **IS DISMISSED**.

44. This action is taken pursuant to authority delegated by § 0.283 of the Commission's rules.[85]

FEDERAL COMMUNICATIONS COMMISSION

John B. Norton
Deputy Chief, Policy Division
Media Bureau

[85] 47 C.F.R. § 0.283.