

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

In the Matter of)
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HERITAGE CABLEVISION, INC. d/b/a)
TCI OF CENTRAL IOWA)
)
)
Appeal of Local)
Rate Order of)
City of Des Moines, Iowa)
)

MEMORANDUM OPINION AND ORDER

Adopted: September 4, 1996

Released: September 11, 1996

By the Chief, Cable Services Bureau:

INTRODUCTION

1. On May 31, 1995, Heritage Cablevision, Inc., d/b/a TCI of Central Iowa ("TCI"), the franchisee in the above matter, filed an appeal of a local rate order adopted on May 1, 1995 by its local franchising authority, the City of Des Moines, Iowa ("the City"). The rate order establishes a new regulated rate schedule for TCI's basic service tier and associated equipment and installations.¹ In the order, the City reduced certain equipment rates proposed by TCI in its FCC Form 1205. On June 1, 1995, TCI filed a request for emergency stay pending resolution of its appeal.² The City did not file an opposition to TCI's appeal or to TCI's request for stay.

2. TCI seeks review of the local rate order with respect to two issues. TCI states that the local order violates federal law and Commission rules (1) by concluding that the labor costs of installing and retrieving converters, and managing converter inventory have already been included within the equipment basket as converter maintenance costs, and consequently prohibiting the inclusion of these costs in Schedule C; (2) by preventing TCI from capitalizing

¹Under the Cable Television Consumer Protection and Competition Act of 1992 ("1992 Cable Act") and the Commission's implementing regulations, local franchising authorities may regulate rates for basic cable service and associated equipment. See Cable Television Consumer Protection and Competition Act, Pub. L. No. 102-385, 106 Stat. 1460 (1992); Communications Act of 1934 § 623(b), 47 U.S.C. § 543(b).

²Because we are deciding this case on the merits by addressing the issues presented, the request for stay is rendered moot.

the material costs of converters, and consequently prohibiting the inclusion of these costs in Schedule C.

3. Under our rules, rate orders made by local franchising authorities may be appealed to the Commission.³ In ruling on appeals of local rate orders, the Commission will not conduct a *de novo* review, but instead will sustain the franchising authority's decision as long as there is a reasonable basis for that decision.⁴ 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.⁵ 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.⁶

DISCUSSION

4. The two issues raised by TCI on appeal involve preparation of FCC Form 1205. The portions of Form 1205 that are relevant to TCI's appeal are Schedule B, "Annual Operating Expenses of Service Installation and Maintenance of Equipment and Plant", and Schedule C, "Capital Costs of Leased Customer Equipment". Form 1205 is the official form used by regulators to determine whether an operator's regulated rates for equipment and installations are reasonable under the revised benchmark rules which apply to operators beginning May 15, 1994.⁷ Pursuant to the 1992 Cable Act, the Commission has established standards for setting, on the basis of actual cost, the rates for installation and lease of equipment used by subscribers to receive the basic service tier.⁸ Equipment rates are derived from total capital and maintenance costs per unit of equipment. Installation rates are derived from a calculation of an hourly service charge and an application of that charge to different types of installations.⁹ The maximum

³See 47 C.F.R. § 76.944.

⁴See Report and Order and Further Notice of Proposed Rulemaking in MM Docket 92-266, 8 FCC Rcd 5631, 5731(1993) ("*Report and Order*"); Third Order on Reconsideration in MM Docket 92-266, FCC Rcd 4316, 4346 (1994) ("*Third Recon. Order*").

⁵*Id.*

⁶*Id.*

⁷See Second Order on Reconsideration, Fourth Report and Order, Fifth Notice of Proposed Rulemaking in MM Docket 92-266, 9 FCC Rcd 4119 (1994) ("*Second Recon. Order*").

⁸Communications Act, § 623(b)(3), 47 U.S.C. § 543 (b)(3).

⁹To calculate the hourly service charge ("HSC"), an operator adds its expenses for equipment necessary for the maintenance of customer equipment and for the installation of basic tier service to its annual capital costs, excluding the capital costs of customer equipment. The operator then divides the total by the total number of person-hours spent in those activities over the past year. The HSC is used as a factor in developing charges for installation and

permitted rates for installation and lease of equipment calculated pursuant to Commission regulations are deemed to be reasonable, and are, therefore, lawful under the 1992 Act.¹⁰ Under Commission rules, cable operators have the burden of proof in demonstrating the reasonableness of existing or proposed rates for their basic service tier and associated equipment.¹¹

5. In the local rate order, the City disallowed TCI's inclusion of \$20 in capital costs for each of its converters, thereby reducing TCI's rates. TCI had derived the \$20 figure by adding the following capital costs: \$7 per converter for the labor costs of installation, \$7 per converter for the labor costs of retrieving a unit from a customer's home, \$3 per converter for inventory management costs, and \$3 per converter for material costs, including cable jumpers, fittings and splitters.¹² By capitalizing its converter costs, i.e., including these costs in Schedule C, "Capital Costs of Leased Customer Equipment," of Form 1205, TCI had calculated a lease rate of \$1.87 per month for addressable converters and \$1.04 per month for standard converters.¹³ In the rate order, the City disallowed TCI's capitalization of converter costs. By excluding the \$20 per unit cost from Form 1205, the City reduced TCI's lease rates for addressable and standard converters to \$1.49 and \$0.66 per month, respectively.¹⁴

A. Costs of Installing and Retrieving Converters and Managing Converter Inventory

6. The first issue raised in TCI's appeal involves the treatment in Form 1205 of the labor costs of installing and retrieving converters and the costs of managing converter inventory. Citing Commission regulations that require equipment rates to reflect actual costs, TCI contends that it must be permitted to recover the costs of installing and retrieving converters, and the costs of managing converter inventory.¹⁵ Moreover, TCI argues that these costs should be capitalized, and thus included in Schedule C of Form 1205.¹⁶ TCI contends that placement of these costs in Schedule C enables the operator to comply most effectively with the Commission's instructions to base its rates on actual costs. TCI claims that the actual cost of installing and retrieving converters and managing converter inventory cannot be recouped through one-time charges, but

monthly lease of individual pieces of equipment. *See* Form 1205 at 14.

¹⁰*See* Communications Act, § 623(b), 47 U.S.C. § 543(b).

¹¹47 C.F.R. § 76.937(a).

¹²*See* TCI's Petition for Review of Local Rate Order at Exhibit 1, City's Report and Recommendation, at 2.

¹³*Id.* at Exhibit 1, City's Report and Recommendation, at 1.

¹⁴*Id.* at Exhibit 1, City's Report and Recommendation, at 4.

¹⁵*Id.* at 2.

¹⁶*Id.*

instead must be reflected in the monthly lease rate for the equipment.¹⁷ TCI also argues that its inclusion of \$20 of capital costs per converter is reasonable and well within the range that other operators charge for the same converter costs.¹⁸ In its rate order, the City asserts that the labor costs of installing and retrieving converters and the costs of managing converter inventory are properly considered part of the converter maintenance expense which TCI has already accounted for in the equipment basket in Schedule B of Form 1205.¹⁹ Moreover, the City maintains that even if these costs have not yet been included within Schedule B, TCI's cost figure of \$20 per converter is unreasonably high. According to the City, regardless of the accounting treatment, i.e., regardless of whether these costs are included in Schedule B or Schedule C, the \$20 of additional costs per converter proposed by TCI overestimates the operator's costs. The City claims that TCI has overestimated both the amount of time required for installing and retrieving converters, and the number of customers in need of these services.²⁰ The City also alleges that TCI has sought to recover costs for converter installation for a period beyond the time that the operator was subject to regulation, and that TCI's proposed rate for installation fails to account for accumulated depreciation.²¹ Regarding inventory costs, the City asserts that TCI has not provided an accounting justification for its proposed \$3 cost figure.²²

7. The Commission rule defining the "equipment basket" states that the basket shall include all "direct and indirect material and labor costs of providing, leasing, installing, repairing, and servicing customer equipment."²³ Pursuant to the 1992 Cable Act, material and labor costs included in the equipment basket must be recoverable by the operator.²⁴ In addition, Commission rules require that rates for equipment and installation reflect their actual costs.²⁵ The costs of installing and retrieving converters and the costs of managing the converter inventory are clearly related to providing and installing equipment, and are properly classified as part of the equipment basket. Thus, TCI must be permitted to recover, on the basis of actual cost, the labor costs of installing and retrieving converters and the costs of managing converter inventory.

¹⁷*Id.* at 4.

¹⁸*Id.* at 3, and at Exhibit 3.

¹⁹*Id.* at Exhibit 1, City's Report and Recommendation, at 4.

²⁰*Id.* at Exhibit 1, City's Report and Recommendation, at 2-3.

²¹*Id.* at Exhibit 1, City's Report and Recommendation, at 3.

²²*Id.*

²³47 C.F.R. § 76.923.

²⁴*See* Communications Act, § 623(b), 47 U.S.C. § 543(b).

²⁵*Id.* *See also* First Order on Reconsideration, Second Report and Order, and Third Notice of Proposed Rulemaking in MM Docket 92-266, 9 FCC Rcd 1164, 1190-1201 (1993) ("*First Recon. Order*").

8. However, TCI does not justify adequately its reasons for treating the labor costs of installing and retrieving converters costs as capital costs and including them in Schedule C. Indeed, the operator does not clearly distinguish these costs from the operating expenses and labor costs that are ordinarily included in Schedule B. Instead, TCI argues that it should include these costs in Schedule C because it has not listed them elsewhere in Form 1205. The Commission's instructions for completing Schedule B ask operators to provide "all annual operating expenses . . . for installation and maintenance of all cable facilities."²⁶ Moreover, operating expenses incurred specifically to maintain and install customer equipment are referenced expressly.²⁷ Schedule C is used only to "compute the annual capital costs of equipment leased to customers."²⁸ The Commission's instructions for Form 1205 clearly indicate that TCI should include the labor costs of installing and retrieving converters in Schedule B rather than in Schedule C.²⁹

9. TCI's decision to capitalize the costs of managing converter inventory is reasonable. Commission rules require operators to adhere to generally accepted accounting principles ("GAAP") when completing Form 1205.³⁰ According to GAAP, it is proper to capitalize costs incurred in storing or handling goods before they are sold. Thus, TCI's decision to capitalize its inventory management conforms with GAAP. However, TCI may not account for the same costs twice, and the operator has not refuted the City's claim that the inventory management costs have already been accounted for in Schedule B. Moreover, TCI has not provided any evidence supporting either its proposed \$3 figure for inventory management costs, or the \$7 figures it proposed for both converter installation and retrieval. The burden of proof in demonstrating the reasonableness of basic service tier rates lies with the operator.³¹ In this case, TCI has failed to meet its burden. Accordingly, TCI's appeal with respect to the capitalization of the labor costs of converter installation and retrieval and the costs of managing converter inventory is denied.

²⁶FCC Form 1205 at 11.

²⁷*Id.*

²⁸*Id.* at 12.

²⁹The issue raised in this case is analogous to one discussed in *ML Media Partners L.P., trading as Multivision Cable TV* (Fairfield, CA), 11 FCC Rcd 1017 (1995) ("*Multivision*"), where the operator sought to capitalize the labor costs associated with inside wiring in its preparation of FCC Form 393. In *Multivision*, we held that, "Cable operators may not capitalize labor costs associated with inside wiring . . . [Such costs] are properly included in the charges for the installation of inside wiring." *Multivision* at 1024.

³⁰See FCC Form 1205 at 3.

³¹See 47 C.F.R. 76.937(a).

B. Capitalization of Material Costs

10. The second issue raised by TCI in this case concerns capitalization of certain material costs associated with TCI's converters (e.g., cable jumpers, fittings, splitters, etc.). TCI has attached to its appeal diagrams of converter installation configurations, which it argues demonstrate the material costs at issue.³² TCI included these material costs in Schedule C of Form 1205. In its rate order, the City characterized these costs as *de minimis* costs, and asserted that they had already been accounted for as part of TCI's converter maintenance expense in the equipment basket in Schedule B.³³ In its review of TCI's Form 1205, the City deleted these costs from Schedule C.³⁴

11. TCI's argument and diagrams fail to indicate clearly whether these materials should be accounted for in Schedule C, "Capital Costs of Leased Customer Equipment," or in Schedule B, "Annual Operating Expenses for Service Installation and Maintenance of Equipment and Plant." The instructions to Schedule C direct operators to "list all customer equipment for which there is a separate charge, including . . . different types of converter boxes, and other equipment (splitters and amplifiers)."³⁵ However, in Schedule B, operators are asked to account for "supplies" for which there are no separate charges.³⁶ While the record is not clear whether the material costs in this case represent customer equipment with separate charges or supplies with no separate charges, they appear to be the latter. We have previously found that cable operators may capitalize the cost of materials by establishing a separate lease rate for these materials.³⁷ If the material costs at issue in this case are customer equipment for which the operator has established a separate charge, the costs should be included in Schedule C of Form 1205. If the costs are simply supplies for which no separate charge has been established, the operator should include the costs in Schedule B.

12. The City's rate order refers to these material costs as *de minimis* costs that have already been accounted for in Schedule B. The amount of the costs is not relevant to their treatment in Form 1205. Commission rules do not distinguish between high-cost and low-cost equipment. All equipment must be accounted for at actual cost.³⁸ However, TCI has not refuted

³²See TCI's Petition for Review of Local Rate Order at Exhibit 2.

³³*Id.* at Exhibit 1, City's Report and Recommendation, at 3.

³⁴*Id.*

³⁵FCC Form 1205 at 12.

³⁶*Id.* at 3.

³⁷As we noted in *Multivision*, "[w]ith respect to the cost of materials associated with inside wiring, cable operators have the option of capitalizing those costs." *Multivision* at 1024.

³⁸See Communications Act, § 623(b), 47 U.S.C. § 543(b).

the City's statement in its rate order that these costs have already been accounted for in Schedule B. The operator has not submitted any evidence to the Commission that indicates that the costs at issue were not included in Schedule B, or that the operator assesses a separate charge for this equipment, thereby justifying the inclusion of these costs in Schedule C. As noted above, under Commission rules, cable operators have the burden of proof in demonstrating the reasonableness of existing or proposed rates for their basic service tier and associated equipment.³⁹ TCI has failed to meet this burden. Accordingly, TCI's appeal with respect to the capitalization of material costs is denied.

ORDERING CLAUSES

13. Accordingly, **IT IS ORDERED** that the appeal by Heritage Cablevision, Inc., d/b/a TCI Cablevision of Central Iowa of the local rate order of the City of Des Moines with respect to the capitalization of the labor costs of installing and retrieving converters and the operating costs of managing converter inventory **IS DENIED**.

14. **IT IS FURTHER ORDERED** that the appeal by Heritage Cablevision, Inc., d/b/a TCI Cablevision of Central Iowa of the local rate order of the City of Des Moines with respect to the capitalization of material costs **IS DENIED**.

15. This action is taken by the Chief, Cable Services Bureau, pursuant to authority delegated by § 0.321 of the Commission's rules, 47 C.F.R. § 0.321.

FEDERAL COMMUNICATIONS COMMISSION

Meredith J. Jones
Chief, Cable Services Bureau

³⁹See ¶4 *supra*, citing 47 C.F.R. § 76.937.