THE COMMONWEALTH OF MASSACHUSETTS

DEPARTMENT OF
TELECOMMUNICATIONS & ENERGY
Cable Television Division

ORDER ON PETITION FOR RECONSIDERATION
AND ON COMPLIANCE FILING

CTV 04-3/04-4

Petition of Comcast Cable Communications, Inc. to establish and adjust the basic service tier programming and equipment rates for the communities currently served by Comcast that are subject to rate regulation.

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I. INTRODUCTION

On August 30, 2005, the Cable Television Division ("Cable Division") of the Department of Telecommunications and Energy issued its decision concerning Comcast Cable Communications, Inc.'s ("Comcast" or "the Company") proposed basic service tier ("BST") programming, equipment and installation rates for its regulated Massachusetts communities. Comcast Cable Communications, Inc., CTV 04-3/04-4 (August 30, 2005) ("Rate Order"). In the Rate Order, the Cable Division directed the Company to make certain adjustments to its proposed BST programming and equipment rates and to submit revised Federal Communications Commission ("FCC") Forms 1240 and 1205 in compliance with the Rate Order. Id.

On September 13, 2005, Comcast submitted its Compliance Filing with the Cable Division. The Compliance Filing included a revised FCC Form 1205, a revised FCC Form 1240 for Newburyport, and refund plans for Newburyport and Hudson. Subsequently, on October 31, 2005, pursuant to 801 C.M.R. § 1.01(7)(l), Comcast filed a Petition for Reconsideration (the "Petition") with the Cable Division, requesting that the Cable Division reconsider certain findings. Specifically, Comcast requested that three determinations in the Rate Order be modified "because they produce unreasonable results" (Petition at 1). These determinations concern, first, the method the Cable Division adopted to determine the initial basic service tier ("BST") rate in Newburyport; second, the Cable Division's exclusion of all commissions from Comcast's FCC Form 1205; and third, the Cable Division's removal of drop labor from Comcast's FCC Form 1205 (Petition at 1-2).

The Cable Division approved Comcast's refund plan for Hudson. CTV 04-3/04-4, "Order on Refund Plan" (January 27, 2006). This Order will address Comcast's Petition and the remaining outstanding issues with respect to the Compliance Filing.

II. ANALYSIS AND FINDINGS

A. Newburyport: Initial Basic Service Tier Maximum Permitted Rate

On April 8, 2004, the City of Newburyport asked the Cable Division to regulate its BST rate. CTV 04-3/04-4, at 26. Accordingly, Comcast was required to establish an initial regulated BST maximum permitted rate ("MPR") for Newburyport. Under the FCC's rules, a cable operator becoming subject to rate regulation in a community should calculate its initial regulated BST on the FCC Form 1200. 47 C.F.R. § 76.922(b)(6). Comcast asserted that the FCC's rules, implemented over a decade ago, were not applicable to a situation where a community seeks regulation after such a significant period had passed. CTV 04-3/04-4, at 27-28. Comcast argued that the FCC's rules would require it to justify current rates using eight- to ten-year old rate, cost, and subscriber data which, in most cases, is no longer available. Id. at 28. Comcast filed an FCC Form 1240 for Newburyport, which established a BST MPR of $9.36.[1] Id. at 27. Comcast calculated this rate using on Line A1, a starting rate of $9.12, Comcast's current Newburyport BST rate, less franchise related costs. Id., see Exh. CTV-7. In support of the reasonableness of its proposed rate, Comcast offered a rate comparison showing that Newburyport's BST MPR was lower than the current BST MPRs in

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[1] The Company implemented an actual BST rate of $9.25 in Newburyport, effective January 1, 2005. Id.

four regulated neighboring communities: Ipswich, Newbury, Rowley and West Newbury. Id. at 27, 28; see RR-CTV-9.

In the Rate Order, we acknowledged that while we have excused the filing of an FCC Form 1200 in the past, we have done so only where there was some other independent verification of reasonableness. Id. at 28. We concluded that Comcast's comparison of Newburyport's BST MPR with the four neighboring communities was faulty because these other communities' rates included a true-up component, a factor that should not have been included in the calculation of the Newburyport BST MPR. Id. at 29-30. Because Newburyport and the other communities had a common ownership history and the same channel lineup, we concluded that a weighted average of these four communities' BST MPRs, with the true-up removed, would be a reasonable method of establishing Newburyport's initial BST MPR.[2] Id. at 29, 30-31. We directed Comcast to refile its FCC Form 1240 for Newburyport with the BST MPR calculated according to this method. Id. at 31. Comcast's Compliance Filing included a revised FCC Form 1240 for Newburyport that established an initial BST rate on Line A1 of $8.95, and a BST MPR of $9.18 (Compliance Filing at Newburyport FCC Form 1240, at 2, 4). This BST MPR was $0.07 less than Newburyport's actual BST rate of $9.25.

Comcast advanced two alternative arguments in the Petition in opposition to the Cable Division's methodology. First, Comcast reiterated the difficulty of establishing an initial

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[2] In addition to not requiring Comcast to recalculate Newburyport's BST rate back to 1994, the Cable Division did not require Comcast to unbundle its equipment rates in Newburyport.

rate for a community that has only now requested regulation, and urged us to permit the Company to proceed under its prospective-only approach (Petition at 2-4). Second, Comcast argued that if the Cable Division again rejected the prospective-only approach, since we had determined that the four neighboring communities were comparable to Newburyport, we should include these communities' true-up in the comparison used to establish an initial Newburyport BST MPR (id. at 4-7). Comcast argued that comparable rate filings should include all components of the filings, including true-up (id. at 5).

As we stated in the Rate Order, we will excuse the filing of an initial FCC Form 1200 only upon some other verification of reasonableness. Comcast has presented no argument to warrant reconsideration of this conclusion. With respect to Comcast's second argument, we understand that Comcast did not present the community rate comparison as a surrogate to the FCC Form 1240. Nevertheless, the Company presented no other independent verification of reasonableness, and our reliance on the comparison as such independent verification remains reasonable.

Comcast argues that if the Cable Division continues to rely on the comparable filings to establish Newburyport's MPR BST, we should reconsider our exclusion of all true-up from the rate calculation, since comparable filings should include all components of those filings, including the true-up components. In evaluating Comcast's argument, we consider the purpose of the true-up component, that is, to reconcile projected costs with actual costs. While Newburyport's BST was not regulated, Comcast's rate, to a limited extent, was based on external cost projections much like those used to establish the rates of the comparable regulated

communities. As we determined in our Rate Order, the actual costs for these communities exceeded the projected costs and, as a result, the rate filings included a positive true-up amount to account for the misprojections. CTV 04-3/04-4, at 30, n.16. Upon reconsideration, the Cable Division agrees that Newburyport's rate calculation should include true-up that resulted from an underestimation of the previous year's external costs and inflation. However, we continue to find that the true-up amounts that have been carried through the forms from previous years, with accumulated interest, should not be included in the comparison. In Newburyport, during previous years, Comcast had been free to adjust the BST rate as it deemed appropriate, unfettered by regulatory controls that restricted the recovery of any unforeseen costs in the subsequent year. Also, in years where Comcast overestimated costs in Newburyport, there was no regulatory-based rate reduction. The Cable Division finds, therefore, no basis for using any prior true-up carried on the other communities' forms as a factor when calculating Newburyport's BST rate.

We determine that to recreate the true-up calculations for the comparable forms would be as administratively burdensome as recreating a rate on the FCC Form 1200. Significantly, Comcast determined that $9.25 was an adequate rate to charge in Newburyport. Since we now determine that some portion of true-up may be included in the rate comparison with other communities, but lack record evidence as to the amount, we approve this rate as reasonable.

We will, therefore, direct Comcast to file an initial FCC Form 1240 that establishes a BST MPR of $9.25, equating the MPR with the actual rate charged.[3]

Because of our conclusions herein, we will not consider Comcast's proposed FCC Form 1240 for Newburyport or refund plan for Newburyport, included in the Compliance Filing, since Comcast did not overcharge Newburyport subscribers and thus, no refund liability exists.

B. Commissions

In its Petition, Comcast stated that the Cable Division had erred in requiring the removal of all commissions from its FCC Form 1205 (Petition at 7). Comcast asserted that while it appreciates that, as a general proposition, "marketing based" costs should not be passed through to subscribers in the regulated rates for equipment and installation, it does not follow that commission costs must be excluded from the FCC Form 1205 in their entirety (id.). Comcast argued that the real problem with the Cable Division's decision is that it overemphasizes the purported marketing-related aspect of the commissions, and underestimates "the critical fact that these commissions are an integral component of the compensation paid to technical staff engaged in regulated installation and maintenance activities" (id. at 8). The Company further argued that "logic dictates" that each compensation component should be included in the FCC Form 1205 calculation (id., citing Implementation of Sections of the Cable Television Consumer Protection and Competition Act of 1992: Rate Regulation, and Adoption

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[3] We recognize that there is no established method to override the function of the form and establish a specific rate. In the next proceeding, we will review the implications of Comcast's methodology on Newburyport's BST MPR going forward.

of a Uniform Accounting System for Provision of Regulated Service, Report & Order and Further Notice of Proposed Rulemaking, MM Docket No. 93-215 and CS Docket No. 94-28, FCC 94-39, 9 FCC Rcd 4527, 4744, at Attachment C, Proposed Accounting Rules, § 76.1197(f)(1) (1994)).

In support of its argument for including commissions, Comcast cites to a provision in the FCC's proposed cost-of-service accounting rules, rules that were never adopted.[4] The applicable FCC rule explicitly states that the equipment basket shall not include marketing expenses. 47 C.F.R. § 76.923(c). The Company agrees with this "general proposition" but attempts to distinguish the commissions it pays as compensation rather than as related to marketing (Petition at 7). The word "commission" is defined as "[a] fee or percentage allowed to a salesman or agent for his services." American Heritage Dictionary, Second College Edition, at 297 (1985). The Company specifically described the commissions at issue as being paid for "selling video services to customers." CTV 04-3/04-4, at 36-37; see Exh. CTV-39. Activities that might generate additional compensation to service technicians, such as an

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[4] 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, MM Docket No. 93-215, CS Docket No. 94-28, FCC 95-502, 11 FCC Rcd 2219, 2272, at ¶ 131 (1996). Even if the FCC had adopted the accounting rules, the inclusion of commissions on the cost-of-service form, FCC Form 1220, would not mean that they would be allocated to regulated services. The FCC Form 1220 specifically allocates cost categories to regulated and unregulated services. Commissions would not have been allocated to regulated services. In fact, the matching principle would assign these costs to the services they were related to, principally advanced unregulated equipment and programming.

incentive to maximize the number of installations per day, would be properly described as bonuses, not commissions.

Furthermore, Comcast's argument that commissions are part of its overall compensation scheme and that the Cable Division is somehow second-guessing that scheme is particularly unconvincing. The Company presented no evidence that any of its compensation elements, such as salaries, bonuses and commissions, are interdependent. Further, the Company has shown that it is fully able to comply with the FCC's rules, because it is able to specifically identify the commissions that it pays to its service technicians.[5] There is nothing illogical in excluding commissions, which are clearly a marketing expense, from the equipment basket.[6]

In further support of its request for reconsideration, Comcast argued that the Cable Division's adjustment would actually increase regulated rates, an unreasonable result according to the Company (id. at 7-8). The Cable Division's responsibility is to enforce the FCC's rate regulations and policies to ensure just and reasonable rates. Occasionally, fair application of the rules results in an increase in a cable operator's rate. Upon our review, we

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[5] Because Comcast presented no evidence showing that the Company is able to identify the amount of time that its service technicians spend on marketing activities, we have not directed the Company to remove these hours and costs from the equipment basket.

[6] We note that in response to consumer complaints about the unnecessary upgrading of cable services when service technicians are visiting a subscriber to make repairs, we have expressed our concern to Comcast, as well as to other operators, that internal compensation policies may encourage aggressive tactics. While we have taken no regulatory action, we are concerned about company policies that encourage technicians to act secondarily as sales representatives.

determine this is not such an occasion. During the proceeding, the Company presented work product in support of its FCC Form 1205 calculation that established the allocation percentage for commissions the Company used (Exh. Comcast-198, at Capital Assets/General Ledger Audit Report 2003, at 3). Based on the work product presented, we concluded that Comcast had followed the FCC's instructions and reported on Schedule B only its annual operating expenses necessary for the installation and maintenance of cable facilities generally. CTV 04-3/04-4, at 37; see Instructions for FCC Form 1205, at 11. Relying on this conclusion, we directed the Company to remove commissions from the form's Schedule B salaries category and from the regulated Equipment Basket at Step A, Line 5. Id. The Company's Compliance Filing incorporated these adjustments, which unexpectedly resulted in increases in both annual customer maintenance and installation costs and the hourly service charge ("HSC") (Compliance Filing at 4, Step A, Line 5; compare Exh. Comcast-198, at 4, Step A, Line 5).

Our subsequent investigation revealed that Comcast had not applied the allocation percentage for commissions that it purported to have derived from its backup information supplied with the FCC Form 1205. Moreover, the Company had included its company-wide costs on Schedule B, instead of following the FCC Form 1205 Instructions by including, on

Schedule B, only its maintenance and installation expenses (Exh. CTV-55).[7] Comcast explained that the increases on the Compliance Filing occurred because the majority of its commissions were paid to personnel in its unregulated "Other" category, and were allocated to the FCC Form 1205 at zero percent (id.). These "Other" commissions had been included on Schedule B, but not on Step A, Line 5. Consequently, removing all commissions from Schedule B increased the percentage of regulated activities compared with total activities (id.).

In response to a further Cable Division request, Comcast submitted a second revised FCC Form 1205 from which it had removed from Step A, Line 5 and Schedule B, only those commissions directly assigned to regulated costs (Exh. CTV-56, Version A). The resulting rate reflects a decrease in both Comcast's annual customer maintenance and installation costs and HSC from the amounts that the Company reported on the initial FCC Form 1205 (compare Exh. Comcast-198, at 4; Exh. CTV-56, Version A, at 4). Given that Comcast's Schedule B includes all operating costs, not just those related to installation and equipment maintenance, Comcast should not have removed those commissions related to regulated costs from Schedule B, since all commission costs, not just those related to the maintenance and installation of equipment, are included in Schedule B. In this way, all operating costs, both regulated and unregulated, would remain in the denominator (operating costs). This approach

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[7] The Cable Division issued two information requests in response to the Compliance Filing. Comcast filed its response to Information Requests 55 and 56 on September 21, 2005, and a revised response to Information Request 56 (without attachments) on September 27, 2005. Comcast's responses are here admitted into the record as Exhibits CTV-55, CTV-56, and CTV-56 (revised).

would simply reduce the numerator (regulated costs), which would reduce the percentage of total costs included in the regulated equipment basket.

Given these findings, we deny the Company's request for reconsideration. We further reject the FCC Form 1205 Comcast submitted in its Compliance Filing, and direct Comcast to file a revised FCC Form 1205 that removes commissions from Step A, Line 5, while leaving these costs in Schedule B, Operating Expenses.

C. Drop Labor Expenses

Comcast challenged the Cable Division's conclusions with respect to the Company's treatment of subscriber service drops installed at the time of the initial installation; also called the primary installation (Petition at 9-12, see CTV 04-3/04-4, at 34-36). The subscriber service drop is the portion of the initial installation that extends from the pole to the demarcation point, i.e., that portion of the wire that is located at or about 12 inches outside of the place where the cable wire enters the subscriber's premises. CTV 04-3/04-4, at 34. Comcast sought to capitalize its labor costs associated with subscriber service drops, and also included the labor costs in the initial installation rate. CTV 04-3/04-4 at 35, 36; Exh. Comcast-198, at 7; Tr. at 121. In the Rate Order, we held that the Instructions for FCC Form 1205 provide cable operators with two alternatives with respect to drop labor expense. Id. at 35-36; see Instructions for FCC Form 1205, at 14, Step A, Note 2. The first option is to include the drop labor costs in the charges for installations. Instructions for FCC Form 1205, at 14, Step A, Note 2. The second option is to capitalize such costs in the distribution plant as part of the cost of drops; in which case, the drop labor costs are recovered

in programming rates, not in installation charges. Id. If an operator chooses the second option, the drop labor costs and associated hours must be eliminated from all charges for equipment and installation. Id. We concluded that the FCC does not permit cable operators to recover labor costs associated with service drops made during initial installations through both the installation rate and through the programming rate as capitalized costs. CTV 04-3/04-4, at 36. Accordingly, we ordered Comcast to remove, from its FCC Form 1205, the time element of the primary installation that is associated with subscriber service drop labor. Id.

In its Petition, Comcast argued that when the FCC created its subscriber service drop option, it specified that a cable operator seeking to exclude these installation costs from the equipment basket must capitalize them, but, Comcast asserted, the FCC never specified that an operator seeking to include the costs in the equipment basket was prohibited from capitalizing them (Petition at 10). The Company reiterated that there is nothing that precludes a cable operator from voluntarily including drop labor costs in the equipment basket, even if the operator also capitalizes these costs as an accounting matter (id. at 11). Comcast thus asserted that it can recover subscriber service drop labor in both the programming rate and the charge for initial installation.

In support, Comcast referenced three FCC orders: Falcon First Communications, L.P., 14 FCC Rcd 7277, DA 99-891 (1999) ("Falcon"), Harron Communications Corp., 10 FCC Rcd 2349, DA 95-160 (1995) ("Harron"), and Comcast Cablevision of Tallahassee, Inc., 10 FCC Rcd 7686, DA 95-1561 (1995)("Comcast of Tallahassee") (id. at 10, n.18, 11, n.19). While each of these cases cite the general proposition that a cable operator is permitted

to include its drop labor costs in the equipment basket, none of them deal with the specific issue of double recovery. These FCC orders do not support Comcast's argument that a cable operator may both include subscriber drop labor costs on the FCC Form 1205 and capitalize these same costs. In Falcon, the operator's capitalization of its drop labor costs, i.e., outside the demarcation point, was not questioned by either the local rate regulator or the FCC. Falcon at ¶ 10. Rather, Falcon's capitalization of its labor costs inside the demarcation point, and its failure to include its labor costs inside the demarcation point in the equipment basket, were at issue. Id. Thus, the FCC's Instructions with respect to subscriber service drops were inapplicable. In that case, the cable operator could not capitalize its labor costs associated with inside wiring. Id. See Implementation of Sections of the Cable Television Consumer Protection and Competition Act of 1992: Rate Regulation, First Order on Reconsideration, Second Report and Order, and Third Notice of Proposed Rulemaking, MM Docket No. 92-266, 9 FCC Rcd 1164, at 1200-1201, ¶ 69 (1993)("First Order on Reconsideration"). The FCC upheld the local rate regulator's conclusion that Falcon could not capitalize its labor costs

incurred inside the demarcation point, but must include them in the equipment basket.[8] Id. In doing so, the FCC noted that "the operator can include the entire labor cost of the primary installation in the equipment basket, not just the cost of labor inside the demarcation point." Falcon at ¶ 9. The FCC in no way held that an operator is also allowed to recover drop labor costs in the programming rate.

Like Falcon, Harron supports the proposition that operators may charge for the entire labor cost of the primary installation, not just that portion inside the demarcation point. Harron at ¶ 18, citing 47 C.F.R. 76.5(mm); FCC Public Notice, Question/Answer 35 (May 13, 1993). However, just as in Falcon, the capitalization of primary installation labor costs was not at issue. See Harron Cablevision of Massachusetts, Inc., Y-93 (1994). At issue in Harron was the improper inclusion of drop material costs in the equipment basket. Harron at ¶ 18. The FCC's Harron order therefore provides no support for Comcast's position.

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[8] The FCC in Falcon also cited a previous ruling that cable operators cannot capitalize labor costs associated with inside wiring. Falcon at ¶ 10, n.24, citing ML Media Partners, L.P., trading as Multivision Cable TV, 11 FCC Rcd 1017, DA 95-1352, at 1024, ¶ 17 (1995). In its Petition, Comcast stated that "cable operators typically capitalize the labor costs associated with installation activities on the 'customer premises' side of the demarcation point, but the operator clearly is required to include these costs in the equipment basket, regardless of the operator's accounting policies" (Petition at 10; see also Exh. CTV-56 (revised)). The practice of capitalizing labor costs inside the demarcation point is clearly inconsistent with the FCC's determinations in Falcon and ML Media Partners. Comcast's filings showed no evidence that it follows this practice. We will specifically monitor cable operators' filings for this issue in future rate proceedings.

At issue in Comcast of Tallahassee was Comcast's practice of including subscriber drop installation hours in determining the overall installation time, but not including its drop labor costs and labor hours in the calculation of the HSC. Comcast of Tallahassee at ¶ 36. The local rate regulator determined that Comcast should have included in its calculation of the HSC the labor costs and labor hours associated with the installation of subscriber drops. Id. at ¶¶ 30, 32. In considering the local regulator's ruling, the FCC stated that its rules "allow one of two options for the recovery of the labor related to the installation of subscriber drops at the time of service installation. These options are: (1) to recover the labor costs … through the installation charges; or (2) to capitalize such costs in distribution plant as part of the cost of drops." Id. at ¶ 35. The FCC observed: "Comcast makes it abundantly clear that it elected the first option -- to recover the cost of labor associated with the installation of subscriber drops through the installation charge." Id. at ¶ 36. In upholding the local regulator's determination, the FCC found that Comcast's removal of drop labor costs from the HSC calculation was inconsistent with the FCC's procedures for recovering subscriber drop installation charges, whereby Comcast is required to include the labor costs and labor hours associated with subscriber drop installations in the HSC calculation. Id. at ¶¶ 36, 37. The FCC's language in Comcast of Tallahassee is unequivocal: a cable operator may choose "one of two options" for the recovery of labor costs related to subscriber drops, not both options. Id. at ¶ 36. Thus, Comcast of Tallahassee explicitly contradicts Comcast's current position.

Finally, Comcast relies on the FCC's First Order on Reconsideration (Petition at 11). The FCC stated the same rule that appears in the Instructions: "[c]onsistent with this alternative, it would also be acceptable to exclude all labor associated with all drops from customer installation charges and capitalize the labor as part of the cost of the drop." First Order on Reconsideration at 1201, ¶ 69, n.99. It is impossible to read this language and conclude that after Comcast capitalizes its labor costs, it can then include these same costs in the equipment basket, and thus affect customer installation charges.

Because Comcast reported that it had capitalized the labor costs and labor hours associated with service drops, we conclude that we properly directed Comcast to remove, from its FCC Form 1205, the time element of its primary installations that is associated with service drops, and therefore decline to reconsider our findings in this regard. Comcast should include on the FCC Form 1205 required by this Order as discussed above, those changes related to primary service drops that the Company made on the FCC Form 1205 submitted with the Compliance Filing. Specifically, we direct Comcast to remove from Step A, Line 5, any costs included in the regulated equipment basket that reflect time spent on primary installations outside the demarcation point. In addition, we direct Comcast to remove the corresponding hours from Step A, Line 6, and from the average hours from Comcast's average rate for an unwired home installation.

III. CONCLUSION

Accordingly, for the above reasons, the Cable Division rejects Comcast's Petition for Reconsideration in part and grants in part.

Upon review and consideration, the Cable Division hereby directs Comcast to submit its FCC Form 1240 for Newburyport, completed in compliance with this Order.

Further, after review and consideration, the Cable Division hereby rejects Comcast's FCC Form 1205 submitted with the Compliance Filing. The Cable Division directs Comcast to refile its FCC Form 1205, with its commission expenses and service drop installation times adjusted in compliance with this Order.

Further, the Cable Division directs Comcast to refile its FCC Forms 1240 and FCC Form 1205 with the Cable Division on or before April 14, 2006.

By Order of the
Department of Telecommunications and Energy
Cable Television Division

/s/ Alicia C. Matthews
Alicia C. Matthews
Director

Issued: March 31, 2006