FOR FURTHER INFORMATION CONTACT: Kathleen Scheuerle, Mass Media Bureau, (202) 418–2180.

SUPPLEMENTARY INFORMATION: This is a synopsis of the Commission's *Report and Order*, adopted February 20, 1996, and released March 4, 1996. The full text of this Commission decision is available for inspection and copying during normal business hours in the Commission's Reference Center (Room 239), 1919 M Street, NW., Washington, DC. The complete text of this decision may also be purchased from the Commission's copy contractors, International Transcription Services, Inc., 2100 M Street, NW., Suite 140, Washington, DC 20037, (202) 857–3800.

List of Subjects in 47 CFR Part 73

Radio broadcasting.

Part 73 of title 47 of the Code of Federal Regulations is amended as follows:

PART 73—[AMENDED]

1. The authority citation for part 73 continues to read as follows:

Authority: Secs. 303, 48 Stat., as amended, 1082; 47 U.S.C. 154, as amended.

§ 73.202 [Amended]

2. Section 73.202(b), the Table of FM Allotments under Alabama, is amended by removing Channel 299A and adding Channel 299C2 at Georgiana.

3. Section 73.202(b), the Table of FM Allotments under Arizona, is amended by removing Channel 229A and adding Channel 231A at Wickenburg.

4. Section 73.202(b), the Table of FM Allotments under Colorado, is amended by removing Channel 296A and adding Channel 296C3 at Aspen.

5. Section 73.202(b), the Table of FM Allotments under Mississippi, is amended by removing Channel 230A and adding Channel 230C3 at Greenwood.

6. Section 73.202(b), the Table of FM Allotments under Texas, is amended by removing Channel 277A and adding Channel 277C3 at Commerce; removing Channel 256A and adding Channel 256C3 at Fairfield; removing Channel 283C3 and adding Channel 284C2 at Ganado; removing Channel 278A and adding Channel 278C2 at New Boston; removing Channel 252C3 at Odem and adding Channel 252C2.

Federal Communications Commission.

John A. Karousos,

Chief, Allocations Branch, Policy and Rules Division, Mass Media Bureau.

[FR Doc. 96–5437 Filed 3–7–96; 8:45 am]

BILLING CODE 6712–01–F

47 CFR Part 76

[MM Docket No. 93–215; FCC 95–502]

Cable Television Rate Regulation; Cost of Service Rules

AGENCY: Federal Communications Commission.

ACTION: Final rule.

SUMMARY: The Commission has adopted the Second Report and Order and First Order on Reconsideration in MM Docket 93–215 to refine existing cost of service rules and to create final rules governing standard cost of service showings filed by cable operators seeking to justify rates for regulated cable services. By refining these rules, the Commission brings greater practicality to cost of service filing procedures and allows operators and regulatory officials increased flexibility in defining the actual costs of providing regulated cable services.

EFFECTIVE DATE: This final rule contains information collection requirements and will not become effective until approval by the Office of Management and Budget, but no sooner than 30 days after publication in the Federal Register. The Commission will publish a document specifying the effective date.

FOR FURTHER INFORMATION CONTACT: Tom Power, Cable Services Bureau, (202) 416–0800.

SUPPLEMENTARY INFORMATION: This is a synopsis of the Second Report and Order, First Order on Reconsideration and Further Notice of Proposed Rulemaking in MM Docket No. 93–215, FCC 95–502, adopted December 15, 1995 and released January 26, 1996.

This Second Report and Order and First Order on Reconsideration contains modified information collections subject to the Paperwork Reduction Act of 1995 (''PRA''), Pub. L. No. 104–13. It has been submitted to the Office of Management and Budget (''OMB'') for review under Section 3507(d) of the PRA. OMB, the general public, and other Federal agencies are invited to comment on the modified information collections contained in this proceeding.

The complete text of this Second Report and Order, First Order on Reconsideration and Further Notice of Proposed Rulemaking is available for inspection and copying during normal business hours in the FCC Reference Center (room 239), 1919 M Street, NW., Washington, DC, and also may be purchased from the Commission's copy contractor, International Transcription Services, Inc. (''ITS Inc.'') at (202) 587–3800, 2100 M Street, NW., Suite 140, Washington, DC 20017.

I. Second Report and Order and First Order on Reconsideration

A. Ratebase—Used and Useful Plant and Excess Capacity

1. In general, except as described below, we make permanent our interim rules regarding ratebase issues. We clarify that used and useful plant is plant that is actually used to send signals to customers. Plant which is not currently used and useful, however, is excess capacity, and operators may include this excess capacity in the ratebase only if it is fully constructed plant that will be used to provide regulated service within 12 months. The Commission clarifies that there are two types of excess capacity. First, where plant is being used but not to its full capacity, the portion of the plant allocated to the unused channels is excess capacity. For example, where a system provides programming over 36 channels but is capable of transmitting 48 channels of programming, the plant associated with the 12 channels not currently being used is excess capacity. In other words, in this example, the operator may only include 75% of the cost of the plant in the ratebase as used and useful plant, and may include the other 25% as excess capacity only if the 12 channels will be activated within one year. Second, excess capacity is fully constructed plant that is not being used at all, such as where the cable operator has extended its distribution line into an unserved portion of the franchise area, is ready and able to provide service to that area, but is not yet providing such service. The operator may include such plant in its ratebase to the extent it intends to place the plant into service within 12 months. However, the operator must make a corresponding adjustment to its subscriber count to include a reasonable estimate of the number of subscribers it expects to serve with that plant by the end of the 12 month period.

2. The Commission also clarifies that plant in service must be allocated between regulated and unregulated services based on a reasonable measure of the current usage of that plant. Section 76.922(g)(6)(i) of our rules currently uses the phrase ''used and useful in the provision of cable services,'' but does not specify that such cable services must be regulated cable services. Since our authority to determine cable rates extends only to regulated services as defined by the Communications Act, only plant used and useful in the provision of regulated services should be included in the ratebase. Accordingly, for our final rules, we will make this point explicit

and will amend the interim rule to specify that tangible plant must be used and useful in the provision of regulated cable services in order to be included in the ratebase. This will ensure that the ratebase for regulated cable service only includes plant used for such regulated cable service, and that subscribers to regulated tiers are not forced to subsidize plant that is used solely for premium services.

3. In addition, we recognize that what constitutes a reasonable measure of the current usage of the tangible plant depends on the circumstances. We believe that in many cases a reasonable measure would be a straight channel ratio. In other words, if an operator provides programming over a total of 40 channels, 32 of which are BST and CPST channels and eight of which are premium and pay-per-view channels, the operator must allocate 80% of its plant in service to regulated cable service and 20% to unregulated service. We do not believe, however, that the channel ratio should be weighted by customer. The cost of physical plant is directly related to the provision of cable channels and the amount of channel capacity which exists on a particular cable system. The cost of that plant does not vary depending on how many subscribers receive each channel. It would be inappropriate to weight the channel ratio by subscriber use when such use does not affect the cost of the plant.

4. With regard to the time period within which excess capacity must be used and useful in order to be included in ratebase, we adopt the interim rule of one year as our final rule. For business purposes, operators commonly project how much capacity will be used within the given year as part of their annual operating budgets. We believe that the 12 month period therefore permits plant associated with all reasonably foreseeable improvements in or additions to service to be included in ratebase.

B. Ratebase—Intangibles

5. Previously, we had concluded that one reason we should not rely on acquisition prices for ratemaking was that it appeared that those prices often include an expectation of supra-competitive profits that market power of cable systems not operating in a fully competitive market might expect to generate.

6. We continue to reject the argument that operators are entitled to include 100% of their intangible costs in the ratebase. Exclusion of some amount of these costs from the ratebase does not result in an impermissible taking without just compensation in violation of the Fifth Amendment. We have no constitutional duty to ensure full recovery of these acquisition costs, we must only ensure that the end result of our ratemaking decisions here is reasonable.

7. We continue to believe that the ratebase should not include costs resulting from any expectation of monopoly profits or expectation of a return on emerging and unregulated services, which we believe the presumptive exclusion of such acquisition costs ensures. However, upon further reflection and based upon our review of cost of service filings, we believe this presumption can be modified, without sacrificing this conclusion.

8. Therefore, we have created a new rule, applicable to systems conveyed prior to the effective date of the interim cost rules, with respect to the treatment of intangible assets. We find the model in which 34% of the purchase price of a system is presumed to be attributable to monopoly expectations, to be the one best suited to these goals.

9. Our final rule presumes, rebuttably, that 34% of the purchase price associated with regulated services of systems purchased prior to regulation represents monopoly expectations and must be removed from the regulated ratebase. Put differently, the ratebase presumptively shall not exceed 66% of that portion of the system price allocable to assets used to provide regulated services. The 34% adjustment must be applied to the entire purchase price associated with regulated services, not just the portion of the price allocable to intangibles, because cable operators derive revenues, including monopoly revenues, from the employment of both tangible and intangible assets. Applying the 34% adjustment to all assets associated with regulated services, rather than only to the associated intangibles, should remove all expectations of monopoly profits.

10. As noted, we recognize that this approach necessarily involves the use of industry-wide averages with respect to certain variables that, while reasonable, will not always reflect with perfect accuracy the circumstances of particular operators. To the extent the 34% adjustment is inexact for certain operators, we are particularly concerned that this adjustment could be used to raise rates unreasonably, given our statutory mandate to guard against unreasonable rates. Therefore, we will allow use of the 34% adjustment only for the purpose of justifying rates in effect as of the effective date of these rules. We believe that this represents a reasonable compromise between the overall integrity of the analysis used to arrive at the 34% adjustment and the concern we have that in some cases this adjustment could prove overly generous to operators. Accordingly, in cost of service cases to which the 34% adjustment is applicable, the operator may include in the ratebase up to 66% of the purchase price allocable to assets used to provide regulated services, but only to the extent necessary to justify rates in effect as of the effective date of these rules. If the current rate can be justified by including in the ratebase less than the 66% amount, then in no event shall the operator seek to use a higher percentage for purposes of any cost of service showing.

11. This adjustment shall be applied only to the purchase price of systems sold prior to May 15, 1994, the effective date of the Report and Order and Further Notice of Proposed Rulemaking, MM Docket 93–215, 9 FCC Rcd 4527 (1994) (''Cost Order'' or ''Further Notice''). The interim rule is made permanent with respect to systems sold after this date. Operators who acquired systems after May 15, 1994 were aware of the interim rule strictly limiting the ability to recover the cost of intangible assets. Thus, to the extent such operators recorded substantial intangibles, we presume those intangibles are associated with investment in unregulated services. As such, they cannot be included in the regulated ratebase.

12. Generally, operators using the cost of service to justify current rates for the first time, will be able to do so using the 34% adjustment. In some rare cases, however, this adjustment may not be adequate. For instance, if an operator acquired a system with tangible assets equal to 70% of the purchase price, obviously allowing a ratebase equal to 66% of the purchase price may not allow the operator to recover reasonably incurred costs. Similarly, if the tangible assets represent 64% of the purchase price, the remaining 2% may not adequately compensate the operator for reasonably incurred intangible assets. Therefore, where the tangible assets approach 66% of the purchase price, the operator may justify rates using 100% of the tangible assets and such intangible assets as are permissible using the interim rules.

13. We further believe it appropriate to adjust our interim rule concerning deferred income taxes. We will now require operators to deduct deferred income taxes from the ratebase only to the extent that such taxes accrued after

the date the operator became subject to rate regulation.

C. Ratebase-Start-Up Losses

14. We are persuaded that the treatment of prior year losses in the Cost Order should be amended. We find that we should not prescribe a specific prematurity phase, rather we find that we should define the prematurity phase as the actual period during which expenses exceed revenues. Although we find that the interim rule should be modified, we continue to reject the claims of commenters who argue that the wholesale inclusion of start-up losses in the ratebase is warranted. We also reject the assertion that we should allow deferred earnings into ratebase. To do so would artificially inflate the ratebase.

15. Thus, we find it appropriate to redefine our current definition of prematurity so as to account for the specific circumstances experienced by individual operators rather than continuing to use the FASB 51 standard. We are persuaded by the arguments that limitations on start-up losses should be governed by the history of individual operators. For capitalized start-up losses, build and hold operators should be permitted to recover reasonably incurred cumulative net losses, plus any unrecovered interest expenses connected to funding the regulated ratebase, over the unexpired life of the longest lived asset in the regulated ratebase, commencing with the end of the loss accumulation phase. In most cases, acquired systems will have recorded accumulated start-up losses as goodwill or as some other form of intangibles. To the extent that purchased systems can demonstrate that start-up losses have been recorded as goodwill or some other category of intangibles, these losses shall be allowed just as if they had been recorded as start-up losses and the system must itemize its assets instead of using the 66% purchase price allowance methodology described above. In allowing this however, we must emphasize this should not be interpreted as authority for the wholesale inclusion of goodwill. The burden remains on the operator to demonstrate that any portion of a class of assets is derived from start-up losses.

16. The end of the accumulation phase (i.e., the prematurity phase) will vary from system to system, depending upon the experience of the particular system at issue. By allowing the recovery to occur over the unexpired life of the longest lived asset in the regulated rate base rather than the remainder of the franchise life, the amortization period for purchased systems will realistically reflect the expected period during which the operating losses can be recovered.

D. Ratebase-Tangibles

17. We continue to believe that original cost is a reliable and fair measure of the value of tangible assets. However, our review of cost of service filings reveals that in many instances it could be difficult, if not impossible, to determine the original cost of a tangible asset. To accomodate this reality, for cable systems constructed before May 15, 1994, we will allow operators to use the book value that was recorded as of May 15, 1994, regardless of whether the system was built or acquired by the current operator. We will continue to require that original cost be used for cable systems constructed after May 15, 1994. Also, an operator that acquires individual cable assets, such as converters or remotes, at arms' length after May 15, 1994 may use its original cost for those items, rather than its seller's original cost.

18. An exception may apply to the original cost rule in the case of assets acquired in an arms-length transaction and without subscribership. In such instances, assets may be recorded at fair market value. Thus, where a cable operator sells converters, for example, to an unaffiliated operator to be used in a different franchise location, it is acceptable for the acquiring operator to record such converters at fair market value, that is, at the price the acquiring operator paid for them.

E. Rate of Return

19. In the Cost Order, we established a single overall rate of return for cable cost of service proceedings. The presumptive rate was set at 11.25% after taxes, although operators could seek different rates if they believed their circumstances justified different rates. The burden of such justification is high, however, and local authorities may counter an operator's effort to obtain a higher rate with evidence to justify a rate below 11.25%. The presumptive 11.25% rate was selected over individualized rates of return to avoid the imposition of undue administrative burdens.

20. The Commission will retain this 11.25% presumptive rate. We are guided to this conclusion by the general absence of challenges to the presumptive rate and our continued concern that the effort to set an appropriate rate of return not be overwhelmed by administrative difficulties that individualized rate estimations could entail. We recognize, however, that a unitary presumptive rate does not provide the most accurate estimation of capital costs for the full range of operators seeking to set cable rates in a cost of service filing. The Commission is interested in developing a rate of return formula that better accommodates capital cost differences among cable operators without imposing unreasonable administrative burdens on operators, franchise officials and the Commission. We will therefore proceed with a further notice of proposed rulemaking to solicit input regarding the development of an alternative rate of return formula. An alternative formula, if adopted, would serve as an alternative to the current presumptive rate method. It would not replace it.

F. Depreciation

21. We indicated in the Further Notice that industry practices with respect to depreciation would shape our ultimate resolution of the issue. Since release of the Further Notice, we have had the opportunity to review numerous cost of service filings. These filings demonstrate that some operators often do not follow any industry standards or other specific guidelines in establishing the useful lives of their assets for purposes of depreciation, or with respect to other aspects of their cost of service filings. As a result, the claimed useful life of a particular asset category can vary significantly among cable operators, even though they all use the same type of equipment and hence should be claiming roughly the same useful life in most instances. Some variation in the claimed useful lives is to be expected since, for example, management plans to replace equipment will affect its useful life and will vary among operators. Thus, when we adopted the interim rules with respect to depreciation, we expressly provided for case-by-case review of filings. However, we neither intended nor expected the substantial variations that the Form 1220s reveal. Our experience since adoption of the Cost Order now convinces us that the benefits of standardizing the useful lives of assets underlying depreciation rates outweigh any resulting burdens.

22. The absence of specific standards or guidelines with respect to useful lives creates uncertainty for operators and regulators alike and, at the local level, creates the risk of inconsistent treatment of similarly situated operators, given the varying practices of the operators and the discretion given to franchising authorities. These factors necessitate heightened scrutiny of cost of service cases before the Commission, as our

staff endeavors to ensure that the rates charged for regulated services are the product of reasonable estimations of useful lives. To provide for consistent treatment of these issues and to ease burdens on operators and regulators, we believe it prudent to establish some certainty and uniformity with respect to several issues.

23. *Depreciation schedules.* A staff survey of cost of service filings reveals significant disparities in the useful lives claimed by cable operators with respect to specific assets. Although for each particular asset category there are a substantial number of filers claiming useful lives within a relatively small range, there are also a significant number of outliers whose claimed useful lives appear to be inappropriate. With respect to headends, for example, 22% of filers claimed a useful life of between seven and nine years while 18% claimed between 15 and 16 years. For transmission facilities, 33% of filers set the useful life at five to six years, while 23% claimed lives of between 15 and 16 years.

24. The variations in the useful lives of various assets, as claimed by cable operators, are due in part to the absence of depreciation schedules in the interim cost rules, which forces operators to establish the useful lives of their assets on some other basis. Thus, it appears that operators do not have a great deal of specific guidance from any source in this regard, resulting in the variations described above.

25. Local franchising authorities face a similar lack of guidance when they attempt to determine the reasonableness of the useful lives that their cable operators claim. And the Commission staff that reviews the cost of service filings, in an effort to ensure equal treatment of similarly situated cable operators, must attempt to reconcile the substantial differences reflected in the individual filings.

26. To eliminate the uncertainty described above, and to facilitate more uniform depreciation practice for use in computing rates for regulated cable services, we will adopt a flexible range of useful lives for use by cable operators seeking to justify depreciation rates in cost of service filings. In general, we have used the data available from these filings to develop a range of years defining the useful life of each of the relevant asset categories identified in Section C, Item 9 of Form 1220, as follows:

Category	Useful life (years)
a. Headend	8–13
b. Transmission Facilities and Equipment	6–14
c. Distribution Facilities	10–15
d. Circuit Equipment	7–14
e. Maintenance Facilities	17–35
f. Maintenance Vehicles and Equipment	3–7
g. Buildings	18–33
h. Office Furniture and Equipment	9–11

27. These figures are derived from 600 cost of service filings. Such filings, including the depreciation data, are required to be made in accordance with generally accepted accounting principles (''GAAP''). GAAP does not dictate specific useful lives, but rather provides general guidelines. Thus, the useful lives reported on the cost-of-service filings reflect, to some extent, the subjective judgments of the operators making the filings. To the extent certain aspects of particular filings raise concerns, we have made adjustments accordingly. For example, we excluded from the observation pool as facially unreasonable the filings of a number of systems that claimed a useful life of one year for all of their assets.

28. Having made such adjustments, staff arrived at an average useful life for each asset category. Staff then established a range, by taking one standard deviation from the average useful life for each asset category. Each end of the range was then rounded to the nearest whole number. We have chosen a range of years, rather than dictating the use of a unitary figure, to provide operators with flexibility in determining depreciation rates for their particular systems, although still within reasonable bounds. By prescribing a range of years, we will permit operators to take into account factors that reflect characteristics of their individual systems. For example, the useful life of a cable distribution system might vary depending upon the presence and nature of a competing multichannel video programming distributor (''MVPD''). Depending upon whether the competing MVPD offers interactivity and other advanced features, the cable operator reasonably might determine that these factors will alter the obsolescence, and hence change the depreciation period, of the operator's assets that do have such features. Thus, while the ranges we have prescribed will provide for more consistent depreciation practices between cable operators, we do not believe it is necessary or prudent to deprive cable operators of all discretion to judge the appropriate useful life of their own property. However, operators seeking to establish useful lives that fall outside the prescribed ranges will have to justify such claims on a case-by-case basis.

29. Given the number of filings, the requirements of GAAP, the ability of operators to adjust for their individual circumstances, and the refinements and adjustments made by the staff, we are confident that the survey captures a representative sampling of data and produces a fair and reasonable range of years for each asset category.

30. For any asset category, we will presume the reasonableness of the useful life claimed by an operator if it falls within the range prescribed above. An operator may seek to depreciate assets over a period of time other than that which we have prescribed, but in that case the operator will have the burden of establishing the reasonableness of the period it has chosen. Thus, while furthering the goals of certainty and uniformity in the area of depreciation rates, our approach will be flexible enough to account for those unique circumstances in which an operator can demonstrate the reasonableness of a rate that falls outside of the prescribed range.

31. In addition, we will require the operator to depreciate its assets in accordance with the straight-line methodology. Our review of the Form 1220s on file with the Commission suggests that some operators are using accelerated depreciation methodologies to increase the amount of their depreciation expense and thus to increase rates. While there are contexts in which accelerated deprecation is a legitimate practice, we have been presented with insufficient justification to show that it would be appropriate for purposes of establishing rates under our cable cost of service rules.

32. *Test-year data.* Our cost of service rules establish a maximum permitted rate based on the operator's costs and ratebase as established during the test year, which is the operator's most recent fiscal year. In some instances, an operator will be able to time the filing of its 1220 such that the test year will be one in which unusually high depreciation write-offs were taken. Higher depreciation expenses translate into higher permitted rates, since rates must cover expenses. Thus, to the extent the operator can control the timing of its filing, it can justify rates that are higher than would be permitted were the operator to use data from a more representative 12 month period. The staff review of the Form 1220s suggests that some operators are pursuing precisely this strategy and thus artificially inflating rates.

33. Our new rules prescribing depreciation schedules and requiring straight-line depreciation should help to curb this practice. Where it nevertheless appears that the test-year data include unreasonably high depreciation write-offs, the operator should determine the extent to which the depreciation claimed for the test year exceeds normal depreciation and exclude the excess from the ratebase.

34. *Relevance of Franchise Life in Defining Useful Life of Assets.* The cost of service filings indicate that operators often claim that the useful life of cable system assets cannot exceed the term of the cable franchise, based on the proposition that the termination of the franchise renders the assets useless. However, this presumes that operators generally are unsuccessful at renewing the franchise, a premise for which there is no evidence and which conflicts with the general experience of the industry. Even in the event of a non-renewal, the operator might sell its asset to the new cable franchisee and thereby realize the value associated with its actual remaining life. For these reasons, we will presume that the term of the franchise is not relevant for purposes of determining the useful life of cable system assets, again subject to rebuttal by the operator if it can show, for example, some threat that its franchise will not be renewed and that in the event of non-renewal the operator will not be able to recover the value of its assets.

G. Taxes

35. In the *Cost Order,* we provided for the recovery in income taxes as an expense incurred by operators as a consequence of providing regulated cable services. Commenters have argued that capital structure assumptions used to calculate the tax expense should parallel the capital structure assumptions used to estimate the rate of return.

36. We agree that use of actual capital structures is the appropriate method of estimating the equity portion subject to tax recovery when the actual, or individualized, capital structure of an operator is used to establish the rate of return. Accordingly, if we adopt the proposed alternative to use actual capital structures when calculating the rate of return, we will rely on actual capital structures derived from the rate of return analysis to determine the amount of tax recovery for operators using the alternative to the presumptive 11.25% rate. However, when hypothetical structures are used to set the rate of return under the initial Cost Order method, we will employ the same capital structure assumptions used in such analysis to the tax calculation.

37. With respect to distributions to individual owners of non-Chapter C entities, we will continue to adjust the income calculation for estimating allowed taxes. We recognize that entities other than Chapter C corporations may pass through income directly to the individual owners and that this income may have been derived from the provision of regulated cable services. Nevertheless, we will continue to adhere to the traditional principle of adjusting the income tax amount to ensure that ratepayers do not pay the taxes of individuals who are structurally separate from the entity providing the regulated service.

H. Cost Allocation

38. While our current cost allocation rules require direct assignment of costs, the rules also allow for operator flexibility in determining specific allocators and allocation schemes. Accordingly, we affirm the Commission's current cost allocation requirements, with the exception of our rule which requires cost allocation of non regulated costs to specific non regulated service categories, which we remove. We also clarifiy that, within our current cost allocation methods which are affirmed by the Order, revenues must be matched with underlying expenses between related lines on FCC Form 1220, and that allocators need to be consistent.

39. The general propositions upon which we continue to base our cost allocation requirements are as follows: (1) costs shall be directly assigned among the equipment basket and service cost categories whenever possible; (2) costs that cannot be directly assigned and which no allocator has been specified by the Commission are to be allocated based on direct analysis of the origin of the costs, and where allocation based on direct analysis is not possible, operators must attempt to make a cost causative linkage to other costs directly assigned or allocated to the service cost categories and the equipment basket; and (3) for costs that cannot be directly assigned and for which no indirect measures of cost allocation can be found, such costs shall be allocated to each service cost category based on the ratio of all other costs directly assigned and attributed to a service cost category over total costs directly or indirectly assigned and directly or indirectly attributable.

40. We eliminate cost allocation of non-regulated costs to specific non-regulated service categories. While the requirement may in some limited instances enable us to more readily ascertain the bases for cost allocations to regulated categories, we believe that it would be overly burdensome to continue to include this requirement in our rules. Therefore, we amend our rules to remove the requirement that non-regulated costs must be allocated among the non-regulated programming service categories, other cable activities, and non-cable activities categories, and replace these categories with a single ''all other'' service cost category. Accordingly, operators electing cost of service regulation and cable operators seeking an adjustment to external costs shall allocate costs among the equipment basket and the following service cost categories: (1) BST, (2) CPST, and (3) all other. The ''all other'' service cost category shall include all costs not included in the BST or CPST service cost categories.

41. We decline to adopt a ''weighted channel'' approach to cost allocation. Generally, incremental increases in plant investment are driven by the number of channels added, irrespective of subscribership to BST channels. The number of subscribers does not impact costs in most cable equipment categories. Accordingly, we believe that in most cases, a straight channel ratio would be a reasonable approach to the allocation of plant costs amongst service baskets.

42. We also reject the proposition that advertising revenues and home shopping services be assigned to the ''other cable services'' category. The allocation approach for cost of service showings reflected in FCC Form 1220 indicates that revenues received for advertising and home shopping on a regulated tier should be allocated to that tier, and used as an offset to providing service on that tier. We adopted this approach because advertising and home shopping shown on regulated channels employ regulated assets and, consequently, these revenues should be distributed as offsets to the regulated tier revenue requirements.

I. Accounting Requirements

43. In the *Cost Order,* we stated that we would adopt a uniform system of accounts for those cable operators that elect cost of service regulation. We concluded that until a uniform system of accounts could be finalized, operators electing cost of service regulation should use an interim summary accounting system. Under the interim system that we adopted, operators using FCC Form 1220 identify costs in 55 summary level accounts, and small operators using FCC Form 1225 identify costs in 32 summary level accounts.

Operators are required to identify all amounts associated with each revenue and cost category at the franchise, system, regional and/or company level, depending on the organizational level at which the operator identified revenues and costs for accounting purposes as of April 3, 1993. Local franchising authorities and the Commission may require operators to provide any additional financial data and explanations necessary to substantiate a cost of service filing and may order appropriate disallowances if an operator fails to provide a reasonable response.

44. We now conclude that a uniform system of accounts would be unnecessarily burdensome for cable operators at this time. Our review of the cost of service filings has shown that FCC Forms 1220 and 1225 generally provide a sufficiently detailed basis for evaluating operators' rates. The additional detail provided by a uniform system of accounts would be of limited value since most of the filing defects we have discovered thus far are company-specific and would not have been prevented by a uniform accounting system. Our practice of issuing deficiency letters when questions arise has proved to be an adequate means of clarifying data. Therefore, we agree that investing the time required to develop a uniform system would be counter-productive to achieving our objective to process cases as expeditiously as possible. We are also persuaded that imposing a different accounting system on the relatively few systems filing cost of service justifications may create administrative inefficiencies for cable operators. Therefore, we will not adopt a uniform accounting system but will require operators electing cost of service regulation to follow the accounting standards required by FCC Forms 1220 and 1225, thus making permanent our interim accounting standards.

J. Affiliate Transactions

45. In the Cost Order, we promulgated rules for valuing transactions between cable operators and affiliated companies. These rules were designed to prevent favorable self-dealing between affiliated companies in order to manipulate our rate rules. We defined an affiliated entity as one that shares a 5% or greater ownership interest with the cable system operator. The interim rules require an affiliated transaction to be valued at the ''prevailing company price,'' if the provider has sold the same kind of asset or services to a substantial number of third parties at a generally available price. If the provider has not been engaged in similar transactions with a substantial number of third parties, the rules distinguish between the sale of an asset and the sale of a service (for the purposes of evaluating affiliate transactions, programming is considered an asset). If the transaction involves an asset, the cable operator is required to value the transaction at the higher of cost or fair market value when the cable operator is the seller and the lower of cost or fair market value when the cable operator is the purchaser. If the transaction involves a service and no prevailing company price can be established, the cable operator is required to value the service at the service provider's cost.

46. We reject the argument to permit a window for new services, i.e., until they can market their services to a substantial number of third parties. In a competitive market, programmers would not be able to subsidize new services with higher rates for competitive services. Similarly, in a regulated industry, programmers cannot expect regulated ratepayers to subsidize new programming ventures.

47. We also requested comment on an appropriate method of valuing an asset absent a prevailing company price. Ruling that cable operators are permitted to value services at the provider's cost is consistent with the current rules for telephone companies and there appears to be no reason to distinguish the two industries in this particular context. This is especially true in light of the more liberal definition of prevailing company price in the cable services regulatory scheme.

48. We also find that the current definition of ''affiliate'' is consistent with the definition used elsewhere in the cable services regulatory scheme.

49. Finally, we requested comment as to whether the interim affiliate transaction rules should be incorporated into a uniform system of accounts. Since we have found that no need exists at this time to adopt a uniform system of accounts, this point is moot.

K. Hardship Rate Relief

50. In the Cost Order, we recognized that, in certain extraordinary cases, rate regulation under either the benchmark or cost of service mechanisms would threaten an operator's financial health or ability to provide service. In such situations, an operator may obtain special rate relief by demonstrating that rate regulation using either of the two standard rate-setting options would cause such financial harm that the operator would be unable to attract capital or maintain credit necessary to operate, despite prudent and efficient management. The operator must show that the requested rate relief would not be unreasonable or exploitative of customers. In other words, rates cannot be excessive compared to competitive rates of similarly situated systems. Hardship showings must be made for the MSO level, or the highest level of the operator's cable system organization. Operators that submit an adequate initial showing of facts which, if proved, might warrant special relief, are subsequently given the opportunity to prove the facts alleged in the showing.

51. We now believe that the process could be shortened by eliminating the requirement of an initial showing. We will therefore allow operators to combine the requirements of the initial factual showing and the subsequent evidentiary showing into one pleading.

52. We continue to believe that we are authorized to consider an operator's unregulated revenues when determining eligibility for hardship relief. An evaluation of an operator's financial health that is based on only a portion of the operator's revenues would be incomplete and inaccurate. Similarly, it is appropriate to consider a hardship pleading in light of an operator's revenues measured at the highest level of the operator's organization. Hardship relief is an extraordinary relief measure reserved for operators whose overall financial health would be seriously threatened under the standard rate regulation mechanisms. It is not designed to bail out struggling cable systems that are owned and operated by prosperous MSOs. Lastly, the requirement that rates cannot be excessive compared to competitive rates of similarly situated systems does not mean that rates cannot exceed competitive rates. Rather, we expect operators to show that their rates would not exceed competitive rates to a degree that would be unreasonable.

II. Regulatory Flexibility Analysis

A. Final Regulatory Flexibility Act Analysis for the Second Report and Order and First Order on Reconsideration

53. Pursuant to the Regulatory Flexibility Act of 1980, 5 U.S.C. §§ 601–12, the Commission's final analysis with respect to the Second Report and Order and First Order on Reconsideration is as follows:

54. Need and purpose of this action: The Commission, in compliance with Section 3 (b) and (c) of the Cable Television Consumer Protection and Competition Act of 1992 pertaining to rate regulation, adopts rules and procedures intended to ensure cable subscribers of reasonable rates for cable

services with minimum regulatory and administrative burden on cable entities.

55. Summary of issues raised by the public in response to the Initial Regulatory Flexibility Analysis: There were no comments submitted in response to the Initial Regulatory Flexibility Analysis. The Chief Counsel for Advocacy of the United States Small Business Administration filed comments in the original rulemaking order. The Commission addressed these comments in the Rate Order (MM Docket No. 92–266, FCC 93–177, 8 FCC Rcd 5631 (1993)). The Chief Counsel for Advocacy of the United States Small Business Administration also filed comments in response to the Further Notice of Proposed Rulemaking. Those comments are addressed herein.

56. Significant alternatives considered and rejected. Petitioners representing cable interests and franchising authorities submitted several alternatives aimed at minimizing administrative burdens. In this proceeding, the Commission has attempted to accommodate the concerns raised by these parties. For example, the revised rules regarding action on rate complaints within two years of a cost of service showing are designed to reduce burdens on both industry and regulators. In addition, the revised rules also reduce burdens on both industry and regulators by simplifying certain calculations involved in producing and reviewing a cost of service showing.

III. Paperwork Reduction Act

57. The Requirements adopted herein have been analyzed with respect to the Paperwork Reduction Act of 1980 and found to impose a new or modified information collection requirement on the public. Implementation of any new or modified requirement will be subject to approval by the Office of Management and Budget as perscribed in the Act.

IV. Ordering Clauses

58. Accordingly, it is ordered that the Petitions for Reconsideration are granted in part, denied in part, and to the extent that Petitions raise issues unresolved in this order, they will be disposed of in future orders.

59. It Is further ordered that, pursuant to Sections 4(i), 4(j), 623 (b) and (c) of the Communications Act of 1934, as amended, 47 U.S.C. 154(i), 154(j), 543(b) and (c) the rules, requirements and policies discussed in this Second Report and Order and First Order on Reconsideration are adopted and Sections 76.922 and 76.924 of the Commission's rules, 47 CFR 76.922 and 76.924, are amended as set forth below.

60. It is further ordered that the requirements and regulations established in this decision shall become effective upon approval by the Office of Management and Budget of the new information collection requirements adopted herein, but no sooner than thirty (30) days after publication in the Federal Register.

61. It is further ordered that the Secretary shall send a copy of this Second Report and Order, First Order on Reconsideration, and Further Notice of Proposed Rulemaking, including the Initial Regulatory Flexibility Analysis, to the Chief Counsel for Advocacy of the Small Business Administration in accordance with paragraph 603(a) of the Regulatory Flexibility Act, Pub. L. No. 96–354, 94 Stat. 1164, 5 U.S.C. §§ 601 et seq. (1981).

List of Subjects in 47 CFR Part 76

Cable television, Reporting and recordkeeping requirements.

Federal Communications Commission.

William F. Caton,

Acting Secretary.

Rule Changes

Part 76 of Title 47 of the Code of Federal Regulations is amended as follows:

PART 76—CABLE TELEVISION SERVICE

1. The authority citation for Part 76 continues to read as follows:

Authority: Sections 2, 3, 4, 301, 303, 307, 308, 309, 48 Stat., as amended 1064, 1065, 1066, 1081, 1082, 1083, 1084, 1085, 1101; 47 U.S.C. 152, 153, 154, 301, 303, 307, 308, 309; 612, 614–615, 623, 632 as amended, 106 Stat. 1460, 47 U.S.C. 532; 623, as amended, 106 Stat. 1460; 47 U.S.C. 532, 533, 535, 543, 552.

2. Section 76.922 is amended by revising paragraphs (i)(6)(i) and (i)(7), redesignating paragraphs (i)(6)(ii) through (i)(6)(vii) as paragraphs (i)(6)(iii) through (i)(6)(viii) respectively, and adding a new paragraph (i)(6)(ii) to read as follows:

§ 76.922 Rates for the basic service tier and cable programming services tiers.

* * * * *

(i) * * *

(6) * * *

(i) Prudent investment by a cable operator in tangible plant that is used and useful in the provision of regulated cable services less accumulated depreciation. Tangible plant in service shall be valued at the actual money cost (or the money value of any consideration other than money) at the time it was first used to provide cable service, except that in the case of systems purchased before May 15, 1994 shall be presumed to equal 66% of the total purchase price allocable to assets (including tangible and intangible assets) used to provide regulated services. The 66% allowance shall not be used to justify any rate increase taken after the effective date of this rule. The actual money cost of plant may include an allowance for funds used during construction at the prime rate or the operator's actual cost of funds during construction. Cost overruns are presumed to be imprudent investment in the absence of a showing that the overrun occurred through no fault of the operator.

(ii) An allowance for start-up losses including depreciation, amortization and interest expenses related to assets that are included in the ratebase. Capitalized start-up losses, may include cumulative net losses, plus any unrecovered interest expenses connected to funding the regulated ratebase, amortized over the unexpired life of the franchise, commencing with the end of the loss accumulation phase. However, losses attributable to accelerated depreciation methodologies are not permitted.

* * * * *

(7) Deferred income taxes accrued after the date upon which the operator became subject to regulation shall be deducted from items included in the ratebase.

* * * * *

3. Section 76.924 is amended by revising the section heading, removing paragraphs (e)(1)(iv), (e)(1)(v), (e)(2)(iv) and (e)(2)(v), and revising paragraphs (e)(1)(iii) and (e)(2)(iii) to read as follows:

§ 76.924 Allocation to service cost categories.

* * * * *

(e) * * *

(1) * * *

(iii) All other services cost category. The all other services cost category shall include the costs of providing all other services that are not included the basic service or a cable programming services cost categories as defined in paragraphs (e)(1)(i) and (ii) of this section.

(2) * * *

(iii) The all other services cost category as defined by paragraph (e)(1)(iii) of this section.

* * * * *

[FR Doc. 96–5427 Filed 3–7–96; 8:45 am]

BILLING CODE 6712–01–P