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No. 05-1237

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**IN THE UNITED STATES COURT OF APPEALS  
FOR THE DISTRICT OF COLUMBIA CIRCUIT**

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ADVANCE/NEWHOUSE COMMUNICATIONS,  
and  
CHARTER COMMUNICATIONS, INC.

*Petitioners,*

v.

FEDERAL COMMUNICATIONS COMMISSION  
and  
UNITED STATES OF AMERICA,

*Respondents.*

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**ON PETITION FOR REVIEW OF AN ORDER OF THE  
FEDERAL COMMUNICATIONS COMMISSION**

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**INITIAL BRIEF OF PETITIONERS AND INTERVENOR NATIONAL  
CABLE & TELECOMMUNICATIONS ASSOCIATION**

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December 27, 2005

## **CERTIFICATE AS TO PARTIES, RULINGS, AND RELATED CASES**

Pursuant to D.C. Cir. Rule 28(a)(1), counsel of record for Petitioners Advance/Newhouse Communications and Charter Communications, Inc. and Intervenor the National Cable & Telecommunications Association certify as follows:

### **A. Parties and Amici.**

(1) The following Parties and Intervenor have appeared before this Court in the above-docketed proceeding:

Advance/Newhouse Communications  
Charter Communications, Inc.  
National Cable & Telecommunications Association  
Consumer Electronics Association  
Federal Communications Commission  
United States Department of Justice

(2) The following parties participated in the proceedings concerning the Federal Communications Commission (“FCC” or “Commission”) ruling at issue:

1394 Trade Association  
Advance/Newhouse Communications  
Adelphia Communications Corporation  
American Antitrust Institute  
Association for Maximum Service Television, Inc.  
Broadcast Music, Inc.  
Cable Television Laboratories, Inc. (“CableLabs”)  
Charter Communications, Inc.

Comcast Corporation

Consumer Federation of America

Consumers Union

Consumer Electronics Association

Consumer Electronics Retailers Coalition

Dell, Inc.

DIRECTV, Inc.

Hewlett-Packard Company

Hitachi America Ltd.

Information Technology Association of America

Insight Communications

Intel Corporation

JVC Americas Corp.

Matsushita Electric Corporation of America/Panasonic

Microsoft Corporation

Mitsubishi Digital Electronics of America, Inc.

Motorola, Inc.

National Cable & Telecommunications Association

Philips Consumer Electronics North America

Pioneer North America, Inc.

Public Knowledge

Scientific-Atlanta

Sharp Electronics Corporation

Sharp Laboratories of America, Inc.

Sony Electronics Inc.

Thomson, Inc.

Time Warner, Inc.

TiVo, Inc.

Toshiba America Consumer Products, LLC

TTE Corporation

## **B. Rulings Under Review.**

The ruling at issue is the FCC's Second Report and Order issued in *Implementation of Section 304 of the Telecommunications Act of 1996; Commercial Availability of Navigation Devices* – CS Docket No. 97-80, 20 F.C.C.R. 6794 (March 17, 2005). A summary of this order was published in the Federal Register at 70 Fed. Reg. 36,040 (June 22, 2005).

## **C. Related Cases.**

There are no related cases currently pending in this court or in any other court of which counsel is aware. A prior FCC decision in the same docket as the decision for which Petitioners are now seeking review was previously under review before this court in *General Instrument Corporation, Petitioner, v. Federal Communications Commission and United States of America, Respondents*, 213 F.3d 724 (D.C. Cir. 2000) (“*General Instrument*”). Petitioners in *General Instrument* sought review of two prior FCC orders in CS Docket No. 97-80.<sup>1</sup>

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<sup>1</sup> Those orders were: *Report and Order*, CS Docket No. 97-80, FCC 98-116, 13 F.C.C.R. 14775 (rel. June 24, 1998) (R-672, JA-\_\_\_), and *Order on Reconsideration*, CS Docket No. 97-80, FCC 99-95, 14 F.C.C.R. 7596 (rel. May 14, 1999) (R-628, JA-\_\_\_).

## **CORPORATE DISCLOSURE STATEMENTS**

The parent companies of Advance/Newhouse Communications (“Advance/Newhouse”) are Advance Publications, Inc., and Newhouse Broadcasting Corporation, neither of which is publicly held, and no publicly-held company owns 10% or more of the stock or interest in Advance/Newhouse. Advance/Newhouse manages Bright House Networks, LLC, which provides video programming, broadband Internet, and other communications services to more than two million subscribers in the United States.

Charter Communications, Inc. (“Charter”) is a widely-held corporation with no parent companies and no publicly-held companies that own 10% or more of its stock. Charter provides video programming, broadband Internet, and other communications services to more than six million subscribers in the United States.

The National Cable & Telecommunications Association (“NCTA”) is the principal trade association representing the cable television industry in the United States. No publicly-held company owns 10% or more of the stock or interest in NCTA.

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<b><u>GLOSSARY</u></b>	
<b>TERM</b>	<b>DEFINITION</b>
CableCARD	CableCARD is the trademarked name of the separated security module referred to in FCC rules as a point of deployment module, or “POD.” These modules are compatible with retail navigation devices made by independent consumer electronics manufacturers. Not to be confused with the DBS “smart card” that does not have separated security.
Cable-Ready	Denotes consumer electronics equipment manufactured for compatibility with cable system transmissions and reception of certain cable programming as specified in 47 C.F.R. § 15.118
CE	Consumer electronics.
Conditional Access	Defined in § 76.1200(e) of the FCC’s rules as “[t]he mechanisms that provide for selective access and denial of specific services and make use of signal security that can prevent a signal from being received except by authorized users.”
Converter Box	Any of a variety of navigation devices containing electronic equipment and typically placed on top of a home television set that is employed to control access to, descramble, and/or enable tuning of, digital and analog signals and other information provided by a cable television system or other multichannel video programming distributor (“MVPD”). A converter box may also include other features and functions related to the distribution and reception of such signals and information.
Direct Broadcast Satellite (“DBS”)	An MVPD that uses satellite facilities to transmit video programming directly to customer homes pursuant to 47 C.F.R. § 25.201.
Headend	Cable system facility with signal generation and processing equipment where signals are received, converted, allocated to channels, encrypted, and/or digitized for customer distribution.
Integration Ban	The FCC rule set forth in the second sentence of 47 C.F.R. § 76.1204(a)(1) that, as of July 1, 2007, prohibits cable operators (but not DBS providers) from providing customers with set-top boxes that include security in addition to navigation functions.
“Integrated” navigation devices	Navigation devices that perform both conditional access (security) and other functions as a single integrated device.

<b><u>GLOSSARY</u></b>	
<b>TERM</b>	<b>DEFINITION</b>
Multichannel Video Programming Distributor (“MVPD”)	Defined in Section 602(13) of the Communications Act of 1934, as amended, 47 U.S.C. § 522(13), as “a person such as, but not limited to, a cable operator, a multichannel multipoint distribution service, a direct broadcast satellite service, or a television receive-only satellite program distributor, who makes available for purchase, by subscribers or customers, multiple channels of video programming.”
Navigation Device	Converter boxes, interactive communications equipment, and other equipment (including televisions, VCRs, cable set-top boxes, personal computers, program guide equipment and cable modems) used by consumers to access multichannel video programming and other services offered over multichannel video programming systems. 47 U.S.C. § 549 and <i>Implementation of Section 304 of the Telecommunications Act of 1996; Commercial Availability of Navigation Devices</i> , Report and Order, CS Docket No. 97-80, 13 F.C.C.R. 14775, at ¶ 25 (1998).
Open Cable Applications Platform (“OCAP”)	A middleware platform that enables cable and advanced retail devices to deliver interactive cable services.
Original Equipment Manufacturer (“OEM”)	A company that produces hardware to be marketed under another company’s brand name.
“Plug and Play” Rules	The FCC rules set forth at 47 C.F.R. §§ 76.640, 76.1901 <i>et seq.</i> governing the interoperability of digital cable systems and digital cable-ready navigation devices, under which cable operators must provide specific operational and technical support to assure the availability of PODs and their compatibility with such devices.
POD	Point-of-deployment module. See CableCARD.
Separate Security Requirement	The FCC rule set forth in the first sentence of 47 C.F.R. § 76.1204(a)(1), which requires that an MVPD “that utilizes navigation devices to perform conditional access functions shall make available equipment that incorporates only the conditional access functions of such devices.” <i>Compare</i> CableCARD (separate security) <i>with</i> DBS “smart card” (integrated security).

<b><u>GLOSSARY</u></b>	
<b>TERM</b>	<b>DEFINITION</b>
Smart Card	A credit card sized object containing a microprocessor and memory used to perform decryption or authentication functions through interface with a host machine or device. Used with DBS equipment. Not to be confused with separated security in CableCARDS.
Set-Top Box	A navigation device typically placed on or adjacent to a television set through which the television set receives multichannel video programming and other services offered over multichannel video programming systems.

### **STATEMENT REGARDING JURISDICTION**

On March 17, 2005, the FCC adopted a final order maintaining and refusing to eliminate a regulation codified at 47 C.F.R. § 76.1204(a)(1) pursuant to a grant of authority under Section 629 of the Communications Act, 47 U.S.C. § 549. The rule was published in the Federal Register on June 22, 2005. On July 5, 2005, Petitioners timely filed a petition for review of this regulation in accordance with 28 U.S.C § 2344. This Court has jurisdiction under 47 U.S.C. § 402(a), 28 U.S.C. §§ 2342 and 2344, and Rule 15(a) of the Federal Rules of Appellate Procedure.

Petitioners and NCTA were parties to the agency proceedings that led to the FCC's final order and are aggrieved by certain rulings therein, and therefore have standing to bring this matter before the Court.

## STATUTES AND REGULATIONS

**Statutes:** The principal statutory provision at issue in this review proceeding is Section 629 of the Communications Act, as amended, 47 U.S.C. § 549, which is set out in full text below.

### **Section 629. [47 U.S.C. § 549] COMPETITIVE AVAILABILITY OF NAVIGATION DEVICES.**

**(a) COMMERCIAL CONSUMER AVAILABILITY OF EQUIPMENT USED TO ACCESS SERVICES PROVIDED BY MULTICHANNEL VIDEO PROGRAMMING DISTRIBUTORS.—**

The Commission shall, in consultation with appropriate industry standard-setting organizations, adopt regulations to assure the commercial availability, to consumers of multichannel video programming and other services offered over multichannel video programming systems, of converter boxes, interactive communications equipment, and other equipment used by consumers to access multichannel video programming and other services offered over multichannel video programming systems, from manufacturers, retailers, and other vendors not affiliated with any multichannel video programming distributor. Such regulations shall not prohibit any multichannel video programming distributor from also offering converter boxes, interactive communications equipment, and other equipment used by consumers to access multichannel video programming and other services offered over multichannel video programming systems, to consumers, if the system operator's charges to consumers for such devices and equipment are separately stated and not subsidized by charges for any such service.

**(b) PROTECTION OF SYSTEM SECURITY —** The Commission shall not prescribe regulations under subsection (a) which would jeopardize security of multichannel video programming and other services offered over multichannel video programming systems, or impede the legal rights of a provider of such services to prevent theft of service.

**(c) WAIVER. —** The Commission shall waive a regulation adopted under subsection (a) for a limited time upon an appropriate showing by a provider of multichannel video programming and other services offered over multichannel video programming systems, or an equipment provider, that such waiver is necessary to assist the development or introduction of a new or improved multichannel video programming or other service offered over multichannel video programming systems, technology, or products. Upon an appropriate showing, the Commission shall grant any such waiver request within 90 days of any application filed under this subsection, and such waiver shall be effective for all service providers and products in that category and for all providers of services and products.

**(d) AVOIDANCE OF REDUNDANT REGULATIONS. -**

**(1) COMMERCIAL AVAILABILITY**

**DETERMINATIONS.** — Determinations made or regulations prescribed by the Commission with respect to commercial availability to consumers of converter boxes, interactive communications equipment, and other equipment used by consumers to access multichannel video programming and other services offered over multichannel video programming systems, before the date of enactment of the Telecommunications Act of 1996 shall fulfill the requirements of this section.

**(2) REGULATIONS.**— Nothing in this section affects section 64.702(e) of the Commission’s regulations (47 C.F.R. 64.702(e)) or other Commission regulations governing interconnection and competitive provision of customer premises equipment used in connection with basic common carrier communications services.

**(e) SUNSET.** — The regulations adopted under this section shall cease to apply when the Commission determines that —

(1) the market for the multichannel video programming distributors is fully competitive;

(2) the market for converter boxes, and interactive communications equipment, used in conjunction with that service is fully competitive; and

(3) elimination of the regulations would promote competition and the public interest.

**(f) COMMISSION’S AUTHORITY** — Nothing in this section shall be construed as expanding or limiting any authority that the Commission may have under law in effect before the date of enactment of the Telecommunications Act of 1996.

**FCC Regulations:** The FCC regulations at issue in this review proceeding are found in Part 76, Subpart P of the Commission’s Rules, 47 C.F.R. §76.1200 et seq., which are set out in full text below.

**§76.1200 Definitions.** - As used in this subpart:

(a) Multichannel video programming system. A distribution system that makes available for purchase, by customers or subscribers, multiple channels of video programming other than an open video system as defined by §76.1500(a).

Such systems include, but are not limited to, cable television systems, BRS/EBS systems, direct broadcast satellite systems, other systems for providing direct-to-home multichannel video programming via satellite, and satellite master antenna systems.

(b) Multichannel video programming distributor. A person such as, but not limited to, a cable operator, a BRS/EBS provider, a direct broadcast satellite service, or a television receive-only satellite program distributor, who owns or operates a multichannel video programming system.

(c) Navigation devices. Devices such as converter boxes, interactive communications equipment, and other equipment used by consumers to access multichannel video programming and other services offered over multichannel video programming systems.

(d) Affiliate. A person or entity that (directly or indirectly) owns or controls, is owned or controlled by, or is under common ownership or control with, another person, as defined in the notes accompanying §76.501.

(e) Conditional access. The mechanisms that provide for selective access and denial of specific services and make use of signal security that can prevent a signal from being received except by authorized users.

**§76.1201 Rights of subscribers to use or attach navigation devices.** - No multichannel video programming distributor shall prevent the connection or use of navigation devices to or with its multichannel video programming system, except in those circumstances where electronic or physical harm would be caused by the attachment or operation of such devices or such devices may be used to assist or are intended or designed to assist in the unauthorized receipt of service.

**§76.1202 Availability of navigation devices.** - No multichannel video programming distributor shall by contract, agreement, patent right, intellectual property right or otherwise prevent navigation devices that do not perform conditional access or security functions from being made available to subscribers from retailers, manufacturers, or other vendors that are unaffiliated with such owner or operator, subject to §76.1209.

**§76.1203 Incidence of harm.** - A multichannel video programming distributor may restrict the attachment or use of navigation devices with its system in those circumstances where electronic or physical harm would be caused by the attachment or operation of such devices or such devices that assist or are intended or designed to assist in the unauthorized receipt of service. Such restrictions may be accomplished by publishing and providing to subscribers standards and descriptions of devices that may not be used with or attached to its system. Such standards shall foreclose the attachment or use only of such devices as raise reasonable and legitimate concerns of electronic or physical harm or theft of

service. In any situation where theft of service or harm occurs or is likely to occur, service may be discontinued.

**§76.1204 Availability of equipment performing conditional access or security functions.**

(a)(1) A multichannel video programming distributor that utilizes navigation devices to perform conditional access functions shall make available equipment that incorporates only the conditional access functions of such devices. Commencing on July 1, 2007, no multichannel video programming distributor subject to this section shall place in service new navigation devices for sale, lease, or use that perform both conditional access and other functions in a single integrated device.

(2) The foregoing requirement shall not apply to a multichannel video programming distributor that supports the active use by subscribers of navigation devices that: (i) operate throughout the continental United States, and (ii) are available from retail outlets and other vendors throughout the United States that are not affiliated with the owner or operator of the multichannel video programming system.

(b) Conditional access function equipment made available pursuant to paragraph (a)(1) of this section shall be designed to connect to and function with other navigation devices available through the use of a commonly used interface or an interface that conforms to appropriate technical standards promulgated by a national standards organization.

(c) No multichannel video programming distributor shall by contract, agreement, patent, intellectual property right or otherwise preclude the addition of features or functions to the equipment made available pursuant to this section that are not designed, intended or function to defeat the conditional access controls of such devices or to provide unauthorized access to service.

(d) Notwithstanding the foregoing, navigation devices need not be made available pursuant to this section where:

(1) It is not reasonably feasible to prevent such devices from being used for the unauthorized reception of service; or

(2) It is not reasonably feasible to separate conditional access from other functions without jeopardizing security.

(e) The requirements of this section shall become applicable on July 1, 2000.

(f) Paragraphs (a)(1), (b), and (c) of this section shall not apply to the provision of any navigation device that:

(1) Employs conditional access mechanisms only to access analog video programming;

(2) Is capable only of providing access to analog video programming offered over a multichannel video programming distribution system; and

(3) Does not provide access to any digital transmission of multichannel video programming or any other digital service through any receiving, decoding, conditional access, or other function, including any conversion of digital programming or service to an analog format.

**§76.1205 Availability of interface information.** - Technical information concerning interface parameters that are needed to permit navigation devices to operate with multichannel video programming systems shall be provided by the system operator upon request in a timely manner.

**§76.1206 Equipment sale or lease charge subsidy prohibition.** - Multichannel video programming distributors offering navigation devices subject to the provisions of §76.923 for sale or lease directly to subscribers, shall adhere to the standards reflected therein relating to rates for equipment and installation and shall separately state the charges to consumers for such services and equipment.

**§76.1207 Waivers.** - The Commission may waive a regulation adopted under this subpart for a limited time, upon an appropriate showing by a provider of multichannel video programming and other services offered over multichannel video programming systems, or an equipment provider that such a waiver is necessary to assist the development or introduction of a new or improved multichannel video programming or other service offered over multichannel video programming systems, technology, or products. Such waiver requests should be made pursuant to §76.7. Such a waiver shall be effective for all service providers and products in the category in which the waiver is granted.

**§76.1208 Sunset of regulations.** - The regulations adopted under this subpart shall cease to apply when the Commission determines that (1) the market for multichannel video distributors is fully competitive; (2) the market for converter boxes, and interactive communications equipment, used in conjunction with that service is fully competitive; and (3) elimination of the regulations would promote competition and the public interest. Any interested party may petition the Commission for such a determination.

**§76.1209 Theft of service.** - Nothing in this subpart shall be construed to authorize or justify any use, manufacture, or importation of equipment that would

violate 47 USC §553 or any other provision of law intended to preclude the unauthorized reception of multichannel video programming service.

**§76.1210 Effect on other rules.** - Nothing in this subpart affects §64.702(d) of the Commission's regulations or other Commission regulations governing interconnection and competitive provision of customer premises equipment used in connection with basic common carrier communications services.

## ISSUES PRESENTED

1. Whether the FCC's determination to prohibit cable operators from providing integrated navigation devices violates the statutory command that the FCC's regulations "shall not prohibit any multichannel video programming distributor from also offering converter boxes, interactive communications equipment, and other equipment used by consumers to access multichannel video programming and other services offered over multichannel video programming systems, to consumers . . . ."
2. Whether it was arbitrary and capricious for the FCC to impose a ban on cable operators' provision of navigation devices with integrated security:
  - a. Without explaining why this "integration ban" was needed and how consumers would benefit from decreased equipment choice;
  - b. Without accounting for evidence of commercial availability of retail cable-ready navigation devices from multiple unaffiliated vendors; and
  - c. Without considering the effect of intense competition from competing multi-channel video programming providers.
3. Whether it was arbitrary and capricious for the FCC to impose, maintain and readopt an "integration ban" on cable operators' provision of navigation devices to consumers although cable operators had satisfied the same criteria as Direct Broadcast Satellite (DBS) operators whom the FCC exempted from the "integration ban."

## STANDARD OF REVIEW

This case presents the question of whether, under the standard articulated in *Chevron U.S.A. Inc. v. Natural Resources Defense Council*, 467 U.S. 837 (1984), the FCC's actions are permissible in view of the statutory provisions that those actions were supposed to implement. Separately, this case requires a determination as to whether the FCC's actions are arbitrary and capricious under the Administrative Procedure Act.

Under *Chevron*, the Court “employ[s] traditional tools of statutory construction” to determine “whether Congress has directly spoken to the precise question at issue.” *Id.* at 842-43. If so, the inquiry is at an end, “for the court, as well as the agency, must give effect to the unambiguously expressed intent of Congress.” *Id.* This case should be so resolved, because the rule at issue squarely conflicts with a Congressional directive set forth in Section 629(a) of the Communications Act.

Where the statute is silent or ambiguous, the Administrative Procedure Act still requires a reviewing court to “hold unlawful and set aside agency action, findings and conclusions found to be arbitrary, capricious, an abuse of discretion, or otherwise not in accordance with the law.” 5 U.S.C. §706(2)(A). Although this standard is generally a deferential one, reviewing courts must and do intervene to ensure that the agency has “examine[d] the relevant data and articulate[d] a satisfactory explanation for its action, including a rational connection between the facts found and the choice made.” *Motor Vehicles Mfrs. Ass'n v. State Farm Mut. Auto. Ins. Co.*, 463 U.S. 29, 43 (1983). In addition, an agency order is arbitrary “[w]here an agency applies different standards to similarly situated entities and fails to support this disparate treatment with a reasoned explanation *and* substantial evidence in the record,” *Burlington Northern and Santa Fe Ry. Co. v. Surface Transp. Bd.*, 403 F.3d 771,

776-777 (D.C. Cir. 2005), or where the agency has “entirely failed to consider an important aspect of the problem.” *State Farm*, 463 U.S. at 43.

Although the Commission previously adopted an integration ban in a prior order, its decision to reopen its rulemaking and issue a new, final order substantially readopting the rule subjects its action to judicial review. *See Harris v. FAA*, 353 F.3d 1006, 1011 (D.C. Cir. 2004) (“[I]f for any reason the agency reopens a matter and, after reconsideration, issues a new and final order, that order is reviewable on its merits, even though the agency merely reaffirms its original decision”).

## STATEMENT OF THE CASE

### 1. Nature of the Case

Petitioners Advance/Newhouse Communications and Charter Communications, Inc. and Intervenor National Cable & Telecommunications Association (“NCTA”), seek review of portions of the Federal Communications Commission’s Second Report and Order in *Commercial Availability of Navigation Devices*, CS Docket No. 97-80, 20 F.C.C.R. 6794 (March 17, 2005) (“*Order*”) (R-1, JA-\_\_\_\_).<sup>2</sup> Specifically, Petitioners seek vacatur of the “integration ban” set forth in the second sentence of 47 C.F.R. §76.1204(a)(1), which the FCC readopted in the *Order*. As of July 1, 2007, the integration ban prohibits cable operators (but not DBS providers) from providing their customers with the type of leased integrated digital set-top boxes they use today – boxes with integrated security and navigation functions. Rather, cable operators will only be able to deploy higher-cost set-top boxes with separate security modules to their customers. The *Order*’s re-adoption of the integration ban violates the statute and is arbitrary and capricious.

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<sup>2</sup> Pending filing of the Joint Appendix (JA\_\_\_\_), all citations are to the FCC’s certified list of the items in the record (“R-\_\_\_\_”) filed September 26, 2005.

## 2. Statutory Background

Section 629, adopted as part of the Telecommunications Act of 1996, applies equally to all Multichannel Video Programming Distributors (“MVPDs”), including the cable systems operated by Petitioners and the Direct Broadcast Satellite (“DBS”) systems operated by DirecTV and DISH Network (“EchoStar”). The statute directs the FCC to “adopt regulations to assure the commercial availability ... of converter boxes, interactive communications equipment, and other equipment used by consumers to access multichannel video programming and other services offered over multichannel video programming systems, from manufacturers, retailers, and other vendors not affiliated with any multichannel video programming distributor.” With this provision, Congress sought to “ensure that consumers are not forced to purchase or lease a specific, proprietary converter box, interactive device or other equipment from the cable system or network operator.”<sup>3</sup> At the same time, Congress explicitly provided that FCC regulations “shall not prohibit any [MVPD] from also offering converter boxes, interactive communications equipment, and other equipment,” so long as the charges for such equipment are “separately stated and not subsidized” by other services.<sup>4</sup> Congress also precluded the FCC from adopting rules which would jeopardize the security of MVPD programming.<sup>5</sup>

The equipment covered by Section 629 – “converter boxes, interactive communications equipment, and other equipment used by consumers to access multichannel video programming and other services offered over multichannel video programming systems” is referred to generically in the statute and FCC orders as “navigation devices.” The FCC found that Congress

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<sup>3</sup> S. Conf. Rep. 104-230 at 181 (1996).

<sup>4</sup> The FCC has held this condition to be fully satisfied through FCC equipment rate regulations. *Commercial Availability of Navigation Devices*, Report and Order, CS Docket No. 97-80, 13 F.C.C.R. 14775, ¶86 (rel. June 24, 1998)(“1998 Order”)(R-672, JA-\_\_\_\_).

<sup>5</sup> 47 U.S.C. §549(b).

intended this “broad” and “expansive” clause to refer to “*any* category of equipment used to access multichannel video programming,” including “televisions, VCRs, cable set-top boxes, personal computers, program guide equipment and cable modems,”<sup>6</sup> and to all MVPDs.<sup>7</sup>

### **3. Course of Proceedings**

The FCC issued its initial rules to implement Section 629 in its *1998 Order*. At that time, a key problem was that different MVPDs used different security technologies in their systems around the country. The Commission believed that the lack of interoperability and national portability deterred development of a retail market for navigation devices.

To address this issue, the FCC decided that its primary mechanism for assuring the availability of commercial navigation devices without jeopardizing system security would be to require MVPDs to provide a stand-alone “security element” that could be plugged into navigation devices obtained at retail that would enable the device to unscramble and deliver only those services ordered by a particular customer and authorized by the service provider. The FCC found that the availability of stand-alone security modules would make it easier for third-parties to develop nationally-marketable retail navigation devices since the devices could work anywhere in the country.<sup>8</sup>

The FCC did not stop there. Deciding it was not enough that MVPDs offer a separate security element that could be used with retail devices, the Commission went on to *prohibit* MVPDs, as of January 1, 2005, from continuing to offer “navigation devices for sale, lease or use that perform both conditional access and other functions in a single integrated device.” The

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<sup>6</sup> *1998 Order* ¶25 (R-672, JA-\_\_\_\_).

<sup>7</sup> *Id.* ¶112 (R-672, JA-\_\_\_\_)(“Congress did not exclude DBS from the reach of Section 629, even though the competitive state of DBS services was known at the time of the enactment of the 1996 Act.”).

<sup>8</sup> *Id.* ¶49 (R-672, JA-\_\_\_\_).

FCC stated that it adopted this “integration ban” in response to comments from the CE industry that integrated devices would give MVPDs an “effective cost advantage” and would “undermine the conditions for a successful competitive commercial market for unbundled devices.”<sup>9</sup>

Commissioner Powell dissented, stating

I fear that the majority decision today denies a cost effective choice for consumers. It is quite plausible to me that the “impediment” to switching to retail may in fact be a consumer preference for distributor-supplied integrated boxes! I see no reason to attempt to control consumer preferences.<sup>10</sup>

Although the FCC had concluded that devices used to access DBS services were equally subject to Section 629, the *1998 Order* exempted DBS from both the requirement to provide separate security modules to customers as well as the integration ban. The FCC offered three reasons for this decision. First, it found that consumers had the ability to purchase DBS navigation devices at retail outlets from ten manufacturers.<sup>11</sup> Second, it was reluctant to regulate a “new” and “evolving” service with “only 8% of the MVPD market,” noting that “the Commission [often] refrains from imposing regulations on new entrants.”<sup>12</sup> Third, it reasoned that regulation was less necessary for DBS because DBS navigation devices were “geographically portable,” in the sense that a DirecTV customer could use his DirecTV box at another location (although not with any other DBS network or cable system).<sup>13</sup>

In 1999, the FCC committed to commence a proceeding in 2000 to review the effectiveness of the Section 629 rules and consider any necessary changes.<sup>14</sup> Commissioner

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<sup>9</sup> *1998 Order* ¶68 (R-672, JA-\_\_\_\_).

<sup>10</sup> *Id.*, Statement of Commissioner Michael K. Powell, dissenting in part (R-672, JA-\_\_\_\_).

<sup>11</sup> *Id.* ¶64 (R-672, JA-\_\_\_\_).

<sup>12</sup> *Id.* ¶¶64-65 (R-672, JA-\_\_\_\_).

<sup>13</sup> *Id.* ¶66 (R-672, JA-\_\_\_\_).

<sup>14</sup> *Commercial Availability of Navigation Devices*, Order on Reconsideration, CS Docket No.

Powell again dissented from reaffirmation of the ban, saying (1) “Section 629 did not direct the FCC to incent customers to go out to buy set-top boxes.... [The ban] goes well beyond the statutory objective to decide that government’s role is not merely to assure availability but also success for manufacturers and retailers”; (2) “The decision to prohibit integrated boxes may deter innovation”; (3) “It is also contrary to good public policy to remove from the market one potentially cost-effective choice for consumers”; and (4) “the ban is likely to skew present business decisions of operators about when they should buy new set-top boxes, how many they should buy and what plans they should make for deploying digital technology.”<sup>15</sup>

Several parties challenged certain aspects of these orders, including the integration ban, in *General Instrument Corp. v. FCC*, 213 F.3d 724 (D.C. Cir. 2000) (“*General Instrument*”).

The Court held that the integration ban was neither compelled by Section 629 nor precluded by the statutory provision that the FCC may not prohibit MVPDs from offering “converter boxes” to consumers. The Court did not rule on whether the FCC’s adoption of the integration ban was arbitrary and capricious, because it held that petitioners had not timely raised the issue.

However, the Court clearly warned the Commission that it had not adequately explained why it believed consumers would be impeded from realizing the intended benefits of Section 629 in the absence of an integration ban:

Consumers might have chosen not to purchase retail devices for perfectly sensible economic reasons—because, for instance, there are efficiency gains captured in the manufacture of an integrated box that lead it to cost less than the combined cost of a separate security module and a retail device, or because consumers view as too high the transaction costs of seeking a separate ancillary device at retail. If this is the case, the integration ban does nothing more than deny the most cost-effective product choice to consumers—an ironic outcome for an order implementing “one of the most pro-consumer, pro-competitive provisions of the Telecom Act.” *Perhaps there are benefits that will flow to consumers from the*

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97-80, FCC 99-95, 14 F.C.C.R. 7596, ¶¶33, 35 (rel. May 14, 1999)(“*Reconsideration Order*”). (R-628, JA-\_\_\_\_).

<sup>15</sup> *Id.* (R-672, JA-\_\_\_\_).

*integration ban, but the Commission did not clearly spell them out.*<sup>16</sup>

Shortly thereafter, the FCC reopened its rulemaking proceeding as promised “to review the effectiveness of the rules and consider any necessary changes.”<sup>17</sup> The FCC “sought comment, *inter alia*, on whether the 2005 date for the phase-out of integrated boxes remains appropriate, on what, if any, incentives the requirement creates for the development of a commercial retail market for navigation devices, and on the economic impacts and costs associated with the requirement.”<sup>18</sup> In 2003, with this review still ongoing, the Commission deferred the effective date of the integration ban to July 1, 2006 and issued another rulemaking notice inviting additional comments on whether the integration ban remained necessary.<sup>19</sup> This latter notice stated: “By January 1, 2005, the Commission shall complete a reassessment of the state of the navigation devices market and determine whether the designated time frame remains appropriate or whether the ban on integrated devices will no longer be necessary.”<sup>20</sup>

The record developed in response to these notices showed remarkable changes in the years since the *1998 Order* had been adopted.

The first was in the commercial availability of alternatives to leased cable set-top boxes. In accordance with the FCC’s rules, the cable industry developed and deployed interoperable separate security modules called “CableCARDS” that are compatible with retail navigation devices made by independent consumer electronics (“CE”) manufacturers. In addition, cable

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<sup>16</sup> *General Instrument*, 213 F.3d at 732 (emphasis added).

<sup>17</sup> *Commercial Availability of Navigation Devices*, Further Notice of Proposed Rulemaking and Declaratory Ruling, CS Docket No. 97-80, FCC 00-341 (September 18, 2000)(“*2000 FNPRM*”), ¶1 (R-595, JA-\_\_\_\_).

<sup>18</sup> *Commercial Availability of Navigation Devices*, Order and Further Notice of Proposed Rulemaking, CS Docket No. 97-80, FCC 03-89, ¶3 (April 25, 2003)(“*2003 Extension Order*”) (R-381, JA-\_\_\_\_), describing the *2000 FNPRM* (R-595, JA-\_\_\_\_).

<sup>19</sup> *2003 Extension Order* ¶5 (R-381, JA-\_\_\_\_).

<sup>20</sup> *Id.* (R-381, JA-\_\_\_\_).

operators and consumer electronics manufacturers negotiated a “plug and play” agreement for the deployment of CableCARDS and support of CableCARD-enabled (“digital cable-ready”) retail navigation devices that the FCC heralded as a “breakthrough in relations between the cable and consumer electronics industries and the establishment of standards for digital cable-ready products.”<sup>21</sup> The FCC codified the critical points of this agreement into its rules in 2003, making cable’s obligations to support CableCARD-enabled devices legally enforceable by the FCC.<sup>22</sup>

As a result of these developments, CableCARDS were manufactured and deployed throughout the cable industry. CableCARDS debuted in July 2004 and were quickly adopted by thousands of consumers.<sup>23</sup> By early 2005, 11 major manufacturers had been certified or verified for the production of more than 140 models of “digital cable-ready” retail navigation devices compatible with CableCARDS.<sup>24</sup>

The second change from 1998 was in the broader MVPD marketplace. What in 1998 had been the “new” and “evolving” DBS service had consolidated to two networks, grown exponentially, and tripled in MVPD market share to 25%. *With over 23 million subscribers, DirecTV and EchoStar are now the second and third largest MVPDs in the nation, far larger*

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<sup>21</sup> *Order at ¶28 (R-1, JA-\_\_\_\_); NCTA Comments, p.8 (February 19, 2004)(“NCTA 2004 Comments”)(R-196, JA-\_\_\_\_). These plug and play digital cable-ready products receive all of cable’s one-way services including premium channels which are unscrambled by the CableCARD. The cable and CE industries are currently in discussions concerning a framework for interactive cable-ready products which can access cable’s “two-way” services like Video-on-Demand.*

<sup>22</sup> Cable operators subject to these rules must supply CableCARDS to customers for use with digital cable-ready products and provide additional headend support for CableCARD-enabled.

<sup>23</sup> NCTA submission, pp. 1-2 (March 7, 2005)(R-19, JA-\_\_\_\_).

<sup>24</sup> NCTA submission, p.6 (January 11, 2005)(R-45, JA-\_\_\_\_); NCTA submission, p. 1 (December 20, 2004)(R-61, JA-\_\_\_\_); NCTA submission, Attachment, p. 2 (November 22, 2004)(R-89, JA-\_\_\_\_). CE manufacturers can manufacture devices to their own specifications, and, after limited testing of their first model, are not required to have other models of their digital cable-ready products tested at a qualified test facility. They can “self-verify” compliance of subsequent models.

than either of the Petitioners.<sup>25</sup> Incumbent local telephone carriers are now entering the video market through multi-billion dollar construction of MVPD systems.<sup>26</sup> Many other entrants are energetically exploring new means of delivering video services to consumers.<sup>27</sup> Consumers nationwide, who may have at one time believed that they had only had one choice for multichannel video programming, now have at least three choices (one cable and two DBS), with more to come.<sup>28</sup>

This intensely-competitive market compels cable service providers to respond to consumer demand far more effectively than regulation ever could.<sup>29</sup> NCTA demonstrated in the record that cable operators' profitability is driven by the sales of services, not equipment.<sup>30</sup> As a general rule, cable operators' rates for equipment leased to consumers are capped by regulation.<sup>31</sup> Cable's economic interest is to increase the number and features of navigation devices that may attract and retain customers and the number of sources where consumers can obtain such equipment. NCTA Reply Comments, p.2 (December 18, 2000)(R-555, JA-\_\_\_)

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<sup>25</sup> *Annual Assessment of the Status of Competition in the Market for the Delivery of Video Programming*, Eleventh Annual Report, 20 F.C.C.R. 2755, ¶¶54-55 (February 4, 2005)(“*Eleventh Competition Report*”); see also “The Dish Cable Loves to Hate”, Multichannel News, January 24, 2005 (EchoStar has become nation's third-largest MVPD with ten million customers).

<sup>26</sup> *Eleventh Competition Report* at ¶125.

<sup>27</sup> *Id.* at ¶¶113-123, 131-134.

<sup>28</sup> *Annual Assessment of the Status of Competition in the Market for the Delivery of Video Programming*, Tenth Annual Report, 19 F.C.C.R. 1606, ¶5 (January 28, 2004)(“DBS has become the most significant national competitor to cable. Today, most consumers have the choice of least two national DBS providers.”) .

<sup>29</sup> Time Warner Reply Comments, pp. 9-10 (December 18, 2000)(highlighting that DBS places competitive pressure on cable and incentivizes cable to foster retail market)(R-553, JA-\_\_\_).

<sup>30</sup> Comments of NCTA, pp. 29-30 (November 15, 2000)(R-577, JA-\_\_\_); see also Reply Comments of NCTA, pp. 8-9 (December 18, 2000)(R-555, JA-\_\_\_); NCTA submission, fn. 10 (January 4, 2005)(R-48, JA-\_\_\_).

<sup>31</sup> NCTA submission, p.3 (January 11, 2005)(R-45, JA-\_\_\_)(citing 47 U.S.C. §543(b)(3) and 47 C.F.R. §76.923).

(with increasing competition from DBS and other service providers, cable operators have “every incentive to maximize, and not limit, the range of equipment options and distribution outlets for devices to enable customers to obtain their service.”); NCTA submission, fn. 3 (December 20, 2004) (R-61, JA-\_\_\_\_)(Given the intense competition, cable operators “must fight vigorously for every cost savings possible” to remain price-competitive with DBS providers).

The third change since 1998 was DBS’ move to *reduce* the equipment choices available to consumers. The FCC based its 1998 exemption of DBS on the fact that DBS navigation devices were available at retail from 10 different manufacturers. But in 2004, DirecTV announced it would “assume complete responsibility for the sale and distribution to retail of all DirecTV set-top boxes” so that DirecTV would have “one box, which EchoStar has.... which we will design” and that “the various consumer electronics brands currently associated with DirecTV equipment will be replaced by the DirecTV brand.”<sup>32</sup> EchoStar already offered consumers only the purchase of proprietary devices under the EchoStar brand. EchoStar and DirecTV issue the specifications to Original Equipment Manufacturers (“OEMs”) to build for “retail” exactly what the DBS provider offers when it sells equipment directly to customers. Beyond that, CE manufacturers have no rights at all to produce competitive DBS navigation devices. This arrangement also enables DirecTV, for example, to stop integrating TiVo in satellite set-tops and replace TiVo enabled devices with DVRs supplied by DirecTV’s affiliate.<sup>33</sup>

At issue in the FCC’s reopened rulemaking was whether cable operators should be required to reengineer their non-portable, integrated, set-top boxes so those boxes could use the

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<sup>32</sup> *NCTA 2004 Comments*, p.19 (R-196, JA-\_\_\_\_)(citing *Press Release*, “DirecTV Debuts New Hardware Strategy at CES 2004,” January 8, 2004).

<sup>33</sup> *See* p. 34, *infra*; *See also* “DirecTV Poised to take on TiVo,” USA Today, August 24, 2005, p.3B; “In a Challenge to TiVo, DirecTV Promotes its Own Box, NY Times, August 7, 2005, p.C5; NCTA submission, p.5, fn. 5, (January 11, 2005)(R-45, JA-\_\_\_\_)(citing “DirecTV Launches Non-TiVo Digital Recorder”, Washington Post, January 6, 2005).

same CableCARDS that retail devices use in order to make retail devices nationally marketable and portable. There was no dispute that reengineering cable's integrated set-top boxes would add no new functionality since an operator's leased boxes remain in its cable system if its customer moves elsewhere.

The cable industry estimated the direct cost to implement the integration ban at over \$1 billion.<sup>34</sup> But even at the low estimates provided by CE manufacturers who favored the ban, the costs would be hundreds of millions of dollars.<sup>35</sup> Removing the already-integrated conditional access functionalities from current products requires a major reengineering to remove the authorization and copy-control functions from the motherboard and placing them in a leased card.<sup>36</sup> In addition, cable operators would incur significant opportunity costs of diverting design, engineering, and business resources from competitive projects to a project that produced no new services and no new functionality for set-top boxes.<sup>37</sup> The imposition of these massive costs saddles the cable industry with an enormous competitive disadvantage in providing a choice of set-top boxes to price-sensitive consumers.

Integrated cable set-top boxes also could have become available at retail during these intervening years had any retailer accepted the cable industry's commitment to support that

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<sup>34</sup> NCTA submission, "Report of the NCTA Regarding Costs to Consumers", p.3, 6-7, fn. 13 (August 2, 2002)(R-470, JA-\_\_\_\_); Advance/Newhouse submission, p.3 (December 22, 2004)(R-56, JA-\_\_\_\_); NCTA submission, p.3 (November 22, 2004) (R-89, JA-\_\_\_\_)(providing expert evidence, indicating that non-integrated devices would cost \$72-\$93 more than an integrated device performing the same functions); Comcast submission, p.1 (March 14, 2003) (R-424, JA-\_\_\_\_).

<sup>35</sup> NCTA submission, p. 4 (December 20, 2004)(R-61, JA-\_\_\_\_); Advance/Newhouse submission, p.3 (December 22, 2004)(R-56, JA-\_\_\_\_)(demonstrating costs of hundreds of millions using calculations from the Intel submission dated November 17, 2004 at p.2, n.5 (R-92, JA-\_\_\_\_)); CEA submission, November 23, 2004, pp. 2-3 (R-88, JA-\_\_\_\_)(supporting Intel's calculations).

<sup>36</sup> Advance/Newhouse submission, p.3 (December 22, 2004)(R-56, JA-\_\_\_\_).

<sup>37</sup> Charter submission, p.2 (December 7, 2004)(R-76, JA-\_\_\_\_)(mandating CableCARDS in leased set-tops would divert resources away from all-digital deployments and other innovations).

option. When the Commission adopted the integration ban in 1998, it was presumed that integrated cable set-top boxes would not be available at retail because of security concerns. The Commission decided that, if retailers could not sell integrated devices, cable operators should not be able to either, to establish parity. After the FCC shifted the focus of its rules from analog to digital set-tops, it became possible (from a security perspective) to offer the same set-top boxes at retail. As a result, in 2001, the cable industry committed to support the retail offering of devices that are “identical” to cable set-top boxes.<sup>38</sup> However, CE chose not to make or market integrated set-top boxes.

Indeed, independent CE manufacturers and retailers wanted CableCARDs to use in expensive navigation devices such as digital televisions with built-in set-top box functionality, rather than low-cost set-top boxes such as those cable operators lease to their customers.<sup>39</sup> The premise cited in the *1998 Order* that an integration ban was needed to prevent cable operators from having an “effective cost advantage”<sup>40</sup> in providing low-cost set-top boxes had turned out to be a mirage.

Despite the evidence of these changed circumstances, on March 17, 2005, the FCC issued a final order that re-adopted the integration ban on cable operators, effective July 1, 2007, but once again exempted DBS providers. 47 C.F.R. § 76.1204(a)(1). The FCC acknowledged that “a prohibition on the use of integrated devices will have certain cost and service disadvantages if implemented using the hardware conditional access technology presently available,” conceding that “it is likely that consumers will face additional costs in the short term as a result of the

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<sup>38</sup> NCTA submission, p.2 (October 10, 2001)(R-515, JA-\_\_\_\_); *See also NCTA 2004 Comments*, pp.7-8 (R-196, JA-\_\_\_\_).

<sup>39</sup> NCTA submission, p.2 (January 4, 2005) (R-48, JA-\_\_\_\_)(“The actual retail devices that CE manufacturers are bringing to market cost \$1000, \$2000 and up – a market on which the lease of a CableCARD has no effect.”).

<sup>40</sup> *1998 Order*, ¶68 (R-672, JA-\_\_\_\_).

prohibition on integrated navigation devices.”<sup>41</sup> However, it concluded that “it seems likely that the potential savings to consumers from greater choice among navigation devices will offset some of the costs from separating the security and non-security functions ....”<sup>42</sup>

The Commission also recognized that “the commercial market for navigation devices used in conjunction with the distribution of digital video programming has expanded and consumers now have increased choice among navigation devices.”<sup>43</sup> But it nonetheless prohibited cable operators from offering integrated devices so that devices provided by cable operators and by retail manufacturers would all have “common reliance” on the same security technology:

We are not inclined, however, to consider any further [postponement or elimination of the integration ban] on the basis of the level of competition in the navigation device market. Absent common reliance on an identical security function, we do not foresee the market developing in a manner consistent with our statutory obligation.<sup>44</sup>

The Commission’s flat refusal to consider evidence of commercial availability of digital cable-ready navigation devices contrasted markedly with its treatment of DBS. The FCC explained that “DBS is not immune from some of the same concerns regarding constraints on independent innovation and competition that arise in the cable context.”<sup>45</sup> Yet the FCC once again exempted DBS from the integration ban. Thus while the FCC was requiring cable operators to do more and more (an integration ban on top of the “plug and play” rules) to protect the ability of third-parties to produce cable-ready devices to their liking, DBS providers had *no* obligation to support *any* retail navigation devices except their own proprietary, integrated devices built by

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<sup>41</sup> *Order* ¶29 (R-1, JA-\_\_\_).

<sup>42</sup> *Id.*

<sup>43</sup> *Id.* ¶1 (R-1, JA-\_\_\_).

<sup>44</sup> *Id.* ¶36 (R-1, JA-\_\_\_).

<sup>45</sup> *Id.* ¶38 (R-1, JA-\_\_\_).

OEMs to their specifications and sold under their own brand names.

The FCC recognized that disparate application of the integration ban could have a significant, skewing effect on free-market competition between cable and DBS services. Noting that DBS had grown quickly to become “the most significant competitor to cable on a national basis,” the Commission stated that it is “an important consideration” to try to avoid “rule based market distortions.”<sup>46</sup> Nevertheless, the Commission stated that “[w]e do not regard this proceeding, however, as providing a record on which the Commission can resolve these issues” – even as it effectively resolved them by imposing an extraordinarily burdensome rule on cable operators while exempting its two largest competitors.<sup>47</sup>

#### **4. Petition for Review.**

Charter and Advance/Newhouse jointly and timely sought judicial review of the *Order* on July 5, 2005. The Court later granted motions to intervene filed by NCTA and the Consumer Electronics Association (“CEA”).

### **SUMMARY OF ARGUMENT**

The FCC’s *Order* prohibiting cable operators from offering integrated set-top boxes violates Section 629 of the Communications Act and is arbitrary and capricious.

Congress adopted Section 629 to help consumers by *expanding* the choices available to them for navigation devices to access multichannel video programming. However, the integration ban *takes away* the option most popular among American consumers: monthly lease of a low-cost integrated set-top box.

In the first place, this “integration ban” violates Congress’ mandate that the FCC’s regulations not prohibit cable operators from offering navigation devices to consumers.

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<sup>46</sup> *Id.* (R-1, JA-\_\_\_).

<sup>47</sup> *Id.* (R-1, JA-\_\_\_).

Second, the FCC fails to provide a reasoned justification for a rule that its own order indicates will cost consumers more than they will save, and whose supposed benefits are *already* being secured by other, less-costly means. While the integration ban purports to assure that cable operators will provide adequate support to navigation devices made by third parties, cable companies have already been required to do so by the Commission's separate "plug and play" rules. When confronted with this fact, the Commission explained that the integration ban is needed because the availability of integrated devices impedes consumers from switching to other devices – but this Court had already suggested that this justification was insufficient, and it is even less compelling than it had been in 1998 due to changed circumstances.

But regardless of the rationality of a generally-applicable integration ban, the basis for the rule clearly fails in light of the FCC's decision to apply the ban to cable but not its largest competitors – the Direct Broadcast Satellite (DBS) operators which Congress made equally subject to the statute. The FCC refused to even *consider* an exemption of cable based upon the level of existing commercial availability of cable-ready navigation devices, even though Congress specifically required it to consider such evidence and even though the FCC had twice exempted DBS from the rule on those grounds. The Commission not only ignored evidence that cable has met or exceeded DBS' level of commercial availability of navigation devices but also stated that it would not be moved by such evidence even if proven.

Finally, the FCC completely failed to consider whether the intense competition in the video market effectively requires service providers to respond to consumer demand, without the need for the further imposition of the integration ban.

The FCC's readoption of the integration ban therefore violates both Section 629 and the Administrative Procedure Act's requirement of reasoned decisionmaking.

## ARGUMENT

### I. THE INTEGRATION BAN IS AN UNLAWFUL AND IRRATIONAL APPLICATION OF CONGRESS' BAR ON REGULATIONS THAT PROHIBIT MVPDs FROM OFFERING NAVIGATION DEVICES.

The first sentence of 629(a) directs Congress to assure commercial availability to consumers of converter boxes, interactive communications equipment, and other equipment used by consumers to access MVPD services. Whatever the scope of the Commission's authority to satisfy this mandate, that authority cannot extend to regulations that were specifically barred by Congress. But in adopting the integration ban, the Commission has squarely done one of the few things Congress explicitly told the FCC it could not do:

Such regulations shall not prohibit any [MVPD] from also offering converter boxes, interactive communications equipment, and other equipment used by consumers to access multichannel video programming and other services offered over multichannel video programming systems, to consumers, if the system operator's charges to consumers for such devices and equipment are separately stated and not subsidized by charges for any such service.

This argument was raised in, but not completely answered by, *General Instrument*. The *General Instrument* Court did not address whether integrated set-top boxes were "other equipment used by consumers to access multichannel video programming" covered by this provision. Instead, it only held that the FCC's determination that such devices were not "converter boxes" was a permissible one.<sup>48</sup> Although the Court noted that FCC's interpretation was "narrow" as opposed to the "more typical" meaning urged by the GI petitioners, it found the term "converter boxes" to be ambiguous and deferred to the FCC's interpretation under the

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<sup>48</sup> This debate in *General Instrument* was diverted by a hypothetical discussion of the FCC's authority to assure the commercial availability of integrated navigation devices. Stating that such an endeavor would be an "unacceptable result" to cable, *General Instrument*, 213 F.3d at 730, the Court and the parties sought to interpret Section 629 in a way that did not provide for that result. However, in 2001 NCTA committed to support the retail availability of integrated digital set-top boxes that are "identical" to those offered by cable operators. NCTA submission, p.2 (October 10, 2001)(R-516, JA-\_\_\_\_\_).

permissive “step two” standards of Chevron. *General Instrument*, 213 F.3d at 730.

This precedent is not immediately dispositive here because it did not consider whether integrated devices were covered by the phrase “other equipment used by consumers.” More importantly, this panel may not simply apply the same analysis to this broader term as *General Instrument* did to the term “converter boxes” to reach the same conclusion. Instead, it is clear from the statute, its purpose, and the FCC’s own prior interpretation of the clause “converter box ... and other equipment” that the FCC is foreclosed from asserting here that integrated converter boxes are not covered by this provision. It is beyond the realm of reasonable possibility that an integrated set-top box is neither a converter box *nor* “other equipment used by consumers” to access multichannel video programming. It is also undisputed that consumers currently use integrated set-top boxes to access cable services and that the charges for these devices “are separately stated and not subsidized by charges for any such service.”<sup>49</sup> Moreover, the integration ban is clearly contrary to Congressional intent that Section 629 *expand* the number of navigation device options available to consumers, because it *takes away* a choice from consumers that the record shows they want – a low-cost integrated device. Because Congress has spoken unambiguously to the precise issue at hand, the Court must give effect to Congress’ intent that cable operators continue to be allowed to offer integrated set-top boxes, without deference to the FCC’s contrary interpretation. *Chevron*, 467 U.S. at 842-43.

But even if the term “converter boxes ... and other equipment” is deemed ambiguous, the Commission is foreclosed from urging a narrow interpretation to exclude integrated devices because it has already adopted an expansive interpretation of this clause in the *1998 Order*:

Section 629(a) enumerates “converter boxes, interactive communications equipment, and other equipment used by consumers to access multichannel video

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<sup>49</sup> NCTA Comments, p.38 (May 16, 1997)(R-809, JA-\_\_\_\_\_).

programming and other services ...”. We believe that the statutory language of Section 629 indicates that its reach is to be expansive and that Section 629 neither exempts nor limits any category of equipment used to access multichannel video programming or services offered over such systems from its coverage. Equipment used to access video programming and other services offered over multichannel video programming systems include televisions, VCRs, cable set-top boxes, personal computers, program guide equipment and cable modems.

The FCC’s interpretation of the clause “converter boxes ... and other equipment” not only covered every conceivable navigation device, but it specifically included “cable set-top boxes” within its meaning. Given that in 1998 all set-top boxes were integrated, it is implausible that this FCC definition did not include such devices. Having taken this position in the underlying rulemaking docket, the FCC is barred from urging a different, contrary definition of “converter boxes ... and other equipment” here. *See Bowen v. Georgetown Univ. Hosp.*, 488 U.S. 204, 212-213 (1988) (declining deference because “the Secretary's current interpretation ... is contrary to the narrow view of that provision advocated in past cases”); *see also KMart Corp. v. Cartier*, 486 U.S. 281, 329 (1988) (“we owe no deference to a construction that is contrary to the interpretation of the agency”) (Scalia, J. dissenting); *City of Kansas City v. Department of Hous. & Urban Dev.*, 923 F.2d 188, 192 (D.C. Cir. 1991) (“deference is [due] the result of agency decisionmaking, and not some post hoc rationale developed as part of a litigation strategy.”). Instead, having made this interpretation in a rulemaking proceeding, the FCC can only undo it through a new rulemaking proceeding (which it has not done). *See Paralyzed Veterans of Am. v. D.C. Arena L.P.*, 117 F.3d 579, 586 (D.C. Cir. 1997) (“Once an agency gives its regulation an interpretation, it can only change that interpretation as it would formally modify the regulation itself: through the process of notice and comment rulemaking.”).

Therefore, the integration ban violates the second sentence of Section 629(a) and must be vacated.

## **II. THE FCC’S ADOPTION OF THE INTEGRATION BAN WAS ARBITRARY AND CAPRICIOUS.**

The integration ban set forth in the second sentence of 47 C.F.R. §76.1204(a)(1) must be vacated because the *Order* adopting it (1) failed to provide a coherent and reasoned explanation of its supposed rationale; (2) arbitrarily applied different decisional criteria in imposing the rule on cable but exempting DBS; and (3) failed to consider important aspects of the underlying problem the FCC stated formed the basis for the ban.

### **A. THE FCC FAILED TO DEMONSTRATE THAT ITS INTEGRATION BAN IS THE PRODUCT OF REASONED DECISIONMAKING.**

The FCC “must cogently explain why it has exercised its discretion in a given manner ... sufficient to enable us to conclude that [its decision] was the product of reasoned decisionmaking.” *State Farm*, 463 U.S. at 52. Here, the FCC has only supplied conclusory assertions, and even to the extent that it attempted to explain its rationale, it failed to spell out a “rational connection between the facts found and the choice made.” *Id.*

#### **1. The *Order* Fails To Establish that the Integration Ban Is Necessary To Effectuate Section 629 or Benefit Consumers.**

In *General Instrument*, the Court said that “[p]erhaps there are benefits that will flow to consumers from the integration ban, but the Commission did not clearly spell them out.” *General Instrument*, 213 F.3d at 732. Having been warned, the Commission could have been expected to provide more analysis and explanation in its new order. Instead, it simply repeated its past “justification” – one that the Court had previously warned was insufficient, and that was even less compelling than it had been in 1998 due to changed circumstances.

When the FCC first adopted an integration ban in 1998, there were no cable-ready navigation devices available to consumers in the retail market, no processes in place that would enable third-parties to develop such products, and arguably no clear record that the cable

industry was compelled by market forces or legal obligations to support them. By 2005, however, all of these factors had changed.

During the intervening years, the cable and CE industries engaged in an extraordinary collaborative undertaking to bring CableCARD-equipped navigation devices to the retail market, and to implement the “separate security requirement” of the *1998 Order*. These efforts resulted in a landmark agreement in 2002, under which the cable industry committed to support CableCARDS and CableCARD-equipped devices. CEA joined the cable industry in a press release announcing that the agreement “will help cable operators establish a strong presence in the retail market.”<sup>50</sup> The FCC subsequently initiated a rulemaking proceeding that resulted in adoption of its “plug and play” rules, which legally bound the cable industry to specific technical and operational commitments to facilitate the commercial availability of digital cable-ready equipment.

These rules will remain in effect regardless of whether the Court vacates the integration ban. In accordance with these rules, CableCARDS were launched in mid-2004 for use in commercially-available navigation devices. Just six months later, the record showed the commercial availability of more than 140 models of CableCARD-compatible navigation devices from 11 different CE manufacturers, with the promise of more given the significant innovation demonstrated in CE manufacturer exhibits at their January 2005 trade show.<sup>51</sup>

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<sup>50</sup> *NCTA 2004 Comments*, p.10 (R-196, JA-\_\_\_\_) citing CEA-NCTA Press Release, “Cable and Consumer Electronics Companies Reach Key Agreement on Digital TV Transition Issues,” December 19, 2002.

<sup>51</sup> NCTA submission, p. 4 (January 11, 2005)(R-45, JA-\_\_\_\_)(describing numerous new navigation device functions featured at the 2005 CES); NCTA Reply Comments, pp. 7-10 (March 10, 2004)(R-175, JA-\_\_\_\_)(“The record in this proceeding has many examples of cable company agreements and developing relationships with leading CE manufacturers and retailers – all aimed at promoting OpenCable equipment and developing new avenues of retail distribution for digital set-top boxes and other navigation devices.”).

Moreover, driven by the wider competitive marketplace, the cable industry has embraced retail. Without regulatory compulsion, cable launched Go2Broadband, a free Internet-based electronic commerce tool that enables CE manufacturers and retailers to identify a customer's local cable operator and services available so they may recommend compatible hardware to the customer.<sup>52</sup> Without regulatory compulsion, the cable industry provided extensive technical and developmental support to CE manufacturers. For example, Petitioner Charter provided technical support for CableCARDS, promotions of CableCARDS, troubleshooting of new technology issues, and free lab time for CE companies in Charter's network operations center.<sup>53</sup> Petitioner Advance/Newhouse cultivated direct relationships not only with large retailers but with the smaller CE retailers who often cater to the high-end users who are using CableCARD-enabled devices.<sup>54</sup> Thirty major manufacturers of digital televisions and related products utilized CableLabs' development testing facilities and personnel to help evaluate, develop and troubleshoot their CableCARD-enabled products.<sup>55</sup> Petitioners also entered into cooperative development agreements with CE manufacturers for the development of advanced retail devices.<sup>56</sup> The cable industry developed the Open Cable Applications Platform ("OCAP"), a middleware platform that enables cable and advanced retail devices to deliver interactive cable services. Three major CE manufacturers signed OCAP licenses by the closing date of the record, and the record was clear that more would follow. All of these developments occurred *without an*

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<sup>52</sup> CableLabs submission, p. 2 (February 3, 2003)(R-440, JA-\_\_\_\_); Joint Status Report of CEA and NCTA (Corrected Copy), p. 2 (July 24, 2003)(R-327, JA-\_\_\_\_).

<sup>53</sup> Charter submission, p.1 (December 7, 2004)(R-76, JA-\_\_\_\_).

<sup>54</sup> Advance/Newhouse submission, p.2 (December 22, 2004)(R-56, JA-\_\_\_\_).

<sup>55</sup> Reply Comments of NCTA, p.3 (March 24, 2004)(R-140, JA-\_\_\_\_).

<sup>56</sup> NCTA submission, p.6 (January 11, 2005)(R-45, JA-\_\_\_\_)("There are virtually no technical impediments to bringing two-way 'plug-and-play' devices to market. This is evident: two manufacturers – Samsung Electronics and LG Electronics – have already signed a CableLabs license enabling them to build such two-way devices."). Panasonic signed on March 11, 2005.

integration ban in effect.

In reviewing this record, the FCC agreed that “CableCARD-equipped devices are available at retail and are being used by consumers.”<sup>57</sup> This should have been a finding of critical significance, given that this result satisfied Congress’ directive to the Commission. The Commission further praised “the enormous efforts [of the cable and CE industries] in the development of technical standards related to digital cable compatibility and navigation devices.... [and their significant] progress towards the development of a retail market for consumer electronics equipment with navigation device functionality.”<sup>58</sup> However, the FCC decided that it could not consider its job completed under Section 629 because the deployment of CableCARD-equipped devices remained “nascent.” *Id.* Of course that market was nascent – CableCARDS had only been launched nine months before the *Order* was adopted. But the record indicated that the market was moving in the right direction and that the ingredients necessary for success were in place. It was arbitrary and without basis in the record for the FCC to conclude that the market would fail without an integration ban, without explaining why it would not continue its course of expansion.

NCTA explained in the reopened proceeding that the separate security requirement and the plug and play rules were proving sufficient to put the industry on a path that would effectuate Section 629, and that the integration ban and its attendant high costs for consumers were unnecessary:

In requiring digital cable systems to support POD [CableCARD]-enabled devices, the rules supercede the rationale proffered by the retailers for retaining the ban – that only if operators are required to rely on PODs themselves, then and only then will retailers and consumers be assured that POD-enabled devices sold at retail will work on cable systems. Cable operators are now obligated, as a matter of law,

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<sup>57</sup> *Order* ¶28 (R-1, JA-\_\_\_).

<sup>58</sup> *Id.* (R-1, JA-\_\_\_).

to make them work. The Agreement and the FCC's rules obviate the need for the costly, consumer unfriendly integration ban which arguably served that purpose.<sup>59</sup>

The Commission rejected NCTA's view:

Contrary to NCTA's assertion, we do not conclude that the one-way MOU and the Commission's implementing rules undermine the basis for the prohibition on integrated devices. Although cable operators now are required by law to support [CableCARDs], [CableCARD] support was not the sole rationale for adoption of the prohibition on integrated devices. More generally, the Commission found that integration presents "an obstacle to the functioning of a fully competitive market for navigation devices by impeding consumers from switching to devices that become available through retail outlets." (quoting *1998 Order*, 13 FCC Rcd at 14803).<sup>60</sup>

The FCC provided no explanation as to how the presence of cable's integrated set-top boxes impedes a consumer from switching to the now-numerous digital cable-ready navigation devices available at retail.<sup>61</sup> Moreover, it is peculiar that the FCC would rely upon this phrase from the *1998 Order*, because this Court in *General Instrument* cautioned that that phrase was insufficient to demonstrate that an integration ban was the product of reasoned decisionmaking: "This statement does not in and of itself tell us very much, without further explanation as to why consumers would be 'impeded.'" *General Instrument*, 213 F.3d at 731. The FCC was clearly on notice that it needed to do more than just assert in a conclusory fashion that the availability of integrated devices "imped[es] consumers from switching to devices that become available through retail outlets." But that phrase is the FCC's only explanation as to its belief that the

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<sup>59</sup> See *NCTA 2004 Comments*, p.8-10 (R-196, JA-\_\_\_\_\_).

<sup>60</sup> *Order* at n. 133 (R-1, JA-\_\_\_\_\_).

<sup>61</sup> In fact, consumers who now lease integrated set-top boxes from cable companies are perhaps the *least* impeded of all consumers from switching to a new device, because they can return their leased box at any time. Consumers who have made an initial up-front investment to purchase at retail an integrated DBS device or a third-party CableCARD equipped device, by contrast, may be less likely to switch to a new device because they would lose their prior investment. Moreover, the record shows thousands of consumers already have switched to commercially available CableCARD products (See NCTA submission, p.1 (December 20, 2004)(R-61, JA-\_\_\_\_\_)) and nothing in the record indicates that the availability of integrated devices is keeping anyone else from doing so.

existing market developments and operative FCC rules had not already put the market on a course that would satisfy Section 629 in the foreseeable future (if not already) *without* the additional imposition of an integration ban.

The *Order* offers a few additional passing references in support of the integration ban, but all are conclusory statements unaccompanied by an explanation of their rational connection to the facts in the record (and, as discussed in Section II.B., none were applied to DBS).

Three of the supposed justifications are designed to provide assurance that cable operators will adequately support (and not undermine) independent navigation devices. These three justifications are that an integration ban would (1) “align MVPDs’ incentives with those of other industry participants so that MVPDs will plan the development of their services and technical standards to incorporate devices that can be independently manufactured, sold, and improved upon”; (2) make it “far more likely that [MVPDs] will continue to support and take into account the need to support services that will work with independently supplied and purchased equipment”; and (3) “assure that cable operator development and deployment of new products and services does not interfere with the functioning of consumer electronics equipment or the introduction of such equipment into the commercial market for navigation devices.”<sup>62</sup>

However, these objectives are already being met through the “plug and play” rules and accompanying market developments.<sup>63</sup> This was the essence of NCTA’s contention that the

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<sup>62</sup> *Order*, ¶30 (R-1, JA-\_\_\_\_).

<sup>63</sup> See NCTA submission, p.2 (January 4, 2005) (R-48, JA-\_\_\_\_)(citing David Pogue, “Streamlined Cable TV in a Card,” New York Times article December 30, 2004 at G1, which explains that the same CableCARDS from the same system work fine with one device but less so with another, demonstrating that the problem is not with the CableCARD or the cable system, but with devices). The record is clear that forcing common reliance by leased set-tops on the CableCARDS used for retail devices does nothing to assure performance of a CE device. Under current FCC rules, CE manufacturers are not required to subject their devices to testing by a qualified lab, or to any testing comparable to what cable operators apply to their set-tops. This is

plug and play rules had mooted any need for the integration ban. And as explained above, the FCC's only response to this contention – that notwithstanding the plug and play rules, “integration ... imped[es] consumers from switching” to third-party devices – has already been considered as inadequate by this Court. Since the Commission has not provided any other explanation as to why these three CableCARD-support objectives are not already being achieved by the plug and play rules, and since its one explanation has been deemed inadequate, these three objectives cannot save the FCC's decision from being found arbitrary and capricious.

The *Order* also asserts that the integration ban is “necessary to facilitate innovation.” But the same *Order* acknowledges that innovation is thriving today even in the absence of an integration ban: “We note that innovation continues to be a hallmark of the navigation devices and digital cable-ready equipment markets.” *Order* at n. 146. For example, the FCC cited evidence from the record describing the numerous new and innovative features of new navigation devices being touted by CE manufacturers at their 2005 Consumer Electronics Show.<sup>64</sup> All of these products have been developed, and can continue to be developed, without an integration ban in effect. The FCC could not therefore reasonably or rationally conclude that an integration ban is “necessary” to facilitate innovation that already exists without the ban. Accordingly, the Commission erred by “offer[ing] an explanation for its decision that runs counter to the evidence before the agency.” *State Farm*, 463 U.S. at 43.

Moreover, the ban will chill innovation by diverting the cable industry's resources away from the development of new functionalities and sinking those resources into reengineering leased set-top boxes in a manner that will offer nothing new to cable customers except higher

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why, as the New York Times reported, some manufacturers' DTVs performed flawlessly with CableCARDs provided by a particular cable system, while others did not.

<sup>64</sup> NCTA submission, pp.4-5 (January 11, 2005)(R-45, JA-\_\_\_).

prices. The FCC has thus contravened Congress' express instruction that, in its regulations under Section 629, the "Commission avoid actions which could have the effect of freezing or chilling the development of new technologies and services."<sup>65</sup>

Finally, the *Order* states that the integration ban is designed to "promot[e] competition and bring[] more choice to consumers." But the *Order* does not explain how the ban will accomplish either of these objectives. In fact, the most obvious result of the ban is to *take away* what is now a very popular choice among consumers – the low-cost leased integrated box. This statement suffers the same infirmity recognized by the Court in *General Instrument*: it claims that the integration ban will achieve a lofty objective, but fails to provide a sufficient explanation to establish a rational connection between the facts found and the choice made.

## **2. The *Order* Fails to Establish that the Enormous Costs of the Integration Ban Are Justified.**

While the benefits of the integration ban remain unproven, the enormous costs that will result from the ban are a certainty. Although there was significant debate in the FCC's rulemaking regarding the exact quantification of the costs that the integration ban would impose, the record clearly shows that the costs to the cable industry would at least total hundreds of millions of dollars. Because cable operators lease, rather than sell, set-top boxes, and must do so at government-prescribed rates, cable operators must bear these costs up front.<sup>66</sup> In addition, implementation of the ban will divert research, engineering and other resources away from critical enterprises into a project that provides operators and their customers absolutely no

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<sup>65</sup> Joint Explanatory Statement of the Committee of Conference, S. Conf. Rep. 104-230, 104th Cong., 2d Sess. at 181 (1996)(*"Conference Report"*).

<sup>66</sup> NCTA submission, p.2 (December 20, 2004)(R-61, JA-\_\_\_\_)(*"With a leased set-top box, the up-front investment rests with the cable operator, who leases the box at a government-prescribed price, and must replace it when the customer tires of its features and wants the next new feature – HD, or a DVR, or more storage capacity."*)

benefit. Although the FCC may have the discretion, when authorized, to adopt a regulation that imposes costs on the cable industry because such costs could produce some benefit to consumers, the agency cannot demonstrate that such a regulation is the product of reasoned decisionmaking *unless* it can articulate a reasonably clear explanation that the social benefits of the regulation will outweigh its costs.<sup>67</sup> This it utterly failed to do.

The FCC acknowledged that the cable industry will bear unspecified costs and consumers will pay higher prices at least during some “short term” of unspecified length, but it hypothesized that “it seems likely that the potential savings to consumers from greater choice among navigation devices will offset some of the costs from separating the security and non- security functions of either MVPD-supplied devices or those that might otherwise be made available through retail outlets.”<sup>68</sup> This rationale cannot withstand scrutiny.

First, the FCC has failed to articulate a reasoned justification for its rules. The FCC stated that, “although we wish to place as little of the cost burden resulting from the ban on the public, the mere fact that consumers will bear some of the costs resulting from the imposition of the integration ban is not a sufficient justification to eliminate the ban.”<sup>69</sup> However, in a reopened rulemaking proceeding, an agency cannot simply readopt a rule on the grounds that there are insufficient grounds to eliminate a rule; any rule readopted must also be supported by reasoned decisionmaking. *See Harris v. FAA*, 353 F.3d at 1011. This is especially true here, where the Court in *General Instrument* previously warned the FCC that its reasoning was wanting the first time around. Yet the FCC has provided nothing new besides conclusory

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<sup>67</sup> *USTA v. FCC*, 290 F.3d 415, 429 (D.C. Cir. 2002)(“[N]othing in the Act appears a license to the Commission to inflict on the economy the sort of costs [inherent in imposing access obligations] under conditions where it has no reason to think doing so would bring on a significant enhancement of competition”).

<sup>68</sup> *Order* ¶29 (R-1, JA-\_\_\_).

<sup>69</sup> *Id.* ¶27 (R-1, JA-\_\_\_).

statements that none of the new information proves that the rule is wrong.

Second, given that the FCC at best only thinks that it “seems likely” that “potential savings” will offset “*some* of the costs,” it follows that even under the optimistic scenario some costs will not be offset. That the huge costs of the integration ban will at most be only *partially* offset by countervailing benefits means, *ipso facto*, that under the FCC’s stated analysis the ban is a net negative for consumer welfare. It may be that there is more to the equation, but if so, the FCC has not spelled it out in its *Order*.

Ultimately, the Court need not determine whether the record evidence relied upon by NCTA is sufficient to show that the integration ban is no longer needed, or whether the benefits of the integration ban (if any) outweigh its costs, or whether the integration ban, even if not necessary, remains a reasonable option for the FCC to adopt. Instead, the instant review first must turn upon the fact that the FCC has once again failed to explain how or why it reached the conclusion that “the availability of integrated devices ‘impedes consumers from switching to devices that become available through retail outlets,’” or that any of its other purported justifications for the ban would not be achieved under the plug and play rules even without an integration ban. Because of its failure to do so, the Court cannot conclude that the FCC’s adoption of the integration ban is the product of reasoned decisionmaking. The *Order* must therefore be vacated as arbitrary and capricious.

**B. THE ORDER ARBITRARILY APPLIED DIFFERENT DECISIONAL CRITERIA IN IMPOSING THE INTEGRATION BAN ON CABLE BUT NOT DBS.**

Even if the Court were to find that the FCC had adequately justified an integration ban as a general matter, the Court should nonetheless conclude that the *Order* is arbitrary and capricious in its disparate treatment of cable and DBS.

When the FCC first adopted the integration ban in 1998, DBS customers could purchase

set-top boxes produced by 10 different manufacturers, whereas cable customers could not obtain set-top boxes at retail at all. By contrast, when the FCC readopted the integration ban in March 2005, the cable industry was supporting more than 140 third-party cable-ready retail navigation devices from 11 different manufacturers, while DBS was pushing new customers to the purchase of the DBS suppliers' own *integrated* proprietary devices to the exclusion of all other options.<sup>70</sup> But rather than analyze these changed circumstances, the FCC insisted on the integration ban for cable no matter what showing cable could make regarding commercial availability. What is *most* relevant for judicial review is *not* that cable had undoubtedly equaled or exceeded the threshold that the FCC believed sufficient to exempt DBS in 1998 and again in 2005, yet was arbitrarily refused similar treatment; instead, what is fatal to the FCC's *Order* is that it refused to even consider an exemption of cable – whatever the evidence – on the same grounds that the FCC had now twice exempted DBS.

“Government is at its most arbitrary when it treats similarly situated people differently.” *Etelson v. OP.*, 684 F.2d 918, 926 (D.C. Cir. 1982). Whatever the FCC's discretion in evaluating commercial availability under Section 629, it does not have the right to apply different standards in deciding whether to regulate cable and DBS, when Congress made all MVPDs subject to the same statute. This Court has “long held that [the FCC] must provide adequate explanation before it treats similarly situated parties differently.” *Petroleum Communications, Inc. v. FCC*, 22 F.3d 1164, 1172 (D.C. Cir. 1994) (citing cases). This Court

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<sup>70</sup> Although DBS devices have smart-cards that plug into the device, the device is still integrated under the standards of the integration ban because its proprietary security remains embedded in the hardware of the device. *1998 Order*, ¶¶10, 59 (R-672, JA-\_\_\_\_)(distinguishing smart cards from separable security and noting DBS industry opposition to separate security requirements); *Reconsideration Order*, ¶¶36-37 (R-628, JA-\_\_\_\_)(declining to treat smart-cards as satisfying requirements for separate security and stating that DBS would not be subject to rule requiring separate security).

recently elaborated on this standard, saying that “[w]here an agency applies different standards to similarly situated entities and fails to support this disparate treatment with a reasoned explanation and substantial evidence in the record, its action is arbitrary and capricious and cannot be upheld.” *Burlington Northern*, 403 F.3d at 776-777. As demonstrated below, the FCC has failed to provide either of these required elements in support of its decision to apply very different standards to DBS and cable in reimposing the integration ban on cable.

The Commission’s disparate treatment of cable and DBS warrants particular skepticism in light of the purpose of Section 629. By allowing DBS to sell its own integrated devices, and simultaneously barring cable from offering its own integrated devices, the FCC ensured that consumers who want an integrated device will only have one choice – the integrated device offered by DBS. This is a peculiar means of implementing a statute whose purpose was to expand consumer choice, and which applies equally to all MVPDs, including DBS and cable. The *1998 Order* found that “Congress did not exclude DBS from the reach of Section 629, even though the competitive state of DBS services was known at the time of the enactment of the 1996 Act.”<sup>71</sup> It further explained that:

We disagree with the comments of several parties that Section 629 should apply only to cable television systems. There is no basis in the law, or the record of this proceeding, to support a conclusion that the statutory language does not include all multichannel video programming systems. Our reading of the law is that consumer choice in navigation devices for all multichannel video programming systems was mandated by Congress when it enacted Section 629.<sup>72</sup>

The Commission must therefore bear a heavy burden in justifying its decision to impose costly regulations upon the cable industry under Section 629 while exempting DBS.

Moreover, the FCC’s decision to adopt new, uneven regulations is particularly inexplicable in

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<sup>71</sup> *1998 Order*, ¶1112 (R-672, JA-\_\_\_).

<sup>72</sup> *1998 Order*, ¶122 (R-672, JA-\_\_\_).

light of its landmark Wireline Broadband Order, adopted not long after the Order at issue here. There the FCC proclaimed that “we should regulate like services in a similar manner” to promote market-based investment decisions, not ones driven by regulatory disparities,<sup>73</sup> and it emphasized the importance of “creat[ing] a regime that is technology and competitively neutral.”<sup>74</sup> While it is true that many disparate regulations exist under the Communications Act, these differences are in most cases based on regulations rooted in an earlier era, where one type of entity is governed by one statute and another type by a different statute. It is quite another thing for the FCC to create new regulatory disparities where none previously existed, especially between entities all subject to the same statutory provision (in this case, Section 629) rather than different provisions under different titles. That the Commission would do so here without any analysis of the impact of this disparity on the competitive market should at a minimum invite skepticism as the Court considers the rationality and legality of the integration ban.

**1. The FCC’s Adoption of a One-Sided Integration Ban in 2005 Cannot Be Justified Based Upon Comparison of the Availability of DBS and Cable Navigation Devices.**

The only proffered premise of the *Order* for applying the separate security requirement and integration ban to cable but not DBS is simple: “geographically portable” DBS-ready navigation devices could be purchased at retail, but cable-ready devices could not.<sup>75</sup> This premise may have been true in 1998, but it was not true when the FCC readopted the integration ban in 2005.

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<sup>73</sup> *Appropriate Framework for Broadband Access to the Internet over Wireline Facilities*, Report and Order, 20 F.C.C.R. 14853, ¶45.

<sup>74</sup> *Id.* ¶3.

<sup>75</sup> *Order* ¶38 (R-1, JA-\_\_\_).

**a. Cable-Ready Navigation Devices Are Commercially Available in 2005.**

In 1998, a retail market for cable set-top boxes did not exist. But at the close of record in 2005, more than 140 models of “digital cable-ready” navigation devices were being deployed by 11 different well-known, major manufacturers: Hitachi, LG Electronics (Zenith), Mitsubishi, Panasonic, Philips, Pioneer, Samsung, Sharp, Sony, Thomson, and Toshiba.<sup>76</sup> These navigation devices are manufactured, marketed, priced and distributed directly by companies unaffiliated with the cable provider, and can include “other non-cable features or functionalities, limited only by the imagination of the CE [consumer electronics] manufacturer.”<sup>77</sup>

Although the Act only requires that the FCC assure commercial availability of retail devices, and not that consumers actually choose to use them, the record is clear that consumers are using these new navigation devices.<sup>78</sup> Motorola reported that “[m]any CE manufacturers are rolling out dozens of such products this year and expect to sell up to one million of these devices in the coming months, even in the absence of a ban on integrated devices.”<sup>79</sup> The FCC’s *Order* agreed that “CableCARD-equipped devices are available at retail and are being used by consumers.”<sup>80</sup>

By contrast, between 1998 and 2005, DBS moved in the opposite direction to *reduce* the choices available to consumers. In 1998, the FCC based its exemption of DBS on the fact that

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<sup>76</sup> NCTA submission, p.6 (January 11, 2005)(R-45, JA-\_\_\_\_); NCTA, November 22, 2004, Attachment, at 2.

<sup>77</sup> NCTA submission, pp. 1-2 (January 4, 2005)(R-48, JA-\_\_\_\_).

<sup>78</sup> CableCARDs were first rolled out in the consumer market in July 2004, and the number of cards in use has grown from 700 initially to 10,000 by late 2004, more than 27,000 at the close of the record, and more than 80,000 as of late 2005. NCTA submission, Attachment p.1 (September 30, 2004)(R-107, JA-\_\_\_\_); NCTA submission, p.8, fn.8 (January 11, 2005)(R-45, JA-\_\_\_\_); NCTA submission, p.2 (March 7, 2005)(R-7, JA-\_\_\_\_); NCTA Report on Two-Way (Interactive) Digital Cable-Ready Television, pp. 5, 19 (November 30, 2005).

<sup>79</sup> Motorola submission, p.2 (November 4, 2004)(R-94, JA-\_\_\_\_)

<sup>80</sup> *Order* ¶28 (R-1, JA-\_\_\_\_).

DBS navigation devices were available at retail from 10 different manufacturers. By 2005, however, DBS providers had moved to equipment strategies that offered consumers only the “choice” of a proprietary, navigation device with integrated security, marketed under the DBS provider’s own brand. DirecTV explained its new hardware and distribution strategy: “[O]ur main move is to have one box, which EchoStar has.... which we will design ... so we can get all the possible benefits of mass manufacturing,”<sup>81</sup> and that “the various consumer electronics brands currently associated with DirecTV equipment will be replaced by the DirecTV brand.”<sup>82</sup> In other words, the DBS providers now offer a choice only between the purchase of their proprietary, standardized, integrated boxes either from a retailer or the DBS provider directly.<sup>83</sup>

In DBS’ present model, CE manufacturers have no rights at all to produce DBS devices except to the extent DBS providers order from them to build as suppliers to be sold under the DBS provider’s brand, with the DBS provider’s specifications. For example, DirecTV used to include TiVo in its set-top box. TiVo warned its investors that it was completely at the mercy of DirecTV,<sup>84</sup> and its fears came true – DirecTV is replacing TiVo in favor of new DirecTV-branded DVRs produced by DirecTV’s affiliate NDS.<sup>85</sup> DirecTV is widely expected to terminate its relationship with TiVo when their current agreement expires in 2007, shutting TiVo

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<sup>81</sup> *NCTA 2004 Comments*, pp. 18-19 (R-196, JA-\_\_\_\_)(quoting DirecTV).

<sup>82</sup> *NCTA 2004 Comments*, p.19 (R-196, JA-\_\_\_\_)(citing *DirecTV Press Release*, “DirecTV Debuts New Hardware Strategy at CES 2004,” January 8, 2004).

<sup>83</sup> NCTA submission, pp. 3-4 (March 7, 2005)(R-7, JA-\_\_\_\_).

<sup>84</sup> NCTA submission, pp. 6-7 (January 4, 2005)(R-48, JA-\_\_\_\_). (citing TiVo Inc. SEC Form 10-K filing for the fiscal year ended January 31, 2004, page 34, disclosing that TiVo is “highly dependant on [its] relationship with DirecTV,” and that its business will be harmed if its “current agreement with DirecTV expires without being renewed, amended or replaced”).

<sup>85</sup> NCTA submission, p.5, fn.5 (January 11, 2005)(R-45, JA-\_\_\_\_)(citing “DirecTV Launches Non-TiVo Digital Recorder”, *Washington Post*, January 6, 2005); *See* “DirecTV Poised to take on TiVo,” *USA Today*, August 24, 2005, p.3B; *See* “In a Challenge to TiVo, DirecTV Promotes its Own Box,” *New York Times*, August 7, 2005, p.C5.

out from the millions of DirecTV subscribers altogether.<sup>86</sup> TiVo responded by developing a retail CableCARD-enabled high-definition cable DVR, a project it expects to be successful whether there is an integration ban or not.<sup>87</sup>

The FCC cannot rationally or reasonably conclude that the growing market in cable navigation devices compares unfavorably with the DBS industry's complete lack of obligation or commitment to independent retail navigation devices. Even without the integration ban, independent, unaffiliated CE manufacturers have legally-enforceable rights under the "plug and play" rules that enable them to develop competing cable-ready navigation devices.<sup>88</sup> It makes absolutely no sense, and is arbitrary and capricious, for the FCC to conclude simultaneously that it is necessary to adopt a separate security requirement and integration ban to protect CE manufacturers from cable operators but not from DBS (which is shutting competitive CE products out of its markets completely). Given the record evidence, the FCC has failed to provide a reasoned explanation, much less one based on substantial evidence in the record, that could justify imposing further, highly burdensome regulations on cable but not DBS.

The arbitrariness of this aspect of the FCC's *Order* is evidenced not only by its failure to rationally connect these critical facts to the decisions it made, but also by its deliberate refusal to even consider the facts. The Commission not only ignored the record evidence that there are more cable retail options than DBS options today, but it also unequivocally stated that it would not be moved by such evidence even if proven. The *Order* held that no matter what the retail cable options were, and no matter what future evidence of retail cable options could be

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<sup>86</sup> NCTA submission, p.7, n.18 (January 4, 2005)(R-48, JA-\_\_\_\_).

<sup>87</sup> *Order*, ¶34, fn.146 (R-1, JA-\_\_\_\_). The Commission cited the development of TiVo's new CableCARD-equipped navigation devices as compelling evidence that deferral of the integration ban would not adversely affect innovation in digital cable-ready equipment.

<sup>88</sup> See p.26, *supra*.

presented, the FCC would still insist on an integration ban for cable.<sup>89</sup> As discussed in Section II.C.1. below, the FCC’s refusal to consider this important evidence is itself arbitrary and capricious. But to refuse to consider this evidence for cable while relying on it to exempt DBS is especially arbitrary and therefore unlawful.

**b. The CableCARD Navigation Devices Now Available at Retail Are at Least as Portable as DBS Devices.**

The second factor cited by the FCC in both orders for exempting DBS was its finding that retail DBS devices are “geographically portable.”<sup>90</sup> But today, all CableCARD-enabled devices are portable geographically *and* interoperable among cable systems, meaning, for example, that a consumer that purchases one of these devices can use it on an Advance-Newhouse system using Scientific-Atlanta security technology and then move to a new home and use it on a Charter system using Motorola security technology.<sup>91</sup> While the integrated set-top boxes cable operators lease to consumers are not geographically portable, there is no need for such portability, since consumers do not own such devices and return them to the cable operator when they move.

DBS devices, meanwhile, are still not interoperable from one DBS service provider to another.<sup>92</sup> What is important for purposes of judicial review is that the FCC exempted DBS because its devices were geographically portable, though not interoperable, whereas it subjected cable to the integration ban despite the fact that retail CableCARD-equipped navigation devices are geographically portable *and* interoperable.<sup>93</sup> The FCC has failed to provide a reasoned

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<sup>89</sup> *Order*, ¶36 (R-1, JA-\_\_\_\_)

<sup>90</sup> *Id.*

<sup>91</sup> NCTA submission, pp. 1-2 (January 4, 2005)(R-48, JA-\_\_\_\_).

<sup>92</sup> NCTA submission, p.3-4 (March 7, 2005)(R-7, JA-\_\_\_\_) (DBS “equipment is not portable across different provider’s systems; i.e., a consumer cannot buy an EchoStar set-top box and use it with a DirecTV system and vice versa.”).

<sup>93</sup> For example, in 1999 the Commission noted the “legitimate distinctions” between DBS and other MVPDs and “reiterate[ed]” its view that “because DBS are widely available to consumers

explanation, much less one based on substantial evidence in the record, that could justify its determination that the criterion of portability supports exemption of DBS but further regulation of cable now.

## **2. The One-Sided Imposition of the Integration Ban Would Have Serious Consequences for the Cable Industry.**

Although courts do not require parties injured by disparate treatment by an agency to prove damages before vacating the agency's order, the significant impact of the integration ban when applied only to cable highlights the arbitrariness of the FCC's decision.

While there was significant debate in the FCC's rulemaking regarding the exact quantification of the costs that the integration ban would impose, two points are clear from the record: (1) the costs to the cable industry would at least total hundreds of millions of dollars and (2) the costs to cable's two largest competitors, DirecTV and DISH Network, would be zero, since the Commission exempted DBS from the rule. In a dynamic industry in which players constantly vie to stay ahead of highly-innovative competitors, there is an enormous opportunity cost to dedicating such massive resources to a project with no return benefit to cable operators or their customers.<sup>94</sup> The record evidenced that "a large and growing proportion of the finite technical resources of cable industry suppliers and of cable operators will need to be dedicated toward meeting" the integration ban deadline.<sup>95</sup> The massive undertaking to roll out millions of

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at retail from multiple vendors, as compared to equipment for other MVPD services, *particularly cable operators*, there is justification for not applying the rule requiring separation of security functions to DBS services." *Reconsideration Order* at ¶37 (R-628, JA-\_\_\_\_).

<sup>94</sup> See NCTA submission, p.2 (January 11, 2005)(R-45, JA-\_\_\_\_) ("Today, DBS is exempted from the rule, does not incur this cost, and can innovate rapidly. . . . In this intensely (and increasingly) competitive environment, cable operators should not be required to divert the development dollars and resources that should be going into new features and new services to a set-top engineering redesign that provides no consumer benefit and only adds to consumer cost.").

<sup>95</sup> Comcast submission, pp. 1-2 (January 19, 2005)(R-40, JA-\_\_\_\_).

non-integrated set-top boxes will thus will divert financial and other resources from future projects,<sup>96</sup> while DBS will remain free to devote its resources to developing new features and less-expensive equipment to try to attract more consumers away from cable.<sup>97</sup>

While the regulations governing leased set-top box rates would permit cable providers to increase set-top rates by approximately \$2-3 per month per box, passing though increased costs to consumers for “new” boxes which do not provide them with any new functionalities saddles the cable industry with an enormous competitive disadvantage in providing set-top boxes to price-sensitive consumers.<sup>98</sup> The *Order* provides no evidence that the Commission considered these serious consequences that result from its arbitrary imposition of the separate security requirement and integration ban on cable but not DBS, even though the FCC had promised to “complete a reassessment of the state of the navigation devices market,” and “to review the effectiveness of the rules and consider any necessary changes” based on comments it specifically solicited on “the development of a commercial retail market for navigation devices, and on the economic impacts and costs associated with the requirement.”<sup>99</sup>

### **3. All Other Stated Rationales for the Integration Ban Reflect that the FCC Arbitrarily Held Cable to a Different and More Stringent Standard than DBS.**

The *Order* makes other passing references to possible justifications for an integration ban on cable. As discussed in Section II.A.1 above, none are sufficiently explained to justify the ban.

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<sup>96</sup> Comcast submission, p.1 (February 3, 2005)(R-34, JA-\_\_\_).

<sup>97</sup> Comcast, Time Warner, and Microsoft submission, p.1 (March 4, 2005)(R-22, JA-\_\_\_) (“implementing the integration ban could unnecessarily raise prices for consumers, place cable at a cost disadvantage with competing multichannel video programming distribution services, and further impede the kinds of collaborative efforts between CE, IT, and cable industries that are needed to devise more forward-looking and effective solutions to the issues that the integration ban was thought to address.”)

<sup>98</sup> NCTA submission, n.3 (December 20, 2004)(R-61, JA-\_\_\_).

<sup>99</sup> *2003 Extension Order*, ¶3 (R-381, JA-\_\_\_), citing *2000 FNPRM at 15 F.C.C.R. 18202, 18203* (R-595, JA-\_\_\_).

But the even more significant failing of the FCC’s decision was that it forced cable operators to support the rationale while letting DBS completely off the hook.

The Commission’s initial premise in adopting rules under Section 629 in 1998 was to establish the initial commercial availability of navigation devices. Under this premise, the Commission concluded it was necessary to regulate cable to create this new market, but unnecessary to regulate DBS because the initial commercial availability of DBS devices had already happened. As demonstrated above, if that premise had been rationally re-applied in the 2005 *Order*, both cable and DBS would be exempt from the ban because both cable and DBS services can now be accessed by consumers using commercially-available navigation devices.

The *Order* also suggests that the integration ban is appropriate to *sustain* a retail market by “facilitat[ing] innovation,” “align[ing] MVPDs’ incentives” with those of retail participants, “continu[ing] to support” retail,” and “assur[ing] that cable operator development and deployment of new products and services does not interfere with the functioning of consumer electronics equipment or the introduction of such equipment into the commercial market for navigation devices.”<sup>100</sup> But if it is necessary for these reasons to have an integration ban in place to sustain ongoing commercial availability of *cable* devices, the FCC was required to provide a reasoned explanation as to why those same reasons do not apply equally to assure ongoing availability of *DBS* devices, which are also covered by Section 629. The FCC cannot permissibly assume, without evidence or analysis, that Section 629 requires the Commission to adopt draconian prophylactic measures for cable to assure ongoing innovation and synchronize incentives, while granting DBS a permanent exemption with none of the supposed protections

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<sup>100</sup> *Order*, ¶30 (R-1, JA-\_\_\_\_).

described above based solely on evidence of current commercial availability (which in any event cable has equaled or exceeded).

In other words, it is clear that the Commission subjected cable to a series of tests not applied to DBS in determining whether an integration ban is necessary. DBS was exempted after clearing its first hurdle (initial commercial availability), but in cable's path the Commission laid hurdle after hurdle after hurdle. Whatever the appropriate test for determining whether DBS should be subject to an integration ban, cable providers must be subject to the same test.

"Elementary even-handedness requires that if all five factors must be met by one petitioner, then all five factors must be met by the next." *Airmark Corp. v. FAA*, 758 F.2d 685, 692 (D.C. Cir. 1985) (vacating agency decision where "different decisional criteria" were applied in determining whether to exempt various carriers from an agency regulation). Here, the FCC applied very different decisional criteria, despite the fact that Congress subjected both cable and DBS services to Section 629.

"Where an agency applies different standards to similarly situated entities and fails to support this disparate treatment with a reasoned explanation and substantial evidence in the record, its action is arbitrary and capricious and cannot be upheld." *Burlington Northern*, 403 F.3d at 777. The FCC has failed to provide any "reasoned explanation" for its decision to exempt DBS upon a mere showing of retail availability of any kind, while demanding more from cable. Not only has the *Order* failed to back up its disparate standards with citations to "substantial evidence in the record," but the substantial evidence in the record suggests, if anything, that cable providers were *at least* as entitled to an exemption in March 2005 as were the two DBS providers. Thus, the FCC's decision to saddle cable companies with a significant and costly regulation while exempting its two largest competitors, DirecTV and EchoStar, fails

to make a “rational connection between the facts found and the choice made.” *State Farm*, 463 U.S. at 43. As NCTA explained to the FCC, “while we did not urge imposition of the Integration Ban on DBS providers or others..., there is no longer any economic or legal basis for singling out cable operators as the only video provider subject to the Integration Ban.”<sup>101</sup> The *Order* therefore is unlawful, arbitrary and capricious, and an abuse of discretion and must be vacated.

**C. THE FCC ARBITRARILY IGNORED IMPORTANT ASPECTS OF THE PROBLEM.**

Agency orders are also arbitrary and capricious where they have “entirely failed to consider an important aspect of the problem.” *State Farm*, 463 U.S. at 43. The FCC has done exactly that by (1) refusing to consider *any* amount of evidence of commercial availability as a basis for relieving cable of the integration ban and (2) failing to articulate any consideration as to whether an integration ban remains necessary in light of the intense competition for video programming that now exists nationwide.

**1. The FCC Refused To Consider Eliminating the Integration Ban for Cable Based Upon Evidence of Commercial Availability of Cable-Ready Navigation Devices.**

While agencies are always obligated by the APA to consider important aspects of the problem being addressed in a rulemaking proceeding, a failure of that obligation is especially arbitrary when the “important aspect” that the agency failed to consider is the specific issue that the statute being implemented directs the agency to address. That is exactly what the FCC has done here in refusing to consider the “the level of competition in the navigation device market” as a basis for determining whether the integration ban is necessary.

Inexplicably, the Commission held that it would insist, now and in the future, upon an integration ban *regardless* of the extent of commercial availability of cable-ready navigation

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<sup>101</sup> NCTA submission, pp. 1-2 (March 7, 2005)(R-19, JA-\_\_\_\_\_).

devices.<sup>102</sup> The Commission’s reasoning is circular and illogical. The statute calls for the Commission to “assure the commercial availability” of navigation devices offered by parties other than MVPDs. Congress explicitly told the Commission to consider such evidence:

One purpose of this section is to help ensure that consumers are not forced to purchase or lease a specific, proprietary converter box, interactive device or other equipment from the cable system or network operator. Thus, in implementing this section, the Commission should take cognizance of the current state of the marketplace.<sup>103</sup>

The FCC’s decision to insist upon an integration ban no matter what the evidence of commercial availability therefore is arbitrary and capricious because it “entirely failed to consider an important aspect of the problem” that Congress intended to be at issue in any Section 629 rulemaking proceeding. *State Farm*, 463 U.S. at 43.

## **2. The FCC Failed To Consider the Impact of Vigorous Competition in the MVPD Market.**

A second critical and arbitrary oversight was the FCC’s failure to articulate any consideration as to whether the integration ban remained necessary (if it ever was) in light of the dramatic intensification of multi-platform competition in the multichannel video programming market. As noted above, DirecTV and EchoStar are now the second and third largest MVPDs in the nation, and incumbent local telephone companies are now entering the video market through multi-billion dollar construction of new fiber networks. In a non-competitive video market, it is conceivable that a monopolist MVPD could favor its own navigation devices by disfavoring or preventing access to its services from third-party navigation devices. However, this cannot be a successful strategy in a competitive market, because competition compels cable operators to respond to consumer demand. NCTA clearly presented this argument to the FCC:

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<sup>102</sup> *Order*, ¶36 (R-1, JA-\_\_\_).

<sup>103</sup> *Conference Report*, 181.

[I]n today's marketplace, cable operators are driven by another powerful economic imperative – intense competition from DBS in the marketing of video services to both current and potential cable customers. This pressure gives cable operators every incentive to maximize, rather than limit, the range of functionally-rich equipment options and distribution outlets for equipment that enables consumers to access their services. And, when cable customers acquire their cable navigation device at retail, cable operators have even more incentive to make certain such devices work on their systems so that these customers can access all of the services they can access with the operators' set-top boxes. Otherwise, of course, cable operators will be unable to sign up these customers for additional services, or, indeed, prevent such customers from switching to DBS or other MVPD alternatives.

....

Cable operators have spent billions of dollars upgrading their facilities and building a platform for advanced digital services. Recovery of this massive infrastructure investment is dependent on cable operators' ability to create new products and services that will retain existing customers and attract new ones in a fiercely competitive marketplace. Again, if cable operators do not ensure that commercially-available, [CableCARD]-enabled devices work on their systems, those disappointed customers can – and likely will – move to DBS.<sup>104</sup>

The *Order* completely fails to address or even acknowledge NCTA's valid argument that vibrant intermodal competition has displaced any remaining justification for the integration ban.

This Court has previously found that the FCC's failure to consider the impact of intermodal competition is an abuse of discretion. In *USTA v. FCC*, the Court vacated the Commission's rules requiring incumbent local telephone carriers to unbundle the high frequency portion of their local loops to competitors for the provision of broadband services. The Court found fault in the sufficiency of the Commission's analysis because it had "completely failed to consider the relevance of competition in broadband services coming from cable (and to a lesser extent satellite)." *USTA v. FCC*, 290 F.3d 415, 428 (D.C. Cir. 2002). See also *Time Warner Entertainment Co. v. FCC*, 240 F.3d 1126, 1134 (D.C. Cir. 2001)(recognizing that increased competition from DBS decreases the ability of cable operators to exercise market power, and therefore disapproving the FCC's failure to account for the impact of DBS competition in

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<sup>104</sup> NCTA Reply Comments, pp. 8-9 (March 10, 2004)(R-175, JA-\_\_\_\_\_).

establishing horizontal ownership rules).

To warrant vacatur, Petitioners need not establish that the competitive MVPD market makes the integration ban unnecessary, nor that it was unreasonable for the FCC to conclude that the ban was necessary under the circumstances. What is relevant is that the *Order*, as written, has entirely failed to address this important aspect of the relevant question. Because it has, it is arbitrary and capricious and must be vacated.

### CONCLUSION

The *Order* is arbitrary and capricious and is in conflict with Section 629(a) of the Communications Act. The Court should therefore grant the petition for review and vacate the second sentence of 47 C.F.R. §76.1204(a)(1).

Respectfully submitted,

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## **CERTIFICATE OF COMPLIANCE**

Pursuant to Federal Rule of Appellate Procedure 32(a)(7)(B) and (C), the undersigned certifies that this brief complies with the type-volume limitation for a principle brief. Exclusive of the portions exempted by Federal Rule of Appellate Procedure 32(a)(7)(B)(iii), this brief contains 13,993 words. This certificate was prepared in reliance on the word-count function of the word-processing system (Microsoft Word 2003) used to prepare this brief.

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John D. Seiver

## CERTIFICATE OF SERVICE

I do hereby certify that on December 27, 2005, I caused a true and correct copy of the foregoing Initial Brief of Petitioners and Intervenors National Cable & Telecommunications Association to be served via electronic mail and U.S. mail, first class postage prepaid, on the following:

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