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Title: Developing Master Communications Ordinances of Municipal Franchising Rights as New Entrants Emerge

by

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Developing Master Communications Ordinances of Municipal Franchising Rights as New Entrants Emerge

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Adrian E. Herbst

Adrian Herbst heads the Minneapolis office of The Baller Herbst Law Group. For more than 35 years he has been on the cutting edge of cable and telecommunications matters, providing regular consulting and legal assistance to municipalities throughout the United States. This has included the initial franchising processes for cable communications as well as renewals, transfers of ownership, and a wide-range of administrative enforcement matters and development of local programming and issues related to local programming. Recently, his work has expanded with the broadband services offered in cable and telecommunications systems to include planning, competition policy, and internet services.

He has served as a key member of many national organizations in programs to provide assistance to local governments, including International Municipal Lawyers Association (IMLA), National Association of Telecommunications Officers and Advisors (NATOA), the Alliance for Community Media and the National League of Cities (NLC). He has served in many capacities on behalf of these national organizations, including developing model ordinances for IMLA and chairing a specialized rights-of-way taskforce for NATOA that developed policies and guidelines for local units of governments throughout the country. He has served as President of the Minnesota Trial Lawyers Association and Vice President of the League of Minnesota Cities and is also a member of various other legal organizations including the Federal Communications Bar Association, and the Telecommunications Committee of the Minnesota State Bar Association.

Mr. Herbst has a unique background in municipal and governmental law and policy, having been a full-time City Attorney and elected City Councilman for 16 years for the City of Bloomington, Minnesota. While serving as City Attorney, Mr. Herbst led a group that was instrumental in the development of the initial franchises for cable services. As a result of this experience, he advised many municipal organizations both on the state and national level to help initiate procedures and guidelines for cable franchising. Further, because of this unique background, he was selected to serve as General Counsel for the Economic Development Authority for the City of Bloomington, Minnesota and was instrumental in the acquisition of land for development, public financing, and spearheaded the creation, development, and negotiation of a development agreement that led to the development of the Mall of America, the largest single shopping mall and attraction center in the country.

Mr. Herbst's cable television and telecommunications services to clients include the following:

- Initial franchising
- Refranchising/renewals
- Franchise administration and enforcement
- Transfer or sale of ownership
- Feasibility studies of construction of municipal fiber optic networks
- Municipal ownership
- Performance audit
- Technical review
- Financial audits
- Franchise fee audit

- Rate regulation
- Litigation
- Negotiation
- Ordinance drafting
- Non-profit access corporations
- Public, educational and governmental operations
- Institutional network, voice, video, and data systems operations
- Programming agreements
- Community needs assessment
- Customer service standards
- Municipal rights-of-way issues
- Telecommunications planning
- Municipal websites and “E” Government
- Internet related matters, including voice over IP
- Wireless services and local ordinances and zoning
- FCC Proceedings
- Cable and Telecommunications Legislation

BACKGROUND

The federal Cable Act establishes minimum requirements for local franchises applicable to cable services. It also provides that a franchise must not be exclusive.

Telephone companies like Bell South, SBC and Verizon are starting to provide cable service. While this will provide competition to existing cable service providers, the franchising authority of local governments is threatened by legislative efforts at a national level and telephone company franchises prepared by Verizon for example, are much worse then what may be included in incumbent franchises. A number of recent articles on this subject make clear industry issues to local franchising. Local governments need to be prepared to protect their rights to the greatest extent possible including revenue derived from the use of public right-of-way.

A recent article[1] (there are numerous articles on this subject) illustrates the current controversy regarding local franchising and telephone entry into video market, "Most cities say that regional Bells must obtain local franchises. Those franchises typically require cable TV providers to wire an entire community – not just the wealthiest areas, with the most lucrative customers -- and pay a 5% fee on revenue."

"But SBC Communications and Verizon want to install fiber-optic networks in the public areas they already cover. They insist they shouldn't have to negotiate franchise agreements to offer pay TV services to customers. Their offerings, they say, are fundamentally different from traditional cable services that must strike franchise deals."

"The battle is pivotal. Franchise requirements could delay or add huge cost to the phone companies' plans. And franchise fees are typically passed on to subscribers. 'It creates a number of problems for the business case.' Legg Mason analyst Blair Levin says."

"Franchise agreements can take months to negotiate. That could slow the phone companies in their race against cable providers to offer packages of voice, video and data services."

"Federal law generally requires phone companies to obtain franchises for video services that use the public right-of-way. SBC and Verizon say their existing arrangements with local governments for their phone network should suffice."

"Most of those agreements, though, do not impose franchise fees, says Marilyn Mohrman-Gillis of the National League of Cities.

"Many cash-strapped cities are hunting for new revenue sources. 'Franchise fees are significant sources of revenue,' says Stephen Stovall, city councilman in Plano, Texas."

"Cable TV companies say it would be unfair to let the phone companies off the hook. 'We should have the same planning field,' says Brian Dietz of the National Cable & Telecommunications Association."

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[1] *Phone Firms Cable TV Plans Hit Local Obstacle*, by Paul Davidson, US Today, February 2005.

"The stakes are especially high for SBC, which doesn't want to have to wire entire towns. It plans to target 90% of high-spending customers, 70% of 'middle-value subscribers' and 5% of 'low-value consumers.'"

The likelihood of the telephone industry seeking to enter the video market is very high. Further, the likelihood of a city being confronted with issues and concerns similar to those outlined above will take place in any proceedings involving the telephone entry. To prepare for this, local governments should consider adopting a Master Cable Services Franchise Ordinance. The goal of the Master Cable Services Franchise Ordinance is to provide a level playing field and ensure that new entrants will not have a "burden to entry" when coming to the city. They will know in advance the rules of the game. The city will have in place a process to deal with their application and ensure prompt response and completion of its review and acting on a franchise request. There will not be undue delay while the city attempts to negotiate new terms and conditions and requirements starting from scratch. The requirements will be in place.

The city will also have flexibility to make sure it can take into account changed and differing circumstances, including differences in law, technology, and services that may exist when a new entrant comes to the city asking for a franchise or when the city believes a franchise is required of a new service provider and so informs such a provider before it offers its services in the City.

CHALLENGES TO LOCAL FRANCHISING AUTHORITY

Over the past year, the local franchise system has been attacked head-on, as telcom companies contemplate entering cable markets in earnest and find that local franchise requirements are not as quick and easy as the telcos would like them to be. The challenges have occurred at both the state and federal levels of government, including legislation and, potentially, federal regulatory action by the FCC.[2]

- In Texas, a high-profile debate took place pitting the telcos against Texas cities and cable operators. Legislation backed by SBC would eliminate local franchising for cable services, enabling providers (SBC in particular) to acquire a franchise at the state level enabling it to provide cable service throughout the state. The Texas legislation passed the bill in a special session, and as of August 24, 2005 it remains on Governor Perry's desk. It is unclear whether or not the Governor will sign the bill into law.

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[2] An August 22, 2005 article in USA Today quoted Chairman Martin as saying that the FCC is exploring "what the commission can do to ensure that local authorities are not unreasonably refusing to award additional competitive licenses." "The chairman's comment is a not-so-veiled reference to a short passage in the 13-year-old Cable Act. The provision — Section 621(a)(1), to be exact — states that local franchising authorities "may not unreasonably refuse to award an additional competitive franchise" for video. It is not at all clear at this point whether or how the FCC may attempt to step into the local franchising reform fray. Leslie Cauley, "FCC Chief Considers Forcing Cable Competition," USA TODAY, Aug. 22, 2005 (online at http://www.usatoday.com/money/industries/telecom/2005-08-22-telecom-usat_x.htm.)

- Following on the heels of Texas, legislation was introduced in North Carolina that would enable BellSouth to enter cable markets in that state with no local franchise approval whatsoever. After intense opposition by North Carolina cities and cable operators, a state Senate committee struck the legislation. It is expected to emerge next year, however.

- At the federal level, the Broadband Investment and Consumer Act of 2005, S.1504, sponsored by Sen. Ensign and Sen. McCain, would do away with the local franchising process. Under the Ensign bill franchise fees—fees paid in recognition of the value of public rights-of-way – would be eliminated. Instead, cities and towns are reduced to recovering the cost of maintaining rights-of-way for use by these corporations. A 72-page deregulatory telecom reform bill, the legislation is essentially a wish list for the large incumbent telecommunications carriers. As such, it is highly unlikely to pass as it stands, although certain aspects of it – including the franchise reform provision – could be acted upon in compromise legislation.

  In addition, the Video Choice Act of 2005 (H.R.3146, S.1349), sponsored by Rep. Blackburn and Sen. Rockefeller, respectively, would nationalize the franchising process for competitive video providers that already operate in the local right of way (such as telcos). According to the Alliance for Community Media, these bills would "eliminate financial and technical support" for PEG services, and would put at risk the ability of localities to insist on institutional network services.

  It is too soon to tell what will come of these federal efforts to eliminate local franchising – in some ways, the debate is just beginning. We think it unlikely that local franchising will be eliminated by Congress during this session, but wholesale reform in the relatively near future is a real possibility.

"LEVEL PLAYING FIELD" REQUIREMENTS

Our experience with new entrants seeking to overbuild or provide competition has made it clear that incumbent cable providers will occasionally to go great lengths to enforce level playing field provisions in local franchise ordinances or agreements. A more cynical perspective would hold that the interest of the incumbent in some cases is not so much to ensure a level playing field among competitors, but, through lengthy litigation embroiling the local government, to delay entry of a competitor altogether.

As Verizon, SBC and other telcos seek to enter local cable markets en masse, level playing field issues promise to come to the forefront as a major competitive issue. [Issue has already created delay in awarding a franchise to Verizon in Bradenton County, FL. It is also clearly on the table in other telco video franchise negotiations that are under way.]

A key point in this context is whether or not the competitive telco video provider must be subject to the usual incumbent obligation to provide services to the entire franchise area within a particular time, or whether the telco is permitted to cherry-pick or "red-line" the most lucrative markets in the area in the raw pursuit of a business plan. [more on this] Undoubtedly, Verizon

and others would respond that the company intends to deploy services within the entire franchise territory at some point in time, but that they cannot be expected to deploy everywhere at once. In addition to the well-meaning objective of universal coverage, local franchising authorities also may be operating under a previously-enacted level playing field provision, and may be compelled to take a hard line with the competitive provider in terms of its deployment obligations. This may well lead to delay, contentious negotiations, and perhaps litigation – which is exactly the sort of conflict that the telco video providers cite when lobbying for some sort of statewide or national franchising legislation in lieu of dealing with hundreds or thousands of local franchise negotiations.

A handful of states have enacted "level playing field" laws, including California, Connecticut, Illinois, Minnesota and Virginia. While the California[3] and Minnesota[4] statutes specify discrete issues on which existing and new franchises must be similar, the Connecticut,[5] Illinois[6] and Virginia[7] statutes use broad language, such as prohibiting the award of a franchise under terms that are "more favorable or less burdensome" than the incumbent's franchise, and/or requiring that the two be "substantially similar."

In addition to level playing field laws enacted at the state level, local franchise agreements and franchise ordinances may also impose level playing field obligations on the locality. Localities should carefully consider the ramification of including such a provision in a franchise agreement or ordinance, recognizing that a well-worded Master Ordinance could in fact help defuse a potentially litigious situation involving the locality and delaying the entry of a competitor.

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[3] California Government Code § 53066(d) provides that "Any additional franchise granted to provide cable television service in an area in which a franchise has already been granted and where an existing cable operator is providing service or certifies to the franchising authority that it is ready, willing, and able to provide service, shall require the franchisee to wire and serve the same geographical area within a reasonable time and in a sequence which does not discriminate against lower income or minority residents, and shall contain the same public, educational, and governmental access requirements that are set forth in the existing franchise. This subdivision does not apply where all existing cable operators certify to the franchising authority that they do not intend to provide service within a reasonable time to the area to be initially served by the additional franchise.

[4] Minnesota Statutes § 238.08(b) provides that "[n]o municipality shall grant an additional franchise for cable service for an area included in an existing franchise on terms and conditions more favorable or less burdensome than those in the existing franchise pertaining to: (1) the area served; (2) public, educational, or governmental access requirements; or (3) franchise fees. The provisions of this paragraph shall not apply when the area in which the additional franchise is being sought is not actually being served by any existing cable communications company holding a franchise for the area. Nothing in this paragraph prevents a municipality from imposing additional terms and conditions on any additional franchises.

[5] Connecticut General Statutes § 16-331(g) provides: "Each certificate of public convenience and necessity for a franchise issued pursuant to this section shall be nonexclusive, and each such certificate issued for a franchise in any area of the state where an existing franchise is currently operating shall not contain more favorable terms or conditions than those imposed on the existing franchise. This subsection shall not apply to the length of the term of such certification as may be determined pursuant to subsection (d) of this section."

[6] In Illinois, 65 ILCS § 5/11-42-11(e) provides in relevant part that a franchising authority may grant additional cable franchises: "provided that no such additional cable television franchise shall be granted under terms or conditions more favorable or less burdensome to the applicant than those required under the existing [ ] franchise...."

[7] Virginia Code § 15.2-2108C provides that "No such governing body shall grant any overlapping licenses, franchises or certificates of public convenience for cable service within its jurisdiction on terms or conditions more favorable or less burdensome than those in any existing license, franchise, or certificate of convenience within such locality. . . . "

Case law concerning level playing field provisions establish the following major principles:

A. Franchises must be compared as entire packages, not on a provision-by-provision basis.

1. *Insight Comms. Co. et al. v. City of Louisville,* No 2002-CA-000701-MR, (Ky. Ct. App. 2002)("There will never be an apple-to-apple comparison . . . .")

2. *United Cable Television Services Corp. v. Dept. of Public Utility Control*, 1994 WL 495402, *aff'd*, *United Cable Television Services Corp. v. Dept. of Public Utility Control*, 663 A.2d 1011, 1025 (Conn. 1995) ("*United Cable*") ("[a] proper inquiry requires consideration of the entire package of terms and conditions required of both cable operators in order to adequately determine whether one has been favored over the other").

3. *New England Cable Television Ass'n v. DPUC*, 717 A2d 1276 (Conn. 1998) ("*New England Cable Television Ass'n*") ("[The franchising authority's] sole duty . . . is to ensure that the specific terms of a competitor's certificate are not, on balance, more favorable than those of the incumbents.").

4. *Cable TV Fund 14-A, Ltd. v. City of Naperville, Illinois*, 1997 WL 209692 *12 (ND. Ill) ("*Naperville*"), quoting *United Cable*, 1994 WL 495402 at *5 (Item-by-item comparisons not appropriate because "'if [the new franchisee] were required to achieve point-by-point equality in terms and conditions, the [franchising authority] would be put in the position of imposing particular requirements on a new entrant not because of any particular need but simply to match the situation that existed at the time of the application of the existing entrant, without regard to new information, new technology or other temporal developments'").

B. Franchises must be compared with due regard for the circumstances existing at the time that each franchise is or was granted

1. *Cable Systems of Southern Connecticut, Ltd. v. Connecticut DPUC*, 1996 WL 661818, at *4 ("*Cable Systems of Southern Connecticut, Ltd.*") ("The comparison between Fibervision's task in creating a new system and Cablevision's rebuild plan is conceded by Cablevision to be of different projects. The Cablevision proposal is to rebuild in a shorter time than Fibervision's construction is not a DPUC mandate. . .. It also represents a different task, which is facilitated by Cablevision's substantial existing customer base").

2. *Comcast Cablevision of New Haven, Inc. v. Connecticut DPUC*, 1996 WL 6611805 at *4 ("*Comcast Cablevision of Southern Connecticut, Ltd.*") ([An item-by-item comparison is especially inappropriate] where Fibervision is creating a "state-of- the-art" system compared with what was installed in the 1970's").

3. *New England Cable Television Ass'n*, 717 A2d at 1293 ("Advances in technology will provide competitive advantages against which the department cannot and should not legislate. If the rules of competition have changed and Personal Vision has a technological advantage that will permit it to provide cable service in a manner not previously possible, it should not be hobbled by the technological limitations of its competitors or because the franchise agreements of incumbent competitors are limited by the fact that they were authorized only for community-based areas during an era in which there was no competition.")

4. *Naperville*, 1997 WL 209692 at 12, quoting *United Cable*, 1994 WL 495402 at *5 (Item-by-item comparisons are not appropriate because "'if [the new franchisee] were required to achieve point-by-point equality in terms and conditions, the [franchise authority] would be put in the position of imposing particular requirements on a new entrant not because of any particular need but simply to match the situation that existed at the time of the application of the existing entrant, without regard to new information, new technology or other temporal developments'").

C. The relevant comparison is between the new entrant's franchise and both the terms and conditions of, and the operator's actual experience under, the franchise awarded to the incumbent or its predecessor(s).

1. *Comcast Cablevision of New Haven, Inc.*, 1996 WL 6611805 at *3 (no unfair advantage "with respect to the build-out schedule imposed on Fibervision compared with the history of Comcast and its predecessors").

2. *New England Cable Television Ass'n*, 717 A2d at 1291 (court compared buildout term in new franchise with the incumbent's actual buildout experiences).

D. Franchising authorities may appropriately take account of the advantages of incumbency and the entrant's added risks of entering a market against entrenched competition.

1. *Insight Comms. Co. et al. v. City of Louisville*, No 2002-CA-000701-MR, (Ky. Ct. App. 2002)("There will never be an apple-to-apple comparison for Insight and other franchisees simply because Insight is the incumbent which in its own right and through its predecessors has been the exclusive provider of cable television services in the City of Louisville for almost thirty years. No new cable television franchisee can ever be in the same position as a thirty-year veteran.")(available online at http://www.baller.com/pdfs/ky-ct-app-louisville-opin.pdf).

2. *New England Cable Television Ass'n*, 717 A2d at 1292 n.26 (incumbents have major advantages that offset any benefits that new providers may enjoy).

3. *Comcast Cablevision of New Haven, Inc.*, 1996 WL 6611805 at *4 ("Plaintiff's argument that the advantage of incumbency is not supported in the record ignores undisputed evidence in the record. The record reveals that Comcast has been the monopoly cable television provider in the franchise area, with 68,000 customers and 'is a subsidiary of one of the largest cable providers in the United States.' Its marketing power is massive, especially in light of its interlocking ties with programming suppliers.").

4. *Cable Systems of Southern Connecticut, Ltd.,* 1996 WL 661818, at *4 ("Fibervision's task in creating a new system and Cablevision's rebuild plan . . . represents a different task, which is facilitated by Cablevision's substantial existing customer base").

E. It is Inappropriate to Compare New Construction to Upgrades of Rebuilds of an Existing System.

1. *Cable Systems of Southern Connecticut, Ltd.,* 1996 WL 661818, at *4 ("Fibervision's task in creating a new system and Cablevision's rebuild plan . . . represents a different task . . .")

2. *Comcast Cablevision of New Haven, Inc.*, 1996 WL 6611805 at *5 ("Comcast also refers to its obligation to rebuild its system in three years. The analogy between initial installation of a system and the rebuild of an existing system with a substantial customer base, is not compelling. The Plaintiff has failed to meet its burden of proof as to its unfair competitive disadvantage with respect to Fibervision's build-out requirements.")

STREAMLINING CITY PROCESSES THROUGH A MASTER FRANCHISE ORDINANCE

To illustrate, the following are some of the important matters that should be considered for inclusion in a Master Ordinance:

- Definitions to broadly define "cable service" so that it is clearly applicable to all similar types of service, without regard to who may be the provider.

- A franchise fee equivalent to 5% of the operators gross revenue paid to the city as compensation for use of public right-of-way. The gross revenue definition should be broadly stated to encompass all forms of revenue derived from the provision of cable service, and should specifically state that revenue from launch fees, advertising revenue, home shopping commissions, etc. are to be included in the "gross revenue" calculation.

- Obligations to provide community access channels that allow local public, educational, and governmental access programming, including funding, facilities and equipment to support PEG services into the future.

- Cable services and perhaps broadband services offered without charge to public buildings, schools, and libraries in the city.

- Emergency alert communications capabilities.

- Construction standards and protections for the right-of-way.

- Obligations to cover a defined service area, with a reasonable time for completion. (Beware of level playing field implications).

- Prohibition against redlining or discrimination based on economic or other reasons.

- Periodic performance and franchise compliance review.

- Customer service standards and requirements.

- Regulation of rates to the extent permitted under applicable rules of the Federal Communications Commission as well as the Cable Acts.

- Right of the local franchise authority to receive periodic reports and information regarding the operations and technical nature of the cable system and, in addition, right of access to books and records to either examine or to verify the accuracy of certain information, including in particular the sources of revenue supporting franchise fee payments. The right to audit should specify how many years back the locality may request records for.

- Insurance and bonding.

- Right to administer and enforce the franchise, including defined enforcement procedures and penalties for violation or default.

CONCLUSION

Local governments need to recognize that changes to the local franchising scheme are quite likely in the near future. The telecommunications industry complaint that local franchising is a burden to entry is taking root at both the state and federal levels of government. While cities

should vigorously oppose legislation that seeks to eliminate franchising, cities also should recognize that local processes should be streamlined to reduce delay as much a possible. A good faith effort among localities to do so could assist in staving off more drastic legislative "fixes."

A Master Ordinance, applicable to incumbent and competitors alike, can effectively demonstrate that the city encourages competition and is completely competitively neutral, and can demonstrate to potential new providers that the city has created an approach to franchising that is fair and reasonable and offers a reasonable degree of flexibility to take into account differing circumstances and requirements that may be applicable to new providers.