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Legislative Review:

The Communications Act

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will new federal and state video franchising laws sideline local governments?

The local cable franchising process – the model that has existed since the advent of cable television several decades ago and which has served subscribers, local governments and industry well – is under legislative siege. The double-barreled attack is sponsored primarily by the former regional Bell operating companies (“RBOCs”) and prompted by their desire to enter the landline multichannel video market without having to bother with local franchising.

First, the RBOCs are pressing state legislatures to enact new state laws that replace local cable franchising with more uniform statewide franchising. As of this writing, at least eight states have enacted such laws.¹ The details of these new state laws vary considerably, but they share one common trait: Each is designed to enable cable providers largely to bypass the local cable franchising process.

Legislative Review: The Communications Act



BY TILLMAN L. LAY

New Federal and State **Video Franchising Laws**

The second prong of industry's assault on local franchising has been the pursuit of federal legislation that either eliminates, or greatly limits, local franchising authority. Last June, the House passed legislation that would radically alter video franchising, replacing local franchising with national franchises issued by the FCC. Video franchising legislation that is similar (but far from identical) is pending in the Senate, but as of this writing, that legislation has not been adopted. Even if video franchising legislation is not enacted in the 109th Congress, such legislation may well arise again in the 110th Congress that begins in January, 2007.

From industry's point of view, federal legislation has two significant advantages over state franchising legislation: It eliminates the necessity of securing legislation from each, or at least most, of the fifty state legislatures, and it also would create more nationwide uniformity than fifty similar, but inevitably not identical, state laws. State legislation, on the other hand, offers a different advantage to industry: It is often much easier to pass than federal legislation.

The bottom line of these developments is that, one way or another, most local franchising authorities ("LFAs") are either already experiencing, or in the next year or so likely to experience, substantial new limitations on their local cable franchising authority. The obvious question becomes: What, if any, roles will new legislative restrictions on local cable franchising leave for LFAs to play?

The answer is that, in most states at least, LFAs will continue to have essential roles to play. Indeed, so-called video franchising "reform" is likely to increase, rather than decrease, the need for LFAs to monitor cable operator performance in several key areas that have traditionally been critical components of local cable franchising.

■ **Franchise Fee Audits.**

Although the details vary, both versions of pending federal legislation and most new state franchising laws still require operators to pay franchise fees to LFAs of up to 5% of gross revenue. But most of these federal and state legislative initiatives also (1) place time limits on LFAs to dispute franchise fee payments, and (2) limit the frequency with which LFAs are permitted to conduct franchise fee audits. A good example is Virginia's new law, which requires an LFA to dispute any fee payment within three years and, at the same time, prohibits an LFA from conducting a fee audit more frequently than once every two years.

The new time limits placed on LFA claims for fee underpayments mean that LFAs should conduct fee audits at least once every two years. This is probably more frequently than most LFAs currently conduct fee audits, but that will need to change. In most cases, the best approach would be for an LFA to mark its calendar and conduct regular fee audits every other year, regardless whether the LFA has any reason to suspect

underpayments. While conducting more frequent audits may cause the LFA to incur more audit costs, the risk of forfeiting fee underpayment claims due to the new time limits will usually outweigh the additional auditing costs.

Thus, in the area of franchise fee audits, new video franchising laws mean that LFAs should be more, not less, vigilant.

■ **PEG Issues.**

New state and federal video franchising legislation generally imposes public, educational and governmental ("PEG") access obligations on cable operators. Typically, the legislation preserves the ability to require an operator to set aside channel capacity for PEG use, and most legislation also permits the operator to be required to provide PEG support, usually in the form of a variable-cost monetary payment (such as a percentage of gross revenue).

With respect to PEG capacity, new video franchising legislation typically requires all operators to provide the same number of PEG channels as the incumbent operator is currently providing. Beyond that, the proposals diverge. Some provide formulas to periodically add PEG capacity in the future, while others do not. Most provide a channel use formula that allows the operator to recapture a PEG channel if it is not sufficiently used.

With regard to PEG support, generalizations are even more difficult, with one exception: Virtually all franchising legislation puts an end to in-kind PEG support in the form of PEG studio facilities and equipment, either immediately or, in the case of the incumbent operator, no later than the end of its current franchise term. As far as monetary PEG support is concerned, there is considerable variation. One pending bill in Congress would set a flat 1% PEG fee, while the other would allow LFAs to choose between a 1% fee or a fee that is the per-subscriber equivalent in PEG support of what the incumbent operator is providing. As for new state laws, Texas and California provide an option of a 1% fee or a per-subscriber equivalent fee. Indiana's law permits a per-subscriber equivalent fee. Virginia's scheme is more indeterminate and procedurally complicated, while North Carolina's law establishes a statewide PEG capital fund and caps any individual LFA's grant from the fund at a meager \$25,000.

Beyond PEG capacity and PEG monetary support, however, there are additional related areas of concern. Among the typical franchise obligations that are addressed in disparate ways by the new franchising laws are institutional networks ("I-Nets"), complimentary service to schools and government buildings, and upstream capacity to carry PEG programming from its origination points to the operator's system. These types of provisions merit particularly careful scrutiny by LFAs, because they often entail "hidden" costs – that is, they shift to the LFA costs previously borne by the operator.

¹ Those states are California, Indiana, Kansas, New Jersey, North Carolina, South Carolina, Texas and Virginia.

New Federal and State **Video Franchising Laws**

The trend is clear: An LFA would be well-advised in most states to adopt a single, uniform ROW ordinance for all utilities, cable and other ROW users.

This means that what monetary PEG support the legislation gives may well have to be spent to replace what the LFA had previously obtained at no charge.

The conclusion, however, is clear: Far from reducing the need for effective LFA management and enforcement of PEG requirements, statewide and federal franchising legislation will increase it.

■ **Rights-of-Way Management.**

Most video franchising legislation preserves local rights-of-way (“ROW”) management authority over cable systems, although it also places new constraints on that authority. A common theme is that all local ROW management of cable systems must be nondiscriminatory and competitively neutral.

The trend is clear: An LFA would be well-advised in most states to adopt a single, uniform ROW ordinance for all utilities, cable and other ROW users. This will mean a shift for some LFAs, which have historically incorporated all cable ROW requirements into their cable franchises while following a more informal permitting process for utilities. But the conclusion is the same: LFAs will need to be more, not less, active in reviewing and revising their ROW management requirements.

■ **Customer Service.**

Authority over cable customer service has, of course, historically been the province of LFAs. Almost all forms of video franchising legislation, however, restrict that authority, albeit to varying degrees. But even here, with a few exceptions, LFAs usually will retain some authority to enforce customer service standards, either directly or indirectly through the ability to file complaints with a federal or state agency on behalf of subscribers.

Again, the lesson is that, to protect local cable subscribers under new video franchising regimes, LFAs will have to be more proactive, and creative, than ever before.

■ **System Buildout.**

Virtually all local cable franchises contain buildout requirements (requiring the operator to offer service throughout its franchise area, at least down to a certain household density) and redlining requirements (prohibiting the operator from discriminating in the availability of service based on income or other suspect reasons). New video franchising legislation, however, either drastically curtails, or eliminates, these types of requirements. And the few new state laws that do preserve some sort of buildout requirements, such as those in California, New Jersey and Virginia, radically alter those requirements from what any LFA had previously required.

LFAs, however, will retain a critical role in buildout and redlining, even if that role is no longer as a regulator. LFAs’ new role will be that of watchdog. Through ROW permitting and inspection information and through feedback from residents, LFAs will be in the best position to gather facts about what neighborhoods are, and are not, being served, and when and where suspicious redlining behavior occurs. Those facts, in turn, can serve as the basis for informing state PUCs or the FCC about what is really happening on the ground. In addition, LFA-collected data on buildout and redlining problems can serve as a vital foundation for justifying future amendments to the new franchising laws if, as some fear, the unregulated marketplace fails to deliver the widespread competition that industry promises.

■ **LFAs’ New Roles.**

Video franchising legislation will change dramatically the scope and nature of LFAs’ duties in overseeing local wireline video service providers. But it will not end those duties. While the changes in LFAs’ responsibilities will vary from state to state, LFAs will still have important roles to play with respect to some or all of the following: franchise fees, PEG access, ROW management, customer service and buildout requirements. All LFAs should review the new laws carefully and actively pursue each of the new roles assigned to them. ■