

M I L L E R & V A N E A T O N
P. L. L. C.

MATTHEW C. AMES
KENNETH A. BRUNETTI*
FREDERICK E. ELLROD III
MARCIL L. FRISCHKORN
WILLIAM L. LOWERY
NICHOLAS P. MILLER
MATTHEW K. SCHETTENHELM
JOSEPH VAN EATON

*Admitted to Practice in
California Only

1155 CONNECTICUT AVENUE, N.W.
SUITE 1000
WASHINGTON, D.C. 20036-4320
TELEPHONE (202) 785-0600
FAX (202) 785-1234

MILLER & VAN EATON, L.L.P.
400 MONTGOMERY STREET
SUITE 501
SAN FRANCISCO, CALIFORNIA 94104-1215
TELEPHONE (415) 477-3650
FAX (415) 477-3652

WWW.MILLERVANEATON.COM

OF COUNSEL:
JAMES R. HOBSON
NANNETTE M. WINTER†
GERARD L. LEDERER
WILLIAM R. MALONE
JOHN F. NOBLE

†Admitted to Practice in
New Mexico Only

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TALKING POINTS RE STATE LEGISLATION

NICHOLAS MILLER
SENATE COMMERCE COMMITTEE STAFF BRIEFING

A. INTRODUCTION

1. There is good and bad in both VA and TX state legislation (and in the pre-existing state level cable statutes).
2. The most significant problem in both VA and TX: both bills fail to address the full range of issues that local governments must deal with in cable services.
3. Beware of the Law of Unintended Consequences—any federal solution must anticipate many transitional problems.
 - a. Rights and obligations of incumbent must be maintained unless and until competitor appears in franchise area. (e.g., Laredo TX: Time Warner takes state franchise to avoid renewal negotiations even though no telco is proposing video service in Laredo.)
 - b. Cash is Not an adequate substitute for in-kind facilities. Particularly in the absence of rate regulation, the incumbent operator's will be able to charge very high prices for the continuing to provide the facilities.

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5. Neither the VA nor TX bills “keep LFAs whole”—while some communities get more than they have had before, the more sophisticated users of cable systems for non-commercial purposes get less.
 - a. 1% in gross revenues does not recover the PEG contributions.
 - i. Fairfax County, Arlington County have existing franchises that generate 3% of gross revenues for PEG and INet support.
 - ii. Major TX communities get 1% in PEG support, plus in-kind facilities that approximate 2% of gross revenues.
 - b. TX definition of Gross Revenues maintains status quo—but VA does not.
 1. VA excludes many sources of revenue currently included in Fairfax and Arlington franchises.
6. Neither VA nor TX got the “process issues” correct:
 - a. Consumers need a single point of contact to address and solve their service/billing/signal quality problems with providers.
 - b. Neither gives effective remedies against bad actors.
 - i. TX gives a franchise in perpetuity, and burden is on municipality to sue in court to terminate the franchise. And an affiliate of the company can reapply and get a franchise 14 days later.
 - ii. VA proposes a 120 negotiation period (not including telcos), before default “ordinance” franchise is available. There is no incentive to deviate from the ordinance franchise terms.
 - iii. Normal contract enforcement mechanisms like damages or revocation in event of default are not available.
 - c. Local police power over PROW is given lip-service, but too expensive and slow for meaningful enforcement.
 - i. Both bills strictly limit the enforcement powers available to community. For example, “stop work” order appears to violate state statutory right of access until after a full-blown court trial.
 - ii. TX eliminates the ability to charge a cost-based fee for permits and inspections.

B. PRE-EXISTING STATE LEGISLATION—The good and the bad.

7. Issue: Buildout:

- a. West Virginia has very good language for a legal test—. . .schedule providing for maximum penetration as rapidly as possible with the limits of economic feasibility.” §§24 D-1-5(a)(4).
- b. Coupled with New Jersey style benchmarks of fixed percentage(s) within specified year(s).

8. Issue: Franchise Process

- a. New Jersey has a very sound approach. LFA negotiates local community issues such as EAS and PEG, then State Board of Public Utilities issues a franchise consistent with local agreement. State sets consumer protection rules. NJS 48:5A-1, et seq.
- b. New York has a similar approach. NY PSC sets MINIMUM PEG requirements and local community can use as default or negotiate its own, subject to PSC review.
- c. In contrast, Connecticut communities have not received PEG and other services comparable to the rest of the country where the entire process has been controlled by state rule making and no negotiations at the local level.

9. Issue: Franchise Fees

- a. New York and New Hampshire set the standard. They both allow the local government to set the fee without negotiation. For example, New York allows the LFA “to impose fee, tax or charge” that does not “exceed maximum permitted by federal law.”
- b. But other states that try to set the fee at the state level have found it impossible to increase the fee, even after decades of inflation. For example, New Jersey remains stuck at 2% of cable subscription fees.

C. TEXAS—WHAT’S RIGHT AND WHAT’S WRONG WITH SB 5?

The table below describes the old and the new of cable franchising in Texas.

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Requirement	Before SB 5	After SB 5	Comments
Local Franchising Authority (LFA) for purposes of the Cable Act	Municipalities	The State of Texas (administered by the Public Utility Commission)	No appropriation or additional staff provided.
Rate Regulation	Cities regulate rates of the “Basic Tier” and equipment rental and services, but only until “effective competition” is found by the FCC to exist in the municipality	No rate regulation	Fails to recognize the problem of discriminatory pricing by incumbent when a competitor enters the franchise area.
Customer service standards	City may enforce customer service standards found in the Cable franchise, which may be more protective than the FCC standards	The PUC may only enforce minimal customer service standards established by the FCC and then only in areas that don’t have an incumbent cable company	PUC is still referring consumer complaints to local government. No Texas entity has authority to help.
Franchise Fee	Franchise fee of up to 5% of the gross revenues derived from the operation of the cable system to provide cable services.	“[F]ive percent based upon the definition of gross revenues as set forth in this chapter”	Applies to all forms of cable service, including IPTV
“Gross Revenues”	Defined in each cable franchise	Defined by the statute, similar to definitions found in most existing franchises	Good definition of “Gross Revenues”
Public, Educational, & Governmental (PEG) channel capacity	Negotiated by each municipality	Same number of PEG channels (up to 10) as were <i>active</i> on 9-1-05, but no fewer than: < 50,000 pop.: 2 channels > 50,000 pop.: 3 channels	Locks PEG in an obsolete model of “channels” rather than “capacity on the network”

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Requirement	Before SB 5	After SB 5	Comments
PEG support payments	Negotiated amount, must be used for capital expenditures, not operating expenses	Same as incumbent cable provider, on a per subscriber basis, until franchise expires, then one per cent of Gross Revenues which is intended to replace PEG support payments and cash value of in-kind services that are no longer provided	1% of Gross Revenues will not sustain PEG if forced to pay for current in-kind facilities.
In-kind services, e.g. Institutional Network (I-Net), free cable service to public buildings, schools, etc., dark fiber, or telecom services	Negotiated with cable company and included in the cable franchise as compensation for the use of the ROW. May require I-Net and free cable service to public buildings, but not other in-kind such as dark fiber or telecom services	In-kind services from incumbent cable provider must be continued for free until the later of the expiration of the incumbent franchise agreement or Jan. 1, 2008, then municipality may require in-kind services at the level prior to expiration of the incumbent agreement. However, provider can deduct the “actual incremental costs” from any franchise fee owed a municipality.	Prohibition on “in kind” PEG facilities is catastrophic to PEG video, which currently receives studio space, personnel services, upstream video feeds, etc. from incumbents.
Community Needs Assessment	As part of franchise renewal process, City can require that cable company meet community needs demonstrated by community needs assessment	Cities and PUC have no authority to require specific services be provided to the community	This assumes role for PEG in future is fixed and unchangeable.

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Requirement	Before SB 5	After SB 5	Comments
Mandatory Build-out requirement with deadline	City may require the cable company to serve the entire community within a certain timeframe.	Build-out requirement prohibited	Telcos, after 7 months, have applied to serve only 3% of state population.
ROW management and other Police Power regulation	May be contained in the franchise or in a separate ordinance	Must be by ordinance. Failure to comply with a city's local ROW ordinance can be ground for revoking state-issued franchise	Cumbersome enforcement mechanism, and no restriction on affiliate of revoked operator from getting a new franchise.
Indemnification of City	Agreed to by city and cable provider and set out in franchise	Mandatory provision set out in statute	Much weaker protections for local government
Insurance and Bonding	Required by most franchises or by ordinance	City may not require if provider is self-insured and can demonstrate 4 year record with no outstanding claims	Insurance should be tied to risk—size of incident and ability of insured to pay. Will vary by city and by operator.
Franchise Transfers	Approved by City.	State issued franchise: No approval required, only notice to PUC and municipality within 14 days <i>after</i> transfer	No protection against unqualified and under-financed operator. Only remedy is post-catastrophic event.
Franchise Renewal	May follow formal or informal process, is an opportunity to negotiate system upgrades, additional benefits to the community	State issued franchise is perpetual, no renewal is required	Perpetual franchise risks substantial constitutional claim if state ever changes law in future.

Requirement	Before SB 5	After SB 5	Comments
Authority to enforce franchise requirements	Municipality has authority to bring suit to enforce the franchise and can seek a spectrum of remedies up to and including termination of the franchise	Municipality has authority to bring suit to enforce statutory state-issued franchise requirements, but court must give provider opportunity to cure, before penalties or revocation can be ordered	Litigation as pre-condition to enforcement is not the solution to traffic jams and hazardous behavior in the right-of-way. Similarly, the local community should be able to encourage adequate performance short of bringing a lawsuit.
Typical "Service Area"	City-wide	Wherever providers chose to sell their services. They determine their own footprint, block by block, if they so desire.	Already evident that this provision is creating real issues as telcos have applied to serve only 3% of state population.
Income Discrimination within provider's service area	Prohibited	Prohibited. But now service areas can be defined by the provider. However, legislative intent indicated that the prohibition on discrimination could extend beyond designated "service area".	

D. VIRGINIA: WHAT'S RIGHT AND WHAT'S WRONG..

1. Process for Obtaining an Ordinance Franchise

A telephone company or incumbent cable operator at the end of its current franchise term qualifies immediately. Any other applicant has a 45-day negotiation period and can then give notice of its intent to begin service within 30 days. The locality must adopt a new cable regulatory ordinance, which may address only those subjects expressly permitted by the legislation.

Comment: There will be no serious negotiations, unless the community is willing to accept terms less than the Ordinance Franchise.

2. Non Discretionary Terms of an Ordinance Franchise

- 15 years.
- The applicant must provide a map showing its initial service area for cable service, as well as the area in which it has telephone facilities.
- Access to cable services is not denied to any group of potential subscribers because of the income of the area in which they reside.
- The locality has the right to monitor and inspect deployment of cable services, and the operator must submit semiannual progress reports.
- The locality may enforce requirements using the same remedies provided under its franchise with the incumbent cable operator, if any.

3. Discretionary Terms of an Ordinance Franchise—12 Topics Only

- i. Public, Educational, and Governmental (“PEG”) channels. Same number of PEG channels as the incumbent. If fewer than three channels, the ordinance may require up to three channels. A locality that is “substantially utilizing” its existing channels may require additional channels, up to a maximum of seven.
- ii. Franchise Fee. Capped at 5% of gross revenues, unless the incumbent is paying a less.

Comment: Many sources of revenue are excluded from “gross revenues”. Communities will have little recourse if operators aggressively challenge the limits of the definition.

- iii. PEG Capital Support.
 1. In-kind compensation, such as a requirement to operate a studio, provide equipment, or provide staff support for PEG channel activities, prohibited.

Comment: The legislation contains no provision for local requirements for emergency alert systems. Interconnection requirement does not specify who will bear the cost of interconnection. Ignores upstream links from PEG access origination sites (such as City Council chambers) to the operator’s headend.

2. PEG Capital Fee is equal to any recurring fee based on gross revenues or a fixed amount per subscriber that is paid by the incumbent.
3. PEG Capital Grant Surcharge Fee applies where incumbent has made lump sum payments or provided equipment. Set as the lower of 1.5% of gross revenues, or a per subscriber amount calculated by amortizing the amount of the incumbent's payments over the term of the franchise.
4. Both expire at the end of the existing cable operator's franchise.
5. At that point, the locality and all operators serving the locality are to negotiate a new fee. If they cannot agree, the locality may set the new fee, but it cannot exceed the amount of the prior PEG Capital Fee.

Comment: This complicated mechanism will ultimately result in only the same level of support, unadjusted for inflation, as the current franchise PEG support. There is no incentive for the operators ever to agree to a higher level of support.

- iv. Customer Service. The locality may adopt customer service requirements, but subject to several ambiguous restrictions.

Comment: Probably results in a lowest common denominator approach. The provisions are unclear as to what authority exists to adopt rules more effective than the FCC's.

- v. Enforcement. The legislation specifies the procedure for local enforcement of noncompliance by an operator. First, informal discussions; then locality must give the operator written notice; then the operator has 15 days to cure or respond; then the locality then may schedule a public hearing, after 30 days notice of the hearing.

Comment: The process will not allow prompt resolution of problems, and prevents handling matters at the administrative level (other than informal discussion). Most issues will not justify the expenditure required to enforce. The procedures are cumbersome and time-consuming if the violation is on-going. There is no provision for revocation.

- vi. Schedule of Uniform Penalties. The locality may adopt a schedule of penalties or liquidated damages governing failure to comply with customer service standard, PEG carriage requirements, payment of franchise fees and PEG capital fees, and reporting requirements. These penalties must be the same as any existing penalties or liquidated damages applicable to the incumbent.

Comment: This is one of many places where the locality cannot impose obligations under the ordinance franchise that are greater than or different from those imposed on the incumbent under its existing franchise. In many cases the provision in an existing franchise will be inadequate, and was adopted only as part of negotiations. Penalties negotiated 10 or 15 years ago are not appropriate for a new entrant bringing a different technology.

- vii. Audit Procedures specified. These restrict in time and scope local government's audit authority.
- viii. Reporting Requirements. The locality may require annual financial information and quarterly customer service information that are no greater than existing requirements.
- ix. Service to Government Facilities. May require free cable service only to public schools and government buildings.
- x. Right-of-Way Management. Limited to those appearing in Va. Code § 56-462(C)(i) and (ii). A locality may adopt construction standards and procedures, but will not apply to a telephone company.

Comment: There is no provision for insurance and indemnification. Such requirements are almost universal in cable franchises today, to ensure that the public does not suffer harm as a result of the activities of providers and their contractors in the rights-of-way, but the legislation does not address the issue at all.

- xi. Fee Allocation. Specifies the amount of gross revenues received from subscribers paying a single fee for bundles of services that include both cable and non-cable services.
- xii. Build-out Requirements. A locality may require service to 100% of residential dwelling units in the initial service area within three years; Operator defines its initial service area. May also require the operator to serve up to 65% of the residential dwelling units within 7 years. In

year 7, locality may require service to 80%. Several limitations and exceptions, including a 30-homes per mile density standard, unable to build for “technical reasons”, and “periods of delay caused by the locality.” On the other hand, the new provider can surrender a franchise without penalty within 3 years of issue.

Comment: The overall build-out concept is sound, except the initial service area should be negotiated, not unilateral, and exclusions threaten to make the requirement unenforceable. It is questionable whether the disruption of the community caused by a three year uncompleted effort should be left without any remedy, such as transferring the facilities to the community. The right of surrender does not call for the reinstatement of an incumbent operator’s original franchise, if the incumbent has sought amendment or conversion of its franchise pursuant.

4. Treatment of Existing Franchises

- a. If a locality grants a competitive franchise to a new operator by negotiation, the incumbent operator may request the same terms and conditions, by an amendment of its existing franchise.
- b. If a locality adopts an ordinance under the new legislation, it must also allow the incumbent to opt into an ordinance franchise.

E. WHAT’S MISSING? IMPORTANT TOPICS OMITTED IN VA AND TX.

1. What happens to the facilities upon termination or abandonment?
2. Can one competitor sell out to the other?
3. No provisions for consumer rebates, refunds and credits when service fails or repairs are faulty.
4. No notices to landowners and subscribers of construction and repairs.
5. No restrictions on the systems RF interference or other safety issues unrelated to rights-of-way.
6. No stand-by power requirements
7. No requirements for CPE and cable-ready TV compatibility.

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8. No requirements for service to the disabled community and ADA compliance.
9. No reporting requirements for customer service complaints.
10. No emergency alert system.
11. No upstream connections for PEG signals.
12. No signal testing or performance evaluations.
13. No restrictions on operator editorial control of PEG channels or PEG management.
14. No description or regulation of “non-standard installations” and location of drop lines.
15. No discussion of consumer rights such as availability of customer service representatives, billing and late fees, notice of service offerings and prices and changes, statements of provider policies.
16. No discussion of privacy rights and disclosures.
17. No discussion of EEO and Small Business Procurement practices
18. No discussion of anti-competitive pricing within the franchise area.