

**STRAYING OUTSIDE A VIABLE AND PREDICTABLE
REGULATORY FRAMEWORK¹ --
IS THERE ANY LOCAL AUTHORITY OVER CABLE MODEM SERVICES?**

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I. INTRODUCTION

The regulatory treatment of cable modem services is a major challenge facing Local Franchising Authorities (LFAs). The Federal Communications Commission (FCC) and the courts are currently addressing cable modem regulatory issues. During this stage of uncertainty, LFAs are questioning how to address franchise fees, universal service requirements, and customer service issues. This article presents an overview of these issues and some consequences of the FCC's classification of cable modem service as an interstate information service. These issues will remain fluid however, at least until they work their way through the courts and the FCC.

Prior to March 2002, most cable operators and LFAs treated cable modem service as a cable service, regulated under Title VI of the Communications Act of 1934 (the Cable Act). Cable companies paid franchise fees by contractual (franchise) agreements with LFAs.² Cable modem service was generally offered throughout an entire franchise area, similar to traditional cable services.

II. FCC ACTION

In March 2002, the FCC issued a *Declaratory Ruling and Notice of Proposed Rulemaking*, concluding that cable modem service is an interstate information service and subject to FCC jurisdiction under Title I of the Communications Act.³ The FCC declared that the Cable Act limits franchise fees to 5 percent of gross revenues received from *cable service*, and revenues from cable modem service should not be used in calculating these fees.⁴ Problematically, the FCC did not provide direction on universal service requirements and customer service standards.

¹ Description used by FCC Commissioner Michael J. Copps, in his Dissenting Statement, *Inquiry Concerning High Speed Access to the Internet over Cable and Other Facilities, Internet Over Cable Declaratory Ruling, Appropriate Regulatory Treatment for Broadband Access to the Internet Over Cable Facilities*, GN Doc. No. 00-185, CS Doc. No. 02-52, Declaratory Ruling and Notice of Proposed Rulemaking, FCC 02-77 (rel. Mar. 15, 2002).

² *Comments of the Alliance of Local Organizations Against Preemption*, FCC Comments, CS Doc. 02-52, http://gullfoss2.fcc.gov/prod/ecfs/retrieve.cgi?native_or_pdf=pdf&id_document=6513198526, (June 17, 2002).

³ *Inquiry Concerning High Speed Access to the Internet over Cable and Other Facilities, Internet Over Cable Declaratory Ruling, Appropriate Regulatory Treatment for Broadband Access to the Internet Over Cable Facilities*, GN Doc. No. 00-185, CS Doc. No. 02-52, Declaratory Ruling and Notice of Proposed Rulemaking, FCC 02-77 (rel. Mar. 15, 2002).

⁴ *Id.* at ¶ 105.

The Ninth Circuit had previously ruled in the *Portland*⁵ case that cable modem service is a telecommunications service -- suggesting the need for FCC regulation of cable modem services under Title II of the Communications Act. However, the FCC stated that it would exercise its forbearance authority, and it will not, at this time, impose Title II type regulations.⁶ After the *Portland* decision, some cable operators stopped collecting franchise fees on cable modem service revenues. The *NPRM* asks whether franchise fees paid on cable modem revenues should be refunded, and if this is an FCC matter regarding national policy altering the regulatory treatment of cable modem service, or a matter for the courts.⁷ Since the FCC decision, many cable companies have stopped paying franchise fees on cable modem service revenues.⁸

III. LEGAL ARGUMENTS IN PENDING PROCEEDINGS

What follows is a brief description of the local government arguments in the pending FCC and court proceedings.⁹

The Alliance of Local Organizations Against Preemption (ALOAP)¹⁰ petitioned the Ninth Circuit to review the FCC's decision classifying cable modem service as an information service.¹¹ ALOAP argues that the plain language of 47 U.S.C. §522(c) and traditional tools of statutory construction compel the conclusion that any information service a cable operator makes available to all subscribers generally, including cable modem service, is a "cable service." Even if the FCC's interpretation is accorded deference, the determination that cable modem service is not a "cable service" must be overturned as an impermissible construction of the statute. Moreover, the Ninth Circuit's decision in *Portland* provides no basis for affirming the *Declaratory Ruling and NPRM* conclusion that cable modem service is not a "cable service."

ALOAP's comments in the *NPRM* provide additional support for LFA regulatory authority.¹² Franchise fees are a matter of local discretion. Economic principles demand that cable modem service providers pay fair market value for the use of the right-of-way. Section 622 does not prohibit cable modem franchise fees and section 622(g) expressly allows local governments to adopt fees other than cable franchise fees. Fees cannot be avoided by arguing that they are taxes or "revenue producers." Moreover, local franchising will not delay cable modem deployment. The current success of the industry proves that deployment concerns are no

⁵ See, *AT&T Corp. v. Portland*, 216 F.3d 871 (9th Cir. 2000).

⁶ See, *Declaratory Ruling and NPRM*, *supra* note 3, at ¶ 106.

⁷ *Id.* at ¶ 107.

⁸ Including the five largest cable companies: Time Warner, Comcast/AT&T, Charter, Adelphia, and Cox.

⁹ It is not the intent of this article to outline and address all of the arguments raised in these proceedings by the various segments of the industry. For those interested, The National Cable Television Association (NCTA) website is a good source of information for the cable industry's position.

http://www.ncta.com/legislative/judicial_cfm?catID=6&filings=ok.

¹⁰ ALOAP is a coalition of the National Association of Telecommunications Officers and Advisors, The National League of Cities, the National Association of Counties, the US Conference of Mayors and the International Municipal Lawyers Association.

¹¹ See, *Brief of Petitioners*, National League of Cities, et. al v. FCC, , *at*, http://www.natoa.org/public/articles/Brief_to_9th_Circuit_10-10-02.pdf.

¹² ALOAP Reply Comments, *at* http://www.natoa.org/public/articles/ALOAP_FCC_Reply_Comments.pdf

basis for preempting local regulation. Indeed, local regulation has enhanced and will continue to benefit deployment. Finally, customer service and subscriber privacy concerns should be paramount -- the absence of competition requires this regulation. Cable modem service has dominant market power in many communities and LFAs must have authority to address customer service abuses.

IV. IMPACT ON LOCAL FRANCHISING AUTHORITIES

1. Franchise Fees

The estimated impact of the FCC's ruling is a revenue loss of approximately \$284 million in 2002. By 2006, LFAs will be losing approximately \$500-\$800 million in revenue annually.¹³ Consider two examples – Aurora (population 277,000) and Arvada (population 104,000), Colorado. In Aurora, 2001 franchise fee revenues from cable modem services were \$271,132 – about 12% of the total franchise fees paid to the City. In Arvada, 2001 revenue from cable modem service was about \$97,000, and about 13% of total franchise fee revenue. As penetration rates increase, these losses will increase as well.

Is there any other legal authority to recover these fees as compensation for the use of public property? Under state law, some LFAs can require compensation of *any* private user of public rights of way. LFAs should refer to their state law and determine whether a franchise or other legal authorization to provide cable modem service can be required. In addition, LFAs should carefully review the language of existing franchises. If “gross revenues” are defined to include more than just revenues from “cable services,” LFAs may claim that franchise fees are due on cable modem service revenues under existing contractual agreements, regardless of the FCC ruling. Rochester, New York and Chicago, Illinois have filed lawsuits making this claim.

2. Universal Service

Loss of LFA regulatory control threatens universal deployment of cable modem service. LFAs can require community wide build-outs of cable facilities and provision of cable services. The FCC's decision seems to limit LFAs' ability to promote the deployment of broadband services. If the pending rulemaking and court proceeding does not result in a decision that clearly authorizes LFAs to require universal build-out and deployment of cable modem facilities and services, the FCC's policy goal of the deployment of broadband to all Americans in a reasonable and timely fashion¹⁴ will be in jeopardy.

LFA regulatory control has not hampered the deployment of cable modem services. According to Cahners In-Stat/MDR, cable modem Internet access was the most popular residential high-speed access technology in 2001 with a 71 percent increase in worldwide subscribers over the year-end 2000 total.¹⁵ While paying franchise fees on cable modem

¹³ See, ALOAP Reply Comments, at http://www.natoa.org/public/articles/ALOAP_FCC_Reply_Comments.pdf.

¹⁴ See, FCC Website, <http://www.fcc.gov/broadband/>.

¹⁵ In-Stat MDR Market Alerts, Jan. 26, 2002, at <http://www.instat.com/newmk.asp?ID=141>.

revenues, cable companies outpace DSL providers with a 64 percent market share.¹⁶ By the end of 2001, cable's margin over DSL grew for the fifth consecutive quarter.¹⁷ In this dominant market, LFA regulatory oversight is an important tool to aid in the ubiquitous availability of broadband Internet access.

3. Customer Service Regulations

The *NPRM* also seeks input on the effect of the information service classification on local regulation addressing consumer protection and customer service issues. The FCC questions whether Section 632 of the Cable Act allows LFAs to enforce customer service requirements on cable modem service.¹⁸ LFAs have regulatory authority to address customer service issues with respect to cable services; however, the FCC decision makes LFAs unsure whether consumer protection or customer service standards apply to cable modem service.

What direction has the FCC given on customer service regulations in light of the *Declaratory Ruling*? Not much. Initially, the FCC suggested to the Local and State Government Advisory Committee (LSGAC) that because cable modem services are not "cable services," customer service issues for these services would be addressed at the FCC. Shortly thereafter, and perhaps recognizing that it did not have sufficient resources, the FCC sent a May 14, 2002 letter to the LSGAC stating that it would continue to refer all consumer complaints about cable modem service to LFAs. In other words, "don't charge franchise fees on cable modem services, and we haven't decided yet whether you have any authority for customer service enforcement, but in the meantime, we'll continue to refer consumers to you with their problems about this service."

Many LFAs do take customer complaints about cable modem service, although they differ in how complaints are addressed. Montgomery County, Maryland and the Metro Area Communications Commission (Portland, Oregon suburbs) report complaints to the cable operator but recognize little authority to enforce standards. Montgomery County has recently passed local legislation authorizing the County Executive to adopt cable modem standards. The new law creates a new Commission to hear complaints and impose fines for violations of up to \$1000. It is yet to be seen whether this local regulation will be challenged. Seattle applies its standards to cable modem service and indicates that its cable operator does compensate customers for violations of the standards related to *both* cable and cable modem services. If the FCC rulemaking does not clarify that LFAs have authority to enforce cable customer service standards on cable modem services, it is likely that LFAs will look to their authority under state consumer protection laws and adopt new regulations, separate from the cable customer service standards, leading to further diversity in cable operators' compliance obligations.

¹⁶ Matt Stump, *Telcos' DSL Dilemmas A Good Sign for Cable*, *BroadbandWeek*, (Dec. 3, 2001), at http://www.broadbandweek.com/news/011203/011203_telecom_dsl.htm.

¹⁷ *Id.*

¹⁸ See, *Declaratory Ruling and NPRM*, *supra* note 3, at ¶ 108.

V. CONCLUSION

The lack of regulatory clarity and the conclusions of the *Declaratory Ruling and NPRM* have created a dangerous uncertainty in the growing market for cable broadband services. By placing cable modem service into the generally deregulated interstate information service category, subject only to the FCC's ancillary jurisdiction under Title I, the FCC has done more than create confusion with the deployment of broadband services over cable systems. As Commissioner Copps stated, decisions addressing how we deploy broadband implicate, "what kinds of options consumers will be able to choose from, what kinds of protections they will have against misguided or fraudulent business practices, and what kinds of opportunities will be available to those in our society who do not share fully in our general prosperity."¹⁹ Local governments must remain committed to forcefully addressing their appropriate regulatory role at the FCC, on Capitol Hill, at State Legislatures and in the courts.

¹⁹Dissenting Statement of Commissioner Michael J. Copps, *supra* note 1, Declaratory Ruling and Notice of Proposed Rulemaking, FCC 02-77.