

FRANCHISING ALERT

**FCC Issuance of Franchising Report and Order
and Further Notice of Proposed Rulemaking**

In a wide-ranging “Report and Order” released March 5, 2007 (the “Franchising Order”), the Federal Communications Commission (“FCC” or “Commission”) has concluded that the “local franchising process in many jurisdictions constitutes an unreasonable barrier to entry” and has therefore adopted rules and policies designed, the Commission says, to “facilitate and expedite entry of new cable competitors into the market for the delivery of video programming, and accelerate broadband deployment....” A summary of the Franchising Order is set forth below.

In addition, the Commission has issued a “Further Notice of Proposed Rulemaking” (“Further Notice”) requesting public comment on a number of issues, including the Commission’s tentative conclusion that the findings in the Franchising Order should apply to incumbent cable operators in the renewal process. A summary of the issues addressed in the Further Notice is also set forth below.

Unless the FCC or a court delays the effectiveness of the rules and policies adopted in the Franchising Order, the Franchising Order will become effective thirty (30) days after it is published in the Federal Register. In addition, Comments on the Further Notice are due thirty (30) days after publication in the Federal Register, with Reply Comments due fifteen (15) days thereafter.

The purpose of this Memorandum is to provide a summary of the key aspects of the Franchising Order and the Further Notice. This Memorandum is not intended to be a comprehensive discussion of every aspect and policy addressed by the Commission. As counsel for NATOA, NLC, USCM, NACo, ACM and ACD, Arent Fox is actively developing with its clients the appropriate responses to the FCC’s actions. Accordingly, this Memorandum is not intended to be, nor should it be interpreted to be, an analysis of, or an agreement as to, the appropriateness of the FCC’s actions, or a discussion of the specific bases on which such actions may be challenged.

SUMMARY OF FCC ACTIONS IN THE FRANCHISING ORDER

FCC Jurisdiction/Preemption

As a general matter, the FCC has concluded that it has jurisdiction to take all of the actions set forth in the Franchising Order, including *the preemption of local laws, regulations and practices which conflict with the “rules or guidance adopted” in the Franchising Order*. The Commission finds that it is not purporting to identify in this Franchising Order “every local requirement that this Order preempts,” but that the local laws that are preempted include those that are in conflict with the FCC’s rules adopted in the Franchising Order (which are summarized below). *The Commission has, however, also held that local laws, regulations and practices are not preempted where the state in which the local franchising authority, i.e., county or municipal level franchise authority (“LFA”), is located has already circumscribed the LFA’s authority with regard to such provisions, or has otherwise specifically authorized such provisions. In addition, by its Order, the Commission does not preempt state law or state level franchising decisions.*

Time Limits

- Maximum Time Limit for Franchise Decision. The FCC has imposed a time limit specifying the maximum length of time that an LFA may take to consider a competitive franchise application. The Franchising Order requires an LFA to render a decision on the application (i) within 90 days (after the new entrant’s submission of an application or other required information and payment of a reasonable application fee, where applicable), where the applicant holds an existing authorization to access rights-of-way in the locality; and (ii) within 180 days, where the applicant does not hold an existing authorization with respect to the rights-of-way. If the LFA and the new entrant agree, the above time periods can be extended. In addition, “an LFA may toll the running of the 90-day or six-month time period if it has requested information from the franchise applicant and is waiting for such information.” Once the information is received, the time period would automatically begin to run again.
- Interim Franchise Deemed Granted if Decision Not Made Within Maximum Time Limit. The Commission held that if the LFA fails to act within the time limits set forth above, the LFA will be deemed to have granted the applicant an interim franchise based on the terms proposed in the provider’s application. This interim franchise would remain in effect until the LFA takes final action on the application.
- Preemption of Pre-Application Negotiations and Other Procedures. The FCC also held that it is preempting any requirement that an LFA imposes on an applicant to negotiate or engage in any regulatory or administrative processes before the applicant files the application.

Build-Out Requirements

- The Commission concluded that “it is unlawful for LFAs to refuse to grant a competitive franchise on the basis of unreasonable build-out mandates.” Examples of build-out requirements that the FCC has found “seem unreasonable” include the following:
 - ◇ Absent other factors, requiring a new entrant to serve everyone in a franchise area before it has begun serving anyone.
 - ◇ Requiring incumbent LECs and other facilities-based entrants to build out beyond the footprint of their existing facilities before they have even begun providing cable service.
 - ◇ Absent other factors, requiring more of a new entrant than an incumbent cable operator (e.g., requiring a new entrant to build out its facilities in less time than originally afforded to the incumbent cable operator, or requiring a new entrant to provide service to areas of lower density than those that the incumbent cable operator is required to serve).
 - ◇ Requiring a new entrant to build out to buildings or developments to which it cannot obtain access on reasonable terms.
 - ◇ Requiring a new entrant to build out to certain areas or customers that it cannot reach using standard technical solutions.
 - ◇ Requiring a new entrant to build out to areas where it cannot obtain reasonable access to and use of the public rights of way.
- The FCC found that, on the other hand, it would seem reasonable for an LFA in establishing build-out requirements (i) to consider the new entrant’s market penetration, and (ii) to consider benchmarks requiring the new entrant to increase its build-out after a reasonable period of time had passed after initiating service and taking into account its market success.

Redlining

- The FCC held that an LFA may deny a franchise to an entity which plans to provide cable service with the intent to redline (i.e., with the intent to deny cable service to a group based on the income of the residents of the local area in which the group resides).

Franchise Fees

- The Commission confirmed that a cable operator is not required to pay franchise fees on revenues from non-cable services.
- The FCC concluded that the following requirements or charges generally count towards the five percent cap on franchise fees: (i) attorneys fees; (ii) consultant fees; (iii) application or processing fees that exceed the reasonable cost of processing the application; (iv) acceptance fees; (v) free or discounted services provided to an LFA; (vi) any requirement to lease or purchase equipment from an LFA at prices higher than market value; and (vii) any requests made by LFAs that are unrelated to the provision of cable services by a new provider in the market (e.g., lump sum grants not related to PEG access for municipal programs such as libraries, recreation departments, detention centers or other payments not related to PEG access would be subject to the five percent cap).
- The FCC held that the only items that are incidental under Section 622(g)(2)(D), and which therefore do not count towards the five percent cap on franchise fees, are those listed in the statute (i.e., bonds, security funds, letters of credit, insurance, indemnification, penalties or liquidated damages), as well as other minor expenses (e.g., application or processing fees that do not exceed the reasonable cost of processing the application).
- The Commission concluded that while payments for the costs of building PEG facilities (i.e., costs incurred in or associated with the construction of PEG access facilities) do not count towards the five percent cap, payments in support of the use of PEG access facilities, such as salaries and training, do count towards the five percent cap on franchise fees.

PEG/Institutional Networks

- The FCC rejected a proposal to adopt standard terms for PEG channels, holding that LFAs are free to establish their own requirements for PEG, provided that the non-capital costs of such requirements are offset from the provider's franchise fee payments.
- The Commission concluded that an LFA cannot impose on a new entrant "more burdensome" PEG carriage obligations than it has imposed on the incumbent cable operator (i.e., the FCC found that it is unreasonable for an LFA to require a new entrant to provide PEG support that is in excess of the incumbent cable operator's obligations). The FCC concluded that a pro rata cost sharing approach is one reasonable means for the new entrant to meet the statutory requirement of the provision of adequate PEG facilities, and that it is reasonable to determine the pro rata shares based on the subscriber base of each provider.

- The FCC concluded that “completely duplicative” PEG and I-Net requirements imposed by LFAs are impermissible, but an I-Net is not duplicative if it would provide additional capability or functionality beyond that provided by existing I-Net facilities.
- The Commission further held that an LFA cannot require, as a condition to granting a franchise, that an applicant pay the face value of an I-Net that will not be constructed.

Mixed-Use Networks

- The FCC concluded that LFAs’ jurisdiction applies only to the provision of cable services over cable systems, and that to the extent a cable operator provides non-cable services or operates facilities that do not qualify as a cable system, an LFA may not refuse to award a franchise based on issues related to such non-cable services or facilities. Similarly, the FCC found that an LFA has no authority to insist on an entity obtaining a separate cable franchise in order to upgrade non-cable facilities (e.g., the FCC concluded that so long as there is a non-cable purpose associated with a network upgrade, the provider is not required to obtain a franchise until it proposes to offer cable services).
- The FCC also held that an LFA may not use its video franchising authority to attempt to regulate a provider’s entire network beyond the provision of cable services (e.g., the FCC found that the provision of video services pursuant to a cable franchise does not provide a basis for customer service regulation by local law or franchise agreement of a cable operator’s entire network, or any services beyond cable services).
- On the issue of regulation of interactive on-demand services, the Commission notes that “Section 602(7)(c) excludes from the definition of ‘cable system’ a facility of a common carrier that is used solely to provide interactive on-demand services.”
- The Franchising Order does not address whether video services provided over Internet Protocol are “cable services.”

Preemption of Level Playing Field Requirements

- Another example of the types of local laws, regulations and practices that the FCC has found are preempted are level playing field laws that require the LFA to refrain from executing a franchise agreement with a new entrant that is more favorable to the new entrant than the franchise agreement executed with the incumbent cable provider.

SUMMARY OF FCC ACTIONS IN THE FURTHER NOTICE

- The Commission seeks comment on its *tentative conclusion that the Franchising Order should apply to incumbent franchise cable operators as they negotiate renewal of their agreements with LFAs*, and the FCC also seeks comment on its authority to implement this finding.
- In addition, the FCC seeks comment on what effect, if any, the findings in the Franchising Order will have on most favored nation clauses that may be included in existing franchise agreements.
- The FCC also seeks comment on its tentative conclusion that it cannot preempt state or local customer service laws that exceed the Commission's standards, nor can it prevent LFAs and cable operators from agreeing to more stringent standards.
- The Commission stated its intention to issue its rulings on the Further Notice within six months after release of the Franchising Order.