The Florida Senate

Interim Project Summary 2007-105 *November 2006*

Committee on Communications and Public Utilities

REVIEW OF COMPETITION AND REGULATION OF CABLE AND VIDEO PROGRAMMING SERVICES

SUMMARY

Federal and state law provide for the regulation of cable services. Innovation and convergence of existing technologies are expanding communications and information services, blurring the distinctions between landline telephone, Internet, cable, wireless, and satellite services. Moreover, the business plan of these service providers has become to bundle all types of services into one package deal. To encourage innovation and investment in Florida, with the desired result being robust competition and maximization of consumer choice, regulations could be standardized and eased, with some continuing ability of local governments to protect their constituent video services customers.

BACKGROUND

This report reviews the effects of regulation and competition on the provisioning of cable and video programming services. Cable service can be viewed as the delivery infrastructure, certain programming, and control of the service by the provider with some subscriber interaction. Video programming is the programming provided by a television broadcast station or that which is considered comparable. Video programming is regulated under the Federal Cable Act and cable services are regulated at the federal, state, and local levels.

The Federal Cable Act (Cable Act)[1], was enacted for purposes set forth in 47 U.S.C. §521. These purposes are to:

- Establish a national policy concerning cable communications;
- Establish franchise procedures and standards which encourage the growth and development of cable systems and which assure that cable systems are responsive to the needs and interests of the local community;
- Establish guidelines for the exercise of federal, state, and local authority with respect to the regulation of cable systems;
- Assure that cable communications provide and are encouraged to provide the widest possible diversity of information sources and services to the public;
- Establish an orderly process for franchise renewal which protects cable operators against unfair denials of renewal where the operator's past performance and proposal for future performance meet the standards established by the Cable Act; and
- Promote competition in cable communications and minimize unnecessary regulation that would impose an undue economic burden on cable systems.

The Cable Act allows a local franchising authority to award one or more franchises within its jurisdiction, except that it may not issue an exclusive franchise or unreasonably refuse to award an additional competitive franchise. The franchise is to be construed to authorize the construction of a cable system over public rights-of-way and through easements. In using the easements, the cable operator must ensure:

- The safety, functioning, and appearance of the property and the convenience and safety of others is not adversely affected by the installation or construction of cable facilities;
- The cost of installation, construction, operation, or removal of such facilities is borne by the cable operator or subscribers, or both; and
- The owner of the property is justly compensated by the cable operator for any

[1] 47 U.S.C. §521 et. seq.

damages caused by the installation, construction, and operation of facilities.

In awarding the franchise, the local franchising authority:

- Shall allow the applicant's cable system reasonable time to be able to provide cable service to all households;
- May require adequate assurance that the cable operator will provide adequate public, education, government (PEG) access channel capacity, facilities, or financial support; and
- May require adequate assurances that the cable operator has the financial, technical, and legal qualifications to provide cable service.

Finally, the local franchising authority must assure that access to cable service is not denied to a group of potential subscribers because of their economic status.

State regulation is set forth in s. 166.046, F.S., which provides minimum standards for cable television franchises between the local government and the provider. The section provides that no municipality or county shall grant a franchise for cable service to a cable system within its jurisdiction without first, at a duly noticed public hearing, having considered:

- The economic impact upon private property within the franchise area;
- The public need for such franchise, if any;
- The capacity of public rights-of-way to accommodate the cable system;
- The present and future use of the public rights-of-way to be used by the cable system;
- The potential disruption to existing users of the public rights-of-way to be used by the cable system and the resultant inconvenience which may occur to the public;
- The financial ability of the franchise applicant to perform;
- Other societal interests as are generally considered in cable television franchising;
- Such other additional matters, both procedural and substantive, as the municipality or county may, in its sole discretion, determine to be relevant.

The section provides that no municipality or county shall grant any overlapping franchises for cable service within its jurisdiction on terms or conditions more favorable or less burdensome than those in any existing franchise within such municipality or county. However, this restriction does not apply when the area in which the overlapping franchise is being sought is not actually being served by any existing cable service provider holding a franchise for such area. Finally, consistent with federal law, the section provides that nothing in the section shall be construed to prevent any municipality or county from imposing additional terms and conditions upon the granting of such franchise as such municipality or county shall in its sole discretion deem necessary or appropriate.

Both federal and state law authorize local governments to require a franchise agreement to use its public right-of-way and operate a cable service within its corporate limits.[2] Cable franchises are the agreement or ordinance setting forth the terms on which a cable company is given permission to provide cable service in a municipality or county. By federal and state law, a cable company must have such a franchise to use the public rights-of-way for its lines and to provide service.[3] Franchises cover what services are to be provided, which company is authorized to provide cable service and what happens if the company changes, where the service is to be provided, the fees and other compensation the company provides the governmental entity, the protections for use of the rights-of-way, customer service requirements, channels for use by the local government, schools, and the public, and the financial support for such channels.

In Florida, franchise agreements are negotiated with either a municipality or a county (and sometimes with both for any given county). The term of these agreements generally are for 15 years. Expiration of these agreements varies throughout Florida. Agreements may be short and contain a few general terms or complex with many specific terms included. Some franchise agreements have specific provisions that cause a renegotiation of the agreement to adopt terms or conditions of subsequently negotiated agreements with a competitive provider that the incumbent believe are more favorable than those in its own agreement. The following topics may be included in a current franchise agreement: definitions; grant of authority, limits, reservations; provision of service and area; system faculties, capacity and operation; public, education, and government services; public benefit support; insurance and indemnification; transfer, renewal, enforcement, and termination of franchise; security fund or letter of credit; remedies and liquidate

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[2] *See* 47 U.S.C. §551, et. seq. and s. 166.046, F.S.
[3] See 47 U.S.C. §541 and s. 366.401, F.S.

damages; and customer services, information, and rights.

METHODOLOGY

Staff met with representatives from Florida landline telecommunications companies, Florida cable companies, city and county associations, relevant state agencies and consumer groups. The Legislature's Office of Economic and Demographic Research (EDR) assisted in determining potential economic impact by sending questionnaires to cities and counties and providing certain results to staff.[4] Staff conducted research into Federal and Florida law, as well as reviewed recent laws enacted in other states.

FINDINGS

The impetus for this project was two bills filed in the 2006 Regular Session, HB 1199 (Cable Television Franchises) and SB 900 (Cable Services and Video Programming). The surface issue this report seeks to answer is how to franchise cable and video programming service to maximize competition among the service providers. The deeper, broader issue, however, is how to view and regulate the total communication services market so as to maximize competition and consumer choice in all forms of communication services, with the initial sub-issue to be determined being how to regulate entry into the video segment of the market to achieve these goals of competition and choice.

Historically, the various forms of communication services, voice, video, and data, developed independently, using different technology. As a consequence, regulation of the services was developed independently as well, with each regulatory plan based upon the technology used to deliver the service. Now, the technologies are converging and one company can provide all three types of communication services, using its same technology for all. This is the general business plan for most communication companies, to bundle voice, video, and data services in one package deal. Bundling appears to provide the most efficient and cost effective method of providing these services to customers.

From a regulatory point of view, a traditional cable company can bundle these services fairly easily. The company would simply need to obtain a certificate to provide voice service from the Florida Public Service Commission (PSC). An Internet company, and some landline telephone companies, *may* be able to bundle easily. Moreover, depending on how the service is provided, such companies *may* not meet the definition of "cable" to trigger the local franchise requirement.

However, most landline companies will have to obtain a franchise for any area they wish to serve, on a local government by local government basis. This process is time consuming, and a longer time to market means less market share and money. Companies that plan on providing a bundle of services must comply with different regulatory schemes for some of the services they provide which is inefficient and could be unnecessary barriers to competition.

In 1995, the Florida Legislature amended Chapter 364, F.S., to allow for competition in the state's landline telecommunication markets. The apparent intent was to stimulate competition between landline companies. The Legislature found that "competition in the telecommunications services is in the public interest and will provide customers with freedom of choice, encourage the introduction of new telecommunications services, encourage technical innovation, and encourage investment in telecommunication infrastructure." This has not happened to any great extent.

The Federal Government soon followed Florida and enacted the Federal Telecommunications Act of 1996 which enabled Competitive Local Exchange Carriers (CLEC) to enter the local telecommunication marketplace nationwide. The Act specifically used the words *all providers* to highlight that the intent of the Act was to open the telecommunication markets to all providers and was expected to blur traditional industry distinctions.[5] This policy would create intermodal competition, that is, competition across technology lines such as cable and voice over Internet protocol (VoIP). Since then, technology has changed the traditional distinction between services provided by landline, wireless, and Internet providers of communication services resulting in nontraditional service providers being able to offer substitutions for traditional landline voice services.

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[4] EDR sent a questionnaire to all municipalities and counties. Copies of all responses and EDR's summary are in committee files.

[5] FCC 96-325, CC Docket no. 96-98, "Implementation of the Local Competition Provisions in the Telecommunication Act of 1996, First Report and Order," August 8, 1996

Landline telecommunication service providers serve a decided majority of basic local service customers (approximately 10.95 million access lines), but intermodal competition is infringing on their market share. In order to retain market share, they or their affiliates have actively expanded their wireless and broadband operations[6] to maintain a presence and experience growth in markets. The PSC's 2006 *Report on the Status of Competition in the Telecommunications Industry* (report) stated that Florida residential landlines had fallen by 8 percent from 2005 to 2006. The report acknowledged that accurate numbers reflecting the effect of wireless, cable, broadband, and VoIP providers are difficult to establish. Forrester Research estimates that nationally to date 8 percent of customers have replaced landline with wireless telephones. The PSC stated that a reasonable estimate of Florida VoIP subscribers is approximately 662,000.

What is clear from this data is that competition for landline access lines is not attracting companies with the market share to compete head to head. For example, AT&T and MCI no longer seek new residential customers, which contributed to the decreased residential access line growth in 2005. The advancement in technology has provided intermodal competition which is capable of providing the benefits which Chapter 364, F.S., and subsequent Florida legislation intended to achieve.

The Florida Legislature again took important steps to develop competition when the communications services tax (CST) law and the rights-of-way legislation were implemented in 2000 and 2001. The Legislature sought to promote competition among providers of communications services and to treat these providers in a nondiscriminatory and competitively-neutral manner when imposing rules or regulations governing taxing and access to rights-of-way.

The Legislature commented on the advantages of competition and the need to create competitively neutral entry into markets when stating intent in the CST law.[7] Section 202.105, F.S., provides that important state interests are fulfilled by reforming the tax laws to provide a fair, efficient, and uniform method for taxing communications services. The findings include, in part, that Chapter 202, F.S.:

- Is essential to the continued economic vitality of this increasingly important industry because it restructures state and local taxes and fees to account for the impact of federal legislation, industry deregulation, and the convergence of service offerings that is now taking place among providers;
- Promotes the increased competition that accompanies deregulation by embracing a competitively neutral tax policy that will free consumers to choose a service provider based on tax-neutral considerations;
- Spurs new competition by simplifying an extremely complicated state and local tax and fee system, lowering the cost of collection, and increasing service availability; and
- Will ensure that the growth of the industry is unimpaired by excessive governmental regulation by streamlining the tax system.

The Legislature realized that in addition to creating a competitively neutral tax policy, it must allow equal access to infrastructure, which led to the creation of s. 337.401, F.S., which provides for nondiscriminatory and competitively neutral treatment of providers of communication services in governing the placement of maintenance of communication facilities in public roads and rights-of-way.

The simplified tax authority under chapter 202, F.S., and the right-of-way legislation in s. 337.401, F.S., allowed providers of communication services equal access to markets which encourages intermodal competition.

The Legislature should consider taking the next step to adapt regulation to changes in consumer demands, technology, and markets. Regulation could be based upon the type of service provided, not the technology used or the history of the industry. If the regulatory paradigm is changed, it will take time and will have far-reaching consequences. The best way to accomplish this transition with the least disruption to the market and consumers is to phase in certain requirements. The first of these could be to create a state-wide video service provider certificate, much like the telecommunications services certificate. The statute could be broadly applicable to any and all providers of video services.

In making a shift from local franchises to state certificates, there are three local issues to be resolved:

[6] Broadband includes data and VoIP
[7] *See* Chapter 202, F.S.

buildout requirements, PEG channels and in-kind contributions, and customer protection.

The first local issue is buildout. Current franchise agreements may require the cable company to build infrastructure and provide service to specified areas in a specified timeframe without regard to the customer demand. To impose a buildout requirement on only one class of video service providers could put those providers at a competitive disadvantage. On the other hand, it could be very costly to require that each provider build a complete, redundant system. Additionally, representatives of consumer groups agree that customers have and will continue to have choice among service providers in obtaining services, with satellite a technologically and economically feasible alternative. Therefore, it appears a buildout requirement is no longer a necessity.

The second local issue is PEG channels and in-kind contributions. PEG channels provide a public benefit, as recognized by Congress. If a PEG requirement is standardized, knowing the current status of franchise terms is important. According to EDR's questionnaire, of 65 responses, there is an average of 1.8 active PEG channels provided by all current cable TV franchise agreements and at least 37 percent of the respondents have a PEG related employee. The average number of hours of original content per day range from 15.4 to 7.5, with the mode of 11.5 hours. To date, EDR was not able to determine a dollar amount for in-kind support currently provided by cable service providers for those PEG channels, but staff anticipates EDR will be able to provide a detailed economic analysis if a bill is introduced.

As another requirement, the Legislature could continue PEG access to all video service customers. However, there is no precedent as to how PEG services will be provided and at what cost in the new bundled services marketplace. As a transition, the Legislature could enact a statute that doesn't impair existing franchises, that provides a PEG standard where there is no existing applicable one, and that provides flexibility to add or remove channels for underutilization or additional need. This could be done by using the PEG standards of existing franchises, where they exist; by creating a statutory standard for use where PEG standards do not exist; or by allowing the parties to an existing franchise to agree to terminate the franchise and apply the statutory PEG standard instead. For example, the statutory standard could set a percentage of some value the statewide franchise holder would pay to the appropriate county or municipality. Also, a provision should be made for modifying both standards when capacity isn't being utilized or more capacity is needed.

The third local issue is customer protection. Both bills filed last session allowed local governments to adopt an ordinance to address certain issues, including consumer protection. Senate Bill 900 allowed local governments five years to adopt such an ordinance. House Bill 1199 allowed local governments one and one-half years to adopt an ordinance, unless a prospective service provider requested an earlier adoption, in which case, the local government had 60 days. Provisions on consumer protection were optional. Whether an ordinance addressed consumer protection or not, the standard was that an incumbent cable service provider had to comply with customer service requirements reasonably comparable to, and not in excess of, the requirements of federal rules, until there were two or more providers in the area, not including satellite. If a local government adopted an ordinance on consumer protection, it could require that cable service quality complaints be filed with an appropriate local government office, with a requirement that the office address the complaints expeditiously by assisting with the resolution of such complaints between the complainant and the certificate holder. The bill also designated the Department of Agriculture and Consumer Services (DACS) as the state entity for resolution of consumer complaints.

To maximize competition and consumer choice, another requirement could be to standardize regulation, including consumer protection, as much as possible. There are, however, possible efficiencies to be had in resolving consumer complaints at the local level. To achieve both of these benefits, all video service providers could be required to comply with the requirements of federal cable regulations on consumer protection; local governments could be given an initial opportunity to resolve complaints should they choose; and otherwise DACS could be the resolution authority.

Finally, as existing local franchise contracts expire, this new regulatory system could replace them. Additionally, parties to each existing local franchise contract could be authorized to agree to terminate the contract and switch to the new system upon meeting any prerequisites such as the franchising cable company becoming certificated and the local government adopting a customer protection and service quality ordinance. Any local government that does not terminate existing franchise agreements could be subject to subsection 166.046(3) F.S., which prohibits the municipality or county from granting any overlapping franchises for video service within its jurisdiction on terms or conditions more favorable or less burdensome than those in any existing franchise within such municipality or county. Such a phased-in implementation would be the most efficient and equitable for local governments whose citizens have concerns about the new system, giving them more time to adopt the new ordinance and otherwise provide for the transition.

This phased-in implementation could avoid any problem with challenges that the new statute unconstitutionally impairs the existing franchise contracts. The issue of impairment arises when legislation has a detrimental impact on an existing contract. The Florida Constitution provides "[n]o . . . law impairing the obligation of contracts shall be passed."[8] Impairment of contract should not be at issue if any revisions or terminations of existing contracts are voluntary and not a consequence of legislation.

If, however, legislation is enacted that revises or terminates an existing franchise contract without the voluntary participation of the contracting parties, a challenge may be brought. Laws which impair the obligations of private contracts may be constitutional if they are reasonable and necessary to serve an important public purpose. *Yellow Cab Company of Dade County v Dade County*, 412 So.2d 395 (Fla. 1982). To determine if an impairment is reasonable and necessary to serve an important public purpose, the court applies a balancing test to weigh the impact on contract rights against the public purpose and the state's interest. In doing so, the court would consider the following factors:

- Was the law enacted to deal with a broad, generalized economic or social problem?
- Does the law operate in an area which was already subject to state regulation at the time the parties' contractual obligations were originally undertaken, or does it invade an area never before subject to regulation by the state?
- Does the law effect a temporary alteration of the contractual relationships of those within its coverage, or does it work a severe, permanent, and immediate change in those relationships irrevocably and retroactively?

Pomponio v Clairdge of Pompano Condominium, Inc., 378 So.2d 774 (Fla.1980).

As a side issue, there has been disagreement on the ability of a local government to raise a challenge of impairment of contract, with both sides presenting arguments. There are Florida Supreme Court cases on this issue that hold that local governments can bring this challenge. While these are old cases, they have not been overruled, and are still good law.

It is unlikely that the foregoing recommendations will raise any immediate issues relating to rights-of-way and the communications services tax laws as they have already been made competitively neutral from a technology perspective, but they may need some conforming, technical revisions. Additionally, as services and technologies continue to converge, it will become necessary to revisit Chapter 364, F.S., and the regulation of landline telephone companies, especially with regard to societal benefit provisions such as carrier of last resort, universal service, Lifeline, and funds to support these programs.

RECOMMENDATIONS

In order to take the next step in regulation of communications services, the Legislature could create a statewide certificate for video service providers. However, video service providers should not be required to buildout a local government's jurisdiction or another physical area. The current franchise contract provisions on PEG channels and in-kind contributions could be the presumed levels for these requirements, with a statutory standard if there is no applicable existing franchise provision. Local governments could be given a set time in which to adopt an ordinance on customer protections and service quality, with the federal standards applying in instances where no ordinance is adopted. Finally, the new system could be phased in, allowing the parties to existing local franchise contracts to agree to terminate those contracts to avoid impairment of contract issues. As these changes are implemented, they may necessitate changes in other statutes, such as local government regulation of rights-of-way and communications services tax rates. Additionally, if the legislation is successful and full competition develops among traditionally non-competitive companies due to convergence of technologies, further changes will be necessary to Chapter 364, F.S., the telecommunications statute.

[8] Art. 1, S. 10, Florida Constitution.