infrastructure."[32] The Commission's exclusive jurisdiction over CMRS has been affirmed on numerous occasions.[33]

The Commission has held that state and local statutes requiring wireless carriers to certify prior to construction and operation that they will serve the public convenience and necessity are prohibited CMRS entry regulation.[34] This is consistent with the Commission's long-standing position that statutes or regulations obligating wireless carriers to make showings of character, technical, or financial fitness also are impermissible entry regulations.[35]

A now vacated Eugene, Oregon ordinance provides an example of how cities are overstepping their proper roles under Section 332. The ordinance required operators of communications facilities, including wireless carriers, to register with the city, obtain a license, and obtain a permit before providing service through facilities maintained or operated upon any public right-of-way.[36] The ordinance also instructed the city manager to evaluate "whether the

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[32] H.R. Rep. No. 103-111, at 260 (1993).

[33] See, e.g., Iowa Utilities Board v. FCC, 120 F.3d 753, 800 n.21 (8th Cir. 1997), cert granted sub nom AT&T v. Iowa Utilities Board, 118 S.Ct. 879 (1998); Connecticut Dept. of Public Util. Control v. FCC, 78 F. 3d 842 (2d Cir. 1996) (recognizing FCC's exclusive jurisdiction over CMRS).

[34] Implementation of the Local Competition Provisions in the Telecommunications Act of 1996, First Report and Order, 11 FCC Rcd 15499, 15763 ¶ 1026 (1996) ("Local Competition Order").

[35] See Preemption of State Entry Regulation in the Public Land Mobile Service, Report and Order, 59 RR 2d 1518, 1519 (1986), remanded on other grounds, National Association of Regulatory Commissioners v. FCC, slip op. No. 86-1205 (D.C. Cir. March 30, 1987), affirmed on remand, Preemption of State Entry Regulation in the Public Land Mobile Service, Memorandum Opinion and Order, 2 FCC Rcd 6434 (1987). In this order, which was issued before the enactment of current section 332(c), the FCC preempted various State and local regulations that had the effect of "prohibiting or impeding the entry of" public land mobile services.

[36] Eugene Code §§ 3.405, 3.410, 7.290(1).

applicant is financially, technically, and legally qualified" to complete a facility.[37] In effect, the city required CMRS providers to obtain local regulatory approval before they could provide service in Eugene, despite the fact that the Commission already requires CMRS providers to demonstrate that they are financially, technically and otherwise qualified to provide service before it authorizes them to construct and operate CMRS systems.[38] Because the ordinance required CMRS providers to obtain additional, special licenses and approvals from the city in order to provide CMRS in the city, it impermissibly regulated the entry of CMRS in violation of Section 332(c)(3)(A).[39]

D. Title VI Limits Local Authority over Telecommunications Services Offered by Cable Operators

Local governments may not use their franchising authority under Title VI of the Communications Act to regulate or restrict the telecommunications services offered by cable operators. Section 621(b)(3)(B) of the Communications Act bars cities from "prohibiting, limiting, restricting or conditioning the provision of telecommunications services by a cable television operator." In response to a complaint by TCI, the Commission specifically ruled that a city may not impose a condition on a cable construction permit in order to force the cable operator to comply with a municipal telecommunications ordinance.[40]

To the extent that cable operators offer telecommunications services, such services are subject to regulation under Title II. But if such telecommunications services are provided over

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[37] Eugene Code § 3.430(b).

[38] 47 USC § 308(b).

[39] See AT&T Communications of the Pacific Northwest, Inc. v. City of Eugene, Oregon, Case No. 16-98-12672 (Or. Cir. Ct. March 1, 1999) (granting AT&T's Motion for Summary Judgment).

[40] TCI Cablevision of Oakland County at ¶ 75.

existing cable facilities, and they impose no additional burden on the public right-of-way, then, as set forth above, there would be no municipal authority under Section 253(c).

In addition, Section 624(e) of the Communications Act states that no franchising authority may "prohibit, condition, or restrict a cable system's use of any type of subscriber equipment or any transmission technology." The Commission has held that Section 624(e) prohibits localities from regulating "in the area[] of transmission technology,"[41/] and that it "eliminates the authority of franchising authorities to interfere with a cable operator's choice of the . . . transmission technology to be used in its cable system."[42/]

E. The Commission Should Adopt A National Policy Regarding the Scope of Permissible Local Rights-Of-Way Ordinances

The Commission should adopt a clearly articulated national policy regarding the scope of permissible local rights-of-way management activity. Recognizing that municipal telecommunications regulation can discourage competition and prevent the development of seamless, statewide networks,[43/] numerous states have taken steps to limit local governments to permissible rights-of-way management activities and prevent municipal telecommunications ordinances from usurping the states' traditional regulatory authority over telecommunications.[44/]

41/ See Implementation of Cable Act Reform, 14 FCC Rcd 5296, 5350-56 (1999).

42/ TCI Cablevision of Oakland County, 12 FCC Rcd at 21399.

43/ See, e.g., Letter from Hon. Susan Clark, Chairman, Florida Public Service Commission, to the Hon. Reed Hundt, CSR-4790 (Dec.11, 1996) (asking the FCC to give appropriate consideration to the authority over telecommunications granted to State commissions pursuant to State law, noting that Florida law gives the FPSC exclusive jurisdiction over telecommunications services); Letter from California Public Utilities Commission to City Attorney, Cupertino, CA (Dec. 9, 1996) (local telecommunications ordinance addressing matters other than disruptions to public rights-of-way exceeds the city's lawful authority and amounts to the "impermissible municipal regulation of telecommunication services, a function expressly reserved to [the CPUC] and the Federal government").

44/ See, e.g., Colo. Rev. Stat. §§ 38-5.5-101-108; Fla. Stat. ch. 364.0361, 337.401; Mich. Comp. Laws §§ 484.2251-2253; Minn. Stat. §§ 237.162-163; Ohio Rev. Code §§ 4939.02-03; see also

While these state efforts can be helpful, a state-by-state approach to reining in impermissible municipal actions is time consuming and leads to a patchwork of differing regulatory regimes. Cities also have challenged these statutes as unconstitutional, tying the states up in litigation and limiting their effectiveness.[45/] A national solution for this problem is clearly needed.

A national policy that clearly establishes the scope and substance of permissible local rights-of-way authority is vital to ensuring the future growth of facilities-based competition. Ideally, carriers and local governments would resolve rights-of-way disputes amicably, but this has proved difficult in practice. Efforts to find "common ground" between carriers and cities should not lead to a muddling of what, for the foregoing reasons, needs to be a clear articulation of principles. Instead, the Commission should adopt principles that are consistent with the requirements of the Communications Act and adhere to the Commission's own and judicial precedent on matters of local authority over rights-of-way.

1. Scope of Rights-of-Way Management.

The Commission should restate its prior holdings that permissible management functions under Section 253(c) are limited to:

- Regulation of time or place of excavations;
- Non-discriminatory requirements that a company place its facilities underground rather than overhead;

"Legislatures Continue Examination of Municipal ROW Policies," Cable Monitor, Feb. 2, 1998, 2-3.

[45/] See, e.g., Complaint for Declaratory and Injunctive Relief, City of Dublin and City of Upper Arlington v. Ohio (Ct. Common Pleas, Franklin County filed Aug. 25, 1999); TCG Detroit v. City of Dearborn, No. 98-803937 (Mich. Cir. Ct., Wayne County March 8, 1999). Even though the State of Florida adopted a statewide rights-of-way statute, and a federal court struck down the City of Coral Spring's ordinance, several Florida cities continue to insist that carriers comply with impermissible requirements before they may provide service.

- Requirements that a company pay its share of street repair and paving costs;
- Enforcement of local zoning regulations;
- Reasonable requirements that a company indemnify the city against claims of injury arising from an excavation;
- Coordination of construction schedules;
- Establishment of standards and procedures for constructing lines across private property;
- Determination of reasonable insurance and indemnity requirements;
- Establishment of local building codes; and
- Local safety requirements that serve a stated safety purpose.

2. Prohibitions on Requirements Unrelated to Rights-of-Way Management.

The national policy enacted by the Commission should specifically prohibit cities from regulating or mandating interconnection among carriers, regulating rates, requiring carriers to complete elaborate application forms or certify their financial, technical and legal qualifications, dictating technical standards, imposing customer service requirements, requiring universal service contributions, enforcing a carrier's compliance with the Communications Act, requiring carriers to waive their rights under federal or state laws, or granting the municipality the right to install or maintain its facilities free of charge on the facilities of a carrier.

The policy promulgated by the Commission should also prohibit cities from imposing conditions requiring prior municipal review of the sale of a carrier; requiring carriers to cut or move carrier facilities at the sole discretion of the city unless the city establishes valid public health and safety reasons; requiring carriers to furnish confidential carrier records such as financials, customer lists, business plans, and customer agreements; requiring a competitor to build underground where the incumbent would be permitted to use poles; prohibiting use of existing aerial facilities by overlashing; requiring a separate permit to provide additional services; restricting resale; permitting a city to take possession of facilities at no cost after the rights-of-way agreement expires or is terminated; or failing to give carriers a cure period in the event of a default under the rights-of-way agreement.

II. Fair and Reasonable Compensation

A. Cities Are Permitted to Collect Fair and Reasonable Compensation for Use of the Public Rights-of-Way

Section 253(c) also permits cities to require "fair and reasonable compensation" from telecommunications carriers for use of the public rights-of-way. A "fair and reasonable" fee is one based on the city's costs or the burden imposed by the provider on the right-of-way. If fee requirements are not limited to compensation necessary to defray local right-of-way management costs, they violate federal standards for "reasonableness." Thus, municipalities may not impose fees for the improper purpose of raising revenues, nor may the amount of rights-of-way fees be based on the perceived "value" of the public rights-of-way to the provider of telecommunications services.

Under established federal standards for "reasonableness," usage fees must be cost-based. In Evansville-Vanderburgh Airport Authority District v. Delta Airlines, Inc., 405 U.S. 707 (1972), the Supreme Court developed the principle that a usage levy is "reasonable" if it is "based on some fair approximation of use of the [State's] facilities," and is not "excessive in relation to the benefits conferred." This test has been applied repeatedly since Evansville to determine if a municipal usage fee is reasonable.[46]

[46] See Northwest Airlines, Inc. v. County of Kent, 114 S.Ct. 855, 864 (1994) (adopting Evansville test); see also American Trucking Ass'n v. Scheiner, 483 U.S. 266, 290 (1987) (invalidating taxes because "they do not even purport to approximate fairly the cost or value of the use of Pennsylvania's roads").

In adopting Section 253, Congress supplied no other standard for judging the reasonableness of a municipal rights-of-way fee. Moreover, the language of Section 253(c) strongly suggests that there must be a nexus between the charges for the use of public rights-of-way and the costs imposed on the municipality by such use. First, there is the principal meaning of the word "compensation": "Indemnification; payment of damages; making amends; making whole."[47/] This definition of compensation is consistent with the view that franchise fees must be cost-based. In addition, Section 253(c) only allows municipalities to recover compensation "for use" of public rights-of-way. The use of the words "for use" indicates that some linkage between the amount of compensation and the extent of use is required.[48/]

In Dallas I, the court concluded that any fee not based on use of the rights-of-way is an economic barrier to entry under section 253(a).[49/] Similarly, in Bell Atlantic-Maryland, Inc. v. Prince George's County, Maryland, the court found that "any franchise fees that local governments impose on telecommunications companies must be directly related to the companies' use of the local rights-of-way, otherwise the fees constitute an unlawful economic barrier to entry under section 253(a)."[50/] The Prince George's County court explained that cities could not set their franchise fees above a level that is "reasonably calculated to compensate them for the costs of administering their franchise programs and of maintaining and improving their public rights-of-way." Id. The fee challenged by Bell Atlantic, which was based on three

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47/ Black's Law Dictionary (6th ed. 1990).

48/ This reading finds support in the legislative history. See, e.g., 141 Cong. Rec. S8170 (daily ed. June 12, 1995) (statement of Senator Feinstein explaining that Section 253(c) was intended to permit localities to require carriers to "pay[] the full costs they impose on State and local governments for the use of public rights-of-way," including "an appropriate share of increased street repair and paving costs that result").

49/ Dallas I, 8 F. Supp. 2d 582 (N.D. Tex. 1998).

50/ 49 F. Supp. 2d 805, 817 (D. Md. 1999).

percent of very broadly defined "gross revenues," was impermissible because it did not appear to be "directly related to Bell Atlantic's actual physical use of the County's public rights-of-way." Id. at 31. The court also concluded that any fee must be apportioned based on actual use, not the carrier's overall level of profitability.[51/]

Because a "fair and reasonable" fee must be linked to the burden imposed on the rights-of-way by the carrier, if a carrier's provision of telecommunications services does not impose any additional burdens on a city's rights-of-way, and the city is compensated already for the rights-of-way costs generated by the carrier, then the city is not entitled to additional compensation.[52/] For example, a cable operator compensates a city for the costs of using the public rights-of-way through the franchise fee paid by the cable operator.[53/] If the cable operator provides telecommunications services over its existing cable television network, it may not impose any additional burdens on a city's rights-of-way. The city would not be entitled to additional compensation under its rights-of-way authority for the operator's provision of the additional telecommunications services, if such services impose no additional burdens on the rights-of-way.[54/]

[51/] Id. at 32. The Bell Atlantic court respectfully disagreed with the contrary conclusion reached by another federal court in Michigan. See TCG Detroit v. City of Dearborn, 16 F. Supp. 2d 785 (E.D. Mich. 1998); appeal docketed, (6th Cir Aug. 28, 1998) (finding four percent fee to be fair and reasonable based on facts of case). In a subsequent Michigan state court case, TCG Detroit v. City of Dearborn, No. 98-803937-CK (Mich. Cir. Ct., Wayne County June 17, 1999), the city's four percent franchise fee was invalidated under state law because the city did not examine the costs it incurred from maintaining the rights of way when it set the fee.

[52/] See Austin I at 941-43; Austin II at 5-7.

[53/] Moreover, the Federal Cable Act limits the compensation that cities and localities may collect from cable operators to five percent of the cable operator's gross annual revenues from the provision of cable services. 47 U.S.C. § 542(b).

[54/] See Austin I, at 941-43.

Non-cost-based fees levied on telecommunications providers by municipalities are often simply unauthorized taxes disguised as fees, and are clearly designed to be revenue-raising measures. In most cases, the authority to institute a tax is vested with the state legislature or state constitution, and municipalities may not use their police powers over public right-of-way to generate revenue.[55] A user fee that is calculated not just to recover a cost imposed on the municipality or its residents, but to generate revenue, is by definition a tax.[56] Such attempts to impose illegal taxes can be precluded by limiting municipalities to cost-based fees.

B. Many Cities Have Imposed Excessive Fees for Rights-Of-Way Use That Are Not "Fair and Reasonable" and Bear Little Relationship to the Burdens Imposed on Rights-Of-Way by Providers of Telecommunications

Rather than imposing reasonable, cost-based fees, many cities see the entry of competitive carriers as an opportunity to generate additional revenues, far beyond the city's costs or the burdens imposed by the provider on the rights-of-way. Municipalities appear to believe that they may use their control over the right-of-way and their "police powers" to extract revenues above costs from telecommunications providers that use the public rights-of-way. Indeed, many municipalities have used "municipal leagues" or hired consultants to advise them precisely how to use this monopoly power to generate local revenues. These consultants often pursue their own interests in generating consulting and legal revenues by convincing

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[55] See, e.g., Or. Rev. Stat. § 307.215 ("On or after January 1, 1982, no county, city, district, or other political subdivision in this state shall levy or impose a tax on amounts paid for exchange access or other telephone services.").

[56] See, e.g., Diginet, Inc. v. Western Union ATS, Inc., 985 F.2d 1388, 1399 (7th Cir. 1992) ("If the fee imposed is a reasonable estimate of the cost imposed by the person required to pay the fee, then it is a user fee and is within the municipality's regulatory power. If it is calculated not just to recover a cost imposed on the municipality or its residents but to generate revenues that the municipality can use to offset unrelated costs or confer unrelated benefits, it is a tax, whatever its nominal designation."). See also Hager v. City of West Peoria, 84 F.3d 865, 870 (7th Cir. 1996).

municipalities that there is substantial revenue to be obtained from competitive LECs, even if such aspirations violate state and federal law.[57]

For example, even though a percentage of revenues fee is not based upon a city's costs, the City of Eugene, Oregon required all telecommunications providers to pay an annual registration fee equal to two percent of the provider's gross revenue derived from telecommunications activity within the city.[58] The ordinance also imposed an annual license fee of seven percent of gross revenue on telecommunications providers that construct, place or locate any telecommunications facilities on or over public property rights of way.[59] In addition to an annual occupancy fee intended to recover right-of-way costs, the City of Coral Springs, Florida imposed a franchise fee on telecommunications providers of ten percent of gross revenue in order to "reflect the value of the right-of-way."[60] This fee structure was invalidated.[61]

At least one city has required competitive LECs to provide facilities and services to the city for the city's use free of charge. Others have included "most favored nation" clauses in their franchise agreements that limit the amount the carrier can charge the city for services. For example, the City of Dearborn, Michigan requires that a competitive LEC provide services to the city at the lowest rate it charges any commercial customer for comparable service.[62] A model

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[57] Under one model ordinance, a city could deny a franchise based on the compensation to be paid to the city.

[58] See Eugene Code §§ 3.405, 3.415.

[59] See Eugene Code §§ 3.410, 3.415.

[60] Coral Springs Code §§ 20-3(1), 20-21(5).

[61] Coral Springs at 7.

[62] TCG Detroit v. City of Dearborn, No. 98-803937 at 15 (Mich. Cir. Ct., Wayne County June 17, 1999) (finding this requirement to be unrelated to the management of the public rights-of-way).

ordinance adopted by the League of Oregon Cities contains similar requirements.[63] Such requirements effectively are additional fees that have no relationship to the burdens imposed on the rights-of-way by the carrier.

Cities are not limiting themselves to impermissible franchise fees, however. Certain cities also impose unreasonable application fees, up to as much as $10,000 for a single application, that bear no relationship to the costs of processing the application. Other cities have required excessive bonds. The City of Eugene required all carriers wishing to provide service in Eugene to pay a registration fee, regardless of whether they planned to make use of the City's rights-of-way.[64] There can be little doubt that such duplicative fees constitute a barrier to entry. Competitors like AT&T simply are not permitted to "enter" a particular market unless and until they pay thousands of dollars in fees, and they may also have to agree to pay an additional percentage of gross revenues fee on top.

In its national policy, the Commission should make clear that a fair and reasonable fee is one based on the burdens imposed on rights-of-way by a provider of telecommunications services or the costs a city incurs as a direct result of a carrier's occupation of the rights-of-way. The Commission should prohibit cities from collecting discriminatory or non-cost-based rights-of-way fees, including but not limited to in-kind services and the construction of municipal facilities.

III. Local Laws Favor Incumbent LECs

A. Section 253 Requires Localities to Exercise Their Authority on a Competitively Neutral and Non-Discriminatory Basis

[63] League of Oregon Cities Master Telecommunications Infrastructure Ordinance § 50 (Nov. 7, 1998).

[64] Eugene Code §§ 3.405, 3.415.

Even where cities engage in permissible rights-of-way management and collection of fees, Section 253(c) mandates that cities do so on a "competitively neutral and nondiscriminatory" basis. This language prohibits the differential treatment of incumbents and new entrants with respect to rights-of-way fees or other requirements. For example, at least one court has found that a city cannot charge a new entrant a fee that the city cannot charge the incumbent.[65/] And the Commission itself has questioned whether a municipality can legally impose requirements on a new entrant that are not imposed on an incumbent.[66/]

The term "competitively neutral" is used in other sections of the Communications Act and the Commission has consistently interpreted it to prohibit regulatory distinctions that give one provider a cost advantage over another. For example, in the Telephone Number Portability Order, the Commission interpreted the term "competitively neutral" in Section 251(e)(2) of the Act to require that the cost of number portability "not affect significantly any carrier's ability to compete with other carriers for customers in the marketplace."[67/] The Commission found that in order to be "competitively neutral," cost recovery mechanisms should not "give one service provider an appreciable, incremental cost advantage over another service provider" or "have a disparate effect on the ability of competing service providers to earn normal returns on their investment."[68/]

[65/] City of Chattanooga v. BellSouth Telecom, Inc., No. 96-CV-1155 (Cir. Ct., Hamilton County, Tenn. Jan 4, 1998). But see TCG Detroit v. City of Dearborn, 16 F. Supp. 2d 785 (E.D. Mich. 1998) (appeal pending) (finding statute is satisfied by imposing comparable burdens on telecommunications providers).

[66/] TCI Cablevision of Oakland County at ¶ 108.

[67/] Telephone Number Portability, First Report and Order and Further Notice of Proposed Rulemaking, 11 FCC Rcd 8352 at ¶ 131 (rel. July 2, 1996).

[68/] Id. at ¶¶ 132, 135.

The Commission reached a similar conclusion when implementing Section 276 of the Communications Act, which requires the Commission to foster competition in the payphone industry.[69] The Commission required states to eliminate any rules that impose market entry or exit requirements on payphone service providers.[70] States could impose regulations to provide consumers with information and price disclosure, but those regulations had to be "competitively neutral."[71] Thus, any such regulations must "treat all competitors in a nondiscriminatory and equal manner, and not involve the state in evaluating the subjective qualifications of competitors to provide payphone services."[72]

Any disparity between the incumbent and competitors in the application of fees or other municipally-imposed requirements gives the incumbent a substantial cost advantage over new entrants. Under Section 253(c), neither a state nor a local government may permit or impose such a disparity. Nondiscrimination and competitive neutrality are federal policies, embodied in the Communications Act, which preempt state and local enactments that are inconsistent with these policies.

It is no response to argue that the locality has no authority to require an incumbent to obtain a franchise or pay a franchise fee. The requirement that any fees or requirements imposed in connection with the use of the rights-of-way be "competitively neutral" is unrestricted. Otherwise, competitors could be substantially harmed by the operation of monopoly-era statutes

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69/ 47 U.S.C. § 276.

70/ Implementation of the Pay Telephone Reclassification and Compensation Provisions of the Telecommunications Act of 1996, Report and Order, 11 FCC Rcd 20541 at ¶ 60 (rel. Sept. 20, 1996).

71/ Id.

72/ Implementation of the Pay Telephone Reclassification and Compensation Provisions of the Telecommunications Act of 1996, Report and Order, Order on Reconsideration, 11 FCC Rcd 21233 at ¶ 140 (rel. Nov. 8, 1996).

or state constitutional provisions that predate the establishment of the pro-competitive policies of the 1996 Act.

Likewise, it is no response to argue that the discriminatory effect of a city's inability to impose fees on incumbent carriers is only a transitional problem and that the city should be allowed to impose fees only on competitive carriers while it makes a good faith effort to address this problem. It is even more important during the transition to competitive markets that incumbent carriers not benefit from built-in cost advantages over new entrants.[73/] As both Congress and the Commission have recognized, imposing costs that are not competitively neutral on new entrants may effectively preclude them from entering the local exchange market, in direct contradiction to the fundamental, pro-competitive objectives of the 1996 Act.[74/] Removing the pro-incumbent bias in state and local regulation was a core objective of the 1996 Act.[75/] To the extent that a city and the incumbent disagree over the city's right to regulate or tax, the city should be prohibited from imposing the disputed regulations or fees on the competitors unless and until it is successful in imposing them on the incumbent.

B. Cities Are Not Exercising Their Authority in a Competitively Neutral and Non-Discriminatory Manner

Uneven regulation exacerbates the advantages that incumbent LECs already enjoy. A competitive LEC generally must negotiate a right-of-way agreement with the municipality in which it seeks to provide service before it may begin deploying its network, while the incumbent LEC is already in the rights-of-way providing service. For example, the City of White Plains,

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73/ H.R. Rep. 104-204, Part 1, at 49-50 (1995) ("House Report") (explaining that one reason the 1996 Act was needed was to eliminate the "government-sanctioned-monopoly status" of local exchange carriers that has historically protected them from competition).

74/ See Telephone Number Portability Order at ¶ 138.

75/ House Report at 49-50.

New York, has required competitive carriers seeking to construct facilities in the public rights-of-way to obtain a franchise agreement, while not requiring the incumbent LEC to obtain a franchise.[76/] Other cities require competitive LECs to put facilities underground, while incumbents are allowed to use aerial facilities.[77/] Such discrepancies greatly increase the costs of competitive carriers.

Because these local ordinances purport to give the municipalities the exclusive right to authorize local entry, competitive LECs must enter such agreements if they wish to provide facilities-based service in the municipality. In AT&T's experience, some municipalities have abused this monopoly power by requiring competitive LECs to agree to onerous terms and conditions as a prerequisite to providing local service through their own facilities. If a competitive LEC does not acquiesce, negotiations and litigation result, delaying deployment and increasing the carrier's costs significantly. Competitive LECs are faced with three undesirable alternatives: agree to the municipality's terms, be denied authorization to provide local service through their own facilities, or engage in protracted negotiation and litigation to obtain reasonable terms. While the Telecommunications Act of 1996 in theory should prevent municipalities from engaging in these practices, it has yet to have that effect.[78/]

In the long term, competitive LECs cannot acquiesce to onerous terms and conditions that preclude local entry or that place them at a competitive disadvantage relative to incumbent

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[76/] Complaint for Declaratory and Injunctive Relief at ¶ 22, TCG, Inc. v. City of White Plains (S.D.N.Y. 1999).

[77/] See, e.g., League of Oregon Cities Master Telecommunications Infrastructure Ordinance § 12(D) (Nov. 7, 1998).

[78/] In addition, in some instances the incumbent LECs have acted as the "franchise police" by demanding that a competitive LEC obtain a right-of-way agreement with a municipality before the competitive LEC is allowed to utilize the incumbent LEC's right-of-way capacity.

LECs.[79] Hence, competitive LECs usually choose to enter into lengthy negotiations and litigation in an attempt to secure reasonable and nondiscriminatory terms and conditions. For example, when TCG has sought right-of-way agreements, the typical negotiation process has taken approximately four to six months to complete. In some instances, however, negotiations have dragged on for years.[80]

In order to address such inequities, the Commission should promulgate "opt in" rules that provide competitive LECs with the option of using the rights-of-way under the same terms and conditions that the incumbent LEC is using. Such rules would be analogous to those adopted by the Commission in the Local Competition Order, which give competitors access to the terms and conditions of interconnection agreements entered into by incumbents.[81]

IV. State and Local Taxes Are Excessive and Often Applied in a Discriminatory Manner

The Notice seeks comment on the nature and prevalence of unreasonable or discriminatory tax burdens on competitive telecommunication providers, in order to reach a common understanding of principles that should guide state and local tax treatment of competitive telecommunication companies. AT&T believes that neutrality to consumers, neutrality to technology, neutrality to the needs of government, and neutrality and fairness to all participants should guide state and local tax policy.

Throughout most of the country, telecommunications companies face greater state and local tax burdens than general business companies. These inequities stem from outmoded

[79] When competitive LECs are forced to accept onerous terms in order to provide service to a customer that otherwise would be lost (usually to the incumbent LEC), competitive LECs attempt to include agreement provisions that allow them to retain their right to challenge the terms and conditions at a later date.

[80] See Affidavit of Beans/Harris at 7-8, attached hereto as Exhibit 1.

statutes and constitutional provisions that originated during the era when telecommunications companies were closely regulated monopolies. These outmoded and discriminatory tax schemes no longer work in today's competitive and highly dynamic environment. Increased competition and the development and convergence of new and emerging technologies create considerable uncertainty in the application of the taxes, and may lead to double taxation and an unlevel playing field.

Unreasonable and discriminatory tax burdens take many forms including (1) extraordinary compliance burdens, (2) higher property tax valuations and effective tax rates, (3) lack of notice regarding the imposition of taxes and fees, (4) inappropriate definitions, and (5) preferential treatment of manufacturers over service providers. These unreasonable and discriminatory tax burdens restrict the development of competitive communications facilities, inhibit the introduction of new services and increase costs borne by consumers.

A. Extraordinary Compliance Burdens Imposed On Telecommunications Services

The complexity and diversity of state and local taxes and surcharges imposed upon telecommunications services creates a compliance burden that is unlike that faced by most industries. Three times as many taxes are imposed upon telecommunications transactions as are imposed on sales by general businesses.[82/] Every level of government, including special local districts such as transportation districts, imposes these taxes. Currently, 10,767 state and local taxing jurisdictions apply taxes to telecommunications service.[83/] Depending on the state, tax

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[81/] See Local Competition Order at ¶¶ 1309-1323 (adopting 47 U.S.C. § 51.809).

[82/] See Committee On State Taxation ("COST") Study presented to the Advisory Commission on Electronic Commerce, Appendix A (Sept. 14, 1999) (comparing 310 tax types applicable to telecommunications verses 103 for general businesses), attached hereto as Exhibit 2 ("COST Study").

[83/] Id.

returns are required to be filed either at the state level or directly to each local taxing authority. Most commonly these returns are filed monthly, although some require more frequent estimated payments. (In Illinois, for example, some returns are due more frequently.) AT&T's tax database for collecting or recovering taxes imposed on product and telecommunications service transactions includes over 10,000 active tax jurisdictions, and this number will only grow as AT&T expands into local telephone service. Making this process more complex are the billions of calls that are subject to these taxes. AT&T files in excess of 80,000 tax returns per year.[84/]

New Jersey[85/] and Massachusetts[86/] provide a positive role model for other states in their approach to transaction level taxes. Both states subject telecommunications services to only a simple state level sales tax. The same tax rate applies to the sale of telecommunications services that applies to other taxable products and services.

Unfortunately, most states impose several taxes that apply to telecommunications services. Texas is the most active state with 966 separate taxing jurisdictions. Main street businesses only have to deal with 422 separate taxing jurisdictions.[87/] Texas has the following taxes that may apply to any telecommunications transaction:

- a state sales tax;[88/]
- a municipal sales tax;[89/]
- a county sales tax;[90/]
- a metropolitan transit authority sales tax;[91/]

84/ This number includes wireline, wireless and cable TV required filings for transactional taxes and property taxes.

85/ N.J. Stat. Ann § 54:32B-3.

86/ Mass. Gen. Laws ch. 64H, § 1 et seq.

87/ COST Study, Appendix B at A-12.

88/ Tex. Tax Code Ann. § 151 et seq.

89/ Tex. Tax Code Ann. § 321.001, et seq.

90/ Tex. Tax Code Ann. § 323.101.

- a city transit district sales tax;[92]
- a special purpose district sales tax;[93]
- a county 911 tax;[94]
- a city 911 tax;[95]
- a poison control surcharge;[96]
- a state universal service fund fee;[97]
- a PUC gross receipts fee;[98]
- a PUC access line fee;
- telecommunications infrastructure fund;[99] and
- various right of way fees.

Illinois is an equally onerous state with 803 separate jurisdictions taxing telecommunications service. Main street businesses only have to deal with one taxing jurisdiction.[100] In addition to their state and local sales and use taxes on products and other services, Illinois has the following taxes that apply to telecommunications services: a state level excise tax[101] imposed on the sale of all non-exempt telecommunications services; a PUC fee[102] imposed on intrastate services only; the municipal infrastructure maintenance fee,[103] which may be imposed by a municipality on all telecommunications services, and an optional state imposed

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91/ 34 Tex. Admin. Code § 3.425.

92/ Tex. Transp. Code Ann. § 453.151.

93/ See, e.g., Tex. Health & Safety Code Ann. § 285.061, et seq.; Tex. Transp. Code Ann. § 452.001, et seq.

94/ Tex. Health & Safety Code Ann. § 771.072.

95/ Id. at 771.071.

96/ 255 Tex. Admin. Code § 255.9.

97/ Tex. Pub. Util. Comm'n Substantive Rule 23.150(g).

98/ Tex. Code Tit. 32, Chap. Ten, Art. XII, Sec. 78.

99/ Tex. Util. Code Ann. § 3.606.

100/ COST Study, Appendix B, at A-12.

101/ 35 Ill. Comp. Stat. 630/1 - 630/21.

102/ 220 Ill. Comp. Stat. 5/2-202.

103/ 35 Ill. Comp. Stat. 635/15(b).

infrastructure maintenance fee[104/] that applies only if a local jurisdiction does not impose such a fee and has no franchise fee or franchise agreement with a carrier predating the infrastructure maintenance fee statute. Local taxes include a 911 fee[105/] imposed as a dollar amount on each local access line. A municipal telecommunications excise tax[106/] is also imposed on all telecommunications services, or in lieu of this, a municipal utilities tax[107/] is imposed on the intrastate revenues of a company. Finally, a state municipal infrastructure maintenance fee[108/] is imposed on all telecommunications services. The total tax rate in Illinois could exceed 19 percent in some locations. AT&T files over 900 returns each month in Illinois alone.

Florida and California are also states that apply a variety of taxes to telecommunications service transactions, in addition to state and local sales and use taxes on products and other services. In Florida these taxes include a state gross receipts tax,[109/] the state sales tax[110/] (business customers pay at a higher rate than the state sales tax on products) and the state dual-party-relay-tax[111/] imposed on each local access line. Florida also has county 911 access line taxes,[112/] county sales taxes[113/] on business local service only, and county utility user taxes[114/] imposed only on intrastate or local telephone service in the unincorporated area of the county.

104/ 35 Ill. Comp. Stat. 635/15(c).

105/ 50 Ill. Comp. Stat. 750/15.3.

106/ 65 Ill. Comp. Stat. 5/8-11-17.

107/ 65 Ill. Comp. Stat. 635-20.

108/ 35 Ill. Comp. Stat. 635/20.

109/ Fla. Stat. Ann. ch. 203.01.

110/ Fla. Stat. Ann. 212.05(1)(e).

111/ Fla. Stat. Ann. 427.704.

112/ Fla. Stat. Ann. 365.171 & 365.172.

113/ Fla. Stat. Ann. 212.054.

114/ Fla. Stat. Ann. 166.231(9).

Municipalities may impose utility user taxes[115] on intrastate or local telephone service. While California does not impose its state sales tax on telecommunications services, it does impose a number of state level charges on telecommunications services including the California High Cost Fund surcharge,[116] a fund to support dual party relay service,[117] the California Teleconnect fund,[118] a state PUC fee,[119] and a state 911 tax.[120] Counties in unincorporated areas and municipalities in California may also impose utility user taxes[121] on local, intrastate, and interstate telecommunications services.[122]

Making the administration of the plethora of transaction taxes on telecommunications services more difficult are the many variations of rates, taxable services, and exemptions. For example, with regard to the California local utility user tax discussed above, cities may impose the tax at any rate within a range from one to eleven percent. The tax may be imposed on any combination of local, intrastate, and interstate communication services. In California, there are sixteen different tax bases for the various taxes and jurisdictions.[123] Exempt customers also vary from city to city. For example, the tax may be imposed on residential customers only or senior citizens may or may not be exempt from tax. The State of Colorado has 179 different tax bases that telecommunications companies have to track. Likewise, the States of Utah and Oregon have

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115/ Id.

116/ Cal. Pub. Util. Comm'n Decision 96-10-066.

117/ Cal. Pub. Util. Comm'n Decision 98-12-073.

118/ Cal. Pub. Util. Comm'n Decision 96-10-066.

119/ Cal. Pub. Util. Comm'n Order.

120/ Cal. Rev. & Tax code § 41020.

121/ Cal. Rev. & Tax Code §§ 7284.2, 7203.5.

122/ In California, 150 jurisdictions apply this utility users tax with a rate up to 11 percent.

123/ COST Study Appendix A.

119 and 85 different tax bases respectively.[124] To make matters worse, cities may amend their ordinances at any time, making keeping current with changes a daunting task.

Apart from the compliance burden, there is also a financial burden on the customer. Many of the taxes are additive so that a single customer will be subject to more than one tax. For example, a customer in Texas may pay a whopping 28.56 percent in tax after local and state taxes and surcharges are paid (excluding the Federal Excise Tax and FCC authorized surcharges). This same Texas customer pays 8.25 percent on purchases from a main street business. Likewise in Florida, telecommunications taxes add 24.47 percent to the bill, while main street purchases add only 7.5 percent. Nebraska, Montana, Colorado, Oklahoma, Pennsylvania, New York, Maryland and Kansas all have telecommunications tax rates of over 20 percent for some locations, while the average tax rate applied to other purchases in those states is about 7 percent.[125]

B. Property Tax

In many states, competitive telecommunications companies face different or additional property taxes than those applicable to general business companies. Some states and localities apply taxes to personal property, construction work in progress, and various categories of intangible property of telecommunication companies that they do not apply to general business companies. In some cases, states and localities classify the property of competitive telecommunications companies as utility property subject to higher tax rates, or they use valuation practices (unit valuation) that create much higher property values. Under the unit valuation methodology, the states value the property of competitive telecommunications companies based upon the value of their business rather than the value of its physical assets. The

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124/ COST Study Appendix A.

125/ COST Study Appendix A.

cumulative effect of all these tax policies results in an unreasonable property tax burden for competitive telecommunications companies across the country.

Three specific areas of property tax discrimination clearly illustrate the above comments: (1) unit valuation discrimination; (2) assessment ratio discrimination; and (3) exemption discrimination.

(1) Unit Valuation Discrimination

In twenty-nine states, telecommunications service assets are reported and taxed by state taxing authorities through a unit valuation approach. Under this methodology, the nationwide business enterprise value of the carrier is established. A portion of this total value is then allocated to the respective states, based upon that state's proportionate share of investment. These state valuations determine the amount of property taxes. Two competitive telecommunications providers with identical property in the state could face completely different tax burdens on similar property.

The assets of a general business company, however, are taxed by the local assessment jurisdiction, typically the county assessor, who bases the valuation (and thus taxes) on the value of the physical assets of the company, without regard to the value of the business enterprise. The value of the physical property is typically only a fraction of the value of the business. Companies taxed as general businesses that operate in the telecommunications sphere enjoy a definite tax advantage and significantly lower operating costs.

Many new technology firms pay the taxes applicable to general businesses, although they compete directly with competitive telecommunications companies. The application of differing tax treatment places competitive telecommunications companies at an economic disadvantage. For example, the value of the physical assets of a high-technology company equates only to a minuscule portion of its overall business enterprise value. This company's property tax burden would increase dramatically if it were based upon the business enterprise assessment, as it is for competitive telecommunications companies.

Unit valuation results in higher and discriminatory tax burdens because it encompasses many factors beyond the physical assets of a company. Unit valuation measures the value of the business which, in turn, includes intangible assets (patents, trade names, customer base, licenses), as well as the incremental value associated with the business operating as a going concern with all assets working in harmony. In fact, fourteen states apply special property taxes to the intangible value of telecommunications companies.[126/] In contrast, the local assessment process encompasses neither the intangible assets nor the going concern component. These differing methodologies result in telecommunications companies assuming a significantly greater tax burden than general business taxpayers.

(2) Assessment Ratio Discrimination

Most states do not apply the property tax rate directly to the estimated market value of the property, often called Fair Market Value (FMV). Rather they typically apply an assessment ratio to the FMV to determine the amount of value that is actually subject to property tax. The tax rate is then applied to the resulting percentage of FMV to determine the total property tax owed. Many states apply a significantly lower assessment ratio to general business property than the assessment ratio applied to telecommunications property. Thus a general business taxpayer would have a lower tax burden, even if it had the same FMV as a telecommunications company within a particular state.

[126/] COST Study Appendix A.

In Alabama, for example, the assessment ratio for utility properties is 30 percent (which includes some of the competitive telecommunications companies), while the ratio for all other property is 20 percent.[127] In Kansas, the assessment ratios are 33 percent for telecommunications taxpayers and 25 percent for general business.[128] The Louisiana ratios are 25 percent for the tangible personal property of utilities and 15 percent for general commercial and industrial properties.[129] The states of Mississippi, Montana, Oklahoma, South Carolina, and Wyoming also have differing assessment ratios that directly discriminate against telecommunications property, resulting in a greater tax burden for the same level of value.

(3) Exemption Discrimination

Certain states have different exemption regulations for general business taxpayers than for telecommunications companies. General business taxpayers in some states have either more categories of property tax exemptions than telecommunications companies, or specific categories of exemptions that are more all encompassing. Discrimination results when the property of a telecommunications company is taxed, while the same property of a general business taxpayer is not.

In Iowa, for example, the tangible personal property of general business taxpayers is exempt, while all telecommunications personal property was subject to property tax each year until January 1, 1996. Beginning in 1996, new investment in personal property became exempt, but investment in personal property prior to January 1, 1996 will be taxed until taken out of service. Thus telecommunications companies are taxed on numerous forms of personal property, while general business taxpayers escape this burden. Discriminatory property tax practices are

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[127] Ala. Code § 40-8-1.

[128] Kan. Stat. § 79-1439(b).

based upon outmoded state statutes that are ill-suited to today's competitive telecommunications environment. State and localities should tax competitive telecommunication service companies as general business taxpayers, regardless of the technology employed to provide the service. This would place all companies and technologies on an equal basis, and create a market in which inequitable tax practices do not curtail technological advancement and competition.

C. Lack Of Notice

Except in a few states, local jurisdictions can impose taxes and charges with limited notice. Most are merely required to publish a new tax ordinance in the legal notices section of the local newspaper. Such publication is clearly insufficient to put telecommunications providers on notice of a new or modified tax they are required to collect. AT&T is forced to call and send letters to municipal officials on a regular basis inquiring as to whether municipalities have amended their taxing provisions, and if so, attempting to obtain a copy of the applicable ordinance. In some cases, the local jurisdictions respond to the initial inquiry. In most instances, multiple letters and calls to the jurisdiction are required before there is an appropriate response. Maintaining an accurate database of such ordinances is nearly impossible in today's environment.

D. Lack Of Clarity Of Definition

The inappropriate classification of cable and information services as "telecommunications" exacerbates the excessive tax burden. Practically, tax classification is important because forty-five states and thousands of local jurisdictions currently impose taxes on telecommunications services but not most other major technology services. For example, no state has yet defined legislatively a specific category of tax exclusive to Internet access services. Rather, taxing jurisdictions with existing telecommunications taxes simply pigeon-hole new

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[129/] La. Const. Art. VII, § 18(B); La. Rev. Stat. Ann. § 47:1854.

services within the existing tax category of telecommunications, without any express statutory authority, in order to increase tax revenues quickly and avoid the often protracted process of enacting new laws.

This has proven to be the case in several states with respect to Internet access. No less than eleven states (including Alabama, Florida, Illinois, Iowa, Massachusetts, Missouri, North Dakota, South Carolina, Tennessee, Texas and Wisconsin), without any change in their applicable laws, sought initially to administratively subject Internet access services to their existing telecommunications taxes. While many of these jurisdictions have since changed their position, three states (North Dakota, Tennessee and Wisconsin) persist in subjecting Internet access to taxation as a "telecommunications" service without express legislative authority.[130/]

Such a result is directly contrary to the FCC's holding that Internet access services generally are information services and not telecommunications services.[131/] It also contradicts the Congress's expansion of the term "cable service" to include cable Internet services.[132/] As the Commission has found, the legislative history of the 1996 Act makes clear that cable operators are not telecommunications carriers.[133/]

[130/] See, e.g., 1996 Tenn. Pub. Acts 96-13.

[131/] In re Federal-State Joint Board on Universal Service, Report to Congress, 13 FCC Rcd 11501 ¶ 73 (1998) ("Universal Service Report to Congress"). See also id. at ¶ 44 ("'telecommunications' and 'information service' are mutually exclusive categories").

[132/] Congress added the words "or use" to the definition of "cable service" in 1996, see Pub. L. No. 104-104, § 301(a)(1), specifically "to reflect the evolution of cable to include interactive services such as game channels and information services made available to subscribers by the cable operator" and thereby to ensure that such interactive information services constituted "cable service." H.R. Conf. Rep. 104-458 at 169 (1996) (emphasis added). See also 142 Cong. Rec. H1145-06 (daily ed. Feb. 1, 1996) (statement of Rep. Dingell) ("the definition of the term 'cable service' has been expanded to include . . . interactive services").

[133/] Universal Service Report to Congress ¶ 44 (quoting 141 Cong. Rec. S7996 (June 8, 1995) (statement of Sen. Pressler)).

The tendency for states to administratively classify entirely new and different services, such as Internet access, as telecommunications service is one of the adverse consequences of the disproportionate taxation of telecommunications services as opposed to other major technology services. A state's decision to tax Internet access as telecommunications cannot be squared with the Communications Act or with the recently enacted Internet Tax Freedom Act.[134/] Indeed, some states have administratively or legislatively rejected the treatment of Internet access as telecommunications service. Instead of providing certainty of administration and uniformity of treatment across tax jurisdictions, the arbitrary and improper classification of Internet access as telecommunications service will likely be challenged and provoke costly and timely litigation.

The tax laws have simply not kept up with the changing technology. This results in considerable uncertainty as to how and when taxes should be applied when new products and services are developed. This issue is compounded as communications technologies converge and carriers bundle services that have historically been subject to different tax types. The state of Maryland, for example, imposes a franchise tax[135/] on gross revenues received by a telephone company. The gross receipts tax does not apply to a cellular company. A cellular company is required to impose a sales tax.[136/] If service providers bundle long distance wireline services with wireless services for a single bundled charge, it is unclear which tax should be charged. There is no clear answer, but the prospect for excessive taxation is evident.

E. Tax Preference To Manufacturers

Not only do telecommunications companies face complex and discriminatory state tax systems, but these state tax systems provide traditional manufacturers with significant incentives

[134/] Pub. L. No. 105-277 (Oct. 21, 1998).

[135/] Md. Code Ann., Tax - Gen. § 8-402.

to invest in their jurisdictions, while incentives for telecommunications providers are limited. Approximately forty-five states currently provide some type of exemption or reduced rate of tax for purchases of equipment used in the manufacture of tangible personal property. In contrast, only twelve states and the District of Columbia currently exempt purchases of telecommunications equipment from sales tax, although at least eight others are considering such an exemption.[137/] State and local tax policy makers should consider similar incentives in order in to encourage investment in telecommunications equipment.

In addition to the preferential property tax treatment afforded manufacturers, state income and franchise tax and sales and use tax statutes continue to favor manufacturers over service providers. There are many forms that the favorable treatment can take. For example, a methodology employed by a number of states to apportion income for income and franchise tax purposes favors manufacturers. Investment credits commonly granted to manufacturers rarely apply to service providers. And manufacturers are typically eligible for sales tax exemptions on capital equipment they purchase, while such exemptions rarely apply to service providers. The impact of this favoritism in the tax structure is compounded for telecommunications services because states tax very few services other than telecommunications.

While this disparate treatment may not be intentional as applied to the emerging communications industry, the impact is evident. It is clear that service providers, in particular telecommunications providers, bear a disparate share of the burden of state and local taxes. Eligibility for sales and use tax exemptions illustrate this disparity. As the sales and use tax laws have developed, the majority of states have thought it appropriate to encourage capital

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[136/] Md. Code Ann., Tax - Gen. § 11-102.

[137/] COST Study at 23-24.

investment in new equipment by providing exemptions for purchases of equipment used in manufacturing tangible personal property. Although classified as service providers, telecommunications companies are capital intensive, yet their purchases of equipment are eligible for a similar exemption in only a limited number of states. To encourage the development of competitive facilities, the disparity should be rectified. States should be encouraged to broaden their exemptions for capital purchases to include purchases of equipment by telecommunications carriers.

F. FCC Guidance Can Ameliorate the Disproportionate Tax Burden on Carriers

AT&T's experience with state and local taxes confirms that telecommunications companies face significant economic burdens from state and local taxes and fees, as well as significant and expensive compliance and reporting burdens. These taxes and fees reduce telecommunications investment incentives and distort telecommunications cost structures. By increasing costs, the various taxes and fees raise retail prices, which in turn suppresses calling and reduces both customer welfare and efficiency. By reducing innovation and investment incentives, these taxes and fees reduce consumer choice, lower service quality, reduce the types of plans and services offered to consumers, and reduce the rate of price decreases that consumers might otherwise enjoy. These economic burdens present a barrier to entry by new market entrants or cause new entrants to ignore the law, placing AT&T at a competitive disadvantage.

While AT&T recognizes that the Commission has limited authority to address problems stemming from inconsistent tax policies, there are actions that the Commission can take to hasten rational taxation of telecommunications by states and municipalities. For example, the Commission can develop model taxation principles to guide states and localities. In addition, the Commission can act as an advocate for simple and sound telecommunications taxation policies, such as neutrality in technology and neutrality by provider, within the federal government and to the federal government representatives on the Advisory Commission on E-Commerce. While non-binding, such actions can help direct states and localities toward more rational tax policies that will foster the growth of facilities-based telecommunications competition.

CONCLUSION

As the Commission recognizes, competitive telecommunications networks will provide new services to the public as well as alternatives to the local services provided today by the incumbent LECs. However, local policies regarding access to the public rights-of-way and state and local taxation of telecommunications providers are acting as barriers to facilities-based competition. To help eliminate such barriers and promote the development of competitive networks, the Commission should adopt a national policy defining the scope of permissible local authority that is consistent with the Communications Act and builds upon the Commission's precedents and those of the courts. The Commission also should develop uniform model taxation principles to guide states and localities, and should act as an advocate for simple and sound taxation policies.

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CERTIFICATE OF SERVICE

I, Michelle Mundt, hereby certify that on this 12th day of October 1999, I caused copies of the foregoing "Comments of AT&T Corp." to be sent to the following by either first class mail, postage prepaid, or by hand delivery (*):

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