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PROFESSIONAL OFFICES OF

InteliCable Group, LLC

Multihousing Telecommunications & Technology Advisors

755 Johnnie Dodds Blvd.
Suite C
Mt. Pleasant, SC 29464

Research
Development
Negotiations
Education

Cable Television
Telephone
High Speed Internet
Utilities

Telephone 843.884.1101
Fax 843.884.1193
E-Mail info@intelicable.com

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December 13, 2001

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Magalie Salas
Secretary
Federal Communications Commission
445 Twelfth Street, SW
Washington, D.C. 20554

RE: Ex Parte Communication in CS Docket No. 95-184 and Docket No. WT 99-217

Dear Madam Secretary,

Enclosed is an article relating to CS Docket No. 95-184, regarding MDU Inside Wiring Rules. It has been submitted to Royce Sherlock and Eloise Gore of the Cable Services Bureau.
Sincerely,

Larry Kessler
CEO
InteliCable

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Boring? Not Any More.

Exclusive and Perpetual Contracts

By Larry Kessler ■ *InteliCable*

In the near future, words such as "regulatory" and "video services" will cease to cause yawns and sleepy eyes. For residential multifamily real estate owners and competitive video service providers, the time of opportunities lost or gained is close by.

STOP! MUST READ.

MDU: Multi Dwelling Unit, also referred to as multifamily and multihousing properties. Such real estate includes apartment complexes, residential high rises, student housing and active adult communities.

Competitive Video Provider: A provider of video services that directly competes with franchise cable operators to serve MDU residents using satellite, wireless and fiber optic technologies. Such providers include private cable operators and franchise system over builders.

Exclusive Contract: A form of agreement between an MDU property owner and video service provider, whereby the video service provider is the exclusive provider of video services to the residents of the property.

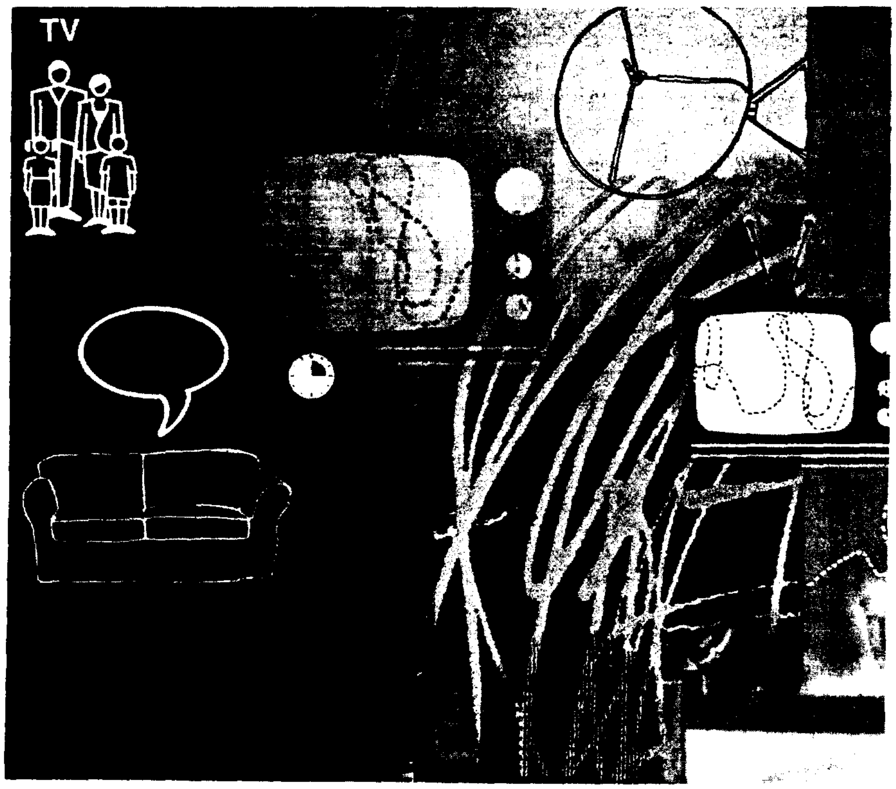
Perpetual Contract: A form of agreement typically between an MDU property owner and a franchise cable operator (i.e., Time Warner, Comcast, Cablevision, AT&T, Cox, Insight), whereby the franchise cable operator has the right to continue serving the property for the life of it's franchise license, including any extensions or renewals of this license.

There are currently two regulatory decisions looming before the Federal Communications Commission that stand to significantly impact the availability of competitive alternatives for video and broadband services in the residential MDU marketplace. Working to amend their earlier Inside Wire Ruling, the Commission is deciding whether or not two consenting parties such as a competitive video provider and MDU property owner should be permitted to continue entering into exclusive service contracts. At the same time, they will decide whether or not franchise cable operators (i.e., Time Warner, Comcast, Cablevision, AT&T, Cox, Insight) should be able to continue serving MDUs under existing, perpetual contracts. And although exclusive and perpetual contract issues were thought to be minor aspects of the initial Inside Wire Ruling, the pending decisions on these two issues stand to impact the growth of competition more than the actual inside wiring issue itself.

Since adoption of the 1996 Telecommunications Act, the Commission has not addressed two more important issues as it relates to competition amongst video service providers for MDU residents. Considering approximately one third of America's population lives in MDUs, the Commission is shouldering a significant burden to make the right decisions. And since both franchise cable operators and competitive video providers offer broadband Internet service using cable modem technology, the Commission's decisions stand to impact the availability competitive options for both video and broadband data services.

Exclusive Contracts: The Argument(s)

Real estate owners and competitive video providers both argue that exclusive contracts are necessary for competition to thrive. As a matter of



> "There are currently two regulatory decisions looming before the Federal Communications Commission that stand to significantly impact the availability of competitive alternatives for video and broadband services in the residential MDU marketplace."

economics, video providers competing with franchise cable operators require seven to ten year exclusive service agreements with MDU properties. The competitive video provider is required to make a substantial investment in each property it serves, much more substantial than that of the franchise cable operator. If the competitive video provider is forced to split the resident customer base with a franchise cable operator on any given property, it is unable to yield sufficient enough returns to justify the investment. As such, should the Commission decide to interfere with the current right of MDU property owners to enter into exclusive video service contracts with the providers of their choice, the MDU property owners and competitive video providers argue that competition amongst video providers in the MDU marketplace will cease to exist.

Franchise Cable: On Exclusives

The franchise cable industry argues that MDU property owners and competitive video service providers should not be permitted to enter into exclusive contracts. Interestingly however, there are exclusive contracts in place between franchise cable operators and MDU property owners. In addition, the franchise cable industry's argument against exclusive contracts is contradictory to their argument that the Commission should continue allowing franchise cable operators to enforce existing, perpetual contracts on MDU properties, which in effect block competition due to the business model economics of competitive video providers.

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The contradiction in franchise cable's argument against exclusive contracts is in their argument for perpetual contracts. Given the business model economics of competitive video providers, a perpetual contract is in essence a perpetual *exclusive* contract since the presence of such a contract effectively eliminates the threat of competition. Such a practice appears to be antithetical to the Commission's objective of creating competition.

"In the multifamily marketplace, there is a strong economic argument for allowing exclusive contracts. – Bruce Lundegren, National Association of Home Builders Multifamily Division"

Real Estate: On Exclusives

On behalf of the National Association of Home Builders Multifamily Division, Bruce Lundegren states "In the multifamily marketplace, there is a strong economic argument for allowing exclusive contracts. A competitive service provider may not be willing to wire a multifamily building unless they are given exclusivity to recoup their investment for at least some set amount of time." This period of time averages between seven and ten years.

Speaking on behalf of the National Multi Housing Council and the National Apartment Association, the two organizations representing the largest and most prominent segments of the MDU industry, Jim Arbury states, "Apartment residents are best served when there is a strong competitive market in which a number of cable providers participate. The economics of the cable industry, however, are such that it is difficult for more than one operator to serve a single building profitably. This means that apartment residents benefit from a system that encourages the development of many providers, while making it easy for an owner to bring in a new provider if an existing provider is not meeting resident needs. Most contracts now written between apartment owners and telecom providers have strong contract default language to ensure that service and programming is held to a high standard. Experience shows that exclusive contracts for a given apartment community are absolutely essential for private cable operators and other competitors, because the first step has to be to create viable competitors to the incumbent cable operator. Exclusive contracts of a limited duration allow providers to recoup their investments and thus encourage the growth of smaller competitors. In markets where exclusives are banned, on the other hand, the economies of scale of the incumbent cable operator create such an advantage that it is much more difficult for competitors to take root. If any provider has the right to go into any building we believe that new and promising start-up providers will eventually find that they simply cannot compete."

Perpetual Contracts & Ancillary Income: The Argument(s)

"Over 99% of cable franchises are renewed. Federal law makes it extremely difficult for a local franchising authority to deny such renewal."

Matthew Ames,
a partner with Miller & Van Eaton

Franchise Cable: On Perpetuals

The franchise cable industry argues that it should be able to continue serving MDU properties under existing perpetual contracts, despite the fact that most such agreements have been in place for 10-20 years. One aspect of its argument is that the majority of these contracts are non-exclusive. However, it does not deny that by default, the presence of even a non-exclusive perpetual contract creates a perpetual exclusive contract by virtue of the competitive video provider's business model.

However, a basic premise of the franchise cable industry's argument is that property owners only wish to remove perpetual contracts, thereby the franchise cable operator, for revenue sharing opportunities offered by competitive video providers. But once again, in contradiction to their argument, franchise cable operators such as Time Warner, Comcast, Cox, Insight and AT&T stipulate revenue sharing in their MDU agreements as well. In many cases, they also dangle signing bonuses to entice property owners into signing long term contracts.

Real Estate: On Ancillary Income

Unfortunately, the important fact lost in this battle of words over revenue sharing is that MDU property owners simply do not base their choice of video service providers on ancillary income opportunities such as revenue sharing. Such a practice appears to be contradictory to their core business models and values. "Our average rents are in the $1,500 range," says Lyn Lansdale of AvalonBay Communities, a company that manages approximately 40,000 apartments around the country. "The average resident's cable bill is $35. Even if we were to receive 10% of that bill as ancillary income [$3.50], it is far more important that we protect the $1,500 rent by not losing a resident because of poor or inadequate cable service."

"Apartment property owners simply cannot base their selection of providers on ancillary income opportunities," says Lori Reeves of Forest City Residential, a company managing 35,000 apartment units. "We stand to lose far more revenue in the loss of a single new lease or lease renewal than we could possibly make from any level of revenue sharing. The apartment industry has shown tremendous growth in competition and therefore, houses a resident population that possesses extremely low tolerance for inadequate video, data and voice services. This forces us to select the best provider for reasons of service, not ancillary income."

"The inability to control or negotiate the type, extent and quality of services provided at a community is a competitive disadvantage for the property and a disservice for the resident who expects access to certain amenities associated with living in a multifamily community," says Laurie Baker of Camden Property Trust, a company managing 51,672 units. "As owners, we have every incentive to act as effective proxies on behalf of our residents. If we don't, our residents will vote with their feet by walking off our communities."

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"Our primary goal is to attract and retain quality residents," says Ted Koros of Metric Property Management, a company managing 15,000 apartment units. "The concept of service extends throughout all aspects of the resident's experience at the property. It extends from the services provided by our staff to those provided by cable companies.

"Apartment property owners simply cannot base their selection of providers on ancillary income opportunities," says Lori Reeves of Forest City Residential."

It is more important to our organization to choose a third party provider that shares similar values in terms of customer service than one that provides higher financial inducements. The revenue participation provided by the cable, phone, or Internet companies is quite small when compared to the opportunity cost of losing a resident due to poor service."

Competitive Video Providers: On Perpetual Contracts

The competitive video provider industry is largely represented by the Independent Multifamily Communications Council (IMCC). The IMCC's position on perpetual contracts has remained the same since the FCC originally addressed this issue. According to a May 8, 2001 filing to Commission, the IMCC states that under a new "fresh look" policy ". . .the incumbent franchise provider would be required to allow the [MDU] owner to terminate the [existing] agreement in favor of a [competitive video provider] with little or no termination liability." The IMCC continues by saying ". . . that perpetual contracts inhibit competition, and that there are an ever increasing number of choices among video service providers [other than the incumbent franchise provider] the [video] market is one in which application of the fresh look doctrine would be effective and appropriate." Competitive video service providers who seek to provide competition for such services in the residential MDU marketplace support this argument.

As a solution to existing perpetual contracts, the IMCC promotes the

Commission's using this "fresh look," which the IMCC and others argue is within the authority of the Commission. In its recent filing to the Commission the IMCC states "[Under a "fresh look" policy] As competitive alternatives become available to a property owner, the incumbent franchise provider would be required to allow the owner to terminate the agreement in favor of a new service provider with little or no termination liability. Of course, the incumbent would be able to resubmit a bid for a new contract that would include making the services more competitive."

Real Estate: On Perpetuals

The MDU industry is represented in a real estate coalition chartered as the Real Access Alliance. The Alliance's constituency consists of leading Washington, D.C. based real estate trade organizations such as the National Multi Housing Council, National Apartment Association, National Association of REITs, National Association of Home Builders Multifamily Division, National Association of Realtors and the Building Owner's and Managers Association.

While leading members of the MDU industry agree that perpetual contracts appear to impose potential hurdles to the growth of competition for video services, they are not actively courting the Commission to intervene on this matter. "Bearing in mind our viewpoint of the desirability of competition, the idea of perpetual contracts is clearly troublesome," said Rick Sheridan of BOMA International. "One cannot argue that a contract that grants exclusive service rights in perpetuity provides residents with multiple service options. We favor exploring options to insure that tenants have the power of choice."

"It seems to go well beyond the economic arguments for allowing exclusive contracts in the residential MDU setting to say that the incumbent franchise cable operator should be economically protected forever through perpetual contracts," said Bruce Lundegren of the NAHB. "However, arguing that the FCC should intervene on the matter of perpetual contracts does fly in the face of the real estate industry's commitment to free market solutions. As such, the MDU industry is not asking the Commission to become involved on a decision regarding perpetual contracts."

"Perpetual contracts written years ago with franchise cable operators are, in some cases, a problem," said Arbury. "Sometimes the difficulty of a perpetual contract can be overcome and sometimes it cannot. The problem with perpetual contracts is that building owners are unable to remove a franchise operator that is performing poorly. He is restrained from providing a video and

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sometimes broadband data service package that meets the desires of residents. The key thing to remember is that the number of outstanding perpetual contracts is dwindling. Also, the real estate industry as a whole has consistently argued to the Commission at the FCC and elsewhere that the government should not interfere with the free market by changing the terms of contracts signed between two consenting parties. Otherwise, the industry would face the threat of the Commission's intervention regarding other issues of importance to property owners. Such regulation would also raise serious Constitutional and legal questions. Therefore, it is difficult for the apartment industry to oppose regulation of exclusive contracts and at the same time argue against perpetual contracts. However, if the FCC were to declare that perpetual contracts could be renegotiated or terminated the real estate industry as a whole would not necessarily oppose such a move. But the real estate industry is not promoting such regulatory action."

Waiting. Acting.

The Commission, and in particular the Cable Services Bureau (CSB) is always willing to listen to those who wish to make comments on pending issues. As such, it is recommended that parties electing to make comments should contact their respective industry's trade organizations. Those companies who compete with franchise cable operators to provide video and data services to the MDU marketplace industry should contact Bill Burhop at the IMCC (bburhop@imcc-online.org). Those companies who develop, own or manage residential MDU properties should contact Jim Arbury at the NMHC/NAA (jarbury@nmhc.org), Bruce Lundegren at the National Association of Home Builders Multifamily Division (blundegren@nahb.com) or Rick Sheridan at BOMA International (rsheridan@boma.org). PWB

About the Author

Larry Kessler is CEO of InteliCable Group, a national firm exclusively representing residential and commercial multidwelling unit property owners, developers and management firms in researching, developing and negotiating digital video and broadband infrastructure, service and contracts. He may be reached with questions and comments via e-mail at lkessler@intelicable.com.