

## MEETING WITH FCC LEGAL ADVISORS AND MEDIA BUREAU STAFF December 11, 2002

### I. Background

The Commission decided, in its declaratory order in March of this year, that cable modem service is not a “cable service.” What this means, as the Commission itself acknowledged, is that “revenue from cable modem service would not be included in the calculation of gross revenues from which the franchise fee ceiling is determined.”<sup>1</sup> Nevertheless, many cities whose franchises arguably require payment of fees on all revenues including cable modem revenues have refused to acknowledge that the Commission’s decision preempts and supersedes such a requirement. Moreover, more and more franchising authorities are taking action against cable operators who, in compliance with the ruling, are not including cable modem revenues in their franchise fee calculations. If this trend continues

### II. The Cities Base Their Claims on Erroneous Arguments.

- A. The decision is not “tentative.”** Some franchising authorities have argued that the Commission’s determination regarding the payment of fees on cable modem revenues is only “tentative” and will not be binding unless and until the Commission reaffirms the determination in its pending rulemaking proceeding. That, of course, is not right. There was nothing “tentative” about the decision that cable modem service is not a cable service – and, as the Commission recognized, Section 622 of the Communications Act clearly provides that only revenues from “cable services” may be included in calculating the franchise fee ceiling.
- B. The decision is “final.”** Some cities have also argued that the Commission’s determination is not “final,” and therefore is not binding, because it has been appealed to the Ninth Circuit. This, of course, also is not right. The Commission’s declaratory ruling was a final order, and such orders are binding during the pendency of an appeal unless they have been stayed by the agency or by the court. There has been no stay of the ruling. (The regulatory implications of the Commission’s declaratory ruling with regard to franchise fees are not at issue in the Ninth Circuit appeal. What is at issue is the determination that cable modem service is

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<sup>1</sup> Inquiring Concerning High Speed Access to the Internet over Cable and other Facilities, Declaratory Ruling and NPRM, GN Docket No. 00-185, CS Docket No. 02-52, Mar. 15, 2002 Declaratory Ruling, ¶ 105.

not a cable service and does not entail the provision of a telecommunications service.)

- C. The decision supersedes cities' contractual rights.** Some cities have simply taken the view that cable operators are contractually bound by the terms of their franchise agreements, notwithstanding the Commission's determination. But the whole point of the 1984 Cable Act was to define and limit what may and may not be insisted upon or agreed to in franchise agreements. Courts have made clear (1) that the restrictions in Title VI may not be waived by cable operators, and (2) that contracts that are inconsistent with the Act's provisions are preempted.<sup>2</sup> (Indeed, some cable operators who continued paying franchise fees on cable modem revenues after the Ninth Circuit held, in the Portland case, that cable modem service was not a cable service found themselves the targets of class actions by subscribers seeking refunds of the franchise fees collected and paid on cable modem revenues.)
- D. Cable franchises authorize the use of the public rights-of-way, and cable modem service imposes no additional burden on those rights-of-way.** Finally, some cities have argued that their cable franchise agreements only grant the use of public rights-of-way to provide cable service and that if cable modem service is not a cable service, then operators must pay additional fees and enter into separate agreements in order to gain permission to use the right-of-way to provide cable modem service. The Commission did not definitively decide this issue in its declaratory order, but it tentatively (and rightly) concluded that cities have no authority in Title VI to require such additional franchises and fees. Since this is an issue on which the FCC sought further comment, we explained in our comments and reply comments why the tentative conclusion was correct, and why cities have no authority under Title VI – or anywhere else – to require additional franchises and fees for the provision of cable modem service.<sup>3</sup>

### **III. Actions Taken by Cities Against Operators Who Have Stopped Paying Fees on Cable Modem Revenues.**

- A. Legal Action.** Based on the foregoing arguments, a number of franchising authorities have threatened legal action against cable operators who have stopped paying franchise fees on cable modem service. Several lawsuits have already been initiated.

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<sup>2</sup> See, e.g., *Cable TV Fund 14-1, Ltd. V. City of Naperville*, No. 96 C 5962, 1997 WL 433628 (N.D. Ill. July 29, 1997). See also *Nashoba Communications Ltd. Partnership v. Town of Danvers*, 703 F. Supp. 161, *rev'd on other grounds*, 893 F.2d 435 (1<sup>st</sup> Cir. 1990).

<sup>3</sup> See NCTA Comments in High Speed Access over Cable NPRM at 43-52; NCTA Reply Comments in High Speed Access over Cable NPRM at 18-29.

- B. Self-Help.** Franchising authorities are threatening to hold the operator in default, terminate the franchise, and/or collect liquidated damages under the “contract.”
- C. Enactment of New Franchise Ordinances Requiring Cable Modem Franchises and Fees.** Some communities are initiating the process of adopting ordinances, wholly apart from the cable franchise, that require cable operators to obtain franchises and/or pay franchise fees in connection with the provision of cable modem service. But they have no authority to do this because:
1. Franchised cable operators already have authority, under Section 621(a)(2) of the Act, to occupy and use the public rights of way.
  2. Any fee imposed only on cable operators is a “franchise fee” subject to the limits of Section 622, even if it is imposed outside the context of a cable franchise agreement.
  3. Even fees of general applicability – *i.e.*, fees or taxes imposed on all providers of broadband services, telecommunications providers and others – may not be levied on cable modem service because, among other reasons, the Internet Tax Freedom Act precludes taxation of Internet services.

**IV. A Final Point: Cities Will Continue To Receive Ample and Ever-Increasing Franchise Fees Based Solely on “Cable Services” Revenues.**

As NCTA showed in its reply comments:

“In 1985, one year after Congress enacted Section 622, the cable industry’s total gross revenues from the operation of cable systems was \$8.831 billion – which meant that cities were entitled to \$441.5 million in franchise fees. In 1996, when Congress amended the franchise fee cap to exclude gross revenues from services other than cable services, gross revenues had more than tripled, so that cities were entitled to \$1.385 billion in franchise fees. By 2001, this amount, based solely on gross revenues from the provision of cable services and not including cable modem service revenues, had skyrocketed to \$2.183 billion. The five-fold increase in franchise fees since 1985 has nothing to do with any increased costs of regulating cable systems or managing the rights-of-way, nor is there any reason to suspect that there have been any such increased costs.”<sup>4</sup>

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<sup>4</sup> NCTA Reply Comments at 25-26.