**Before the**
**Federal Communications Commission**
**Washington, D.C. 20554**

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| In the Matter of: | ) | |
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| Annual Assessment of the Status of Competition in the Market for the Delivery of Video Programming | ) | MB Docket No. 05-255 |
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# COMMENTS OF VERIZON ON THE STATUS OF COMPETITION IN THE VIDEO MARKETPLACE


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**COMMENTS OF VERIZON[1] ON THE STATUS OF COMPETITION IN THE VIDEO MARKETPLACE**

## INTRODUCTION AND SUMMARY

Most Americans currently have no choice in wireline video services other than the incumbent cable company in their area. The nearly complete lack of wireline competition to incumbent cable providers results in higher (and ever-increasing) prices and poorer service for cable subscribers. The GAO recently found that wireline cable competition exists in fewer than 2% of all markets, but that in those areas, cable prices average approximately 15% lower while customer service improves.[2] Such facts demonstrate that, in the limited areas in which wireline video competition exists, it produces tangible consumer benefits and illustrates why public policymakers should do their utmost to encourage widespread overbuilding of cable operators.

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1 The Verizon companies ("Verizon") are the affiliated local telephone companies of Verizon Communications Inc. These companies are listed in Attachment A.

2 U.S. General Accounting Office, *Telecommunications: Subscriber Rates and Competition in the Cable Television Industry*, GAO-04-262T, at 6 (March 25, 2004) *available at* http://www.gao.gov/new.items/d04262t.pdf; U.S. General Accounting Office, *Telecommunications: Issues Related to Competition and Subscriber Rates in the Cable Television Industry*, GAO-04-8, at 3-4 (Oct. 24, 2003) *available at* http://www.gao.gov/new.items/d048.pdf.

These facts also reveal the significance of the fact that Verizon is now poised to enter the video market on a large scale and will compete head-to-head with incumbent cable providers, thus providing consumers with a meaningful choice in video services providers. The provision of video services is important to encourage deployment of next-generation broadband networks, like Verizon's fiber-to-the-premises ("FTTP") network, and making it easier for broadband providers to provide competing video services over their networks will further the national policy of promoting the availability of broadband services for all Americans.

While Verizon is firmly committed to entering the video market, several significant roadblocks – some regulatory and some created by the cable incumbents – inhibit competition from Verizon and other competitive video services providers:

First and foremost among these barriers to competitive entry in the video market is the outdated and burdensome local franchising regime that increases significantly the costs and time-to-market for new entrants, thereby shielding incumbent cable providers from competition and providing them with advance notice and time to further entrench their position. This process is inherently slow and expensive, and becomes an even higher barrier to entry as a result of the practices of some local franchising authorities. A complete solution to this problem obviously could be provided through legislative action, and the Commission should encourage Congress to quickly reform the locality-by-locality franchise process for new entrants. But the Commission also has ample authority to improve the current state of affairs. For example, as Chairman Martin recently suggested, the Commission has authority to adopt rules interpreting and implementing the Congressional mandate in Section 621(a) that franchising authorities may not "unreasonably refuse to award" a competing franchise.[3] And by acting now to curb the delays and unreasonable demands associated with the franchise process, the Commission can promote the availability of competing video services that benefit consumers, and further the national policy goal of widespread broadband deployment.

Second, gaining fair access to video programming is an important concern for new entrants like Verizon. These program access concerns are the result of both loopholes in the current program access regulations and anticompetitive practices by some market participants intent on disadvantaging competitive providers. The Commission and Congress should act swiftly to remove these obstacles to widespread and meaningful video competition from competitive video providers.

Third, the Commission should consider the impact of several of its current cable regulations on new competitors in the video services market, and should revise these regulations as appropriate in order to encourage competitive entry into the market. For example, the Commission should revise some of its rules in order to ensure that competitive video services providers have a fair shot at competing for subscribers who live in multi-dwelling units. Likewise, the Commission should ensure that technological standards be crafted in such away that they ensure fair and open competition, rather than being tilted in favor of incumbent cable providers or any other set of competitors.

Finally, certain aspects of the regulations imposed on cable companies are redundant or otherwise unnecessary for competitive video services, particularly when the provider is already

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[3] Leslie Cauley, *FCC Chief Considers Forcing Cable TV Competition*, USA Today (Aug. 22, 2005) *available at* http://www.usatoday.com/money/industries/telecom/2005-08-22-telecom-usat_x.htm.

subject to common carriage regulation. The Commission should consider revising those regulations to make them more encouraging of new competition.

Each of these issues requires the attention of the Commission and/or Congress to hasten the day when widespread, wireline competition for video services is a reality. Moreover, if these concerns are resolved in a manner that encourages new entry into the video market, the Commission and Congress also will further their national policy of encouraging the ubiquitous deployment of broadband networks by increasing the incentives for deployment of fiber and other advanced broadband networks over which video can be transmitted.

## BACKGROUND: VERIZON'S ENTRY INTO THE VIDEO MARKET

In 2004, Verizon began a massive rollout of its FTTP network, installing a new, all-fiber network with sufficient capacity to meet consumers' voice, data, and video communications needs for decades to come. By the end of 2005, Verizon will have passed over three million homes and businesses with its fiber network, spread out over 15 states.[4] The customers currently served by Verizon's FTTP network can receive voice service and Verizon's FiOS broadband data services,[5] with download speeds ranging from 5 mbps to 30 mbps – speeds equal to or exceeding the fastest cable modem speeds. And Verizon will be able to increase these speeds in the future as needed through equipment upgrades.

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[4] Verizon already has begun deploying FTTP in portions in California, Connecticut, Delaware, Florida, Indiana, Maryland, Massachusetts, New Hampshire, New Jersey, New York, Oregon, Pennsylvania, Rhode Island, Texas, and Virginia. Additional deployments are announced regularly.

[5] "FiOS" is Verizon's name for the broadband and video services that it will provide over its FTTP network.

The next step in allowing consumers to realize the benefits of Verizon's FTTP network will be the offering of Verizon's FiOS TV video services. The provision of video services is an important component driving the deployment of advanced broadband networks like Verizon's FTTP network, and allowing providers to enter the video business without undue regulatory burdens will promote widespread broadband deployment by Verizon and others. So far, Verizon has obtained nine local cable franchises for FiOS TV from various local franchising authorities ("LFAs") in California, Florida, Virginia, and Texas, and it will begin to offer service in some of these locations before the end of this year. Verizon is also in various stages of franchise negotiations with scores of other LFAs throughout its service area.

FiOS TV video services will combine aspects of both the current, state-of-the-art technology used by cable companies and many of the advanced features made possible by the developing IP platform. Therefore, all FiOS TV subscribers will have available to them the benefits of digital cable, video-on-demand, digital video recorders, interactive programming guides, and, in the near future, other interactive video features. Moreover, because of the tremendous capacity offered by Verizon's FTTP network, Verizon will be able to provide FiOS TV subscribers with a diverse range of programming choices, including a wide range of high definition, video-on-demand, and foreign-language content.[6]

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[6] Verizon has already reached carriage agreements with many content providers, including NBC Universal Cable, Turner Broadcasting System, Showtime Networks, Starz Entertainment Group, NFL Network, Discovery Communications, A&E Television Networks, TVN Entertainment, Varsity TV, Gospel Music Channel, Soundtrack Channel, MavTV, GolTV, SiTV, Black Family Channel, The America Channel, BlackBelt TV, Expo TV, LIME, and the Pentagon Channel. Some of the channels that Verizon has agreed to carry include independent content producers, like The America Channel, who have been denied carriage by the large cable companies based on a supposed lack of bandwidth. *See* Jonathan Make, *America Channel Gets Verizon Carriage Deal; Competitive Issues Raised*, Communications Daily (Aug. 31, 2005). Negotiations continue with the owners of other programming.

## DISCUSSION

While Verizon has made huge strides towards entering the video market on a large scale and will begin offering video service in the very near future, several significant regulatory and market barriers to entry have slowed the introduction of competition by Verizon and other competitive video services providers. The remainder of these comments will focus on these issues which warrant immediate regulatory reform. The Commission, Congress, state legislatures and local officials could all play an important role in addressing these issues in a way that encourages greater investment in broadband network deployment and more choices for consumers when they select their video services provider.

### A. The Local Franchising Process Impedes Competition in the Video Market.

The single biggest obstacle to widespread competition in the video services market is the requirement that a provider obtain an individually negotiated local franchise in each area where it intends to provide service. As long ago as its first annual report on video competition in 1994, the Commission recognized that "[t]he local franchise process is, perhaps, the most important policy-relevant barrier to competitive entry in local cable markets."[7] That remains true today.

#### 1. Problems with the Franchising Process.

The local franchising process inhibits competition in the video market for several reasons. First, the franchising process results in inherently anticompetitive effects by requiring a new entrant into the market to give notice to the incumbent cable operator that competition is coming, thereby giving the incumbent the opportunity to delay the process and to take other steps

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[7] *Implementation of Section 19 of the Cable Television Consumer Protection and Competition Act of 1992, Annual Assessment of the Status of Competition in the Market for Delivery of Video Programming*, 9 FCC Rcd 7442, Appendix H at ¶ 43 (1994) ("First Video Competition Report").

to entrench its position. Second, the very process of going town-to-town to negotiate video franchises is inherently expensive and slow, thus creating enormous entry costs for any provider who wants to compete against the cable incumbents – particularly for a provider who intends to compete on a large scale. Third, the burdens heaped onto new entrants are further increased by so-called "level playing field" and build-out requirements imposed by many LFAs, often at the urging of the incumbent cable operators. These policies, cloaked in the rhetoric of "fairness," primarily serve to increase the costs of new entrants and shield incumbents from competition. Finally, many LFAs use the franchising process as a method for forcing prospective video providers to furnish a municipality with a variety of goodies completely unrelated to video services or to the purposes of the franchising requirement. Such overreaching adds additional time and expense to the franchising process. In these respects, the local franchising regime is fundamentally broken, and needs the attention of the Commission and Congress to be fixed.[8]

**Advance Notice to Incumbent.** The very nature of the franchise system can lead to anticompetitive effects because the franchise requirement forces a new entrant to telegraph its deployment plans to the incumbent video competitor. This advance notice that competition is on the way, often months or more before the new entrant is allowed into the market, allows the incumbent not only to take steps to prolong the franchise process and delay the onset of competition, but also to entrench its position in the market before the new entrant has the opportunity to compete. Verizon has already observed this type of behavior in places where it

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[8] States and local authorities should also be encouraged to address this important issue. For example, the State of Texas recently enacted legislation that will permit video services providers to obtain authorization from the state to provide video services in place of individually negotiated, local franchises. Verizon applauds any such efforts to streamline the cumbersome franchising process, and anticipates that the result will be accelerated deployment of competitive video services in the state.

has sought franchises and is deploying FTTP. After learning of Verizon's deployment plans, incumbents frequently take steps to further entrench their positions in those specific areas before Verizon gains permission to enter the market with its competitive services and before consumers have a real opportunity to choose among competing providers. Allowing incumbents this head start on competition makes it all the more difficult for a new competitor to successfully enter the market and for consumers to make an informed choice among service providers.

**Delay.** One of the biggest, inherent problems with the current franchise requirements is that the process simply takes too long. The process – including application, review, negotiation, and approvals – routinely takes many months, and often more than a year. The problem of delay results in part from factors such as inertia, arcane or lengthy application procedures, bureaucracy or, in some cases, inattentiveness or unresponsiveness at the LFA level. For example, in one franchise area, Verizon has been required to submit multiple rounds of applications over the course of many months, and the process still has not even reached the level of gaining the approvals necessary even to begin the negotiation process, let alone to obtain a competing franchise. The initial vote on the application is now scheduled for approximately one year after Verizon filed its initial application. And that is just the beginning of the process. While not all application processes take as long as this one, the process routinely stretches out over many months.

In other cases, the delay in the franchising process is created by statutory formalities that impose waiting periods before a franchise may be granted. Massachusetts is one example where franchising procedures contain procedural hurdles and public notice periods that not only inhibit creative negotiations but also make it impossible to obtain a franchise in less than six months *even if the regulators and all parties agree on all the terms of the franchise*. Obviously, disagreement over terms can lead to even longer delays. As discussed below, some LFAs make outrageous demands on new entrants, thereby requiring protracted delays and increasing the cost of entry (assuming the provider decides to go ahead at all).

And the problems caused by this delay are exacerbated for a provider who seeks to provide video services on a national or regional basis – something important to gaining economies of scale and scope and obtaining sufficient bargaining power to get desirable content on reasonable terms. Such a provider can face time-consuming negotiations for individualized franchise agreements with hundreds or even thousands of different LFAs. For example, even Verizon's initial waves of FTTP deployment will require franchise negotiations with hundreds of separate LFAs in order for Verizon to offer cable service. And that number could easily reach into the thousands as the FTTP rollout continues in coming years. Even if everything with each of these negotiations were to go as smoothly as possible, the process will require huge amounts of time and resources that could be better spent on increased deployment or innovation.

**"Level Playing Field" and Build-Out Requirements.** Exacerbating these burdens associated with the franchising process are efforts by LFAs – often at the prompting of incumbent cable companies – to enforce anti-competitive so-called "level playing field" ("LPF") laws and franchise provisions that the incumbents have won in some areas. Citing these monopolist protection laws, incumbent cable providers pressure LFAs (under threat of litigation) to require the new entrant to build-out and serve an entire franchise area on an expedited basis or to match all of the concessions previously provided by the incumbent in order for it to gain its original monopoly position in the local area, despite the vastly different competitive situation facing the new entrant.

At least 11 states have these statutes which can inhibit competitive video entry by requiring new entrants to undertake franchising obligations at least as burdensome as those imposed on the incumbent. Similar provisions appear in some incumbents' franchise agreements. The negative effects of these requirements on competition may not at first be apparent because, as a general rule, creating a level economic playing field makes eminent sense. The problem is that, as an economic matter, the ostensibly equal burdens required under these laws in fact impose a heavier burden on new entrants than on incumbents, and thus create barriers to entry. In exchange for the costs they incurred to enter the market, the incumbents generally received exclusive franchises and enjoyed all of the benefits of being monopoly providers for years, and often decades. In contrast, competitive video providers who enter the market today are in a fundamentally different situation, facing ubiquitous competition from strong and entrenched competitors. As one noted commentator and former FCC chief economist has explained:

> Labeling nominally symmetric obligations borne by entrants and incumbents as "equal" burdens ignores the greater likelihood that the residual profits anticipated by the entrant will be insufficient to cover fixed costs, relative to the incumbent that entered without rivals.[9]

In other words, forcing a new entrant into the video business to incur – as a prerequisite to entry into a competitive market – the kinds of costs that the incumbent was able to recover over the years when it enjoyed a monopoly franchise acts as a barrier to entry.[10] Such requirements

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[9] *See* Thomas W. Hazlett & George S. Ford, *The Fallacy of Regulatory Symmetry: An Economic Analysis of the 'Level Playing Field' in Cable TV Franchising Statutes*, 3 Business & Politics 21, 24 (2001) *available at* http://www.manhattan-institute.org/hazlett/the_fallacy _of_regulatory_symm.pdf.

[10] George S. Ford *et al.*, *Competition After Unbundling: Entry, Industry Structure and Convergence*, Phoenix Center Policy Paper No. 21, at 39 (July 2005), *available at* http://www.phoenix-center.org/pcpp/PCPP21Final.pdf (noting that the costs that the incumbent

blindly tax new video entrants without even taking into account the need for such expenditures (*e.g.*, whether a redundant "institutional network" or "I-Net" is really necessary) and the considerably smaller upside to the provider after entering the market, given the presence of competition. That these requirements, couched in "fairness" terms, are really intended to protect the incumbents is confirmed by a cable trade publication's headline describing the introduction of LPF legislation in California: "California Anti-Competition Bill Pending."[11]

In contrast, the Commission and the states have never required cable companies and other telecommunications services competitors to match all of the obligations imposed on the incumbent telephone companies ("ILECs"). For example, ILECs are generally required to provide telecommunications services throughout their service areas, and are subject to carrier of last resort obligations. Competitive telephone providers – including all the major incumbent cable companies – on the other hand, are generally permitted to provide service where and to whom they choose within each state, after making the minimal showing required to become certified as a competitive provider.

Even when state franchising statutes impose somewhat narrower obligations on new entrants to match incumbents' investment – for example, build-out requirements – the effect can be to deter entry. This is particularly true when the build-out requirements are related in some way to the historical boundaries of political subdivisions that may have no correlation either with the location of a telephone company's wire centers or with the pattern of current population growth. Suppose that a telephone company wishes to deploy FTTP around a wire center that

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had to incur to enter the market "are sunk and essentially irrelevant to that firm's subsequent business decisions," while for a prospective new entrant, "sunk costs are a *marginal* cost and before spending them, the prospective entrant will consider other uses for those funds").

[11] *California Anti-Competition Bill Pending*, Cable TV Franchising, Aug. 31, 1998, at 2.

serves multiple political subdivisions, each of which may be served by a different incumbent cable company. If, as a condition of obtaining the necessary franchises, the new entrant is obliged to commit to offer service to all or substantially all of the locations in *each* of the multiple political subdivisions, then the necessary capital expenditure may become astronomical, the deployment may become uneconomical, and, as a result, *no* consumers in those subdivisions will have the benefit of additional choice in video services.

**Outrageous Demands by LFAs.** Many local franchising authorities unfortunately view the franchising process as an opportunity to garner from a potential new video entrant concessions that are in no way related to video services or to the rationales for requiring franchises. In Verizon's first year of seeking franchises for FiOS TV, it has repeatedly encountered outrageous demands by some LFAs that prevent, or at least slow, entry into particular markets. Whether or not some of the things sought by LFAs are laudable or well-intentioned, they are essentially a hidden tax that discourage deployment by new video competitors and increase the costs of video services.

Verizon frequently has received demands by LFAs that are completely unrelated to its proposed video operations. For example, one county has demanded that Verizon connect all of the traffic signals in the county with fiber. In that vein, another LFA wants Verizon to fund the municipality's purchase of street lights from the local power company. That same LFA also proposed that Verizon allow parking for the town library at a Verizon facility, build a mobile telephone repeater at city hall, and provide city employees with mobile telephone service. Yet another LFA is demanding that Verizon provide the county with free use of Verizon conduit and manholes as well as free attachments to all Verizon utility poles. Other frequent demands by LFAs include connecting all city or county buildings with fiber and providing the local government with free data services – sometimes wired, sometimes wireless, sometimes both. One LFA, for example, would like Verizon to construct an additional I-Net for the county, at a cost of over $4.9 million. Similarly, one LFA demanded that Verizon provide 6 fiber-strand I-Nets to 120 municipality sites (or pay the cash equivalent). Likewise, some LFAs even demand that fiber be provided to other private individuals or organizations. For example, one county seeks to require that Verizon provide fiber to 60 "human services" organizations that work with the county.

Other demands, while perhaps arguably related to video services, still far exceed what should reasonably be expected of a new entrant in the market. For example, one county seeks to require Verizon to carry 18 or more Public, Educational and Government ("PEG") channels in the franchise area – approximately 6 times the average. Another LFA has requested that Verizon provide free video services to all houses of worship within the municipality.

Many LFAs also want money from the new video provider. Examples include an "application filing fee" in excess of $50,000, a "franchise acceptance fee" in excess of $250,000, and an up-front "PEG support" grant in excess of $250,000. One LFA demanded that Verizon post a $20 million performance bond and provide a $500,000 letter of credit guaranteeing satisfaction of performance standards. Many LFAs also request that Verizon fully indemnify them for lawsuits brought by the cable incumbents, thus making Verizon foot the bill for fighting off the anticompetitive tactics of some cable companies.

Demands such as these show that some LFAs view a franchise application by a new entrant as an opportunity to obtain a variety of goodies, without concern for the resulting decrease in video competition and/or increase in cable prices.

When faced with an LFA that makes outrageous demands or that seeks to impose unreasonable "level-playing field" or build-out requirements, Verizon must decide whether investment and deployment are justified in that particular area, or whether deployment in more receptive communities is preferable. Particularly for a provider such as Verizon who already has authority to install the networks over which the video services would be offered by virtue of its independent authority to provide voice and data services, allowing such obstacles to delay or prevent the offering of video services makes little sense and deprives consumers of a competitive source for video services.

### 2. Legislation Is Necessary to Fully Cure the Problems Caused by the Local Franchising Regime.

Given the inherent inhibitive effect of the local franchising process on video competition, the Commission should urge Congress to comprehensively revise the local franchise system. Even if all of the current abuses were removed from the system – a tall task – the requirement that a competitor go town-to-town to obtain permission to provide video services creates a substantial and unwarranted barrier to entry. As discussed above, the franchising process itself inhibits competitive entry by tipping incumbents off that competition is on the way. This gives the incumbent the opportunity to take steps to delay the approval process and entrench its position in the market, thereby gaining an unfair head start on competition before the new entrant is permitted into the market. This process also is inherently slow and expensive, thus delaying and discouraging competitive provider from entering into the market. Therefore, Congress should act now to eliminate the enormous barrier to entry created by the current local franchising system.

### 3. The FCC Should Act Now to Prevent LFAs from Unreasonably Refusing to Award a Franchise to a Competitive Video Services Provider.

Short of comprehensive legislative reform of the local franchise requirement, there are still important steps that the Commission could take that would make the current system more efficient. In enacting the 1992 Cable Act, Congress decided that consumers would benefit more from competition among video providers than from the exclusive and *de facto* exclusive franchise arrangements that were dominant at the time. Accordingly, Congress imposed a significant new requirement on franchising authorities, providing in Section 621(a) that "a franchising authority may not grant an exclusive franchise and may not *unreasonably refuse to award* an additional competitive franchise." 47 U.S.C. § 541(a)(1) (emphasis added). Unfortunately, experience has shown that many LFAs have failed to heed this requirement, and the desired level of competition has failed to materialize. Consumers still lack a choice of wireline video providers in over 98% of franchising areas, and, as shown above, many LFAs seem more interested in obtaining give-aways from new entrants than in permitting competition among video providers. Therefore, the time has come for the Commission to give effect to Congress' intent, and to prevent LFAs from taking steps that amount to an "unreasonabl[e] refus[al] to award an additional competitive franchise."

#### a. <u>Section 621(a) Was Intended to Reduce Barriers to Competitive Entry Caused by the Franchising Process.</u>

The history giving rise to Section 621(a) shows that Congress intended to prevent the types of practices which continue to frustrate competition in the video market. Prior to the 1992 Cable Act, the Commission issued a report to Congress, as required by the 1984 Cable Act, in which the Commission explained how the "regulatory activities of some local authorities may discourage or even preclude competing cable systems or other competing multichannel media."

*See Competition, Rate Deregulation and the Commission's Policies Relating to the Provision of Cable Television Service*, MM Docket No. 89-600, 67 Rad. Reg. 2d (P & F) 1771, ¶ 131 (July 31, 1990) ("*FCC Video Recommendation Report*"). In a finding that echoes the concerns that Verizon mentions above, the Commission described the problems faced by a new competitor:

> [T]he record in this proceeding reveals competing systems face several problems that can be eased by changing the franchise process. First, cable companies interested in competing with existing franchisees assert that some franchise authorities require second systems to serve the entire market (i.e., "universal service" requirements), thus precluding a more economically feasible incremental approach to service. Second, some franchising authorities require new entrants to meet a variety of municipal requirements that apply to existing operators and which, it is argued, are more sustainable for a sole operator. Third, some franchising authorities require second entrants to meet certain requirements, such as the posting of a bond or letters of credit, not imposed on the incumbent. Fourth, some jurisdictions have granted exclusive franchises, an unwise policy in our judgment.

*Id.* ¶ 134. The Commission concluded that there was "no valid reason to discourage or forbid competing systems," *id.* ¶ 138, and made a number of recommendations to Congress on changes that should be made to the franchising process:

> We recommend that Congress amend the Cable Act to forbid local franchise authorities from unreasonably denying a franchise to applicants that are ready and able to provide service. Congress should also make it clear that local authorities may not pass rules whose intent or effect is to create unreasonable barriers to entry of potential competing multichannel video providers. Franchise requirements should be limited to appropriate governmental interests, such as establishing requirements concerning public health and safety, repair and good condition of public rights-of-way, and the posting of an appropriate construction bond.

*Id.* ¶ 141.

In particular, the Commission concluded that imposing immediate build-out requirements on a new entrant would be an "ill-advised" policy, given the competitive benefits that can result for consumers in a market, even when a competitor does not serve all parts of an area. *Id.* ¶ 139.

The Commission recognized that concerns with “cream skimming” were overblown because “the nature of the broad-based demand for cable services should minimize the prospect that in the long term new entrants would find it profitable to only serve limited groups of homes within a metropolitan area.” *Id.* ¶ 139 n.198. Therefore, the Commission encouraged Congress to permit “incremental” entry into a market by a competitive video provider. *Id.* ¶ 141.

Congress embraced the Commission’s recommendations in the 1992 Cable Act, and responded by revising Section 621(a) to place several limitations on the ways that LFAs can exercise their franchising authority. The revised Section 621(a) not only prohibited exclusive franchises, but also provided that an LFA “may not *unreasonably refuse to award* an additional competitive franchise.” 47 U.S.C. § 541(a)(1) (emphasis added). It also provided LFAs with a set of instructions and a limited list of factors that can be considered to guide LFAs’ franchising decisions. The statute recognized that an LFA (1) must permit a new entrant “a reasonable period of time to become capable of providing cable service” within the franchise area, *id.* § 541(a)(4)(A); (2) may “require adequate assurance” that the new entrant will “will provide adequate public, educational, and governmental access channel capacity, facilities, or financial support”, *id.* § 541(a)(4)(B); and (3) may “require adequate assurance” that the new entrant “has the financial, technical, or legal qualifications to provide cable service,” *id.* § 541(a)(4)(C).

The legislative history of these provisions confirms Congress’ intent to restrict LFAs from taking actions that would unreasonably delay or prevent new video services providers from entering the market. The Conference Report on the 1992 Cable Act explained that “the conferees believe that exclusive franchises are directly contrary to federal policy and to the purposes of [the 1992 Cable Act], which is intended to promote the development of competition.” *Cable Television Consumer Protection and Competition Act of 1992*, H. Rep. No.

102-862, at 77 (1992). The report expressed a desire to prevent LFAs from "artificially protect[ing] the cable operator from competition." *Id.* Discussing the limited list of factors that an LFA may legitimately consider, the report goes on to explain that the Section 621(a)(4) factors were intended to "specify that franchising authorities may require applicants for cable franchises to provide adequate assurance" concerning both PEG requirements and the applicant's qualifications. *Id.* at 78.

The House and Senate Reports on the legislation similarly reveal an intent to cabin LFAs' discretion and foster competition. The House Report endorses the Commission's recommendation that Congress encourage competition by "prevent[ing] local franchising authorities from unreasonably denying a franchise to potential competitors who are *ready and able to provide service*." *Cable Television and Consumer Protection and Competition Act of 1992*, H. Rep. No. 102-628, at 46 (1992) (emphasis added). That report then goes on to identify the limited factors that ultimately were included in Section 621(a)(4) as determinative of the "unreasonabl[eness]" of an LFA's refusal to award a competitive franchise. *Id.* at 90. Similarly, the Senate Report indicates that similar factors in the Senate version of the bill were meant to determine the reasonableness of an LFA's actions. *See Cable Television Consumer Protection Act of 1991*, S. Rep. No. 102-92, at 91 (1991). Together, these three reports confirm that Congress intended the restrictions of Section 621(a)(1)'s "refusal to award" provision to be a meaningful restriction on an LFA's actions, and that the factors listed in Section 621(a)(4) were intended to limit the factors that an LFA could legitimately consider in reviewing a franchise application.

The statements of the supporters of 1992 Cable Act bear out this interpretation. For example, Senator Lieberman's statements in support of the 1992 Cable Act confirm the broad, pro-competitive purpose behind Section 621, explaining that the legislation:

> [P]romotes the development of competition by lowering the barriers to entry of competitors in the marketplace. . . . The conference report supports competition by *making clear that local franchising authorities cannot create de facto exclusive local cable franchises by refusing to grant franchises to competitors*. . . . It lowers the barriers to a whole host of new competitors . . . .

Statement of Sen. Lieberman in Support of the Conference Report on S. 12, 138 Cong. Rec. S14583 (Sept. 22, 1992) (emphasis added). And Senator Dodd recognized that the changes to the franchise rules were intended to encourage the entry of competing providers "so that families have real choices." Statement of Sen. Dodd in Support of S. 12, 138 Cong. Rec. S712 (Jan. 31, 1992).

Thus, Congress clearly intended for the provisions of Section 621(a) to place meaningful limits on the actions of LFAs in order to encourage competition among video service providers.

### b. <u>The Commission Should Alleviate Franchising Burdens.</u>

Despite the important role intended by Congress for Section 621(a) in fostering competition among video providers, these provisions appear to have been largely ignored so far, not only by many LFAs but also by prior Commissions and the courts. Since 1992, the Commission appears to have only made reference to the relevant provisions of Section 621(a) in the context of two, early video competition reports.[12] Likewise, only a small handful of reported

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[12] *See First Video Competition Report*, at ¶¶ 55, 56, 250 (noting that Congress had incorporated Commission's recommendations on franchise reform, and noting, in light of limitations of judicial review provision, that it would "monitor whether undue delays in granting final determinations on overbuild franchise applications interfere with the effectiveness of Section 621"); *Matter of Annual Assessment of the Status of Competition in the Market for the Delivery of Video Programming*, 11 FCC Rcd 2060, ¶¶ 40-44, 212 (1995) (noting potential barrier to

court cases have addressed these provisions at all, and even the only two cases that concern the "unreasonable refusal to award" part of Section 621(a) fail to explore the types of LFA actions that should be considered unreasonable.[13] In the meantime, competition between wireline video competitors remains almost completely absent and the local franchising process remains a barrier to competitive entry. Therefore, the Commission should move promptly forward to finally give force to Congress' intent in enacting Section 621(a). In particular, the Commission should establish interpretive and implementing rules that improve the efficiency of, and prevent the delays and unreasonable demands generated by, the local franchising process, thereby decreasing the barriers to entry for competitive video providers.

In adopting rules implementing and interpreting Section 621(a), the Commission should address the aspects of the franchising process, discussed above, that are the biggest impediment to competitive entry. These include unreasonable delay, unreasonable build-out and "level playing field" requirements, and unreasonable demands by LFAs, including any that are unrelated to the provision of video services. Both the limitations provided by Congress in Section 621(a)(4) and the parallel provision addressing the franchise renewal process – Section

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entry caused by local franchise requirements, and encouraging broad reading of Section 621(a) to apply to existing, exclusive franchises).

[13] In *Qwest Broadband Services, Inc. v. City of Boulder*, 151 F. Supp.2d 1236, 1242-44 (D. Colo. 2001), a district court found that a city ordinance requiring voter approval for a franchise to be granted was preempted in that it conflicted with, among other things, the "unreasonable refusal to award" requirement. In *Nepsk, Inc. v. Town of Houlton*, 283 F.3d 1, 9-11 (1st Cir. 2002), the First Circuit concluded that a cable company had failed to state a claim under the "unreasonable refusal to award" requirement because it had never filed an application for a "second franchise." All of the remaining cases addressing Section 621(a) focus on the issue of whether the prohibition on exclusive franchises should apply retroactively. *See James Cable Partners v. City of Jamestown*, 43 F.3d 277 (6th Cir. 1994); *Cox Cable Communications, Inc. v. United States*, 992 F.2d 1178 (11th Cir. 1993). Therefore, the existing case law reveals little more than a lack of enforcement.

626 – can help the Commission to craft interpretive rules that account for any legitimate concerns and interests of LFAs, while making the overall franchise process more accommodating of competitive entry.

**Reasonable Time Limits.** As discussed above, one of the primary problems with the current franchising process is the delay that it causes, slowing by months (and over a year in some cases) the process of making competitive video services available to consumers and taxing a new entrant's resources as it seeks to negotiate with a large number of LFAs simultaneously. Such delays are particularly unjustified in the case of a provider like Verizon who already has permission to run the physical network plant over which the video services will be transmitted. In that situation, an LFA's concerns with managing rights-of-way or protecting public health and safety as a result of the entry of a new video competitor are minimal. *See National Cable Television Ass'n v. FCC*, 33 F.3d 66, 73 (D.C. Cir. 1994) (noting that "use of public rights of way . . . provide[s] a key justification for the cable franchise requirement"). So delay does little other than deprive consumers of a choice in video providers.

Both Section 621(a) and Section 626 reflect concerns with preventing delay in franchising decisions. Congress' very choice of words – "unreasonably refuse to award" – reflects an intent to ensure that the franchising process moved forward at a reasonable pace. Notably, by its express terms, this provision does *not* apply only when an LFA affirmatively *denies* a competitive franchise. On the contrary, it also applies when a franchising authority unreasonably fails to grant a competitive franchise, as it might do through simple inaction or delay. And for good reason. One of the key concerns underlying the provision is that franchising authorities could simply string out the process and deter entry by not acting in a reasonable period of time on a franchise application. So the provision applies fully when a franchising authority unreasonably withholds action, or simply fails to act within a reasonable period of time.

Likewise, Section 626(c)(1) itself reveals what Congress thought was "reasonable." It recognizes that a reasonable period of time for an LFA to grant a renewal application filed by an incumbent cable operator would be four months. 47 U.S.C. § 546(c)(1). This provision provides an apt benchmark for action on a franchise application by a provider like Verizon who is already authorized to construct and operate the network over which its video services will be transmitted. Like the incumbent cable operator who already has its network in place, the LFA's interest in managing the public rights-of-way – the principal rationale for franchise requirements – is largely lacking for such providers.[14] And Section 621(a)(4) narrowly limits the factors that can be considered in determining whether to grant a competing franchise in any event. Therefore, especially for a provider who simply seeks to add an additional service to its offerings, Section 626's four month time period would be an appropriate time limit for the LFA to review an application and would give effect to Congress' view of what constitutes a reasonable amount of time.

**Reasonable Interpretations of Level Playing Field and Build-Out.** The Commission also should clarify that so-called "level playing field" requirements and unreasonable build-out requirements are inconsistent with Section 621(a). As explained above, such requirements create

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[14] *See National Cable Television Ass'n v. FCC*, 33 F.3d 66, 73 (D.C. Cir. 1994) (noting that "use of public rights of way . . . provide[s] a key justification for the cable franchise requirement"); *Telephone Company-Cable Television, Cross-Ownership Rules, Sections 63.54-63.58,* 7 FCC Rcd 5069, 5072 ¶ 11 (1992) ("[i]n enacting Section 621 of the Cable Act, Congress was primarily concerned with the use of public streets and rights-of-way by cable television operations and the ability of state and local entities to regulate such use").

a major – and unjustified – barrier to entry.[15] The costs incurred by the incumbent were generally in exchange for gaining a monopoly position in the market, and those costs likely have been recovered over the years or decades in that position. For a new competitor, on the other hand, any such costs imposed by the LFA must be borne as a cost of entering the market, and the payoff for the competitor is also less because it then will face intense competition from the entrenched incumbent. Accordingly, the Commission should recognize that such provisions are inconsistent with Section 621(a)'s command that LFAs not "unreasonably refuse to award" a competitive franchise.

Congress was obviously concerned that so-called build-out requirements could deter competition. In fact, that was the purpose for Congress' instruction in the statute that an LFA must "allow the applicant's cable system a reasonable period of time to become capable of providing cable service." 47 U.S.C. § 541(a)(4)(A); *see, e.g.*, Statement of Sen. Gorton in Support of the Conference Report on S. 12, 138 Cong. Rec. S14222, at S14248 (Sept. 21, 1992) (noting that this requirement would encourage competition by "assuring that adequate time is given the new franchisee to build a system"). As the Commission previously recognized, requiring franchise-wide build-out in an expedited manner harms new entrants and consumers. Such a policy is both unnecessary – in light of the incentives to respond to the "broad-based demand for cable services" – and "ill-advised" – in light of the benefits to consumers even from partial competition. *FCC Video Recommendation Report* ¶ 139.

[15] *See* Thomas W. Hazlett & George S. Ford, *The Fallacy of Regulatory Symmetry: An Economic Analysis of the 'Level Playing Field' in Cable TV Franchising Statutes*, 3 Business & Politics 21, 24 (2001); George S. Ford *et al.*, *Competition After Unbundling: Entry, Industry Structure and Convergence*, Phoenix Center Policy Paper No. 21, at 36-39 (July 2005).

Moreover, although the statute speaks of allowing a reasonable time for a provider to become capable of providing service to "all households in the franchise area," the Commission should make clear that it does not require providers with existing networks to build out where they do not have facilities, just like a cable company is not required to offer telephone services throughout an ILEC's service area just because it enters the telephony market. As mentioned above, Verizon's network does not correspond to the boundaries of local franchise areas, and when it converts a wire center to FTTP, those facilities could serve parts of several different local franchising areas. The burden would be enormous if Verizon were then required to provide video service throughout each local franchise area touched by the wire center that had been converted. Therefore, rather than imposing unreasonable requirements that fail to account for this significant difference in network architecture, the Commission should instruct LFAs to limit build-out requirements to locations where Verizon is providing telephone service.[16]

**Reasonable Limits on Legitimate LFA Demands.** Finally, the Commission also should place limits on an LFA's ability to make outrageous demands of a potential video entrant for money or for other things completely unrelated to the provision of video services or that otherwise go beyond the limited list of factors in Section 621(a). As both the Commission and Congress recognized, the proper focus for an LFA should be on whether the applicant is "ready and able to provide service," *FCC Video Recommendation Report* ¶ 141, and not on imposing a hidden tax on video customers and competition. Accordingly, the factors listed in Section

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[16] Of course, LFAs may consider Section 621(a)(3)'s command that "access to cable service" not be "denied to any group of potential residential cable subscribers because of the income of the residents in the local area in which such group resides." 47 U.S.C. § 541(a)(3). Verizon will not discriminate against potential subscribers based on income. Verizon has consistently exhibited a commitment to make advanced technologies available to Americans of all income levels.

621(a)(4) focus on ensuring compliance with PEG requirements and with reviewing the applicant's "financial, technical, or legal qualifications to provide cable." 47 U.S.C. § 541(a)(4)(B), (C). This provision itself shows that an LFA may not legitimately base its franchising decisions on whether the provider is willing to accede to demands for funds or items that do not relate to the provision of video services, but instead that the focus should be limited to only those interests that can legitimately be considered under Section 621(a)(4). The Commission should make this explicit, and instruct LFAs that they are not permitted to sacrifice competition and consumer welfare in a gambit to obtain unrelated goodies for the municipality.

While rules along these lines would not completely eliminate the competitive barriers to entry for a new entrant in the video market, they could go far in reining in the excesses of the local franchise regime and effectuating Congress' intent of fostering competition in the video services market.

**c. The Commission Has Authority to Act.**

The Commission's authority to promulgate such rules that interpret and give effect to the express provisions of the Cable Act is beyond question. The Supreme Court has repeatedly confirmed that the Commission possesses such authority to use its general rulemaking authority to effectuate the provisions of the Communications Act. *See, e.g., AT&T Corp. v. Iowa Utilities Board*, 525 U.S. 366, 378 (1999). The Commission has undertaken literally scores of rulemakings interpreting and applying various provisions of the 1992 Cable Act as well as the 1996 Act, including numerous proceedings not specifically required by those Acts.[17]

[17] *See, e.g., Implementation of Section 11 of the Cable Television Consumer Protection and Competition Act of 1992,* CS Docket No. 98-82; *Implementation of Sections of the Cable Television Consumer Protection and Competition Act of 1992: Rate Regulation*, MM Docket No. 93-215; *Implementation of Section 304 of the Telecommunications Act of 1996, Compatibility*

Moreover, the Commission has ample experience with crafting rules that implement statutory requirements like those in Section 621(a). The Commission routinely decides – both in the context of adjudications and rulemakings – the content of statutory provisions that hinge on whether particular actions are "reasonable" or "unreasonable."[18] For example, on some occasions the Commission has adopted rules that establish presumptions of reasonableness or unreasonableness for certain types of action.[19] Therefore, the Commission has ample authority to promulgate rules that interpret and give effect to Section 621(a)'s prohibition on LFA actions

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*Between Cable Systems and Consumer Electronics Equipment*, PP Docket No. 00-67; *Closed Captioning and Video Description of Video Programming, Implementation of Section 305 of the Telecommunications Act of 1996, Video Programming Accessibility*, MM Docket No. 95-176; *Implementation of Section 203 of The Telecommunications Act of 1996 (Broadcast License Terms)*, MM Docket No. 96-90.

[18] *See, e.g., Implementation of Sections of the Cable Television Consumer Protection and Competition Act of 1992: Rate Regulation*, 8 FCC Rcd 5631, ¶ 1 (1993) (setting rules to ensure reasonable rates for basic cable service tier); *Star Lambert and Satellite Broadcasting and Communications Association of America*, 12 FCC Rcd 10455, ¶¶ 2-3 (1997) (determining that local ordinances violated Commission rules prohibiting unreasonable delays and unreasonable increases in costs for satellite providers); *Local Exchange Carriers' Rates, Terms, And Conditions For Expanded Interconnection Through Physical Collocation For Special Access And Switched Transport*, 12 FCC Rcd 18730, ¶ 2 (1997) ("Pursuant to Sections 201 through 205 of the Communications Act of 1934, as amended (Act), we are using the tariff review process to ensure that LECs provide interstate expanded interconnection service at rates, terms and conditions that are just, reasonable, and nondiscriminatory"); *IT&E Overseas, Inc., Complainant, v. Micronesian Telecommunications Corporation, Defendant*, 13 FCC Rcd 16058, ¶ 21 (1998) (evaluating claims of unreasonable preferences given in violation of § 202(a)).

[19] *See, e.g., Preemption of Local Zoning Regulation of Satellite Earth Stations*, 11 FCC Rcd 5809, ¶¶ 25, 26 (1996) (adopting rules creating a rebuttable presumption of unreasonableness for local ordinances that hinder DBS deployment); *Amendments of Part 69 of the Commission's Rules Relating to the Creation of Access Charge Subelements for Open Network Architecture Policy and Rules Concerning Rates for Dominant Carriers*, 7 FCC Rcd 5235, ¶ 11 (1992) ("[W]e will consider non-uniform overhead loadings presumptively reasonable whenever a LEC uses them to justify the introduction of a new service at a level below the imputed 'old' price of the service from which the new service is attracting customers").

that amount to an "unreasonabl[e] refus[al] to award an additional competitive franchise." 47 U.S.C. § 541(a)(1).

The Commission's authority in this regard is not diminished by the judicial review provision included in Section 621(a)(1), which provides one method by which an applicant can challenge an LFA's actions. It states that an applicant "whose application for a second franchise has been *denied* by a final decision of the franchising authority may appeal such final decision pursuant to the provisions of section 635 for failure to comply with this subsection." 47 U.S.C. § 541(a)(1)(emphasis added). This provision does not deprive the Commission of authority to interpret the provisions of the Cable Act, including Section 621(a). To the contrary, any interpretive rules adopted by the Commission would have the salutary effects of creating *ex ante* standards to guide LFAs as they review applications for franchises and of providing objective benchmarks by which courts can judge the reasonableness of an LFA's actions.

Moreover, action by the Commission is necessary in this case because, absent further Commission guidance, the judicial review provision alone is not likely fully to protect the interests animating Section 621(a) to the extent it is construed in some cases to limit an applicant's recourse until the LFA issues a "final decision" on a franchise application. Of course, at some point an LFAs refusal to act presumably would rise to the level of a constructive denial warranting district court action. But Congress clearly recognized that delay short of a denial or constructive denial would inhibit competition. On its face, therefore, Section 621(a) was intended to reach further, as illustrated by Congress' careful choice of words prohibiting the "unreasonabl[e] refus[al] to award" a competitive franchise, rather than just the unreasonable denial of a franchise application. This choice of language reveals a concern with LFA actions, short of an outright denial or constructive denial, that have the effect of imposing unreasonable delays that act as barriers to entry to competitive video providers.

The Commission previously recognized this gap between the protections of Section 621(a) and the jurisdiction of the courts, noting the concern that "the provision of Section 621 that allows an appeal only from a *final* decision of denial by a franchising authority potentially could be used by a franchising authority to delay or preclude a potential entrant from availing itself of the remedies in the Act," thus potentially "frustrat[ing] . . . the purpose of Section 621." *First Video Competition Report*, ¶ 56 n.127. The Commission committed at that time to "monitor whether undue delays in granting final determinations on overbuild franchise applications interfere with the effectiveness of Section 621." *Id.* ¶ 250. Therefore, the Commission recognized early on that delay and other actions short of a denial could frustrate the purpose of the "refusal to award" prohibition, and that judicial review might be an inadequate mechanism to address such concerns.

#### 4. A Telephone Company That Provides Video Services Limited to Interactive, On-Demand Programming Is Not Required to Obtain Video Franchise.

The Commission asked in the Notice of Inquiry whether telephone companies who develop an exclusively IP-based, on-demand video service are subject to local franchising requirements. *Video Competition NOI*, FCC 05-155, ¶ 56 (rel. Aug. 12, 2005). Although the fact that a service is or is not IP-based has little bearing on that question under the terms of the statute, the nature of the service offering does have a direct bearing.

The statute is very clear that "the term 'cable system' . . . does not include . . . a facility of a common carrier which is subject, in whole or in part, to the provisions of title II of this Act, except that such facility shall be considered a cable system (other than for the purposes of section

621(c)) to the extent such facility is used in the transmission of video programming directly to subscribers, *unless the extent of such use is solely to provide interactive on-demand services*." 47 U.S.C. § 522(7) (emphasis added). In other words, if a common carrier's facilities are used to transmit video programming that is limited to "interactive on-demand services," those facilities are not considered a "cable system." "Interactive on-demand services," in turn, are defined as video programming provided "over a switched network[] on an on-demand, point-to-point basis," but do not include programming that is "prescheduled by the programming provider." 47 U.S.C. § 522(12). That means that a common carrier whose video services are limited to interactive on-demand and that do not include pre-scheduled programming is not considered a "cable operator," – and is not subject to the franchise requirement – because that term only applies to a provider of "cable services *over a cable system*." *Id.* § 522(5) (emphasis added); *see* 47 U.S.C. § 541(b)(1) ("a cable operator may not provide cable service without a franchise").

Likewise, only "cable services" are subject to the franchise requirement and the payment of franchise fees, but such services are defined to include *only* the "one-way transmission" of video programming (and any subscriber interaction needed to select or use that one-way programming). 47 U.S.C. § 522(6). So under that definition as well, any services that are two-way or that that qualify as interactive on-demand services are not subject to a franchise requirement or to the payment of franchise fees under existing law.

### B. <u>Effective Program Access Regulation Is Essential to Competitive Entry.</u>

In addition to obtaining franchises, new entrants need access to programming content on fair and reasonable terms. The Commission has previously recognized that programming is a "vital input" for a video services provider, and that incumbents can "erect a potential entry barrier that impedes or deters competitive entry" by foreclosing a new competitor's access to desirable programming. *First Video Competition Report*, App. H ¶ 43. "This foreclosure can occur either through the bargaining power of a large incumbent (an MSO for example), or by the downstream firm vertically integrating into the programming market and refusing to sell its programming to actual or potential rivals." *Id.* In order to minimize this potential barrier to entry, the Commission should consider revising the program access regulations to close the "terrestrial loophole," which allows large cable operators to shield certain must-have programming – most especially regional sports programming – from the program access rules. The Commission should also strictly enforce the current program access regulations to prevent other anticompetitive practices that harm new entrants into the video market.

**1. The Terrestrial Loophole Must Be Closed.**

Incumbent cable companies have long enjoyed close corporate ties to producers of video programming. Thanks to this vertical integration, programmers affiliated with cable companies either refused to sell their programming to competing distributors like satellite carriers and cable overbuilders or sold it on discriminatory terms calculated to suppress competition. To put a stop to these discriminatory practices, the 1992 Cable Act contained program access rules that prohibit exclusive contracts between cable companies and affiliated programmers, absent express FCC approval. These rules require that any cable network programming that is at least in part owned by a cable operator and delivered by satellite must be made available to competitors.[20]

Under the terms of the Act, the FCC was required to determine in 2002 whether those rules should continue to apply, and it concluded that they should.[21] The FCC found that

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[20] *See* 47 U.S.C. § 548(c)(2); 47 C.F.R. § 76.1002(c).

[21] *See Implementation of the Cable Television Consumer Protection and Competition Act of 1992*, 17 FCC Rcd 12124, ¶ 80 (2002).

"marketplace evidence . . . tends to confirm that, where permitted, vertically integrated programmers will use foreclosure of programming to provide a competitive edge to their affiliated cable operators. The evidence suggests that the ability to foreclose vertically integrated programming is especially significant in the regional programming market, which may not be covered by the rules if the programming is distributed terrestrially."[22] Nevertheless, although the Commission noted that "terrestrial distribution of programming could have a substantial impact on the ability of competitive MVPDs to compete in the MVPD market," the Commission in 2002 declined to extend the program access rules to cover terrestrially distributed programming.[23] This loophole remains an issue today, as the Commission's most recent annual report on video competition makes clear.[24]

Without access to much terrestrially delivered programming – especially "must have" items like regional sports and news programming – new entrants are at a serious disadvantage when competing against incumbent cable companies. For example, in some areas (*e.g.*, Philadelphia), the local incumbent owns a regional sports network that controls the rights to the majority of the professional sports teams in the market. If, through use of the terrestrial loophole, the incumbent is permitted to deprive competitors of reasonable access to this highly desirable and unique programming, then a large percentage of consumers simply will not consider switching to the competitor.

Certainly, access to such programming is one key factor that competitive video providers must consider when planning where to deploy their networks. In order to promote more

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[22] *Id.* at ¶ 59 (footnote omitted).

[23] *Id.* at ¶ 73.

[24] *Annual Assessment of the Status of Competition in the Market for the Delivery of Video Programming*, 20 FCC Rcd 2755, ¶¶ 155, 156 (2005).

competitive video offerings, the Commission should extend the program access rules so as to close the loophole for terrestrially delivered programming. Although Congress focused on whether programming was delivered by satellite in some portions of Section 628, technological changes since 1992 (including the proliferation of dark fiber) have made terrestrial delivery an easy alternative for the delivery of video programming and an appealing option for a cable operator who seeks to shield must-have programming from the program access rules. These changes create the real possibility for the exception built into the current Commission rule – the exemption of terrestrially delivered programming from program access requirements – to swallow the rule – the sharing on fair and non-discriminatory terms of all other content produced by vertically integrated programmers. Therefore, Congress' goal of "promot[ing] the public interest, convenience, and necessity by increasing competition and diversity in the multichannel video programming market," 47 U.S.C. § 548(a), will be frustrated unless the Commission takes steps to address the new problems that have developed since the time that Congress passed Section 628 by closing the terrestrial loophole.

The Commission possesses sufficient authority to enact such rules that are necessary to promote and protect the purposes of the Act, and should promptly move forward to do so. *See Southwestern Cable Co.*, 392 U.S. 157, 178 (1968) (noting FCC authority to take steps that are "reasonably ancillary to the effective performance of the Commission's various responsibilities" and that further the purposes of the Act). Just as the Commission determined, long before the passage of the Cable Act or the creation of Title VI, that regulation of cable providers was necessary in order to effectuate the broadcasting provisions of the Act, *see id.*, so too here. Unless the Commission acts now to close the terrestrial loophole, Section 628 could become a dead letter and the protections intended by Congress in that provision could become largely meaningless. Accordingly, closing the terrestrial loophole in order to effectuate the provisions of section 628 is within the scope of the Commission's authority. If the Commission nonetheless disagrees and decides that it cannot do that, however, then, at the very least, it should encourage Congress to do so.

#### 2. Carriage Terms that Have a Discriminatory Impact on Competitive Video Services Providers Should Not Be Permitted.

Not only is it essential for a new entrant in the video services market to have access to desirable programming, it is also important that content owners who are affiliated with the cable incumbents provide that programming to competitors on fair terms and conditions. Section 628 seeks to accomplish this by prohibiting "unfair methods of competition or unfair or deceptive acts or practices, the purpose *or effect* of which is to hinder" competitive providers' ability to compete. 47 U.S.C. § 548(b) (emphasis added). In particular, this rule "prohibit[s] discrimination by a satellite cable programming vendor in which a cable operator has an attributable interest or by a satellite broadcast programming vendor in the prices, terms, and conditions of sale or delivery of satellite cable programming or satellite broadcast programming among or between cable systems, cable operators, or other multichannel video programming distributors." 47 U.S.C. § 548(c)(2)(B). The Commission should rigorously enforce this anti-discrimination provision in order to ensure that vertically integrated cable operators and content owners do not, as a practical matter, foreclose a competitor's access to content.

A good example illustrating Verizon's concern is the pricing structure being used by iN DEMAND – a programming vendor specializing in HD content that is affiliated with several incumbent cable operators. As DirecTV and Echostar explain in their recent program access complaints, iN DEMAND previously charged providers based on the number of subscribers actually receiving the HD content that it provides – as is standard in the industry. In an apparent attempt to make it uneconomical for satellite providers and others with advanced, digital systems to obtain its HD programming, however, iN DEMAND instituted a pricing scheme that instead charges the provider based on its total number of *digital* subscribers, and not just the percentage of those subscribers actually capable of receiving the HD content that iN DEMAND sells. Although this scheme may at first appear facially neutral, it has a large discriminatory impact against satellite providers – whose customers are 100% digital – as well as other video providers like Verizon who make digital content available to all subscribers. The practical impact is to charge such digital providers many times more per HD customer than is being charged the affiliated, incumbent cable operators, who have comparatively few digital subscribers. As a result, after reaching an impasse with iN DEMAND over precisely this issue, Verizon eventually was forced to give up negotiating with iN DEMAND and sought HD content elsewhere.

This example illustrates clearly the types of efforts taken by some incumbents and their affiliated programming partners to block their competitors' access to desirable content. The Commission should recognize that, despite the facial neutrality of such a pricing scheme, the discriminatory effect (particularly in light of the ample evidence of discriminatory intent) of such practices violates Section 628. As Section 628(b) expressly indicates, these rules are intended to reach actions that result in such an "effect." 47 U.S.C. § 548(b). This example further illustrates the necessity for the Commission to closely monitor the activities of the large incumbent cable operators to prevent similar efforts to shirk their statutory obligations in order to delay or foreclose meaningful competition.

### 3. The Commission Should Scrutinize Exclusive Content Agreements by Incumbent Cable Operators.

Finally, the Commission should take steps to ensure that any exclusive content agreements entered into by incumbent cable operators comply with Sections 616 and 628, given the potential anticompetitive effect of such agreements. As the Commission has previously recognized, incumbent cable operators can effectively foreclose a new entrant's access to necessary programming either through their market power or through control over affiliated programmers. *First Video Competition Report*, App. H ¶ 43. Congress tried to prevent such anticompetitive conduct in two ways. First, Section 628 generally prohibits exclusive arrangements between a cable operator and an affiliated programmer. 47 U.S.C. § 548(c)(2)(C). Second, Section 616 prohibits a cable operator from taking advantage of its position in the market to unduly influence independent content owners, such as by demanding an exclusive arrangement or coercing the programmer to discriminate against a competing video services provider. 47 U.S.C. § 536.

Given the potential impact on a new entrant if it is unable to obtain desirable programming, the Commission should take steps to ensure that cable companies are not able to effectively foreclose access to programming by new entrants through arrangements that give an incumbent an exclusive right to carry particular programming. For example, the Commission should consider imposing reporting requirements on incumbent cable operators to ensure that their programming arrangements comply with Sections 616 and 628, and are not otherwise creating barriers to entry for new competitors. And if they are, the Commission should take steps to prevent the use of exclusive arrangements as a way to deny access to entrants.

### C. Competitive Video Providers Need Access to MDU Subscribers.

Another concern for Verizon and other new entrants into the video market is obtaining reasonable access to the residents of multi-dwelling units ("MDU"). As discussed above, consumers of video programming currently face a very limited array of choices in video services providers. For the large number of Americans who reside in MDUs, the range of choices is frequently even more constrained – often to the incumbent cable operator who serves the building. For many of these consumers, satellite providers are not currently an option, either because of physical inability or lack of permission to install a receiving dish. And even in those few communities where wireline competition exists, choice is often limited for MDU customers in light of exclusive access arrangements between MDU owners and cable companies or because of MDU owners' unwillingness to allow competitors to take the steps necessary to run wiring to those residents who desire service. The Commission should ensure that video competition not be available only for those who own their own houses, but instead that the millions of Americans who live in MDUs receive the benefits of video competition.

#### 1. No Exclusive Access Contracts Should Be Permitted.

The Commission has previously addressed the permissibility of exclusive and perpetual contracts between video providers and MDU owners, and, while recognizing the anticompetitive potential of such arrangements, concluded that the record at the time included insufficient evidence to support a prohibition on such arrangements.[25] Therefore, cable incumbents are currently permitted to reach agreements with MDU owners that would lock-in all of the residents of an MDU completely and forever, foreclosing any possibility of competitive entry. The Commission should reconsider this ill-advised policy and recognize that exclusive access arrangements – particularly those that are permitted to remain in effect perpetually – are anticompetitive. At the same time, the Commission should recognize that, in contrast, exclusive marketing arrangements further competition and benefit consumers.

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[25] *Telecommunications Services Inside Wiring; Customer Premises Equipment; Implementation of the Cable Television Consumer Protection and Competition Act of 1992*, 18 FCC Rcd 1342, ¶¶ 71, 77 (2003) ("*Cable Wiring Order*").

The Commission has previously recognized the anticompetitive potential of exclusive access agreements, concluding for telecommunications services that such arrangements were impermissible in the context of commercial MDUs.[26] In that proceeding, the Commission concluded that exclusive access contracts were an anticompetitive vertical restraint that "pose[] a risk of limiting the choices of tenants in [MDUs] in purchasing telecommunications services, and of increasing the prices paid by tenants." *Id.* ¶¶ 27, 28. Moreover, for an incumbent, "an exclusive [access] contract may essentially constitute a device to preserve existing market power." *Id.* ¶ 29.

Verizon has consistently argued – both in the context of video and telecommunications services – that exclusive access arrangements are anticompetitive and should not be permitted. Exclusive access arrangements reduce or eliminate tenants' ability to obtain services offered by their choice of service providers. MDU owners and incumbent cable companies should not be permitted to deprive MDU residents of the benefits of competition, whether for telecommunications or for video. And this is especially true if such exclusive access arrangements are permitted to extend forever – thereby taking away any argument that exclusivity is necessary in order to recover the provider's cost of installation. Instead, such deals create safe havens for monopolists, at the expense of MDU residents.

By contrast, exclusive or preferential marketing arrangements differ both conceptually and from a policy perspective from exclusive access arrangements, because they do not restrict the consumer's available choice of providers. Instead, exclusive marketing arrangements

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[26] *Promotion of Competitive Networks in Local Telecommunications Markets*, 15 FCC Rcd 22983, ¶ 27 (2000). In that order, the Commission decided that it lacked sufficient record evidence to decide whether exclusive access agreements were permissible in residential MDUs, and issued a further notice on that issue. *Id.* ¶¶ 33, 161.

facilitate the sharing of information with consumers by creating an active role for MDU owners in distributing information about a provider's services. Such information allows subscribers to better understand the available services and select between available providers, but without dictating who the provider will be. As a result, it would harm competition – and violate the First Amendment – to restrict exclusive marketing arrangements between video providers and MDU owners.

In order to both lower the barriers to entry for competitive video service providers, and to extend the benefits of that competition to all consumers, the Commission should revisit its policies on exclusive and perpetual *access* agreements in the MDU context, and should prohibit such arrangements.

### 2. Adequate Access To Inside Wiring

The Commission should also act quickly to address another MDU "access" concern for competitive video service providers. The Commission has implemented rules aimed at ensuring that competitive video providers have reasonable access to the home wiring and home run wiring in MDUs. *See* 47 C.F.R. 76.800-806. These rules are important in facilitating video competition because, as a practical matter, many MDU residents and owners will forego selecting a competitive provider if that selection requires the expense and disruption of running new wiring. In fact, many MDU owners simply will not permit a competitor to serve their residents if that requires the installation of redundant wiring. Therefore, the denial of access to the existing wiring on a reasonable basis will often be an insuperable barrier to entry for a competitive video services provider.

One important, lingering issue remains for the Commission to decide in the application of its MDU home wiring rules. The Commission previously decided that the demarcation point between "home wiring" (*i.e.* the cable wiring within a living unit in an MDU) and "home run wiring" (*i.e.*, the dedicated wiring that the runs from a feeder cable to a particular living unit) in an MDU cannot be located behind sheetrock because such wiring is "physically inaccessible." *Cable Wiring Order* ¶ 52. This sensible conclusion has important implications because incumbent cable companies have less ability to deny a competitor access to "home wiring" than "home run wiring." Also, if a competitor is required to run new home run wiring behind the sheetrock in the halls and ceilings in the common areas of MDUs, many MDU owners will deny access altogether in order to avoid the disruption and damage caused by such activities. Therefore, this issue has important implications for whether a competitor will be able to compete for MDU customers.

On appeal, the D.C. Circuit reversed the Commission's previous order – not because of the correctness or permissibility of the position adopted by the Commission, but instead because of the dearth of supporting evidence in the record. *See National Cable & Tel. Assoc. v. FCC*, No. 03-1140, 2004 U.S. App. LEXIS 8506 (D.C. Cir. Feb. 17, 2004). On remand, however, Verizon and other commenters have provided the Commission with ample factual support for the common sense approach that it previously embraced.[27] The Commission should act quickly to conclude this proceeding in order to help ensure video competition reaches MDU residents.

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[27] *See* Comments of Verizon on Cable Wiring Rules, *Telecommunications Services Inside Wiring; Customer Premises Equipment; Implementation of the Cable Television Consumer Protection and Competition Act of 1992: Cable Home Wiring*, CS Docket No. 95-184, MM Docket No. 92-260 (filed Nov. 15, 2004); Declaration of Daniel J. VanRoekel, attached to Letter from Leora Hochstein, Verizon, to Marlene H. Dortch, FCC, CS Docket No. 95-184, MM Docket No. 92-260 (filed June 22, 2005).

### D. <u>Technical Standards Must Be Adopted That Are Open and Competitively Neutral.</u>

FTTP represents an exciting source of new, facilities-based competition to cable companies, but the technical standards and rules that the Commission has developed or will develop for cable operators have the potential of leaving Verizon and other competitors who do not use traditional cable technology at a disadvantage. For example, the development of technical standards and rules is currently pending before the Commission in the "plug and play" proceeding.[28] In that proceeding and in any others that involve technical standards, the Commission should adopt technology-neutral standards rather than cable-centric ones. Only by doing so can the Commission ensure that FTTP and other modes of video services delivery can emerge and compete with traditional cable technology.

So, for example, it would be inappropriate for the Commission, as it has done in the past, to allow a dominant role in any such proceeding for CableLabs – an entity that lacks independence from the traditional cable television industry by and for whom it was created. Given CableLabs' dedication to serving the needs of the cable industry, it cannot be relied upon to remain neutral and impartial when asked to make determinations on technologies that affect competitors to traditional cable providers.

Indeed, CableLabs previously has pushed independent equipment manufacturers to adopt standards that would focus on the needs of the traditional cable industry, but that would not work for competing technologies. If it were allowed to be the gatekeeper for the approval and deployment of new technological standards, such as plug-and-play technologies, CableLabs'

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[28] *Implementation of Section 304 of the Telecommunications Act of 1996*, CS Docket No. 97-80 & PP Docket No. 00-67.

singular focus on the traditional cable providers' needs would allow it to prevent alternative technologies from being approved, thereby threatening competitors' abilities to provide innovative new products and services.

In fact, the problems associated with CableLabs' standard-setting role already have presented themselves in the context of the development of two-way plug-and-play standards. For example, CableLabs has been instrumental in creating and implementing DOCSIS 2.0, a set of industry standards now being used by cable companies as a blueprint for developing additional coaxial cable facilities. CableLabs has urged the Consumer Electronics Association to adopt the same standard for consumer electronics manufacturers. However, the DOCSIS 2.0 specifications do not address the needs of competing technologies, such as FTTP and digital broadcast satellite. Specifically, DOCSIS 2.0 specifies an upstream path that is not consistent with the IP over Ethernet (IEEE 802.3i) alternative for upstream transmission. Thus, accepting CableLabs' urging would create standards for the development of consumer equipment that would work for traditional cable providers, but not their competitors. By contrast, the International Electrical and Electronic Engineers ("IEEE"), an independent, accredited and open standards setting organization, has developed the IEEE 802.3i standard that takes into account the needs of competing technologies. Verizon's planned video FTTP deployment will be able to interface with equipment manufactured to meet the IEEE 802.3i standard with an RJ-45 interface for upstream transmission, but would not be able to use DOCSIS 2.0-designed technology.[29] Accepting the standards advocated by CableLabs thus would lead to the development of equipment, such as connectors, set-top boxes, and interfaces built into the television sets, that

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[29] The RJ-45 Ethernet connection is an interface that is used by ADSL modems, cable modems conforming to DOCSIS 1.0 and 2.0, and FTTP optical network terminals.

would require additional costs to connect to FTTP or digital broadcast satellite infrastructures. Therefore, when the Commission considers the standards to be adopted for two-way digital television receivers, it should not adopt DOCSIS 2.0 or any other standard that would be centered on technology only used by traditional cable providers.[30]

Likewise, other neutral, standards-setting bodies are developing open, competitively neutral standards to govern a variety of other technical issues. For example, the Alliance for Telecommunications Industry Solutions ("ATIS") is currently exploring technical standards for IPTV. As part of that process, ATIS – which includes cable companies such as Comcast and Cox as members – has invited wide industry participation and actively seeks to achieve open standards and solutions that acknowledge the needs of the entire industry. Similarly, the Multimedia over Coax Alliance ("MOCA") – an industry alliance body – is actively developing specifications for transport of digital content over home networks. The existence of these neutral, standard-setting bodies and industry alliance initiatives obviates the need for the Commission to rely on CableLabs, or any other association that represents only one segment of the market's competitors, when it sets technical standards for video services providers. Therefore, in any proceedings where technical standards are at issue, the Commission should adopt open standards that accommodate both traditional cable technology and other, competing technologies.

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[30] The Commission is first working on establishing the plug and play frame work for one-way digital television receivers, and will only turn to developing a two-way standard in the second phase of this proceeding. *See* Statement of Commissioner Abernathy, *Section 257 Triennial Report to Congress; Identifying and Eliminating Market Entry Barriers for Entrepreneurs and Other Small Businesses*, 19 FCC Rcd 3034 (2004). When the Commission develops that two-way standard, it should adopt the IEEE 802.3i framework, or another one that will work with all competing technologies, rather than DOCSIS 2.0.

## E. <u>Redundant and Unnecessary Cable Regulation Should Be Removed for Competitive Cable Providers.</u>

The Commission should also consider amending some of its cable regulations in order to facilitate competitive entry into the video services market. Several regulations, in their current form, unnecessarily burden video services providers and inhibit video competition. Some regulations – such as the cable EEO regulations – pose logistical challenges for a provider like Verizon who is subject to similar regulations by virtue of being a common carrier for telecommunications services. Harmonization of overlapping or redundant regulations is necessary in order to take into account the convergence of telecommunications and video services. Other regulations, like customer service standards, are unnecessary in markets where competition exists, and should, at the very least, be standardized nationwide in markets where they continue to be required. Finally, other regulations, such as the public inspection file requirements, should be modified in order to lower the cost of compliance, while fulfilling the purposes of such regulations. By taking these steps, the Commission can further encourage video competition while doing justice to the concerns that animate these regulations.

### 1. Cable EEO Regulations Should Be Harmonized with Common Carrier EEO Rules.

Verizon fully supports the goals of EEO regulation, and is actively involved in ensuring diversity throughout its workforce. By virtue of being a common carrier for telecommunications services and a federal contractor, Verizon already complies with a variety of pervasive EEO regulations that apply to its employees. After it begins selling video services, Verizon will also be subject to the cable EEO regulations. *See* 47 U.S.C. § 554; 47 C.F.R. §§ 76.71-79. While Verizon in no way seeks to avoid any of these EEO obligations, the Commission could make compliance more efficient and affordable – yet equally effective – if it were to harmonize the common carrier and cable EEO regulations.

This type of harmonization is necessary given the practical, logistical difficulties in complying with two (or more) sets of redundant, yet different, regulations. Verizon's FTTP network exemplifies the converged, broadband network of the future. Voice, data, and video services will be provided over this network, and Verizon does not intend to draw artificial lines separating these applications or the employees who work on them. In most cases, the same employees who work on video issues will also work on telecommunications and data services. Therefore, it makes no sense to force employees into the old regulatory silos simply for purposes of EEO compliance, and in fact doing so may result in EEO reporting that is less meaningful. In order to alleviate this type of difficult and unnecessary line-drawing, the Commission should explore ways of facilitating EEO compliance for providers of video services over converged networks. For example, the Commission should consider allowing a provider's compliance with Title II EEO requirements to satisfy the separate Title VI EEO rules – at least for those employees who would otherwise be subject to both sets of rules.

#### 2. Performance Standards

The Commission can also advance competition in the delivery of video programming by encouraging marketplace solutions to customer service needs, rather than relying on a patchwork of varying local regulations. In a competitive environment, when consumers have choice, customer satisfaction will be the basis by which video service providers attract and retain customers. The Commission itself has cited with approval reports from the General Accounting

Office indicating that increased competition "generally leads to lower cable rates *and improved quality and service* from the incumbent cable operator."[31]

Ironically, by *imposing* excessively demanding customer service standards on new entrants, the Commission and LFAs may *impede* the deployment of competitive video offerings. In the one-cable-company world, it is understandable that local authorities are eager to beef up their customer service standards, particularly where incumbent cable operators have a less than stellar customer service record. But the proliferation of idiosyncratic requirements across different localities creates a very expensive problem for companies attempting to build and operate a network that stretches across the country. Because it is by far more efficient to operate uniform systems, procedures, and technology throughout the network, each LFA's peculiar customer service items must, as a practical matter, be implemented on a national scale, so that common systems, procedures, and technologies can be maintained on the network nationwide.

Instead of each locality developing its own customer service wish list, the Commission should encourage the elimination of customer service obligations to both *enable* a competitive market for video services and to enable that competitive market to find marketplace solutions to customer service. At the very least, the Commission should encourage localities to follow national customer service standards. The Commission's customer service standards set out in 47 C.F.R. § 76.309 – with some minor modifications to account for some differences between traditional cable companies and video providers who use different technical or network approaches – could serve that function. Such standards are readily available and could be made

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[31] *Annual Assessment of the Status of Competition in the Market for the Delivery of Video Programming*, 19 FCC Rcd 10909, ¶ 9 n.7 (2004) (emphasis added) (*citing* U.S. General Accounting Office, *Issues Related to Competition and Subscriber Rates in the Cable Television Industry* at 9-11, GAO-04-8 (Oct. 2003)).

suitable for nationwide application. This approach would be more efficient for both LFAs and companies that provide video services than requiring compliance with a mish-mash of potentially contradictory requirements.

### 3. Public Inspection File

Finally, the Commission should consider revising its public inspection file rules. These rules require that a variety of information concerning a provider's video operations in individual markets be maintained and made available for public inspection at the local level. *See* 47 C.F.R. § 76.1700, et seq. The expense and logistical difficulty of compliance with these regulations creates an obstacle to entry into the video market – particularly for a provider like Verizon that seeks to compete on a regional or national basis. The Commission should consider whether the public benefit of these rules justifies the expense and effort that they require. Furthermore, the Commission should consider whether alternative mechanisms (*i.e.*, providing information to the public only upon request, maintaining information at one state-wide or company-wide location, etc.) could protect the public interest in a more efficient manner.

## CONCLUSION

Although Congress and the Commission have long expressed an interest in encouraging competition in the video services market, many of the regulations that apply to this market have the opposite effect. The Commission, Congress, and state and local authorities should not delay in removing these barriers to entry and embracing video competition.

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## THE VERIZON TELEPHONE COMPANIES

The Verizon telephone companies are the local exchange carriers affiliated with Verizon Communications Inc. These are:

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The Micronesian Telecommunications Corporation
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Verizon Maryland Inc.
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