BACKGROUND INFORMATION ON MUNICIPAL PUBLIC RIGHTS-OF-WAY FEES SET BY STATUTE: KEY LEGISLATION FROM 1999, 2005 AND 2011.

August 13, 2012

Submitted by:
The Texas Municipal League ("TML"), and
The Texas Coalition of Cities for Utility Issues ("TCCFUI)

To the Honorable Committee Chair and Members:

The Texas Municipal League is a statewide organization representing most municipalities in the State. Texas Coalition of Cities for Utility Issues is an organization of over 100 cities that has been active for well over a decade concerning the use of public property by utilities. TML and TCCFUI submit this background information to assist the Committee in any review of these issues in their historic and legal context.

1.) LEGAL BASIS FOR MUNICIPAL RIGHTS-OF-WAY COMPENSATION;

2.) TELECOMMUNICATION SERVICES ACCESS LINE FEES PAID PURSUANT TO CHAPTER 283, TEX. LOC. GOV. CODE AND;

3.) CABLE TELEVISION SERVICES FRANCHISE FEES PAID PURSUANT TO CHAPTER 66, TEX. UTIL. CODE.

Thank you very much for allowing TML and TCCFUI to make this submission.

For any addition information, please contact:

Snapper Carr, General Counsel, Focused Advocacy, LLC, 512-917-0044.
snapper@focusedadvocacy.com

Clarence A. West, Attorney, 512-573-9537.
cawest@cawestlaw.com

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> No man has the right to use a street for the prosecution of his private business….. Not having the absolute right to use streets for the prosecution of private business…... This is a self-evident proposition, for, if it were not so, sidewalks and streets could be rendered impassable by those vending their wares or soliciting patronage.
> *Green v. City of San Antonio,* 178 S.W. 6 (Tex.Civ.App.-San Antonio 1915, writ denied).

1. LEGAL BASIS FOR MUNICIPAL PUBLIC RIGHTS-OF-WAY FEES AND COURTS AFFIRMING THEY ARE RENT.

Q: Are cities required to receive market-based payments for use of public rights-of-ways?

A: The Texas constitution prohibits the "gift" of public property. Neither the State nor municipalities may give, or allow, public property to be used by private entities for less than market value by, as that is a prohibited "gift" of public property under the Texas constitution.[1]

If the public rights-of-ways are used by a private entities without payment of a value-based rental fee that would be a prohibited gift of public property, in violation of the Texas Constitution. This is no different than when the State of Texas rents its land out to receive oil royalties, or where the state capitol rents space in the Capitol for its cafeteria and receives rent from that cafeteria.

Q: Are rights-of-way fees "rental" payments or "taxes"?

A: Both state and federal courts have repeatedly held such payments are rent and not taxes. The U.S. Supreme Court in 1893, the Texas Supreme Court in 1940, and the Federal Fifth Circuit Court of Appeals again in 1997 have all considered the issue, and all have determined that rights-of-way user fees are "rental" payments, not "taxes".[2]

Q: Has the attorney general ever considered the issue concerning whether franchise fees are "taxes" for purposes of tax exemptions for governmental entities?

A: The Texas attorney general has considered this issue several times and issued opinions that have all determined rights-of-way fees are rental fees and are not taxes.[3]

2. ACCESS LINE FEES PAID BY TELECOMMUNICATION PROVIDERS PER CHAPTER 283, TEX. LOC. GOV'T CODE.

In 1999 the Texas legislature adopted House Bill 1777 ("HB 1777") concerning rights-of-way fees paid by telecommunication providers, codified as Chapter 283 of the Local Government Code. HB 1777 was crafted to apply a new municipal right-of-way compensation methodology equally to Incumbent Local Exchange Carriers ("ILECs") and Competitive Local Exchange Carriers ("CLECs") and to precipitate settlements of pending lawsuits between cities and telecom providers concerning "gross revenue" compensation under city franchises. Chapter 283 replaced the almost century-old percentage of gross revenue rights-of-way compensation system by a transition to a "fee-per-access line" methodology where access line fees were proxies for the former percent of gross revenue franchise fee.[4] There are three categories of access lines: residential voice (category 1), business voice (category 2), and high capacity data lines (category 3). In 2005 (SB 5) an amendment added all "voice service" providers via wireline in the rights-of-way, "without regard to the delivery technology, including Internet protocol technology."[5]

Q: Were wireline "over-the-top" VoIP providers included in the 2005 SB 5 amendment adding all wireline "voice service" providers regardless of the technology employed?

A: In 2006 the Public Utility Commission of Texas (PUC) agreed that wireline "over-the-top" VoIP providers, like Vonage, were included in 2005 SB 5 amendment adding all wireline "voice service" providers but declined to include them principally due to their relative scarcity at the time, and technical problems in tracking them for compliance.[6]

Q: Are all "over-the-top" VoIP providers paying access line fees?

A: Currently "over-the-top" VoIP providers are exempted by PUC rules. In May 2010 the PUC Staff recommend "over-the-top" VoIP providers pay access line fees, as they delivered voice services through wireline facilities in the rights-of-ways. To date the PUC has declined to adopt that recommendation.[7] This "exemption" effectively results in a PUC rule that is not competitive neutrality and discriminatory in the application of Tex. Local Gov't Code, Chapter 283.

Q: Are high capacity data line providers paying their fair share at one tenth of 1% on a high capacity data line tariff rates?

A: High capacity lines are being used more frequently to provide voice services in call centers. This "trend" toward using high capacity data lines started a number of years ago.[8] Access line fees are frequently less than 1% of the customer service charges on these high capacity data lines, a disproportionate low access line fee payment relative to the cost of the service, i.e. a high capacity data

line may pay an access line fee of $30 or 0.1% on a customer service charge of $30,000 per month on a high capacity data line, based on a category 3 private line access line rate of $15.00 per termination point per month.[9]

Q: Have telecommunication access line fees increased or decreased since implementation of access line fees in 2000?

A: Telecommunication access line fees paid pursuant to Chapter 283 have decreased approximately 20% since its implementation in June 2000.[10] The decrease may be attributable to a number of factors, including market trends of significant migration from landlines to wireless, an expanded use of high capacity lines, and increasingly due to new wireline voice service technologies, such as "over-the-top" VoIP providers, like Vonage, not paying access line fees.

Q: Can cities increase access line fee rates?

A: Cities may not change access line fee rates. The only change in the access line fee rates are PUC inflation adjustments. The PUC makes an annual ½ the inflation rate adjustment to access line rates. Therefore, while overall access line fee payments have decreased by approximately 20% in the last decade, access line rates have declined by one-half of the inflation rate in the last decade.[11]

Q: Does the PUC currently have statutory authority to redefine access lines to address changes in the telecommunications market and technological changes?

A: Chapter 283 allows the PUC to "redefine" access line and the categories of access lines "as necessary to ensure competitive neutrality and nondiscriminatory application and to maintain consistent levels of compensation, as annually increased by growth in access lines and consumer price index, as applicable, to the municipalities."[12] Access line rates also do not increase when there is a redefinition of an access line. A redefinition may only add formerly excluded provider or service, i.e., digital packet switched voice services were added by the PUC in 2003.[13] The last redefinition of an access line was in 2010.[14]

Q: Does Chapter 283 provide a remedy to telecommunication providers for a city access line rate allocation that is unreasonable, not competitively neutral, or discriminatory?

A: A city may not change its overall amount received, but a city may allocate of its total amount among the three categories of access lines, each having a different rate for each category. Any city allocation may be challenged by a telecommunication provider and not implemented if *"the commission*

determines that the allocation is not just and reasonable, is not competitively neutral, or is discriminatory."[15]

3. CABLE FRANCHISE FEES, PAID PER CHAPTER 66, TEX. UTIL. CODE.

In 2005 the state adopted SB5, Chapter 66, Tex. Util. Code, allowing cable franchises to be granted by the State through the PUC instead of municipalities. Cable franchise fees paid under Chapter 66 cannot and do not exceed the cable franchise fees paid under large city negotiated cable franchises.

Q: Why is the state issued cable franchise fee 5%?

A: The 5% cable franchise fee was established in the 1984 Federal Cable Act.[16] Since 1984 in negotiated cable franchises, including most of the larger cities, the standard fee has been a 5% franchise fee. In 2005, to be consistent with federal law and to maintain revenue neutrality with the 5% franchise fee in large cities, that same 5% franchise fee was used in SB 5 to allow cities to stay "whole" at 5%, i.e. a 5% franchise fee under a local franchise was continued after it expired at the same 5% rate under the state law franchise. No more, no less. While there are some smaller cities in Texas which may have less than a 5% fee in an unexpired franchise, after the local franchise expires the franchise fees will go to 5% under Chapter 66.

Q: Why is there a separate fee paid to fund the public, educational, and governmental access channels (PEG)? And why was 1% used in the state law, Chapter 66, as the amount of the PEG Fee?

A: Federal law, since at least 1984, has explicitly authorized cities to charge a separate amount to fund PEG access channels. PEG access channels are the ones that provide live viewing of council meetings, local school district programs on the educational channel, emergency programming with information on shelters in the event of a hurricane or tornado and other programming provided by the city.

Many legislative members may be familiar with the PEG programming provided the Texas legislature during the session on the City of Austin's PEG access channels. Austin's PEG provides live video streaming of the House Chamber, the Senate Chamber, and selected Committee Meetings during the session on Austin PEG channels that may be watched live on a full screen television.

The 1% PEG Fee was selected in Chapter 66, as that was a range which was agreed to by the stakeholders negotiating on SB 5. While some cities had a higher fee (at least one city had a $1 per

subscriber fee) and some had no PEG fee, nationally PEG fees were up to at least 3%. To maintain equity and to continue the funding for PEG access channels, the 1% PEG fee was used.[17]

Q: What is the status of the Texas Cable Asso. and Time Warner litigation concerning SB 5?

A: SB 5 has been the subject of subsequent legislative hearings and extensive litigation brought by cable providers. That litigation has recently concluded. In Jan. 2012, an appellate court found the legislative transition tool of grandfathering the locally negotiated franchises a violation of the 1st amendment, and in May 2012, there was a final Order striking those legislative grandfathering provisions.

Originally existing franchised incumbent cable service providers (the provider with the largest number of subscribers in the city) were grandfathered until their local franchise expired, when they could apply for a PUC-issued franchise. Chapter 66 was amended in 2011 by SB 1087 to allow unilateral termination by cable providers of all unexpired cable franchises in Texas cities of less than 215,000, leaving only four local franchises grandfathered until they expire, absent a negotiated early termination.[18] In January 2012 the local franchise grandfathering provisions, including those from 2011 (SB 1087), were ruled unconstitutional on 1st Amendment grounds, so now all cable incumbents can unilaterally, and immediately terminate local franchises, and apply for a PUC issued franchise at the PUC.[19]

Q: Do Internet broadband service providers pay a separate local rights-of-way fee?

A: No, There is no charge to use the rights-of-way to provide broadband services.

There are no separate charges for use of the public rights-of-way in providing wireline broadband services. The PUC determined over ten years ago that broadband over telephone lines, e.g., DSL, is not an "access line" for purposes of access line fees under Chapter 283, therefore "access line" fee rights-of-way charges do not apply to DSL/broadband service.[20]

Similarly, cable service providers have not paid any cable service franchise fee on cable modem service revenue since 2002, when the FCC declared that "cable modem service" was not a "cable service," but rather an interstate "information service".[21] In addition, since 2005 municipal broadband over power lines ("BPL") rights-of-way charges may not exceed what a city charges other broadband providers, such as DSL and cable modem service providers.[22] Because neither DSL broadband service providers nor cable modem broadband service providers pay a rights-of-way fee in Texas, there can be no local municipal fee on BPL providers in Texas.[23]

[1] 1876 Texas Constitution, Article III, Section 52 (a) and Article. XI, Sec. 3, prohibits governmental entities, such as cities, from the granting for less than market value the use of public property to any individual or corporation for private profit. *State v. City of Austin*, 160 Tex. 348, 355; 331 S.W.2d 737, 742 (1960) "a gift or loan of the credit of the state ….amounts to a grant of public money in violation of Article III, Section 51. The purpose of this section and of Article XVI, Section 6, of the Constitution is to prevent the application of public funds to private purposes; in other words, to prevent the gratuitous grant of such funds to any individual or corporation whatsoever….."

[2] *Fleming v. Houston Lighting and Power,* 138 S.W. 2d 520, 522-23 (Tex. 1940) Held that a 4% electric franchise fee was a street "rental" fee; *Fleming v. Houston Lighting and Power,* 143 S.W.2d 923, 924 (Tex. 1940) Rehearing held that the 4% fee was not a "tax" but a reasonable street rental fee paid for the use of the streets citing as its authority *St. Louis v. Western Union Telegraph Co.,* 148 U.S. 92, 13 Sup.Ct. 485, 37 L.Ed. 380, (U.S. Sup. Ct. 1893) telegraph company payments to City were "rental" payments not "taxes"; *City of Dallas, Tex. v. F.C.C,* 118 F.3d 393, 398 (5th Cir. 1997) Held that cable franchise fees were rental payments.

[3] Tex. Atty. Gen. Op. H-1265 (1978) (State agencies must pay the municipal charge on telephone bills, as it is a rental payment, there is no "tax" exemption); Tex. Atty Gen. Op. JM-16 (1983) (municipal fee may be passed through to the county as a customer as it is a rental payment; there is no "tax" exemption).

[4] *Rulemaking Relating To Outstanding HB 1777 Implementation Issues, Commission Order Adopting Amendments to § 26.465*, P.U.C. No. 22909, at 22 (September 24, 2001) ("*2001 Commission Order*").

[5] S.B. 5, 79th Legislature, 2nd Called Special Session, Section 28, effective September 1, 2005. ("SB 5") Amended Chapter 283, sec. 283.002 (2) to expand the definition of a CTP to include not only a Commission certificated telecommunication provider, but "*a person that provides voice service*" and added to Tex. Local Gov't Code, Chapter 283, Sec. 283.002 (7), a new definition of "*voice service*" to mean "*voice communications services provided through wireline facilities located at least in part the public right-of-way, without regard to the delivery technology, including Internet protocol technology*." Excluding only commercial mobile voice service providers.

[6] *2006 Commission Order*, at 7-9, 17-19.

[7] May 7, 2010, PUC Project No. 37498, the PUCT staff recommended adding "over-the-top" VoIP providers, that recommendation was not adopted.

[8] P.U.C. 2001, *Report to the Legislature on the Scope of Competition in Telecommunications Markets*, at 28-29, and at 82 (January 2001) ("2001 Report").

[9] A high capacity data line, such as an "OC-48" can provide over 32,000 voice grade lines and can cost $30,000 per month based on SBC Interstate Tariff FCC 773, 2005; cost does not include monthly per-mile transport charges of $300 - $450. Prior to Chapter 283, compensation to cities on these high capacity lines was paid on a percentage of the gross revenue paid to the telecommunication provider on those high capacity lines. The more revenue generated by these services, the more the franchise fees increased. As traditional switched lines migrate to high capacity category 3 private lines, both the number of access lines and the access line fees decrease, the inverse of the percent of gross revenue fee compensation model prior to Chapter 283.

[10] Cities since the enactment of Chapter 283 in 1999 have seen a dramatic decrease in access line fee revenue, *e.g*. Addison – 38.9% [2000 vs. 2008]; Bedford -24% [2000 vs. 2008]; Dallas -15% [2001 vs. 2008]; Houston -18.53% [2001-2009], and this after a decade of population growth, business growth and annexations in those cities. (Only those cities that have had extraordinary population or business growth may have remained close to June 2000 levels.)

[11] Tex. Local Gov't Code, Chapter 283, Sec. 283.055(g).

[12] Tex. Local Gov't Code, Chapter 283, Sec. 283.003 (b), "the commission by rule may modify the definition of 'access line' and the categories of access lines as necessary to ensure competitive neutrality and nondiscriminatory application and to maintain consistent levels of compensation, as annually increased by growth in access lines and consumer price index, as applicable, to the municipalities." This PUC review is required at least once every three years.

[13] *Commission Order Adopting Amendments to § 26.465*, P.U.C. No. 26412 (February 13, 2003) ("*2003 Commission Order"*).

[14] The most recent redefinition project was in PUC Project No. 37498 (Initiated Sept. 2009), in which the PUCT staff recommended adding "over-the-top" VoIP providers, that recommendation was not adopted (May 7, 2010). The last PUC activity was PUC Workshop/Public Hearing on Aug. 13, 2010.

[15] Tex. Local Gov't Code, Chapter 283, Sec. 283.055. (d). *See* P.U.C. Subst. R. 26.467 (i) as to "Resolution of Municipal Allocations".

[16] The Cable Communications Policy Act of 1984, (codified in 47 U.S.C. Sec. 521, et seq.), as amended in 1992 and 1996. Cable television franchises and franchise fees are detailed in 47 U.S.C. Sec. 541 and 542.

[17] Under Chapter 66, Sec. Sec. 66.006 (b) Cities may also elect to continue to have a "per subscriber" PEG Fee if they had one before under their local franchise rather than the 1% fee.

[18] Acts of 2011, 82nd Tex. Leg., R.S., ch.1077, eff. Sept. 1, 2011 (S.B. 1087). Municipal franchises expire in: Irving in 2013, Lubbock in 2014, Dallas in 2015, and Corpus Christi in 2017. While Time Warner testified in support of SB 1087 (Texas Senate Business and Commerce Committee Hearing, SB 1087, March 29, 2011. At: http://www.capitol.state.tx.us/tlodocs/82R/witlistbill/pdf/SB01087S.pdf#navpanes=0) , they challenged some of these very same amendments in the grandfathering in litigation, which recently were struck by the courts, see footnote below.

[19] The Texas Cable Association (TCA) [incumbent cable providers] and Time Warner Cable, brought suit in federal court asserting that Chapter 66 was unlawful on a number in grounds, including the legislative transitioning tool of "grandfathering" unexpired cable franchises as being a First Amendment violation. In 2010 an Austin District Court upheld Chapter 66 in its entirety, including the grandfathering. *TCA and Time Warner v. PUC Commissioners*, *et al*, No. 05-CV-721, (W. Dist. Tex., U.S. Dist. Ct., Austin). (Oct. 29, 2010). However, on appeal that 2010 District Court decision was reversed as to the grandfathering provisions, including provisions of SB 1087 (2011) amendments, based on 1st amendment grounds. *TCTA v. Hudson, et al*, 667 F.3d 630 (5th. Cir. [Jan. 13] 2012). An order was finalized on May 31, 2012 striking the sections of Chapter 66 which grandfathered local franchises.

[20] *Implementation of H.B. 1777*, Project No. 20935, Commission Order Adopting Rule § 26.465, at 33-36 (adopted December 17, 1999; filed December 20, 1999). *See also Commission Order Approving Amendments to P.U.C. Subst. Rule § 26.465*, Project Number 26412, at 15-16 (Approved Feb. 13, 2003).

[21] *Inquiry Concerning High-Speed Access to the Internet Over Cable and Other Facilities, Declaratory Ruling and Notice of Proposed Rulemaking,* 17 F.C.C. Rcd. 4798, 4802-4803 [¶¶ 7, 33-59] (Mar. 15, 2002) ("*2002 Cable Modem Declaratory Ruling*"), *aff'd sub nom. National Cable & Telecomms. Ass'n v. Brand X Internet Servs*., 125 S. Ct. 2688, 2702-10 (2005) ("*Brand X*"). This analysis may have to be revised in light of the FCC's "Third-Way" proceeding to reconsider its characterization of Internet broadband services an "information service" to also have a separate component that is a "telecommunications service". *In the Matter of Framework for Broadband Internet Service*, Notice of Inquiry, GN Docket No. 10-127, FCC 10-114 (June 17, 2010).

[22] Tex. Util. Code, § 43.101 (e). (Acts 2005, 79th Leg., 2nd C.S., ch. 2, Sec. 2, eff. Sept. 7, 2005).

[23] Texas cities have long taken the position they can charge a separate rights-of-way rental charge for use of the rights-of-way to provide broadband services, a position not abandoned. The issue of whether a separate local rights-of-way franchise is required to provide a particular service depends on the extent and purpose of the existing statutory or franchise grants of access. Chapter 283 grants the right to use the rights-of-way to provide "telecommunication services". Chapter 66 grants the right to use the rights-of-way to provide "cable" or "video" services. Neither grants the authority to provide broadband Internet access service using public rights-of-way. To use the rights-of-way in providing a different service may require separate city authority. *See General Tel. Co. v. FCC*, 449 F.2d 846, 855, 860 (5th Cir. 1971) providing cable television services was not incidental to providing telephone services. *See also City of Dallas v. FCC*, 165 F.3d 341, 347 (5th Cir. 1999), holding that an "Open Video System" provider [OVS was created in 1996 in 47 U.S.C. § 573 as an alternative to traditional cable] could be required to have a local franchise.] While several cities have litigated this issue, including a Texas city, those cases have thus far precluded any separate rights-of-way charge for cable modem/broadband services. *City of Chicago v. Comcast Cable Holdings,* L.L.C.900 N.E.2d 262, (Ill. 2008). Chicago's cable franchise contract was preempted by federal law, citing the FCC's *2002 Cable Modem Declaratory Ruling* and 47 U.S. C. § 542, the 5% franchise fee "cap". *Comcast Cable of Plano, Inc., v. City of Plano*, 315 S.W.3d 673 (Tex. 5th App. Dist.-Dallas, 2010). Held that federal preemption barred the franchise fee on cable modem service as a contract claim, but remanded on other claims, e.g. breach of implied contract, quantum meruit, unjust enrichment, and trespass. Those claims were not pursued on remand. No Texas city is currently charging a fee to broadband providers, nor is there any pending litigation in Texas on this matter.