

March 26, 2002

Cable Franchise Fees May Be Decreased Due to FCC Ruling

We are writing to alert you to a recent FCC decision with serious implications for local franchise authorities. On March 14, 2002, the FCC adopted a Declaratory Ruling (No. FCC 02-77) in which it determined that cable modem internet access service is to be classified as an "information service" under the federal Communications Act (rather than a "cable service"). This decision, which was welcomed by the cable industry, could impact local government finances and local regulatory authority significantly.

The FCC's order includes a tentative finding that cable operators should not pay franchise fees on cable modem revenues. Currently, local franchising authorities receive franchise fees of up to 5% of their cable operator's gross revenues. In some areas, the calculation of gross revenues has included revenues from cable modem service, which may represent as much as 20% or more of total gross revenues (and thus franchise fees). Further, cable modem revenues are expected to grow substantially in the future.

The Declaratory Ruling was issued in conjunction with a Notice of Proposed Rulemaking (NPRM) which requests comment on a number of important local government issues raised by the FCC's decision, including:

- The effect of the FCC's classification of cable modem service as an information service upon local regulation of such services, such as customer service standards or "open access" requirements;
- Whether the classification of cable modem service as an information service will require local governments to reimburse cable subscribers for franchise fees paid in the past on cable modem service;
- The effect of the FCC's determination upon local right-of-way (ROW) and franchising issues.

The FCC's action has already been challenged in court, and further challenges are expected. For the most part, cable operators have not yet announced if, how or when they may change their policies with respect to payment of franchise fees (for instance, changes could be delayed until the FCC rulemaking process and the legal challenges are concluded). Although it is not clear at this time how these issues will eventually be resolved, the issues at stake are important local government interests. The FCC has invited comments, and it only stands to reason that the louder the local government voice in the rulemaking process, the better the result may be.

This is only a summary of some of the important issues raised by this FCC action. The full Declaratory Ruling and NPRM is available on the FCC website (www.fcc.gov) in text, .pdf and Word® formats. For more detailed information or to discuss these issues or the comment procedure, please contact us.

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