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**Recommended Citation**


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Telecommunications Update: Keeping Up With the Cable, Telephone, and Wireless Business

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The relationship between your city or town and the various pieces of the telecommunications industry that you deal with should be re-visited periodically to keep up with this fast-changing area and its potential impact on your local government and your citizens. This short briefing does not include everything there is to know on this subject, but it will answer some frequently asked questions, give decision makers new or changed information, keep you current on changes in this area, and highlight what you should watch for when working with these businesses in your city.

OVERVIEW

Even though the recent downturn in the U.S. economy hammered the telecommunications industry—especially those firms whose business plans were dependent on the continued exponential growth of the Internet for their future—there is still a lot of long-range planning for more homes and businesses using high-speed telecommunications (through either a hard-wired or wireless connection) for entertainment, telephony, and e-commerce. Growth in telecommunications has not accelerated at the pace projected as recently as two years ago, but the industry is still growing very quickly compared to most other business sectors. Telecommunications growth in Tennessee, as in the rest of the country, has been substantial. One clear indicator of that expansion is that we’ve grown from two to six Area Codes in less than five years, and another split in Middle Tennessee is anticipated soon.

This growth, and the recent boom-and-bust cycle, has also brought many changes to the companies who provide these services, and to their strategies for doing business. Entire new companies, which didn’t even exist five years ago, are now major players in Tennessee telecommunications. The landscape has changed in the cable TV, wireless, and traditional local and long distance telephone businesses. These changes can affect your citizens, your regulation of these businesses, and the way you operate your city government.
CABLE TELEVISION

The Major Players

In the past, there were up to two dozen different companies operating cable systems in the state. Over time, this number has gradually decreased through consolidation and takeovers, but recently this process has accelerated. While there are still a few “Mom and Pop” cable operations around, the vast majority of cable systems in Tennessee are now controlled by three companies: Time-Warner, Comcast, and Charter.

Time-Warner has always had its Tennessee base of operations in Memphis but has recently consolidated its territory by selling franchises in outlying areas and parts of East Tennessee, and concentrating on cities in and near Shelby County. Time-Warner is part of the AOL-Time-Warner media and Internet conglomerate which owns America On-Line, Time Magazine, CNN, Turner Broadcasting, HBO, and Warner Brothers, among others. Time-Warner Cable is the third largest cable operator in the U.S.

Comcast, which a few years ago bought the former Scripps-Howard franchises in Knoxville, Chattanooga, and surrounding areas, acquired the former InterMedia/AT&T Broadband franchises in the Nashville metropolitan area two years ago. This particular deal was part of AT&T’s acquisition of Media One, another large cable company. With that buy, AT&T would serve more than the Federal Communications Commission (FCC) prescribed limit of 30 percent of all U.S. cable customers, so approval of the deal required the sale of some customers to another company. One of those sales was the transfer of the Nashville area franchises to Comcast. Comcast is a Philadelphia-based, family-owned company and is currently the second largest cable operator in the U.S. Comcast will soon become the largest cable operator in the U.S. by far, pending regulatory approval of their recent proposed acquisition of all of the cable systems of the largest operator, AT&T. While this acquisition would clearly put Comcast over the 30 percent threshold, the new leadership of the FCC has indicated they plan to repeal that Clinton-administration-era rule.

Charter Communications, under the ownership of Paul Allen, co-founder of Microsoft, has expanded aggressively in the past three years through acquisitions. It now has a majority of the franchises in Tennessee outside of the Big 4 metro areas, stretching literally from Martin to Bristol and Mountain City. Charter, headquartered in St. Louis, is now the fourth largest U.S. cable provider.

All three of these companies are very professionally operated and technically capable. They have the financial and personnel resources to upgrade and keep their systems state-of-the-art. However, because they are large national companies, it may be more difficult to negotiate special considerations in services provided, or favorable franchise language that may differ from the company’s “standard” approach.

Cable Systems and Services

A typical upgraded cable system today is a “hybrid fiber-coax” system, which has fiber-optic cable from its starting point at the “head end” (where all of the cable signals are collected from satellites and land lines) to neighborhoods, where the fiber is mated to standard coaxial cable for the last run to residences. Such a system has a typical bandwidth of 500 to 800 MHz, which, using the standard method of measuring capacity, would carry 80 to 125 channels of service. However, the operator is probably providing high-speed Internet access with some of that bandwidth and uses a digital compression system to make better use of the rest of the bandwidth. An average fiber-coax system now has 60 to 75 regular channels of cable service in one or more tiers and then offers a digital service with different menus of up to 200 more channels, using a special set top box, as well as offering high-speed Internet access through a rented or purchased cable modem installed on your PC.

If this description doesn’t fit your city’s cable system, your next question to your operator should be “When are you going to upgrade?” The only acceptable answer should be “Within the next 24 months.” Anything less will mean that your city will be below the norm for most cable systems.

Rate Regulation

The Catch-22 of upgrading your cable system is that you can expect increased costs to pay for that upgrade. The cable TV rate regulation scheme established by the 1992 Cable Act is now virtually extinct. Under that system,
local governments could regulate the rates charged for “Basic Service,” the lowest tier of cable service which legally must include all of the local broadcast TV stations and which typically consists of 9 to 13 channels. All the channels in higher-level tiers could be regulated directly by the FCC upon request of a local government, using the same pricing standards as Basic Service.

With the passage of the 1996 Telecommunications Act, the FCC’s regulatory authority over upper tiers was repealed, and now only basic service is rate-controlled in those cities who chose to exercise that authority. Whether your city regulates basic service or not, virtually all cable companies, as a prudent business practice, price their basic service as if they were rate-regulated. This means that basic rates are increasing slowly for everyone, based on allowable increases for additional costs of providing the service. At the same time, all of the new channels, improved services, and programming changes are happening in the upper tiers of service, which are no longer regulated. This means that even if your city is currently regulating basic rates, cable bills are increasing at least annually as the operator adds channels, upgrades the hardware, and pays more per customer for existing popular cable channels on the upper tiers.

The bottom line: cable rates will continue to increase at a rate faster than inflation as cable operators add more channels of service and upgrade the cable system. While some of your citizen cable customers may not want those additional channels, it is usually impossible to avoid a higher bill without opting for only the minimum basic service. The only possibility for better rates is to attract competition for the incumbent cable operator.

**Prices and Competition for Cable**

Ten or fifteen years ago, the cable company was the only alternative for what is termed “multichannel video.” If you wanted more TV than an antenna on the roof could bring in, it was take-it-or-leave-it from the cable provider, and the resulting relationship between cable customers, as represented by their local government and the cable operator was frequently less than cordial. This too, has changed. The cable industry has been losing market share to direct broadcast satellite (DBS) services over the past few years and now perceives its franchising local governments as allies in the fight with satellite signal providers, since DBS providers don’t pay franchise fees or deal with the city at all. As a result, cable operators are more concerned with communications to customers and local governments than was formerly the case, and they are more attentive to customer service and pricing issues.

In addition to DBS providers, there is a new type of company providing competition to existing cable operators. These companies are “overbuilding” existing cabled areas and are providing not only cable TV, but also Internet access and local telephone service over their networks. The best example of such a company in Tennessee is Knology, a Georgia-based company that is currently building systems in the Knoxville and Nashville metro areas in competition with Comcast and Charter. Knology has similar existing operations in cities in Alabama, Georgia, and South Carolina, and is also building systems in Louisville, Kentucky, and other mid-size southern cities.

With this new competition, cable operators are much more price-sensitive. While it may not seem like it, the average cost per channel of basic and expanded cable has been relatively flat for the past two years. What has been causing the regular price increases recently has been the continuous addition of new, ever-more-specialized cable channels. The average price of a cable channel across the U.S. ranges from 57 cents per month in areas with a competing cable system to 66 cents per month for operators facing only satellite dish competition. Rates in Tennessee are generally at, or slightly below, these national averages.

**Second Franchises**

When negotiating a franchise with a second cable operator, cities should be aware of the requirement of Tennessee Code Annotated 7-59-203, which prohibits a city or county from granting a second franchise which is “more favorable or less burdensome” than the terms of the existing franchise with the first operator. Some existing operators will attempt to include language in a franchise renewal which requires the city to notify the existing operator any time a second franchise is sought, and which would require the city to amend its existing franchise with any new language offered in a franchise to the second operator. Such provisions are burdensome and unnecessary since the language of T.C.A 7-59-203 does
not define “terms more favorable or less burdensome” as requiring word-for-word identical language in both franchises. There has never been a case brought under this statute, but existing operators frequently cite it to coerce cities into agreeing to more restrictive franchise language than is necessary to meet the stated purposes of the law.

Franchise Fees and Internet Access

One of the major concerns for most cities when negotiating a cable franchise is the amount and coverage of the cable franchise fee. Federal law permits a 5 percent of gross revenues fee, and most cities provide for a fee at that level in the franchise. There was an ongoing debate over whether the provision of cable Internet access should be subject to the franchise fee. In cases from Oregon, California, Florida, and Virginia, the federal Circuit Courts of Appeals disagreed on this question. As a result, the FCC initiated a rulemaking process to resolve the issue. Recently the FCC decided that Internet access was not a cable service; therefore, it was not subject to regulation by franchising authorities. The revenue from Internet service provided by a cable company is also not subject to the franchise fee. While there is still an effort underway by local government lobby groups to challenge this ruling, any new franchise language should conform to the FCC rule. Until there is a final resolution, if you are negotiating a cable franchise, you should include language that states that cable modem and Internet access fees are included in the definition of gross revenues on which a franchise fee is due, but only if permitted by Federal law and/or the rules of the FCC.

Telephone Services in a Cable Franchise

A detailed discussion in the following section on Telephone Services regarding municipalities’ authority over telephone and other similar companies basically says that, under Tennessee law, cities can’t franchise telephone companies. With that in mind, when your city is negotiating a cable franchise with a cable company that may want to enter the local telephone market at some future date, you should make it clear that the city has no control over that activity. (This is not the case in some other states, and the cable operator may not be aware of that distinction.) The language of the franchise should explicitly state that the franchise does not include authority to provide telephone services because the city does not have the power to either deny or authorize that activity. Some operators perceive, incorrectly, that the city is trying to prohibit them from providing telephone service by stating that the franchise doesn’t cover it. The response should be that the city has no authority to either authorize or prohibit telephone services; the Tennessee Regulatory Authority (TRA) handles those decisions.

Model Cable Franchise Available

MTAS has a model cable franchise available for your use if your city or town is coming up on a renewal date with your cable operator. For more information, contact your Municipal Management Consultant or Jim Finane, Special Projects Consultant at (865) 974-0411.

TELEPHONE SERVICES

Franchising Telephone and Other Telecommunications Companies

Some confusion exists among Tennessee cities regarding cities’ authority over telecommunications companies other than cable television companies. It is easier to understand if you divide the question into two parts:

1) Can municipalities require a franchise and franchise fee from telephone and telecommunications companies?

2) What can municipalities do to control companies in their right-of-way?

1) No, municipalities have no right to require telephone and telecommunications companies to obtain a franchise. This question was resolved in the case of City of Chattanooga vs. BellSouth Telecommunications, 2000 WL 122199 (Tenn.Ct.App., 2000). In this case, Chattanooga required BellSouth to obtain a city-issued franchise and pay a franchise fee to the city based upon BellSouth’s revenues in the city. The city cited as its authority T.C.A. 65-21-103 which provides that a city

...within which such [telephone] line may be constructed shall have all reasonable police powers to regulate the construction, maintenance, or operation of such line within its limits, including
the right to exact rentals for the use of its streets and to limit the rates to be charged; provided, that such rentals and limitations as to rates are reasonable and imposed upon all telephone and telegraph companies without discrimination.

The court ultimately ruled that the city did have limited authority to “exact rentals,” but that such rentals were limited by its police power, which meant the rentals could only amount to the city’s actual and reasonable costs of allowing BellSouth in its rights-of-way. Previous court action in the same case also held that BellSouth did not need a franchise from the city to legally operate. While the City of Memphis is pursuing a challenge that seeks to—at least for Memphis—reverse this decision, the Chattanooga vs. BellSouth decision is currently the law in Tennessee.

(2) Cities can prescribe any reasonable procedures for pavement cuts and/or rights-of-way usage and restoration by any company and recover whatever costs the city may incur as a result of that activity, but cities can’t charge the company a fee to be in the right-of-way or call the requirements a “franchise.” A document such as a “Right-of-Way Use Agreement” or a simple permit with associated rules and regulations would suffice.

More Competition in Local and Long Distance Telephony

One of the major issues for all of the Regional Bell Operating Companies (RBOC’s) like BellSouth is their future ability to re-enter the long distance telephone market for their current local service customers. After the AT&T break-up, the newly formed regional phone companies were not permitted to provide long distance service other than calls within their local service area. The rationale was that since they were a local monopoly, the RBOC’s would have an unfair competitive advantage over AT&T and other long-distance-only companies because they could subsidize long distance rates with their monopoly local revenues.

The FCC set up a review system after the passage of the 1996 Telecommunications Act that provided for a multi-step process for RBOC’s to gain the right to enter the long distance business. Each company had to prove, on a state-by-state basis, that they had sufficiently opened up access to their system and services to competitors for the local telephone market to allow for actual local phone service competition. Each case has to originate with the state body that regulates telephony and, if approved, would then proceed to the FCC for a second determination. BellAtlantic (now Verizon) was the first RBOC to complete this process 3 years ago, allowing them to provide long-distance service in New York. Twelve other states have subsequently been similarly opened to competition, including recently, Georgia and Louisiana. BellSouth has made this trip for Tennessee service, but has been turned down by the FCC. This year, another try will move through the TRA to Washington sometime before the end of the year, and BellSouth is optimistic that it will receive approval this time, although their success is by no means assured.

Should this approval occur, the already competitive long distance market would be even more competitive; therefore, at the first opportunity, every city in the state should review their long distance service to see if there is some money to be saved by either changing providers or re-negotiating existing service agreements.

Cable Telephony

There are a number of cable operators around the country who are now offering local telephone service, using a number of different technologies. In fact, nationwide, roughly 5 percent of the customers who use Competitive Local Exchange Carriers (CLEC’s), which are those companies who are competing with the existing “phone company” for local business, are cable television providers who are entering the telephone business. At present in Tennessee, the only company that has definite plans to offer this service is Knology, the overbuild specialist that has cable franchises in the Knoxville and Nashville metro areas.

Wireless Communications & Tower Siting

Controlling the Proliferation of Wireless Antennas

Cellular service towers are fast becoming as common in both the urban and rural landscape as utility poles. While your city or town may welcome better cellular service, you
may also find that you want to control the placement and design of these cell towers. This is clearly an achievable goal, but you should realize that the only way to control cell tower siting is with zoning. If your town doesn’t have zoning, then any attempts to control only communications towers, but not any other land use, will not withstand a legal challenge. If your city or town has a well-developed zoning scheme, and needs help with cell tower siting, MTAS can supply tested zoning provisions that have proven successful in other Tennessee cities and towns.

**Siting Wireless Antennas on City Property**

As wireless services for everything ranging from paging to Internet access continually expand, appropriate sites for antennas are becoming harder to find. Many cities and towns in Tennessee have been able to profit from this market by renting space on existing water storage tanks and public safety radio towers to private enterprises. MTAS frequently receives calls from cities wanting to know what an appropriate rental fee is for such use. There is no “standard” amount for accommodating a private antenna on a municipal site, but recent experience shows that the annual rentals actually being collected by cities range from as high as $18,000 per year for a cell tower site for a major wireless telephone provider in a metropolitan area, to as little as $5,000 per year for a paging service antenna on a municipal water tower in a small town. A significant advantage to leasing municipal property for antenna sites is the control over size, shape, and placement of the antenna that the city can exercise in that process. This control would be difficult to achieve through even the most detailed zoning ordinance procedure for a similar antenna on private property.

**Wireless Broadband**

One of the newer technologies that local governments need to be aware of is a service termed “wireless broadband,” which is being deployed at the two population extremes in some areas. On one hand, there are companies providing mobile Internet access in large urban areas through small (12”) antennas, mounted in a shoebox-sized piece of hardware that is typically installed on streetlight standards or utility poles, that may be spaced less than a quarter of a mile apart. There is some revenue potential from this technology in pole rental fees for municipal utilities. Another plus is that this technology tends to cause little or no disruption to the utility’s normal operations. However, the one company that was actually in business to provide this service in a number of large cities around the country, including Nashville, declared bankruptcy last year, so the prospects for immediate deployment are now indefinite. There are also indications that systems using standard cellular technology may actually supplant these other alternatives, and like many new telecommunications initiatives, “wait and see” is a good policy.

At the other extreme, in small towns and rural areas where the local telephone company may not have chosen to install high-speed access using Digital Subscriber Line (DSL) technology, wireless broadband systems are being installed as the only way to achieve broadband Internet speeds that normally would use hard-wired cable modem or DSL technology in urban areas. While such systems have not appeared yet in Tennessee, they could occur in areas where the market conditions are right.

**FOR MORE INFORMATION**

If you need further information on any telecommunications subject, or need help with a model cable franchise, a right-of-way use agreement, or a wireless tower zoning ordinance, contact either your Municipal Management Consultant, or Jim Finane, Special Projects Consultant at (865) 974-0411.

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