TESTIMONY OF KYLE McSLARROW
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on

THE COMMUNICATIONS OPPORTUNITY, PROMOTION, AND ENHANCEMENT ACT OF 2006

before the

COMMITTEE ON ENERGY AND COMMERCE
SUBCOMMITTEE ON TELECOMMUNICATIONS AND THE INTERNET
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Chairman Barton and Members of the Committee, my name is Kyle McSlarrow and I serve as President and CEO of the National Cable & Telecommunications Association (NCTA), which is the principal trade association representing the cable television industry in the United States. Its members include cable operators serving more than 90% of the nation's cable television subscribers, as well as more than 200 cable programming networks and services. NCTA's members also include suppliers of equipment and services to the cable industry. The cable industry is the nation's largest broadband provider of high speed Internet access after investing $100 billion over ten years to build out a two-way interactive network with fiber optic technology. Cable companies also provide state-of-the-art digital telephone service to millions of American consumers.

Thank you for inviting me to comment on proposed legislation to reform the video franchising process. I would also like to thank you, Chairman Barton, Chairman Upton and Congressmen Dingell, Markey and Pickering, and the members of this Committee for your work on these issues and your willingness to listen to the concerns and views of the cable industry throughout the process.

Cable Embraces Competition and Less Regulation

Mr. Chairman, the cable industry fully embraces, and thrives today in, a robust, competitive marketplace. Our policy for several decades has been to minimize regulation on us and our competitors. The cable industry has never asked Congress for a handout and we don't seek to obtain regulatory advantages over our competitors. Nor have we

opposed efforts designed to lighten regulatory burdens on our competitors in order to foster fair competition on a level playing field.

For example, in 1999 the cable industry supported the Satellite Home Viewer Improvement Act (SHVIA), which authorized direct broadcast satellite (DBS) providers to offer local broadcast signals. DBS providers were given "local-into-local" authority but were required to follow the same rules as cable and other MVPDs when they offered local signals. SHVIA established a fair and level playing field for multichannel video competition. And as a result, growth in DBS subscribership exploded and competition in the multichannel video marketplace is thriving. Today, two national DBS providers have captured nearly 30 percent of the MVPD marketplace.

The cable industry did not oppose a key provision of the 1996 Telecom Act that eliminated rules prohibiting telephone companies offering video service. Rather, we supported that legislation because it offered all competitors the ability to enter new markets on fair, market based terms and established a stable deregulatory environment.

And, more recently, the cable industry supported the efforts of the telephone companies to deregulate their high speed Internet access service so that they could compete with all broadband providers on a level playing field.

Franchise Reform Legislation Should Streamline the Process and Establish a Level Playing Field

Our primary interest in franchise reform is to ensure that all competitors in the video marketplace compete under the same set of rules, rules that can undoubtedly be streamlined in a more deregulatory market.

To the extent that Congress believes that the franchise process needs to be modernized, the cable industry has clearly stated its preferred path to reform. We have expressed support for franchise reform that embodies the following principles:

- First, in order to expedite entry to market for new competitors, we believe that Congress should streamline the process by limiting the time that local franchising authorities have to consider an application to provide video service.
- Second, it is critical for all providers of video services to be treated on a level playing field. An incumbent should have the right to opt into any new franchise agreement that has better terms and conditions. The government should not pick winners and losers in the broadband industry by establishing a different set of rules that favor one provider over another.
- Third, local governments should maintain oversight with respect to rights-of-way management, meeting community needs and interests (including the equitable sharing of PEG and institutional network responsibilities), and enforcement of non-discrimination requirements.

The Telephone Companies Have Had a Decade to Enter the Video Market

In 1996 when Congress lifted the ban on telephone entry into the video business, it was a significant change in federal telecommunications policy. For decades, Congress kept the telephone companies out of the video business for fear that their monopoly control over the local phone market would allow them to exert market power in a way that would harm video competition. This threat was based on the telephone companies' anticompetitive behavior regarding pole attachments and their incentive and ability to shift costs associated with video service into their regulated telephone rate base and thereby unfairly cross-subsidize their entry into the video business with revenues from their telephone monopoly.

However, Congress lifted the ban in 1996 largely because the '96 Telecommunications Act also established rules to promote competition in the local voice market. Congress hoped that such competition would inhibit the ability of the Bells to use their telephone monopoly to enter the video marketplace in an anticompetitive manner.

The '96 Act gave the phone companies four options for entering the video business and expressly stated that if they chose to enter as a cable system, they would be subject to the same requirements of Title VI as any other cable operator. At that time, the telephone companies didn't complain that the local franchising process was a barrier to entry and Congress evidenced no interest in freeing telephone companies that chose to enter the cable business from any of the traditional requirements that apply to cable

operators, whether they were first to the market or last. To the contrary, recognizing that large incumbent telephone companies were fully capable of competing vigorously in the video marketplace, Congress stipulated that cable operators would be free from any remaining rate regulation whenever a telephone company entered an operator's franchise area.

Now a decade later, having made little effort to enter the video business, the phone companies are back claiming that they need special rules that would allow them to enter the video marketplace in a manner that would give them a regulatory advantage over their competitors. It is remarkable that Congress would even entertain the Bells new pleas for special favors when the very rationale for allowing the Bell companies to enter the video business in the first place has yet to materialize—competition in the local voice market. Rather than spending the last ten years offering video competition, as they promised, they have invested their time and tremendous financial resources in the courts and at the FCC attempting to frustrate Congressional efforts to promote voice competition. They have successfully crushed most of their local voice competitors and swallowed their long distance competition. Ten years after the passage of the 1996 Telecom Act, the incumbent telephone companies still have a vice grip on 85% of the local telephone marketplace.

Meanwhile, during those same ten years, competition to cable operators from two large DBS companies has increased dramatically. In stark contrast to the behavior of the Bell companies, the cable industry responded to the deregulation of the 1996 Telecom

Act and vibrant DBS competition by investing $100 billion in private risk capital to upgrade its facilities with state of the art fiber optic technology. The industry made this investment without government subsidies and with no guarantee of a return on its investment. And just like it created a multichannel video service from scratch, cable pioneered the residential broadband marketplace, while the telephone companies kept DSL technology on the shelf in order to preserve their high priced T1 business service. Cable's innovation and risk taking created the nation's largest broadband provider of high speed Internet access. Cable's broadband platform delivers digital video, high definition television, digital telephone service, and an array of new interactive services.

The Existing Franchise Process Is Not a Barrier to Entry

Despite a promise ten years ago that they would compete in video, the Bells are back, smaller in number but much larger in size with annual revenues of $150 billion more than twice that of the cable industry, telling Congress that they can't compete in video, in fact won't compete in video unless they are granted another special favor. They want to enter the video business on favored terms without obtaining a local franchise agreement.

The Bells complain that the franchising process is a barrier to entry and that it takes too long to obtain franchise agreements. An examination of the facts shows that those claims are simply unfounded.

Telephone companies – and other new video entrants – have long received local cable franchises. Shortly after Congress repealed the ban on telephone companies entering the video business, Ameritech obtained more than one hundred cable franchises. Ameritech did not waste time complaining about or seeking to avoid the franchising process. It simply went about obtaining cable franchises and it did so without resistance, unreasonable demands or delays by local franchising authorities. Ameritech's rapid progress in obtaining franchises continued until the company was acquired by SBC, which promptly sold off Ameritech's systems just as it terminated the efforts of Pacific Telesis and Southern New England Telephone to offer competitive cable service after acquiring those companies.

Smaller broadband competitors with a fraction of the Bells' resources like WideOpenWest, Knology and RCN have managed to obtain franchises to compete with cable companies in hundreds of communities across America. And it looks like the telephone companies are managing to do so, too.

Verizon CEO Ivan Seidenberg told investors in a January conference call that his company was making "good progress" on video franchising and that the franchising process does not pose "any impediment to our rolling out FiOS during the year 2006." [1] As he explained to *Business Week*, "We haven't been turned down anywhere we've gone."[2]

[1] Conference Call Transcript, VZ-Q4 2005 Verizon Earnings Conference Call, Jan. 26, 2006.
[2] Business Week Online, Sep. 28, 2005, "Verizon: "We've Got to Fix It".

And he's right. Verizon already has franchises covering approximately two million households, and there are many examples of Verizon obtaining approval in as little as 19 days to 4 months (Beaumont, California; Sachse, Texas; Herndon and Fairfax County, VA). In fact, in several instances Verizon has obtained franchise agreements faster than they are able to deliver service. For example:

- In Sachse, Texas, Verizon obtained a franchise in less than two months but took over a year to deploy video after being granted a franchise on December 6, 2004.

- In Fairfax County, Virginia, Verizon obtained a franchise in less than 3 months, but it took more than 5 months after receiving the franchise before it began offering video service in that community.

- In Beaumont, California, where Verizon obtained a franchise in less than 3 weeks, it did not begin to offer video service until more than 15 months after it was granted a franchise.

- In Bellefonte, Delaware, where Verizon obtained a franchise in less than 50 days, it still does not offer video service more than 3 1/2 months later.

Ironically, some local governments complain that Verizon is actually responsible for delays in the franchising process. Several counties in Maryland have told the FCC that Verizon's own internal bureaucratic machinery creates substantial delay and has significantly contributed to much of the regulatory lag about which Verizon complains.

The bottom line: a review of Verizon's franchises shows an average of 4.3 months to obtain a franchise, and interestingly, an average of 5.3 months after they get a franchise before they deliver video service.

Most interestingly of all, AT&T can make no legitimate complaints about the franchising process at all because they, wrongly, assert that their video service does not require them even to comply with federal franchising rules. In other words, they haven't even tried.

What the Bells Truly Seek Is a Green Light to Serve Only "High Value" Consumers

So the Bells' complaints about process are nothing more than a smokescreen to hide the fact that what they really seek is to avoid the obligations that come with obtaining a video franchise.

Specifically, what the Bell monopolies refuse to accept is the notion that the new competition they promise should be afforded to all of the communities they serve. It's really that simple. Having built their networks on the backs of ratepayers as a regulated monopoly for nearly a century, the Bells do not believe that they should be required to *upgrade those* networks in a manner that is equitable and nondiscriminatory.

The Bells are making the case that their video service will bring widespread benefits to consumers while, at the same time, telling Congress that they should not be required to provide such service to all communities within their service area. For example, SBC (now AT&T) has announced to Wall Street that it would serve 90% of "high-value" customers, 70% of "medium-value" customers, and only 5% of what they deem to be "low-value" customers.[3]

Ironically, in the past the Bells attacked voice competitors for the same type of cherry-picking they now want to practice as they enter the video business. SBC paid for advertising in major newspapers criticizing competitors who wanted to selectively target their customers. *"We proudly make SBC service available to everyone, in every neighborhood, in every region we serve,"* the SBC ads declared. SBC should have added a disclaimer: "But when it comes to video, we're not interested in serving 'low-value' customers."

If Congress believes that increased video competition is an important public policy, then it must confront how to ensure that the benefits of competition are made available to all citizens. Otherwise, the Congressional goal of promoting widespread deployment of advanced broadband services to all Americans will never be achieved and households in urban and rural America will be relegated to second-class service.

The Committee Print is a Significant Step Forward

The committee print under consideration today represents a significant step forward. Unlike previous drafts, the bill does not grant regulatory relief based on the technology used to offer video service. And the current proposal does not include new regulations on video services.

As we have stated, we believe the better course is to reform and streamline the existing franchising process; however, we strongly support the policy decision reflected in the bill to seek to ensure a level playing field for video competition. While we can

[3] SBC Project Lightspeed Investor Relations Call, Nov. 11, 2004

continue to debate the rules upon which new entrants offer video services, it is critical to ensure that all competitors compete under the same rules. There are also a number of areas where we believe the level playing field provisions of the Committee Print can be strengthened and clarified. Giving all providers of video services the ability to compete on a level playing field ensures that the marketplace rather than the government will choose winners and losers. Competitors will have the freedom to innovate and make business decisions based on marketplace realities rather than the vagaries of a skewed regulatory framework.

A level playing field also creates a predictable and stable regulatory environment which is crucial for continued investment and innovation. In testimony before the Senate Commerce Committee on March 14, 2006, Aryeh B. Bourkoff (senior analyst at UBS Investment Research) said regarding franchise reform, "I stress the importance of maintaining a level playing field among all operators while allowing consumer preferences to dictate the changes to current models. Uncertainly among investors will persist if the rules surrounding obtaining a video franchise fluctuate based on the nature of the new entrants."

Establishing a level playing field for video competition should be welcomed by the Bell companies who have argued for years that they should operate under the same regulatory framework as cable operators in the provision of high speed Internet access. AT&T said it best in comparing the regulatory treatment of cable modem and DSL

service, "companies that provide similar services should be regulated the same. There is no reason for treating them any differently." [4]

Rights and Obligations of VoIP Providers

We are pleased that the Committee Print includes language that seeks to clarify that the interconnection rights Congress established in 1996 to promote voice competition apply to all providers of voice services on a technology neutral basis. The 1996 Telecom Act provided interconnection rights to competitive local exchange carriers (CLECs) so they could exchange traffic with the Bells on an economic basis, without glitches or delays, in order to promote local voice competition. Limiting interconnection and related rights to providers of voice services using traditional technology would ensure the Bells retain their market dominance by hampering the introduction of digital voice services – the best hope for competition in the voice market. The bill correctly recognizes that any legislation to promote competition would be incomplete without addressing voice competition where the Bell companies still control 85% of the market.

Network Neutrality Regulation Threatens Continued Investment

We are concerned, however, that the committee print would, for the first time, impose regulation on the Internet. While simply codifying the FCC's network neutrality principles may, at first blush, look like a reasonable and innocuous attempt to ensure that network providers maintain openness; it could lead to endless and expensive litigation.

[4] Press Release, SBC Communications, Inc., "SBC Urges FCC To Enact Regulatory Parity For Broadband, "Aug. 6, 2002.

With bandwidth usage growing at a rapid pace, continued investment will be needed to keep broadband services robust. If broadband providers are to continue to make these investments, and if consumers are going to be given the levels of services and innovative new products and features they desire, all at prices they can afford, broadband providers need to have continuing flexibility to develop new business models and pricing plans. Network neutrality rules will stifle that flexibility and discourage capital investment.

The marketplace is highly competitive, where no real world problems needing a solution have been identified, and where the pace of technological development is breathtaking. There can be no better circumstances than these to leave regulation to the marketplace rather than government.

Practical Issues Raised by the Committee Print

While we have only had a few days to review the draft bill, we have identified a number of practical issues that would create uncertainty and ambiguity and frustrate the stated objective of replacing local franchising with a national scheme. We describe these issues below. They include the limitations imposed on the availability of a national franchise for incumbent cable operators, but the problems are by no means limited to that section of the bill. At a minimum, these issues should be resolved before the bill moves forward.

Clarifying that All Providers Are Covered. While the draft bill establishes a national franchise to enable faster entry by "new cable providers" and appears intended to capture video services provided by the telephone companies, the failure of the bill to amend the definitions of cable service or cable system undermines this purpose. AT&T has argued extensively that its proposed service does not fall within the existing statutory definitions because it has incorporated IP technology into its delivery system, and that therefore it should not be subject to any franchise requirements. Nothing in the draft bill precludes AT&T from continuing to assert this position. While we believe AT&T's argument is meritless, Congress should use this opportunity to remove any ambiguity. Not to do so would abdicate to the FCC and the courts the fundamental question of whether this bill even applies to AT&T and other "IPTV" providers which, of course, could easily include cable operators. One could reasonably ask what the point of this bill is in such a circumstance.

Ensuring A Level Playing Field. While the bill clearly seeks to establish a national franchising scheme allowing all providers to compete on a level playing field, in fact it creates a complicated structure in which providers offer cable service pursuant to a hodgepodge of national, state, and local franchises. It is, in short, a recipe for confusion. For instance, whether an existing cable operator is eligible for a national franchise is wholly out of its hands. Instead, it depends on the decisions and even the identity of its video competitor. In "franchise areas" that are unserved by a "new operator" on the date of enactment, for instance, an incumbent operator is ineligible for a national franchise unless and until a new operator "is providing service under a national franchise." Thus:

- No new entrant; no national franchise for the incumbent operator.
- New entrant elects a local franchise; no national franchise for the incumbent operator.
- New entrant obtains a national franchise; no national franchise for the incumbent operator until the new entrant actually starts providing service.
- New entrant's "franchise area" covers only a portion of the incumbent operator's service area; unclear whether operator can obtain a national franchise for its entire service area.

In areas where an incumbent local exchange carrier is already providing service on the date of enactment in competition with an existing cable operator, *neither* is eligible for a national franchise. Each must wait until its current franchise is no longer in effect until it can obtain a national franchise -- and then can only do so if the other provider is still providing service in that area. This means that a cable operator can be locked into a municipal franchise for years while a telephone company operates under a more favorable state franchise, and then, when it is finally eligible for a national franchise, its ability to obtain one is dependent on the decision of the telephone company to remain in the market.

Oddly, too, the bill does not even ensure that both providers are eligible for a national franchise at the same time. Where the telephone companies have negotiated franchises that allow them to walk away from the agreement in only a few years, they will be able to terminate such franchises and enjoy the benefits of a single, national franchise long before cable operators are eligible to request one.

All providers must be able to predict their regulatory environment with more certainty in order to continue investing in the market. If the policy objective is a national franchise, then that objective should be available to all providers under the same terms and conditions. At a minimum, the regulatory status of one provider should not be dependent on the business decisions of a competitor.

"Snapback" Provision. Related uncertainty is created by the provision that automatically terminates an incumbent operator's national franchise in any franchise area where there is no competing cable operator for one year. Upon termination, the operator is left with no continuing authorization to provide service. The operator may obtain a new local franchise, but getting one is not automatic and the terms of the new local franchise are not established by the bill. Again, the operator's fate is dictated by the actions of its competitor. If the competitor pulls out of a market, the operator must apparently start from scratch to negotiate a new franchise with the local franchising authority. This entire section is absurd and should be deleted.

No Meaningful Anti-Redlining. While the bill would prohibit a national franchisee from denying service to residential subscribers on the basis of income, it essentially allows a franchisee to self-define the "franchise areas" it will serve. A prohibition on redlining is essentially meaningless if a franchisee can simply limit its rollouts to wealthier communities or even neighborhoods. At a minimum, a "franchise area" should be defined as co-extensive with existing political subdivisions to limit the opportunity for the most blatant cherry-picking.

The bill also undermines the redlining prohibition by moving responsibility for oversight of this requirement from localities to the FCC. Nondiscrimination is most effectively overseen and enforced by local officials who know their community best, not by the FCC. Further, the FCC is directed only to ensure that the cable operator extends access to the avoided group; a national franchisee violating the anti-redlining requirement faces no penalty for its discrimination and is not required to make service available within any particular time limit. Even though a nationwide franchise is the chosen method to ensure competitive entry, it is still important to preserve local input into that process. Localities are best positioned to determine whether deployment comports with anti-redlining rules.

Large Increase in Fees. The bill substantially increases the fees paid by cable operators. First, the bill codifies an expansive definition of the "gross revenue" on which franchise fees are based, including revenues from advertising and promotional support. Second, all national franchisees would be required to pay up to an additional 1 percent of gross revenues to support PEG programming and institutional networks. This obligation would fall disproportionately on an existing cable operator which obtains a national franchise -- first, since 1 percent of its revenues would far exceed 1 percent of a new entrant's, and second, because the existing operator would also have to continue to provide -- apparently in perpetuity -- any institutional network that was required under its superseded local franchise. By contrast, local franchising authorities are expressly barred from requiring other national franchisees from constructing such networks.

Finally, in addition to requiring national franchisees to pay 6 percent of gross revenues -- and forcing existing operators to continue to provide institutional networks -- the bill authorizes new "rights-of-way management" fees. The intent may be to limit these fees to management-type activities such as permitting, inspection, etc., but unless the bill specifies that these fees must be "cost-based," there will inevitably be litigation -- as there as been over the provision in the 1996 Act authorizing "fair and reasonable," rather than "cost-based," rights-of-way compensation -- over whether this provision authorizes localities to collect market-based rents. The bill should impose clear limits on the fees imposed on all providers, if we are to continue innovating and offering consumers new services and products. The bottom line is that the bill represents an increased tax on consumers for no additional benefits and should be substantially modified and reduced.

Consumer Protection Requirements. The bill authorizes local franchising authorities to enforce the FCC's cable consumer protection rules, permitting them to issue orders requiring compliance with such rules. What the bill doesn't say is how a locality would enforce such an order. Would it be able to impose a fine? Would it be able to take an operator to state court, leading inevitably to a plethora of inconsistent interpretations of the FCC's rules? In the absence of further guidance, the objective of a nationally consistent set of consumer protection rules will be undermined.

Net Neutrality. I have already explained our strong reservations about codifying the FCC's principles as binding requirements, enforceable by the Commission. Here I would only observe that the adjudication authorized by this section of the bill is without reference to any procedural safeguards, such as those applicable to cease-and-desist orders against broadcasters under section 312(b) of the Act or the imposition of forfeitures under section 503(b)(4).

Interconnection. We recognize and applaud the bill's inclusion of a provision to make sections 251 and 252 of the 1996 Act applicable on a technology-neutral basis to competitive voice providers using IP technology. It is a step in the right direction, but what it gives with one hand it may take away with the other. IP-voice providers get the rights and duties of a competitive local exchange carrier (CLEC) under sections 251 and 252 of the Communications Act -- but only "with respect to interconnection" and "associated" rights and duties "necessary to effectuate interconnection." Since these sections address more than just interconnection, such as numbering, access to unbundled elements of the incumbent's network, and collocation at incumbent central office, IP-voice providers effectively have fewer rights than what CLECs presently have. Moreover, the language invites years of disputes over which parts of sections 251 and 252 are "necessary" to "effectuate" interconnection.

The bill also misses an opportunity to resolve the disputes pending in a growing number of states between rural carriers and CLECs over whether the latter can use their interconnection agreements in the provision of wholesale telecommunications service to

IP-voice providers. While we are hopeful the FCC will address this issue, Congress can cut years off the process and provide needed certainty by clarifying the issue in law rather than also abdicating this issue to the agency and the courts.

Municipal Broadband. The bill would overturn laws in over a dozen states that limit municipalities from constructing and operating broadband networks. These states have made the judgment that the risks to taxpayers outweigh any putative benefits of letting local governments enter this risky and competitive industry. The 1996 Act was successful in promoting substantial private sector investment in broadband facilities. The cable industry alone has invested nearly $100 billion since 1996. Government-provided service in areas served by private enterprise will impose substantial burdens on taxpayers and undermine competition from non-government providers who must rely on risk capital.

At a minimum, municipal broadband should be limited to areas where the private sector does not or is not likely to serve. To oversee their entry into broadband, governments should have to establish entities separate from the agencies that regulate communications providers in order to avoid conflicts of interests. Finally, the possibility of cross-subsidization through a wide range of devices, from tax revenues to below-cost loans relying on government borrowing power to discriminatory access to poles and conduits that are exempt from the Pole Attachment Act, demand more specific safeguards than the general language contained in the bill.

Conclusion

As Congress drafts changes to the Telecommunications Act of 1996, we urge you to treat like services alike, preferably in a deregulatory environment. We will do the rest by raising private risk capital, investing in new technology, offering better customer service, creating innovative new programming, and competing with other multichannel video providers in order to provide consumers with the best voice, video, and data services possible.