

# What Will The New Telecom Act Mean for Fiber?

National franchising, net neutrality and the Universal Service Fund loom large

By Steven S. Ross ■ *Editor-in-Chief*

**T**he House and Senate moved rewrites of the 1996 Telecommunications Act along separate tracks this spring. The issue of “net neutrality” – particularly important to telecom giants like AT&T and Verizon – captured most of the public’s attention. But the bills’ provisions for nationwide video franchising are likely to be even more important to most local cable operators and independent telcos, and to national cable firms like Comcast and Time-Warner.

The trains may never arrive; passage of a final bill is hardly assured. The House version, H.R.5252, sponsored by Rep. Joe Barton (R-TX), has already passed. It does not cover many contentious issues being tackled in the Senate, including a new way to calculate the telephone user tax for the Universal Service Fund (which subsidizes rural and nonprofit telephone service, and service to the poor and elderly). Sen. John Sununu’s subcommittee (R-NH) held Senate hearings on S.2686 in June. Sununu himself wanted to legislate thorny issues involving the Universal Service Fund separately. But the Senate leadership forced everything into one package, sponsored by Ted Stevens (R-Alaska), who seems as interested in a la carte pricing, pornography, broadcast flags and

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other minutia as he is in the big issues.

The telco giants also pledged to induce a train wreck if a final bill passes with onerous “net neutrality” rules. They would withdraw support for any rewrite of the 1996 law. That, in turn, would probably cut forecasts for the speed at which the country moves totally to fiber, because it would delay the telcos’ video rollouts.

The Congressional delay, due in part to the complexity of the industry and in perhaps an even larger part to Congress’s bias toward stretching contentious bills over several election cycles to maximize campaign contributions, has left a power vacuum that is being filled by the Federal Communications Commission and by the states.

All that having been said, the 1996 act is already a train wreck. In the past decade, the FCC has only written about two-thirds of the regulations mandated under it, and a quarter of those were overturned in court.

## NET NEUTRALITY

Neither the House nor the Senate bill says much about net neutrality, other than that the FCC should study it and maybe apply pressure where needed.

The issue is deceptively simple on the surface. The Internet’s ideological guardians – including Tim Berners-Lee, who thought up the World Wide Web in the first place – say the system should provide a level playing field for all users. Most technical observers seem to agree, however, that video and voice packets should get priority on the network over other data packets. Data can be delayed for short periods without anyone noticing. Voice and video have to flow smoothly.

The Internet, however, is a “network of networks,” offering many possibilities for bottlenecks. The major national com-

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munications companies minimize that problem for their own voice and video services by setting up virtual networks. These pre-arranged routes (enhanced by SBC buying AT&T and Verizon buying MCI) give their own voice and video the priority, and thus the quality-of-service, customers demand. Large private organizations – HP, GM, and so forth – also pay the major carriers for “virtual private networks.”

Why, then, should Google, Vonage, or other private organizations without their own networks be any different from GM or HP? Would lack of a strong net neutrality provision in current legislation get them to start their own networks, thus bringing more capital to meeting the nation’s broadband needs?

What about the little guys who could never justify their own national net?

#### **BANDWIDTH**

This magazine has suggested that if bandwidth were adequate, it would not matter much. But rationing by price, at a time when video demands seem about to overwhelm the plans major carriers have for adding local (metro-area and first mile) capacity, creates the possibility of a de facto monopoly despite the availability of plenty of intercity bandwidth. One small telco even used that power to block third-party VoIP outright, and was taken to the woodshed.

A monopoly would, in turn, carry the possibility of cutting off innovation, of the kind we have seen in Asia. Tens of thousands of IP video channels are possible, if the packets can get to customers. But several of our own columnists have noted that balancing the needs of the carriers for capital to expand (at a time when Wall Street seems rather hostile to broadband) and the national need for job-creating, economy-boosting innovation is not easy, and that laws and FCC regulation are blunt instruments, astoundingly unsuited to tuning net neutrality – or even to defining it.

The nuance has gotten lost; arguments about net neutrality have descended to the “class warfare” stage in the general press. The large telcos have pledged not to entirely block third-party packets,

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but they want some guarantee that they will not be forced to give service away. The Internet activists note that the telcos fell far short of their original promises to regulators in the 1990s, and that rate increases back then should have paid for broadband expansion we’d be enjoying now. The telcos say the technology wasn’t there. The activists ask why, then, didn’t the telcos know that before they made their promises?

At TelecomNext in Las Vegas, Tom Tauke, executive vice president for public affairs for Verizon, and Jim Cicconi, senior executive vice president for AT&T, said their companies have no intention of intentionally degrading or blocking other companies’ traffic that rides over the public Internet. “This debate is all about movies,” Cicconi said. “A handful of companies who have plans to stream movies want to ensure their product is as good as ours. Or they want ours to be dumbed down for them.”

#### **CONTENT PROVIDERS**

They say carriers should be able to charge different fees to content providers for assuring better quality. “There’s been a misconception about the network we are building and how we plan to deliver services,” said Cicconi. “What we plan to do amounts to creating dedicated services,” and it is unreasonable for companies offering competing video services to demand AT&T offer the same quality it provides through its dedicated service.

The final law, if there is one, will probably leave it up to the FCC to study the

issue and to determine whether AT&T, Verizon and others are charging a “justifiable” price to assure such services. But the law will not likely give the FCC any additional power to do so. It all comes to a head when promises telcos made last year, to stay net neutral until mid-2007, expire (see box).

The House bill devotes only a few sentences to this. The Senate bill calls for the FCC to study the issue for the next five years. Section 901 of the Senate bill, titled “Neutral Networks for Consumers,” says:

(a) Beginning 1 year after the date of enactment of this Act, the Federal Communications Commission shall report annually to the Senate Committee on Commerce, Science, and Transportation and the House of Representatives Committee on Energy and Commerce for 5 years regarding

(1) the developments in Internet traffic processing, routing, peering, transport, and interconnection;

(2) how such developments impact the free flow of information over the public Internet and the consumer experience using the public Internet;

(3) business relationships between broadband service providers and applications and online user services; and

(4) the development of and services available over public and private Internet offerings.

(b) ... If the Commission determines that there are significant problems with any of the matters described in subsection (a) the Commission shall make such rec-

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## WHAT ABOUT MUNICIPAL BROADBAND? UNDER THE HOUSE BILL, STATES AND LOCALITIES MAY NOT GRANT ANY PREFERENCE TO SYSTEMS THEY OWN, CONTROL, OR ARE OTHERWISE AFFILIATED WITH.

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ommendations in its next annual report under subsection (a) as it deems necessary and appropriate to ensure that consumers can access lawful content and run Internet applications and services over the public Internet subject to the bandwidth purchased and the needs of law enforcement agencies. The Commission shall include recommendations for appropriate enforcement mechanisms but may not recommend additional rulemaking authority for the Commission.

### UNIVERSAL SERVICE FUND

The FCC issued its own temporary revision of the Universal Service Fund tax system after Sununu's Senate hearings. It was effective June 21, but the FCC says it is interim, pending new legislation or a complete review of the issue, and will expire in December.

USF taxes are going up, although the 8.7 percent tax rate stays the same. The FCC, at least in the interim, is sticking with a tax based on carriers' estimated interstate revenue in an increasing flat-rate telephony world. It raised the existing wireless "safe harbor" percentage used to estimate interstate revenue from 28.5 percent to 37.1 percent of total end-user telecommunications revenue to better reflect growing demand for flat-rate wireless services. Companies, if they have the data, can calculate a lower percentage and thus pay less toward the fund. This interim wireless safe harbor was last updated in 2002.

The FCC also decided to tax VoIP revenue for the first time. For VoIP providers interconnected with the conventional switched network, the FCC set the safe harbor percentage of interstate revenue at 64.9 percent of total VoIP service revenue.

As with cellular carriers, interconnected VoIP providers also may calculate

their interstate revenues based on their actual revenues or by using traffic studies. VoIP providers of computer-to-computer calls remain untaxed.

### FRANCHISING

The telco giants want a national franchise law, but are not willing to bend much on net neutrality to get it. Part of the reason lies in state actions. States seem quite willing to do away with local control; seven have already passed statewide franchising legislation; at press time, five

states (Kansas, Indiana, Texas, Virginia, and South Carolina) had enacted reform legislation, and bills in another two (Louisiana and New Jersey) were awaiting governors' signatures. Nine others are considering legislation – California, Iowa, Michigan, Missouri, New York, North Carolina, Oklahoma, Pennsylvania, and Tennessee.

Both the House and Senate bills make clear that telcos are indeed covered by video franchise rules. Verizon has accepted this approach publicly. AT&T has issued conflicting statements in the past year and is fighting California local community franchise laws. Under the House bill, IPTV is still TV, but Web sites that have video, even TV-quality video, are apparently exempt. The House bill does say the use of Internet-Protocol technology does not exempt a video provider from franchising or licensing rules, but

## FCC "Net Neutrality" Policy Statement, Released September 23, 2005 – and an update

The Commission has jurisdiction necessary to ensure that providers of telecommunications for Internet access or Internet Protocol-enabled (IP-enabled) services are operated in a neutral manner. Moreover, to ensure that broadband networks are widely deployed, open, affordable, and accessible to all consumers, the Commission adopts the following principles:

- *To encourage broadband deployment and preserve and promote the open and interconnected nature of the public Internet*, consumers are entitled to access the lawful Internet content of their choice.
- *To encourage broadband deployment and preserve and promote the open and interconnected nature of the public Internet*, consumers are entitled to run applications and use services of their choice, subject to the needs of law enforcement.
- *To encourage broadband deployment and preserve and promote the open and interconnected nature of the public Internet*, consumers are entitled to connect their choice of legal devices that do not harm the network.<sup>13</sup>
- *To encourage broadband deployment and preserve and promote the open and interconnected nature of the public Internet*, consumers are entitled to competition among network providers, application and service providers, and content providers.

But as Congress wrestled with net neutrality, FCC Chairman Kevin Martin added that broadband providers must be permitted to invest in their networks and "recoup their costs." His statement was widely viewed in the industry as taking issue with the idea of strict net neutrality mandates.

The FCC did not flesh out its sentiment with regulations, but SBC agreed to abide by the principles for two years as a condition of its acquisition of AT&T, and Verizon did the same when it acquired MCI.

**A BROADBAND SERVICE PROVIDER CANNOT REQUIRE A SUBSCRIBER TO PURCHASE VIDEO, DATA, OR VOIP SERVICE OFFERED BY THE PROVIDER AS A CONDITION FOR THE PURCHASE OF ANY OTHER BROADBAND SERVICE; THEY MUST BE AVAILABLE SEPARATELY. BUT... A DISCOUNTED "BUNDLE" PRICE IS PERFECTLY ACCEPTABLE.**

this refers to facilities-based providers. The issue goes back to a regulatory construct that showed up in the Telecommunications Act of 1996 – the idea of Open Video System (OVS) licenses. OVS was reaffirmed in the House bill.

The OVS idea was originally envisioned as allowing phone companies to provide video services under federal license. But OVS was of course marginal in the pre-fiber age due to bandwidth requirements. In 1999 the Fifth Circuit U.S. Court of Appeals in Dallas ruled that the federal OVS provisions did not preclude municipalities from requiring franchises.

The House bill prohibits cable-programming vendors from denying a holder of a national franchise access to programming solely because the national franchisee uses a shared headend. (Rural phone companies in particular often share headends.) Section 102 of the House bill, which defines terms, is not supposed to change any of the definitions, including Section 602(7)(B) of the Communications Act (47 U.S.C. Sec. 522(7)(B)), which exempts private cable operators from franchise rules if they do not use public rights-of-way.

What about municipal broadband? Under the House bill, states and localities may not grant any preference to systems they own, control, or are otherwise affiliated with. Also, a broadband service provider cannot require a subscriber to purchase video, data, or VoIP service offered by the provider as a condition for the purchase of any other broadband service; they must be available separately. But there's nothing in the House bill that forces the provider to offer a stand-alone

version of any broadband service at the same price; a discounted "bundle" price is perfectly acceptable.

The House bill has a provision that allows a person or group to elect a national franchise instead of a local or statewide franchise, or OVS certification, if it meets the criteria spelled out in new Section 630(d). The ability of states to allow statewide franchises is specifically preserved in the House bill. So video providers would be able to apply under state or federal law, whichever is most advantageous in a given situation.

Under it, any entity not currently providing cable service in a franchise area may obtain a national franchise to provide cable service there. If the entity is already providing video service on the date of enactment in the area, it may also get a national franchise if another person or group already has a franchise or OVS certification. (The FCC says 99 percent of U.S. television households are already in an existing franchise area.)

Do you have to serve the entire franchise area? Maybe not. There's an interesting income-antidiscrimination rule; it prohibits a cable operator with a national franchise that provides cable service in a franchise area from denying access to its cable service to any group of potential residential cable service subscribers there, because of the income of that group.

In other words, a new national franchisee is in violation of the provision if it is offering service to parts of a franchise area identified in its certification, but not to another part of that franchise area because of the income of a group in that other area. Section (a)(3)(F) of the House bill requires the entity filing the certifica-

tion to identify where it intends to offer video service. This could limit the law's use by private cable operators, which would need enough capital to bite off a huge new territory in one gulp.

The House bill recognizes that a household may be in more than one franchise area (an incumbent's and an overbuilder's for instance). If the household falls within more than one existing franchise area, an entity seeking a federal franchise license can select any of the existing franchise areas that contain the household.

Apparently, a national franchise holder (as it would in the current system of local franchises) cannot cherry-pick its market, at least on the basis of income. The national license would cover at least the smallest "unit of general local government."

This can be as large or as small as the entity wishes so long as it covers the entire geographic area within that unit and as long as that geographic area is within the jurisdiction of only one local franchising authority.

The entity can identify as many franchise areas as it wants in each certification, and can add more later. **BBP**

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