TO: HONORABLE CITY COUNCIL

FROM: CITY MANAGER DEPARTMENT: ADMINISTRATIVE SERVICES

DATE: APRIL 9, 2007 CMR: 171:07

SUBJECT: ADOPTION OF AN ORDINANCE AMENDING AND ADDING SEVERAL CHAPTERS TO TITLE 2 AND TITLE 12 OF THE PALO ALTO MUNICIPAL CODE TO REGULATE VIDEO SERVICE PROVIDERS THAT HOLD VIDEO SERVICE FRANCHISES ISSUED BY THE CALIFORNIA PUBLIC UTILITIES COMMISSION

RECOMMENDATION
Staff recommends that the Council adopt an ordinance:

1) Amending Chapter 2.10 and adding a new Chapter 2.11 to Title 2 of the Palo Alto Municipal Code to regulate video service providers that hold video service franchises issued by the California Public Utilities Commission (Commission).


BACKGROUND
On May 22, 2000, the Council adopted Ordinance 4636, amending Chapter 2.10 of the Palo Alto Municipal Code to franchise and regulate the occupancy and use of the public rights-of-way by cable television and open video system operators. Among other things, this ordinance provides for: 1) the establishment of franchise and license requirements; 2) minimum construction, operation, and maintenance and repair requirements; and 3) customer service standards. Its purpose is to establish the same requirements and standards for all cable service and open video system providers that seek franchises issued by the City.

On September 29, 2006, Governor Schwarzenegger signed into law Assembly Bill 2987, the Digital Infrastructure and Video Competition Act of 2006 (DIVCA). The primary purpose of DIVCA is to create a ministerial process for the granting of franchises to providers of cable and open video system services in an effort to foster the rollout of technology; encourage video, voice and broadband service competition; and expand customer choice.
This new law permanently changes the franchising and regulatory structure for the provision of cable television and other video services in the State of California. Under DIVCA, video service franchises are now granted exclusively by the Commission rather than by local franchising entities. DIVCA leaves largely unchanged the City’s authority to enforce its current cable franchise with Comcast in accordance with Title 2 for the remaining term of Comcast’s franchise, which expires on July 25, 2010. On July 24, 2000, the Council adopted Resolution 7991, consenting to the transfer of the Cable Co-op franchise to AT&T Broadband, which merged with Comcast.

Although the City will no longer be the franchising authority, it will acquire certain rights and responsibilities under DIVCA with respect to any holder of a state franchise (Holder). DIVCA provides that these rights and responsibilities must be established by local ordinance before they become effective and enforceable. Towards that end, staff has developed the proposed ordinance.

**DISCUSSION**

The key provisions of the proposed ordinance are as follows: 1) a franchise fee requirement of 5% of gross revenues; 2) rights-of-way permitting requirements that include the approval or denial of encroachment permits within 60-days and the right of appeal to the Council; 3) the number of public, educational and governmental access (PEG) channels that must be provided; 4) a PEG fee requirement of $0.88 cents per residential subscriber per month; 5) audit authority; 6) penalties for violations of customer service standards; and 7) emergency alert system requirements.

DIVCA will bring about dramatic changes in how cable television franchises are granted and enforced, and how, by whom and to what extent video service providers are regulated. The proposed ordinance addresses these changes. Although DIVCA preserves (subject to certain limitations) the City’s authority to impose franchise fees and manage the public rights-of-way, it will have many potential impacts on the City, the most important of which are addressed below, as follows:

**Franchise Fees:** DIVCA allows local government (local entities) to assess a 5% franchise fee on Holders. While DIVCA establishes a new definition of gross revenues that differs somewhat from the City's current definition in Chapter 2.10, the differences between the two, it is now believed, are not material. Only experience, however, will reveal the true fiscal impact of this change. DIVCA also provides for a three-year statute of limitations on the City in seeking to collect unpaid or underpaid franchise fees, meaning that the City will most likely have to conduct fee audits more often (at least once every 2 or 3 years for each provider), at additional expense. Also, unlike Chapter 2.10, DIVCA provides that the City is responsible for paying the cable operator’s audit costs if the audit reveals no underpayment.

**Permitting and Public Rights-of-Way:** Under DIVCA, with respect to rights-of-way permitting and other public rights-of-way management activities, Holders must generally be treated in the same manner as telephone corporations that are certificated by the Commission. This means that Holders should be considered as “utilities” under Title 12 of the Palo Alto Municipal Code, rather than being subject to different, or additional, public rights-of-way obligations under Chapter 2.10 or new Chapter 2.11. In addition, under DIVCA, Holders are subject to local encroachment permit requirements and the California Environmental Quality Act (CEQA) when
installing, constructing, and maintaining facilities in the public rights-of-way. DIVCA requires the City to act on completed encroachment permit applications within 60 days of filing and provide applicants with an appeal process to the Council for any adverse initial decisions on their permit applications.

**PEG Channel Capacity:** Under DIVCA, the Holder must provide the same number of PEG channels as the number activated by the incumbent cable operator as of January 1, 2007. In addition, all video service providers must place the PEG channels on the basic tier, and, to the extent feasible, locate them on the same channel numbers as the incumbent cable operator and group them together with other basic tier channels. This preserves Palo Alto’s seven current PEG channels for both Comcast (the City’s current incumbent franchisee) and any new Holders. Under DIVCA, however, it will be more difficult (as compared to the Comcast franchise) for the City to obtain and keep additional PEG channels as demand for PEG capacity may grow.

**PEG Support:** DIVCA allows the City to continue to collect a PEG support fee of $0.88 cents per residential subscriber per month from Comcast and from any new Holder for the remaining term of Comcast’s franchise. Upon expiration of the Comcast franchise, the City can choose (by ordinance) between its current PEG support fee ($0.88 cents per subscriber per month) or a PEG support fee of 1% of the Holder’s gross revenues in the City. At the present time, a PEG fee of $0.88 cents per subscriber exceeds what a 1% PEG fee would yield. DIVCA also will require the City to re-authorize by ordinance its PEG fee at the expiration and renewal of each Holder’s state franchise. Under DIVCA, the term of a state franchise will be 10 years. Although the City will continue to collect PEG fees under DIVCA, support for all in-kind PEG services (e.g., free cable service to schools and other public and governmental buildings and free inclusion of PEG program information on a “TV Guide” channel, etc.) will be discontinued at the expiration of Comcast’s current franchise.

**Customer Service:** The City’s authority over a Holder will be limited to enforcing federal and state customer service standards. These standards are weaker in some respects than the City’s existing cable customer service standards. As an example, the City’s existing standards require a local customer service office, an automatic credit for outages of 24 hours or more, and credits for missed appointments. The City’s current standards also provide for monetary sanctions for violations that are higher than the maximum monetary sanctions permitted by DIVCA. Further, DIVCA requires that the City submit to the State one-half of any penalties collected for customer service standard violations.

**I-Net:** The City is in the process of establishing an institutional network (I-Net) that will connect 70 schools, libraries, and government facilities in the Joint Power Authority’s (JPA) service area for delivery of data, video, and voice services. Under DIVCA, existing local franchise obligations regarding I-Net facilities will continue only until the expiration date of the current Comcast franchise (July 25, 2010). Holders are not obligated to fund or provide I-Net facilities, and Comcast will no longer be required to do so after July 25, 2010.

**Service Availability:** Holders are permitted to determine the area of a city where they will provide service. DIVCA sets forth statewide build-out requirements based on the Holder’s customer base, setting three- and five-year time limits for the provision of video service to a pre-determined percentage of low income households in the Holder’s statewide territory. DIVCA also provides, however, for numerous extensions and waivers of these build-out
requirements. Parenthetically, this could result in, and there certainly would be little protection against, a widening of the digital divide that separates low income residents in the JPA’s service area.

**Temporary Dual Franchising Regimes:** Under DIVCA, a dual system exists under which Comcast will continue to operate under the City’s franchising authority until at least January 2, 2008, and as late as July 25, 2010, while all new entrants will be able to receive state franchises from the Commission after April 1, 2007. Both City and Commission franchisees will be monitored by the City, but in different ways. For example, the City will continue to enforce the City’s more stringent customer service standards against Comcast for a time, but it can only enforce the less-demanding DIVCA standards against the Holders. Similarly, the City will perform audits of both City and Commission franchisees but under a different framework for each.

**NEXT STEPS**
The cities of Palo Alto, Menlo Park, East Palo Alto, the Town of Atherton, and portions of San Mateo and Santa Clara Counties entered into a Joint Exercise of Powers Agreement for purposes of obtaining cable television service for residents, businesses, and institutions within these jurisdictions. The JPA gives the City of Palo Alto the sole authority to grant and administer the cable franchise process on behalf of its members. Under DIVCA, Palo Alto no longer has the authority to grant franchises to providers of cable or video services in the JPA’s service area. DIVCA does, however, allow the JPA to continue to serve as the “local entity” for DIVCA purposes, thereby permitting the JPA members (if they wish) to continue to rely on Palo Alto for such activities as franchise fee and PEG fee collection, PEG oversight, customer service and the like with respect to all Holders in the JPA’s service area. In the coming months, the JPA will consider amending its Agreement to reflect changes in the law due to DIVCA.

On May 9, 2007, staff plans to bring proposed amendments to Chapter 18.76 and 18.77 of Title 18 of the Palo Alto Municipal Code to the Planning and Transportation Commission for review. These amendments are needed to conform the architectural review process to the requirements of DIVCA.

**RESOURCE IMPACT**
The City’s incumbent franchisee and new Holders will continue to provide compensation (e.g., franchise fees, funding for PEG access services, etc.) for the use of public streets and rights-of-way. In 2006, the City received franchise fees in the amount of $581,000. Franchise fee revenue serves (among other things) to defray the City’s franchise administration costs. Staff does not currently anticipate any material impacts to franchise fee revenues as a result of DIVCA. In order to properly respond to the changes brought about by DIVCA, however, additional staff and consulting resources may need to be allocated to this effort.

The potential loss of the I-Net after July 25, 2010, could have a significant, but undetermined, adverse fiscal impact on government facilities and schools in the JPA’s service area that are relying, or will rely, on the I-Net. It may require JPA members to expend money to procure comparable communications capacity from the private sector to replace the I-Net.

The Commission plans to recover the cost it incurs administering state video service providers through application fees and a recurring fee to Holders. There is a risk that Holders will offset
these fees against the City’s 5% franchise fee, thereby reducing franchise fee revenues by the amount of Commission fees.

Also, under DIVCA, the City is responsible for paying the cable operator’s audit costs if the audit reveals no underpayment.

**POLICY IMPLICATIONS**

This proposed ordinance change will bring existing City policies into compliance with current State law for video service franchises.

**TIME LINE**

The Commission commenced accepting applications for state franchises in March. The Commission has 30 days to determine whether a franchise application is complete, and is required to issue a state franchise within 14 days of determining an application is complete. On March 7, 2007, AT&T applied for a state franchise for a service area that includes Palo Alto. The Commission granted AT&T its statewide franchise on March 30, 2007.

Prior to offering video service, the Holder is required to notify the local entity. The notice shall be given at least 10 days, but no more than 60 days, before the video service provider begins to offer service. The City anticipates receiving such notice from AT&T in the near future.

Palo Alto will continue to operate under its current franchise with Comcast until at least January 2, 2008, and possibly as late as July 25, 2010, when Comcast’s current franchise term expires. Although Comcast may seek a state franchise from the Commission after January 1, 2008, if a Holder enters the Palo Alto market, some of the obligations contained in the City’s current franchise with Comcast will remain in place until that franchise’s original expiration date of July 25, 2010.

**ENVIRONMENTAL REVIEW**

This is not a project under the CEQA.

PREPARED BY: ____________________________
MELISSA CAVALLO
Cable Coordinator

DEPARTMENT HEAD APPROVAL: ____________________________
CARL YEATS
Director, Administrative Services

CITY MANAGER APPROVAL: ____________________________
FRANK BENEST
City Manager

**ATTACHMENTS:**

Attachment A: Ordinance