



Memorandum

TO: HONORABLE MAYOR
AND CITY COUNCIL

FROM: Les White, City Manager
Richard Doyle, City Attorney

SUBJECT: Acceptance of Formal Proposal
For Cable Franchise Renewal

DATE: November 3, 2006

COUNCIL DISTRICT: City-Wide

RECOMMENDATION

- (a) Approval to consider the recommendations in (b-c) below pursuant to the Early Distribution Process Rule (2/3 vote required).
- (b) Approval of an Ordinance Granting a Cable Franchise to Comcast of California II, LLC
- (c) Approval of Ordinance Amending Chapter 15.28 of Title 15 of the San Jose Municipal Code to regulate the occupancy and use of Public rights of way by cable systems and open video systems

OUTCOME

With approval of the above recommendations, the City will grant a Cable Franchise renewal to Comcast of California, for a term of 10 years. The franchise will provide for: 1) the maximum lawful franchise fee of 5% of annual gross revenues; 2) a plan for one free outlet of cable service to all educational and government institutions in the City; 3) up to 10 channels for public, educational and government (PEG) programming; and, 4) a one-time, up front \$2.25 million contribution for PEG access capital equipment and facilities, plus \$0.43 per subscriber per month during the life of the franchise.

BACKGROUND

Status of Existing Cable Franchise

The cable franchise under which Comcast is currently serving the City of San Jose was drafted in 1985 and became effective January of 1986. This franchise was originally granted to Gill Cable. There have been several successors to Gill Cable, most recently AT&T and now Comcast of California. The franchise was originally set to expire in 2000, but was extended on several occasions for short periods while the City attempted to reach agreement with the cable provider on the terms for a new franchise. The last extension has expired. Comcast's authority to operate in the City is disputed by the City for a variety of reasons including the fact that the transfers of the

franchise were made without the City's approval. As a result, one way to describe Comcast's current status is that they are operating in a holdover status under the expired franchise.

Franchise Renewal Efforts

During the last several years the City has participated in informal renewal negotiations with AT&T, and Comcast, the current provider, to reach agreement on a renewal franchise. These discussions have been unsuccessful.

At the same time the informal renewal negotiations were being conducted, the City in 2001 moved forward with what is called the Formal Process for renewal of cable franchises as provided in the Federal Cable Act. The Formal Process, which was initiated by the cable operator, involves four steps:

1. The City surveys the community to ascertain its cable-related needs and interests
2. The City then provides the cable company with a *Request for Renewal Proposal* (RFRP), which incorporates the needs and interests and sets out the acceptable terms for renewing the franchise.
3. Once the incumbent cable operator submits a Formal Proposal for Renewal, the City evaluates it to decide whether it appears adequate.
4. Finally, if the City determines that the proposal appears inadequate, the City conducts an administrative proceeding to decide finally whether to grant or deny renewal.

The City conducted the community ascertainment and issued an RFRP in June 11, 2002. The City received the Formal Proposal from the cable company on September 11, 2002. The Formal proposal included revisions to Chapter 15.28 of the Municipal Code regulations of cable television systems. The Municipal code changes that were proposed substantially follow the model code provisions proposed by the City. These changes to Chapter 15.28 serve the purpose of updating these provisions. The City Council, on December 10, 2002 made a preliminary determination that the Proposal was inadequate. Pursuant to the requirements of the Federal Cable Act the next step was to establish and begin, at the operator's request, a Formal Administrative Hearing Process. At the end of the hearing process the hearing officer is to make a recommendation to the Council on the issue of renewal or nonrenewable of the franchise.

For a variety of reasons that have been previously reported to the Council, including the Federal court action filed by Comcast to stop the Formal Process, to date the City has not completed the Formal Process. The Formal Process is currently in the discovery phase of the Administrative Hearing before the Hearing Officer. Likewise informal negotiations have not resulted in agreement on a renewal franchise.

ANALYSIS

As discussed in item 3.5 also on this agenda, AB 2987 the State Cable franchise legislation has been passed and will become effective on January 1, 2007. This legislation allows a Cable provider to obtain a State franchise to provide cable services in a community under the terms provided in the

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Act. The new legislation significantly alters the City's ability to meet the needs and interests of the community and presents a dilemma for the City. With the availability of the State franchise for a cable provider, the ability for the City to negotiate a cable franchise on terms more favorable to the community than the terms of the State franchise is very limited. In addition, if the Formal Process was completed and the Process resulted in a denial of the franchise renewal, the state franchise may still be available to Comcast to allow Comcast to provide video services in San Jose.

The language in AB2987 is unclear, but may limit the circumstances under which the City can require the incumbent cable operator operating under an expired franchise to seek a State franchise. The legislation is clear that San Jose could require Comcast to seek a state franchise if a new video provider first met two conditions: 1) the new provider would need to seek a state franchise for its operation; and, 2) the new provider would have to notify the City that it will begin to provide video service in San Jose.

As noted above, the City Council in 2002 made a preliminary determination that the Formal Proposal for Renewal of Cable Franchise proposed by Comcast was inadequate to meet the needs and interests of the community. In light of the new legislation, the City Council should consider its options.

Currently, Comcast continues to operate under the terms and conditions set out in its 1985 franchise. Under the 1985 agreement, the City receives franchise fees equivalent to 5% of gross revenues. However, the definition of gross revenues is not as broadly defined as in newer franchises and excludes categories such as advertising which would increase the amount of Franchise Fees received by the City. Both the state Franchise and the formal proposal submitted by Comcast in 2002 have a broader definition of gross revenues. In addition, the existing franchise includes only minimal dollars and support for Public, Education, and Government (PEG) access, while both the state Franchise and the Formal Proposal are more generous. As compared to the 1985 franchise, the terms and conditions found in the 2002 Formal Proposal and those available through the new state Franchising process are roughly equivalent. A brief description and comparison of the terms of each is attached (Attachment A).

For all of the reasons above, plus the fact that Comcast continues to operate under the terms of the outdated 1985 franchise and the City has limited ability to compel Comcast to seek a state Franchise, we do not believe it is productive to continue to challenge the sufficiency of Comcast's Formal Proposal in the Administrative Hearing, or to reinitiate informal negotiations for renewal of the cable franchise. Instead we believe it is in the best interests of the City to accept the Formal Proposal provided by Comcast in 2002.

Accepting the Formal Proposal, absent an agreement with Comcast on a renewal franchise, is the most expedient way to replace the expired franchise with a franchise containing more favorable terms.

ALTERNATIVES

Rather than taking this action, the City could take no official action at this time and continue to work to obtain clarification of the new state franchise legislation. If the City took this approach, it is

possible that Comcast could continue to operate under the 1985 franchise until the formal process is completed at some undetermined future time.

PUBLIC OUTREACH/INTEREST

There was significant public outreach at the start of the franchise renewal process, which led to the needs and interests identified in the Request for Franchise Renewal Proposal. This outreach included a citywide survey and 15 focus groups with interested stakeholders. The Council Action taken as a result of this recommendation does not trigger any of the criteria below. However, when revenue resulting from this action becomes available in the future to support Public and Education Access programming in San Jose, additional council action will be necessary to formalize the City's relationship with any entity that would manage Public and Education Access in San Jose on behalf of the general educational community and the public.

- Criteria 1:** Requires Council action on the use of public funds equal to \$1 million or greater; **(Required: Website Posting)**
- Criteria 2:** Adoption of a new or revised policy that may have implications for public health, safety, quality of life, or financial/economic vitality of the City. **(Required: E-mail and Website Posting)**
- Criteria 3:** Consideration of proposed changes to service delivery, programs, staffing that may have impacts to community services and have been identified by staff, Council or a Community group that requires special outreach. **(Required: E-mail, Website Posting, Community Meetings, Notice in appropriate newspapers)**

COORDINATION

N/A

COST SUMMARY/IMPLICATIONS

The 2006-2007 Adopted Operating Budget contains franchise fee revenue projections of \$5 million annually from Comcast. Because the new cable franchise broadens the definition of gross revenues on which franchise fees are based, Comcast's annual franchise fee payments to the City would grow by an as yet undefined amount.

As noted above, the new franchise fee will also result in a stream of revenue that could only be used to support Public, Education, and Government Access programming. Additional action by the City Council would be necessary before any action could be taken to use these new dollars.

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FISCAL/POLICY ALIGNMENT

This action is consistent with the City Council's long-standing policy and direction to achieve an upgraded cable system that supports Public, Educational and Community Access programming in San Jose.

BUDGET REFERENCE

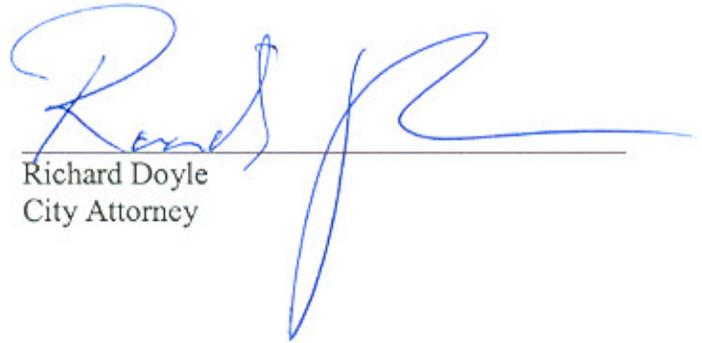
N/A

CEQA

This is not a project.



Les White
City Manager



Richard Doyle
City Attorney

For questions please contact Tom Manheim, Public Outreach Manager, at (408) 535-8170.

Attachment A
Comparison of State Franchise and 2002 Formal Proposal

Franchise Term:

- **State Franchise**
 - 10-year term.
 - State franchise can be terminated by Comcast prior to expiration of term.
- **Comcast Formal Proposal**
 - 10 year term.
 - Comcast can terminate the franchise and obtain a state franchise instead when a state franchise holder such as AT&T notifies to the City that it intends to start providing video service in any part of the City.

Commencement of Franchise:

- **State Franchise**
 - Comcast cannot get state franchise until January 2, 2008.
 - Other companies can state franchise as soon as February, 2007.
- **Comcast Formal Proposal**
 - Franchise effective upon acceptance by Comcast.

Renewal:

- **State Franchise**
 - State franchise can be renewed by PUC for additional 10-year terms.
- **Comcast Formal Proposal**
 - At expiration, Comcast would have the option of either renewing with the City or obtaining a state franchise, if it has not already terminated.

Service Area:

- **State Franchise**
 - No service area requirement.
- **Comcast Formal Proposal**
 - Comcast is required to serve all “residents” in the franchise area.
 - Density and line extension requirements apply in certain areas of the City.

Franchise Fees:

- **State Franchise**
 - 5% of gross revenues (as defined by the statute) paid quarterly.
- **Comcast Formal Proposal**

Attachment A
Comparison of State Franchise and 2002 Formal Proposal

- 5% of gross revenues, as defined in the Cable Ordinance.

Franchise Fee Audits:

- **State Franchise**
 - City may annually audit fee payments.
 - If audit shows franchise fee underpayment of more than 5%, Comcast shall pay reasonable costs of audit.
- **Comcast Formal Proposal**
 - Comcast shall pay reasonable costs of audit if underpayment of more than 5%, or \$100,000, which ever is less.

Initial PEG Channels:

- **State Franchise**
 - State franchise holder shall match the number of channels activated and provided (utilized at least 8 hours a day) under existing local franchise.
- **Comcast Formal Proposal**
 - Comcast will provide (upon completion of rebuild) a minimum of 5 analog channels.

Additional PEG Channels:

- **State Franchise**
 - State franchise holder will provide an additional PEG channel when “non-duplicated locally produced video programming” on a “given channel” exceeds 56 hours per week measured on a quarterly basis.
- **Comcast Formal Proposal**
 - Comcast will provide up to 5 additional analog channels, for a total of 10, and following digital conversion, up to 10 additional digital channels once first 10 have been activated, when, during 16 consecutive weeks, all existing channels designated for the same purpose as the requested channel cablecasts at least 70 hours per week of qualified programming.

Fiber Links for PEG Programming

- **State Franchise**
 - State franchise holder must interconnect with the incumbent cable provider where “technically feasible,” for purposes of providing PEG programming.
 - If no technically feasible interconnection point exists, the holder shall make an interconnection available to City, and shall provide the facilities necessary for the interconnection, at state franchise holder’s costs.

Attachment A
Comparison of State Franchise and 2002 Formal Proposal

- **Comcast Formal Proposal**
 - Comcast will provide fiber link between:
 - Central Access Center and Comcast's headend
 - City Hall and the Central Access Center
 - Comcast will pass through the costs of this fiber construction to subscribers. City will be responsible for all equipment costs.

PEG Funding

- **State Franchise**
 - The City can require all state franchisees will pay 1% of their gross revenues from video services for PEG funding, unless the incumbent cable provider is paying more than 1% under the local franchise on December 31, 2006, in which case, the City can require all state franchisees to match the amount the incumbent is paying, up to 3%.
- **Comcast Formal Proposal**
 - Comcast will pay the City:
 - \$ 2.25 million as an initial capital grant.
 - \$0.43 per sub/per month in ongoing capital PEG support.
 - Using Comcast's projected subscriber count of 175,602, this equates to approximately \$906,106 per year.
 - Total funding of approximately \$11,311,060 over the ten year term.
 - If a competing state franchise holder such as AT&T begins providing service in the City, the City must divide any remaining cash payments for PEG due under the Comcast franchise among both providers, on a pro rata, per subscriber, basis, until all the obligations are satisfied.
 - When all of Comcast's cash payment obligations are satisfied, the City can require all state franchise holders to pay a fee equal to what was required in the Comcast franchise, which, based on Comcast's projected subscriber count, would be approximately 1.13% of gross revenues.

Enforcement of PEG Obligations

- **State Franchise**
 - Courts of competent jurisdiction have "exclusive jurisdiction" to resolve disputes regarding PEG.
 - No franchise termination remedy is available.
- **Comcast Formal Proposal**
 - City has all traditional franchise remedies available, including liquidated damages, revocation, renewal, and transfer approval.

I-Net

Attachment A
Comparison of State Franchise and 2002 Formal Proposal

- **State Franchise**
 - No I-Nets obligations on state franchise holders.
- **Comcast Formal Proposal**
 - Comcast shall provide and maintain:
 - I-Net Backbone fiber
 - I-Net fiber capacity to the neighborhood nodes
 - Fiber construction may be passed through to subscribers based on incremental construction cost standards.
 - City must pay for fiber construction from nodes to the individual sites, charged at Comcast's incremental cost.
 - If Comcast terminates the franchise early and obtains a state franchise, the I-Net obligations continue until the date its franchise would have expired if it had not terminated.

Service/Drops to City and School Facilities:

- **State Franchise**
 - No provisions imposing obligations for drops or service to schools and City buildings.
- **Comcast Formal Proposal**
 - Comcast shall provide free drops and service to public facilities
 - Line extension charges for such facilities that are outside the Universal Service Area where the residential density requirements are not met.
 - If Comcast terminates the franchise early and obtains a state franchise, the I-Net obligation will continue until the date its franchise would have expired if it had not terminated.

Customer Service Obligations:

- **State Franchise:**
 - State franchise holder obligated to comply with state and federal customer service and consumer protection standards.
 - City shall enforce such standards "with respect to complaints received from residents within the jurisdiction."
 - City may not adopt any other customer service standards, and may not enforce any other performance standards.
- **Comcast Formal Proposal**
 - Comcast shall comply with City customer service standards as well as all applicable state and federal standards.

Attachment A
Comparison of State Franchise and 2002 Formal Proposal

Enforcement of Customer Service Obligations:

- **State Franchise**
 - City may impose penalties for material breaches of applicable customer service standards.
 - City shall pay 50% of penalties collected to the state “Digital Divide Account.”
 - Comcast has right to seek court review of any decision to impose penalties.

- **Comcast Formal Proposal**
 - City has all standard franchise remedies, including liquidated damages, revocation, renewal, and transfer approval.
 - City may also impose statutory penalties pursuant to the cable ordinance.

Right-of-Way Management

- **State Franchise**
 - City may manage the “time, place, and manner” of construction of facilities in the rights-of-way.
 - City must approve or deny applications for encroachment permits within 60 days of receiving a completed application.
 - City must provide opportunity to appeal denials of permit applications to the full Council.

- **Comcast Formal Proposal**
 - Comcast will comply with the ROW and construction provisions in the franchise and the cable ordinance.
 - Comcast will comply with future City regulations adapted as part of lawful exercises of the City’s police powers.