

# Putting a Price on Dirt: The Need for Better-Defined Limits on Government Fees for Use of the Public Right-of-Way Under Section 253 of the Telecommunications Act of 1996

Thomas W. Snyder\*

William Fitzsimmons\*\*

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\* Mr. Snyder is a partner in the Denver office of the law firm Kutak Rock LLP and practices in the area of commercial litigation with an emphasis on communications law. He is formerly in-house counsel with Qwest Communications, since acquired by CenturyLink, Inc. He received his B.A. from the University of Colorado and his J.D. from Loyola University Chicago.

\*\* Mr. Fitzsimmons is a Senior Consultant with Charles River Associates with a concentration in the analysis of economic issues related to telecommunications. He received his Ph.D. in Resource Economics from the University of Massachusetts at Amherst. Mr. Fitzsimmons has more than two decades of experience analyzing telecommunications issues, including as an in-house consultant with BellSouth Corporation.

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I. INTRODUCTION

The ubiquitous wires and cables that carry telephone calls to friends, data to the Internet, and communications between offices generally occupy space on poles or in the dirt under streets, which is otherwise known as the public rights-of-way (“PROW”). These cables also carry “wireless” traffic, as communications generally are only wireless for the distance between towers and cell phones, smart phones, or computers. Most of the wireless backhaul and long-haul transport services are provided over cables installed at least partially in the PROW.<sup>1</sup>

Local government units (“LGUs”) have varied widely in their PROW management practices. Many LGUs have recognized that communications are a beneficial service and crucial for economic development, and, thus, they have allowed carriers to occupy the PROW in return for one-time permit charges or similar fees that are limited to recovering the cost of PROW management and maintenance.<sup>2</sup> Other LGUs have seen the

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1. PETER BLUHM & ROBERT LOUBE, *COMPETITIVE ISSUES IN SPECIAL ACCESS MARKETS* (rev. ed. 2009), [http://nrri.org/pubs/telecommunications/NRRI\\_spec\\_access\\_mkts\\_jan09-02.pdf](http://nrri.org/pubs/telecommunications/NRRI_spec_access_mkts_jan09-02.pdf); CRAIG LEDDY, *Cellular Backhaul: Is There Gold in Them Thar Towers?*, LIGHT READING CABLE (Feb. 26, 2010), [http://www.lightreading.com/document.asp?doc\\_id=188451&site=lr\\_cable](http://www.lightreading.com/document.asp?doc_id=188451&site=lr_cable).

2. FCC, *CONNECTING AMERICA: THE NATIONAL BROADBAND PLAN* 1, 131 (2009), <http://download.broadband.gov/plan/national-broadband-plan-chapter-6-infrastructure.pdf> [hereinafter NBP] (relating to Recommendation 6.6). The NBP relies on a comprehensive 2003 study of PROW fees in all states conducted by the National Telecommunications and Information Administration. See *Rights-of-Way Laws by State*, NAT’L TELECOMM. AND INFO.

opportunity for a large and continuous revenue source, and they have used their monopoly control over the PROW to extract large fees that are used to subsidize other LGU services.<sup>3</sup> These revenue-generating fees are often established as annual fees, typically either tied to the total linear feet of PROW occupancy or set as a percentage of a carrier's gross revenue.<sup>4</sup>

In the years before 1996, when local telecommunications essentially was a monopoly industry, carriers generally tolerated revenue-generating fees as a form of indirect taxation on consumers. These carriers either passed the fees through as line items on customer bills or they absorbed the fees but added them as expenses to the rate base, and the fees were then reflected in the carriers' regulated rates. In either case, customers ultimately paid the inflated PROW charge, presumably in lieu of paying higher taxes that otherwise would be necessary to support government services.

Although this arrangement may have been acceptable at the time, two industry-changing events have occurred that have exposed the danger in subsidizing other LGU services with revenue-generating PROW fees. The first is the dramatic increase in competition. Enabled in part by provisions within the Federal Telecommunications Act of 1996 ("FTA"),<sup>5</sup> which required incumbent carriers to lease access to their established networks at regulated rates, competitors have obtained large market shares in voice and Internet services.<sup>6</sup> To the extent that these competitive carriers have leased network facilities from the incumbent carriers, they generally have avoided directly engaging LGUs in PROW arrangements and have avoided many, if not all, of these revenue-generating fees. By continuing to charge revenue-generating fees to the incumbents, LGUs have created an uneven playing

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ADMIN. (May 21, 2003), <http://ntia.doc.gov/ntiahome/staterow/rowtableexcel.htm> [hereinafter NTIA PROW Study]; see NBP, *supra* note 2, at 135 n.34.

3. NBP, *supra* note 2, at 131. For example, the Texas Municipal League reports that "right-of-way rental fees constitute nearly ten percent of many Texas cities' general revenues . . ." *FCC Appoints Task Force to Study Right-of-Way Rental Fees*, TEXAS MUNICIPAL LEAGUE, [http://www.tml.org/leg\\_updates/legis\\_update040610c\\_rightofway.asp](http://www.tml.org/leg_updates/legis_update040610c_rightofway.asp) (last visited Nov. 15, 2011).

4. NBP, *supra* note 2, at 131; see also NTIA PROW Study, *supra* note 2.

5. The Telecommunications Act of 1996, Pub. L. No. 104-104, 110 Stat. 56 (codified at scattered sections of 47 U.S.C.).

6. The FCC reports that, as of the end of 2009, service to approximately thirty percent of the 153,000,000 local telephone lines was provided by competitive providers rather than the incumbents. FCC, LOCAL TELEPHONE COMPETITION: STATUS AS OF DECEMBER 31, 2009, 5 (2011), [http://www.fcc.gov/Daily\\_Releases/Daily\\_Business/2011/db0111/DOC-304054A1.pdf](http://www.fcc.gov/Daily_Releases/Daily_Business/2011/db0111/DOC-304054A1.pdf). Approximately sixty percent of households resided within areas where there were *three or more* available providers of wireline or fixed mobile Internet access services. FCC, INTERNET ACCESS SERVICES: STATUS AS OF DECEMBER 31, 2009, 8 (2010), [http://www.fcc.gov/Daily\\_Releases/Daily\\_Business/2010/db1208/DOC-303405A1.pdf](http://www.fcc.gov/Daily_Releases/Daily_Business/2010/db1208/DOC-303405A1.pdf).

field by forcing certain carriers to pay for inflated cost inputs designed to subsidize other LGU services, while their competitors are often immune. This competitive imbalance threatens the vitality of incumbent carriers and ultimately threatens the deployment of new and advanced services.

The second event is the explosion of broadband Internet use and its ascension to becoming an essential service. The Bush and Obama administrations have established accelerated broadband deployment as a national priority.<sup>7</sup> In furtherance of these goals, the FCC has established numerous policies and aspirations for broadband deployment.<sup>8</sup> To upgrade and build out their networks, carriers naturally need increased access to the PROW. LGUs that seek to subsidize other government services by charging revenue-generating PROW fees are a formidable obstacle to this goal.

Congress recognized the potential for LGUs to use their monopoly power over the PROW to create competitive imbalances and to obstruct network expansion. Congress, therefore, included a provision in the FTA at 47 U.S.C. § 253 (“Section 253”) to preempt certain LGU practices. Section 253(a) preempts any LGU requirement that “*may prohibit or have the effect of prohibiting*”<sup>9</sup> the provision of telecommunications services. Congress included at Section 253(c) a limited exception to preemption, which saves LGU requirements setting “*fair and reasonable compensation...on a competitively neutral and nondiscriminatory basis . . .*”<sup>10</sup> The intent of Sections 253(a) and (c) was to balance the national goals of fostering competition and encouraging deployment of advanced services with the LGU’s historical management interests over the PROW—including the collection of fair and reasonable fees.<sup>11</sup>

As discussed below, many LGUs unfortunately—although not surprisingly—have ignored Section 253 and pressed forward with fee structures based upon localized revenue needs rather than concepts of

7. Declan McCullagh, *Bush: Broadband for the People by 2007*, CNET (Apr. 26, 2004), [http://news.cnet.com/2100-1028\\_3-5200196.html](http://news.cnet.com/2100-1028_3-5200196.html) (“In a speech in Minneapolis on Monday, Bush said ‘every corner’ of the United States should be in reach of high-speed Internet links by 2007.”); John Poirier, *Obama Announces Broadband Grants to Spur Jobs*, REUTERS (Jul. 2, 2010), <http://www.reuters.com/article/2010/07/02/us-obama-broadband-idUSTRE6612KD20100702> (“U.S. President Barack Obama announced on Friday nearly \$800 million in loans and grants for the build-out of broadband networks to reach homes, schools and hospitals.”).

8. See, e.g., NBP, *supra* note 2.

9. 47 U.S.C. § 253(a) (1996) (emphasis added).

10. § 253(c) (emphasis added).

11. See, e.g., Puerto Rico Tel. Co. v. Municipality of Guayanilla, 450 F.3d 9, 15 (1st Cir. 2006) (Section 253 intended to balance interests in competition with LGU management practices); see discussion *infra* Part II.

fairness and reasonability. Equally as unfortunate, the federal courts have inconsistently applied both Sections 253(a) and (c).

With respect to Section 253(a), courts initially closely followed the FCC's 1997 *California Payphone* decision, where the FCC had defined "effect of prohibiting" as a requirement that "materially inhibits or limits the ability of any competitor or potential competitor to compete in a fair and balanced legal and regulatory environment."<sup>12</sup> These courts recognized that a LGU requirement that conditions use of the PROW on payment of revenue-generating fees quite naturally meets this standard. They then analyzed whether the fees were saved as "fair and reasonable compensation" under Section 253(c).<sup>13</sup> More recently, however, the Eighth and Ninth Circuits issued decisions in which they paid lip service to *California Payphone* while they errantly applied a much more stringent standard that essentially demands proof that the LGU requirement *actually* prohibits the provision of services.<sup>14</sup> Under these decisions, a carrier would need to show that the revenue-generating fees actually prevented it from providing services before the courts would analyze whether the fees were "fair and reasonable" under Section 253(c). This actual prohibition standard under Section 253(a) reduces Section 253 to a toothless standard in these circuits, imposing no practical limit and allowing LGUs to hold the PROW hostage to extract exorbitant rates.

With respect to Section 253(c), courts have continuously struggled over the definition of "fair and reasonable compensation." Some courts have required fees to be limited to PROW management costs or at least to be related to management costs.<sup>15</sup> Other courts have allowed for a "fair market value" element for the PROW to be included in the fee, but they have done so without explaining what an appropriate value methodology would be other than determining the highest dollar amount that carriers are willing to pay.<sup>16</sup> No court has engaged in a serious economic analysis as to whether the PROW was a *scarce resource* that generates any value in a

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12. California Payphone Ass'n, *Memorandum Opinion and Order*, 12 F.C.C.R. 14191, para. 31 (1997) [hereinafter *California Payphone*] (emphasis added).

13. See e.g., *XO Missouri, Inc. v. City of Maryland Heights*, 256 F. Supp. 2d 987, 994–95 (E.D. Mo. 2003); *New Jersey Payphone Ass'n, Inc. v. Town of West New York*, 130 F. Supp. 2d 631, 638 (D.N.J. 2001), *aff'd*, 299 F.3d 235 (3d Cir. 2002); *Bell Atlantic-Maryland, Inc. v. Prince George's Cnty*, 49 F. Supp. 2d 805, 817 (D. Md. 1999), *vacated on other grounds*, 212 F.3d 863 (4th Cir. 2000); *AT&T Communications of the Southwest, Inc. v. City of Dallas*, 8 F. Supp. 2d 582, 593 (N.D. Tex. 1998). See discussion *infra* Part II.B.

14. See *Sprint Telephony PCS, L.P. v. County of San Diego*, 543 F.3d 571 (9th Cir. 2008), *cert denied*, 129 S. Ct. 2860 (2009); *Level 3 Communications, LLC v. City of St. Louis*, 477 F.3d 528 (8th Cir. 2007). See discussion *infra* Part II.C-D.

15. See discussion *infra* Part II.B.

16. *Id.*

competitive market. The result of these inconsistent decisions has created uncertainty both for carriers and LGUs.

The FCC now has an opportunity to end these inconsistent interpretations and restore Section 253 to its rightful role in the process of ensuring a fair field of play for all competitors. As part of the America Recovery and Reinvestment Act of 2009, Congress directed the FCC to develop a plan with the goal of ensuring that “all people of the united states [sic] have access to broadband capability . . . .”<sup>17</sup> On March 16, 2010, the FCC issued its “National Broadband Plan” (“NBP”),<sup>18</sup> in which it set forth a comprehensive plan for accelerated broadband deployment. Among other things, the FCC acknowledged in the NBP that “[t]he cost of deploying a broadband network depends significantly on the costs that service providers incur to access conduits, ducts, poles and rights-of-way on public and private lands.”<sup>19</sup> The FCC estimated that “[c]ollectively, the expense of obtaining permits and leasing pole attachments and rights-of-way can amount to 20% of the cost of fiber optic deployment.”<sup>20</sup> The FCC further acknowledged that “[s]ecuring rights to [PROW] is often a difficult and time-consuming process that discourages private investment.”<sup>21</sup> To streamline this process, the FCC stated that LGUs “should take steps to improve utilization of existing infrastructure to ensure that network providers have easier access to poles, conduits, ducts and rights-of-way.”<sup>22</sup> The FCC recognized that “there are [already] limits to state and local policies; Section 253 of the [FTA] prohibits state and local policies that impede the provision of telecommunications services while allowing for rights-of-way management practices that are nondiscriminatory, competitively neutral, fair and reasonable.”<sup>23</sup> The FCC also acknowledged, however, that “disputes under Section 253 have lingered for years, both before the FCC and in federal district courts.”<sup>24</sup> Based on this proliferation of disputes, the FCC on April 7, 2011 issued a *Notice of Inquiry* focused on PROW issues (“*PROW NOI*”).<sup>25</sup> The *PROW NOI* seeks comments on

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17. American Recovery and Reinvestment Act of 2009, Pub. L. No. 111-5, § 6001(k)(2), 123 Stat. 115, 516 (2009).

18. See NBP, *supra* note 2.

19. *Id.* at 127 (footnote omitted).

20. *Id.* (footnote omitted).

21. *Id.*

22. *Id.*

23. *Id.* at 131.

24. *Id.* (footnote omitted).

25. Acceleration of Broadband Deployment: Expanding the Reach and Reducing the Cost of Broadband Deployment by Improving Policies Regarding Public Rights of Way and Wireless Facilities Siting, *Notice of Inquiry*, WC Docket No. 11-59 (2011) [hereinafter *PROW NOI*].

methods by which to improve PROW access, including a method by which to set reasonable charges.<sup>26</sup> The FCC stated that the *PROW NOI* “is a necessary step towards determining whether there is a need for coordinated national action to improve rights of way and wireless facilities siting policies, and, if so, what role the [FCC] should play in conjunction with other stakeholders.”<sup>27</sup>

This Article calls on the FCC to use the *PROW NOI* as an opportunity to state a uniform standard for application of Sections 253(a) and (c). As the agency charged with implementation, the FCC clearly is empowered to issue regulations and interpretative decisions under the FTA, which it has done on many occasions.<sup>28</sup> The FCC can use the *PROW NOI* either to serve as a formal rulemaking or as a forum in which it can issue guidance for Section 253 standards. Indeed, in a recent amicus curiae filing with the Supreme Court, the FCC recognized the inconsistent application of Section 253 and vowed to bring harmony to these decisions by issuing authoritative rulings when the opportunity arose.<sup>29</sup> It now has that opportunity.

Part II of this Article traces the enactment and inconsistent application of Section 253, and it explains the faults in the analyses undertaken by some of these courts. Part III of this Article explains why—based on these inconsistent court decisions—it is important and necessary for the FCC to reconfirm its *California Payphone* standard for showing an “effect of prohibiting” under Section 253(a), and to then make clear that a requirement meets this standard if it conditions use of the PROW on the payment of revenue-generating fees. This would remove the focus from the impact that PROW fees have on a particular carrier—which is a subjective

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26. The *PROW NOI* specifically identifies six categories for consideration: (1) timeliness and ease of the permitting process; (2) the reasonableness of charges; (3) the extent to which ordinances or statutes have been updated to reflect current communications technologies or innovative deployment practices; (4) consistent or discriminatory/differential treatment; (5) presence or absence of uniformity due to inconsistent or varying practices and rates in different jurisdictions or areas; and (6) other rights of way concerns including “third tier” regulation or requirements that cover matters not directly related to rights of way use or wireless facilities siting. *Id.* at paras. 12–33.

27. *Id.* at para. 9.

28. The FCC includes on its website a chart that (although out-of-date) describes the various rulemakings and other proceedings it has undertaken to implement the FTA. FCC, DRAFT FCC IMPLEMENTATION SCHEDULE FOR THE TELECOMMUNICATIONS ACT OF 1996 (1997), available at <http://transition.fcc.gov/Reports/implsched.html>. Although the FCC issued guidelines once before concerning the enforcement of Section 253, the guidelines did not address the issues raised in this Article. See Suggested Guidelines for Petitions for Ruling under Section 253 of the Communications Act, *Public Notice*, 13 F.C.C.R. 22970 (1998). Further, the FCC specifically proposed issuing rules as a potential remedy in response to issues raised in the *NOI. PROW NOI*, *supra* note 25, para. 10.

29. See *infra* Part II.C.

factor that varies based on the size and economic efficiency of the carrier—and would place the focus on whether the fee is objectively “fair and reasonable compensation” under Section 253(c). Part IV then explains why it is important and necessary for the FCC to also clarify that “fair and reasonable compensation” under Section 253(c) means payment for management costs plus the price LGUs could charge if the PROW space were offered in competitive markets. This would return sound economic principles to determining a PROW fee rather than allowing courts to continue to rely simply on the highest dollar amount carriers are willing to pay, which is the cornerstone of monopoly pricing and clearly is not within the “fair and reasonable compensation” component of Section 253(c).

## II. SECTION 253 AND CASES DECIDED THEREUNDER

### A. *Enactment of Section 253*

The goals of the FTA are expressed in its formal title as follows: “An Act [t]o promote competition and reduce regulation in order to secure lower prices and higher quality services for American telecommunications consumers and encourage the rapid deployment of new telecommunications technologies.”<sup>30</sup> To accomplish these goals, Congress included provisions in the FTA at 47 U.S.C. §§ 251–52 that require incumbent local exchange carriers to interconnect and to lease unbundled elements of their networks to competing providers in order to allow these providers to offer competitive services without having to replicate the incumbent networks in their entirety.<sup>31</sup> The Supreme Court characterized the FTA as a procompetitive act designed to end local monopolies by opening up the incumbents’ networks:

Until the 1990's, local phone service was thought to be a natural monopoly. States typically granted an exclusive franchise in each local service area to a local exchange carrier (LEC), which owned, among other things, the local loops (wires connecting telephones to switches), the switches (equipment directing calls to their destinations), and the transport trunks (wires carrying calls between switches) that constitute a local exchange network. Technological advances, however, have made competition among multiple providers of local service seem

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30. Telecommunications Act of 1996, Pub. L. No. 104-104, 110 Stat. 56 (codified at scattered sections of 47 U.S.C.).

31. See *AT&T Comm., Inc. v. City of Dallas*, 8 F. Supp. 2d 582, 586 (N.D. Tex. 1998). For a comprehensive article discussing the purpose and progress in implementing Sections 251 and 252, see Roy E. Hoffinger, “Cooperative Federalism” *Gone Wrong: The Implementation of the Telecommunications Act of 1996*, 2 J. TELECOMM. & HIGH TECH. L. 375 (2003).



possible, and Congress recently ended the longstanding regime of state-sanctioned monopolies.<sup>32</sup>

Congress recognized that the interconnection and unbundling obligations in Sections 251 and 252 were of little value if LGUs could use their historical monopoly power over the PROW to impede competition within the telecommunications market and the deployment of advanced services by all.<sup>33</sup> It, therefore, included Section 253, which preempts certain LGU actions with respect to regulation of carriers and their use of the PROW. Section 253 states in relevant part:

(a) In General

No State or local statute or regulation, or other State or local legal requirement, may prohibit or have the effect of prohibiting the ability of any entity to provide any interstate or intrastate telecommunications service . . . .

(c) State and Local Government Authority

Nothing in this section affects the authority of a State or local government to manage the public rights-of-way or to require fair and reasonable compensation from telecommunications providers, on a competitively neutral and nondiscriminatory basis, for use of public rights-of-way on a nondiscriminatory basis, if the compensation required is publicly disclosed by such government.<sup>34</sup>

The legislative history of Section 253 reveals that it was intended to have a broad preemptive scope and reserve very limited PROW management

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32. *AT&T Corp. v. Iowa Utils. Bd.*, 525 U.S. 366, 371 (1999). The Court further stated that the intent of the FTA was to take “the regulation of local telecommunications competition away from the States.” *Id.* at 378 n.6. *See also* *Reno v. ACLU*, 521 U.S. 844, 857 (1997) (explaining that the FTA was “an unusually important legislative enactment” that has changed the landscape of telecommunications regulation).

33. *See, e.g.*, Petition of Minnesota, *Memorandum Opinion and Order*, 14 F.C.C.R. 21697, para. 9 (1999) (Section 253 “is designed to ensure that state and/or local authorities cannot frustrate the [FTA’s] explicit goal of opening all markets to competition.”); Pub. Util. Comm’n of Texas, *Memorandum Opinion and Order*, 13 F.C.C.R. 3460, para. 23 (1997) (“Sections 251 and 252 complement and supplement Section 253 by removing operational and economic barriers to entering the local market.”); *see also AT&T Comm., Inc.*, 8 F. Supp. 2d at 591 (“Congress’s intent was to remove all barriers to entry in the provision of telecommunications services by preempting all state and local legal requirements that directly or indirectly prohibit market entry.”).

34. Telecommunications Act, 47 U.S.C. § 253(a), (c). Section 253(b), which is omitted from above, provides, “Nothing in this section shall affect the ability of a State to impose, on a competitively neutral basis and consistent with section 254, requirements necessary to preserve and advance universal service, protect the public safety and welfare, ensure the continued quality of telecommunications services, and safeguard the rights of consumers.” *Id.* at § 253(b). This provision was intended to preserve the rights of state utility commissions in areas of historical concern and, because it only applies to states, it is rarely invoked in Section 253 cases challenging LGU PROW provisions. Section 253(b) would only arise in a challenge to an LGU PROW regulation if “a state specifically delegated the state authority to its local governments.” *Bellsouth Telecomms., Inc. v. City of Coral Springs*, 42 F. Supp. 2d 1304, 1307 (S.D. Fla. 1999).

activities for local governments. Senator Gorton in his comments said that Section 253 is a “very, very broad prohibition against state and local” regulations of telecommunications companies.<sup>35</sup> Senator Feinstein in her comments offered specific examples of the types of limited restrictions that Congress intended to permit under Section 253(c), including:

- (1) Regulat[ing] the time or location of excavation to preserve effective traffic-flow, prevent hazardous road conditions, or minimize noise impacts; . . .
- (4) Requir[ing] a company to place its facilities underground, rather than overhead, consistent with the requirements imposed on other utility companies; . . .
- (6) Requir[ing] a company to pay fees to recover an appropriate share of the increased street repair and paving costs that result from repeated excavation; . . .
- (8) Enforc[ing] local zoning regulations; and
- (9) Requir[ing] a company to indemnify the City against any claims of injury arising from the company's excavation.<sup>36</sup>

#### B. *Initial Decisions Under Section 253*

Shortly after the FTA's enactment, the FCC in 1997 issued its decision in *California Payphone*,<sup>37</sup> in which the FCC examined a local ordinance that prevented payphone providers from installing outdoor payphones on private property in a particular area, while permitting the installation of payphones indoors on private property and outdoors on public rights-of-way.<sup>38</sup> The FCC examined whether the ordinance “‘ha[d] the effect of prohibiting’ the ability of any entity to provide payphone service in [the relevant area].”<sup>39</sup> In answering that question, the FCC established the test for “effective prohibition” under Section 253(a) by stating that a local regulation effectively prohibits the provision of a telecommunication service if it “*materially inhibits or limits* the ability of any competitor or potential competitor to compete in a fair and balanced legal and regulatory environment.”<sup>40</sup> The FCC concluded that, in light of

35. 141 CONG. REC. S8212 (daily ed. June 13, 1995) (statement of Sen. Gorton).

36. 141 CONG. REC. S8172 (daily ed. June 12, 1995) (statement of Sen. Feinstein, quoting letter from the Office of City Attorney, City and County of San Francisco).

37. *California Payphone*, *supra* note 12.

38. *See id.* at para. 28.

39. *Id.* at para. 31.

40. *Id.* (emphasis added). The FCC soon reiterated this standard. *See* Pub. Util. Comm'n. of Texas, *Memorandum Opinion and Order*, 13 F.C.C.R. 3460, para. 22 (1997); TCI Cablevision of Oakland Cnty., Inc., *Memorandum Opinion and Order*, 12 F.C.C.R. 21396, para. 98 (1997).

the options available to payphone providers in the area in question and the absence of proof that these other options were less economical, the ordinance did not prohibit payphone providers from providing service in the area.<sup>41</sup>

Federal courts soon were confronted with challenges to local PROW practices following *California Payphone*.<sup>42</sup> These courts settled on a two-step analysis when considering federal preemption under Section 253: (1) determine whether the local provision is prohibitory under Section 253(a); and (2) if so, determine whether the LGU has met its burden of showing that the fees are fair and reasonable under Section 253(c).<sup>43</sup> Courts were clear that a regulation “need not erect an absolute barrier to entry in order to be found prohibitive.”<sup>44</sup> Applying this framework, courts initially preempted a broad array of franchise fees and other excessive PROW charges on telecommunications carriers. This included decisions issued by the Northern District of Texas in *AT&T Communications of the Southwest, Inc. v. City of Dallas* (preempting four percent gross revenue fee),<sup>45</sup> the District of New Jersey in *N.J. Payphone Ass’n, Inc. v. Town of West New York* (preempting fee based on highest bids submitted for exclusive PROW use),<sup>46</sup> and the Eastern District of Missouri in *XO Missouri, Inc. v. City of Maryland Heights* (preempting five percent gross revenue fee).<sup>47</sup> Several of

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41. *California Payphone*, *supra* note 12, at para. 31.

42. These claims initially were presented under both the Constitution’s Supremacy Clause and 42 U.S.C. § 1983, which provides the vehicle for a private right of action. The majority of courts now hold, however, that there is no private right of action under Section 253 and that the Supremacy Clause provides the exclusive vehicle for recourse in federal court. *See, e.g.*, *NEXTG Networks of NY, Inc. v. City of New York*, 513 F.3d 49, 52 (2d Cir. 2008); *Sw. Bell Tel., LP v. City of Houston*, 529 F.3d 257, 262 (5th Cir. 2008); *Sprint Telephony PCS, L.P. v. County of San Diego*, 490 F.3d 700, 716–18 (9th Cir. 2007), *aff’d en banc*, 543 F.3d 571 (9th Cir. 2008), *cert. denied*, 129 S. Ct. 2860 (2009); *Qwest Corp. v. City of Santa Fe*, 380 F.3d 1258, 1265–67 (10th Cir. 2004).

43. *See, e.g.*, *Puerto Rico Tel. Co. v. Municipality of Guayanilla*, 450 F.3d 9, 15–16 (1st Cir. 2006); *City of Santa Fe*, 380 F.3d at 1269; *Qwest Corp. v. Elephant Butte Irrigation Dist.*, 616 F. Supp. 2d 1110, 1118 (D.N.M. 2008); *New Jersey Payphone Ass’n, Inc. v. Town of West New York*, 130 F. Supp. 2d 631, 636 (D.N.J. 2001); *see also* *Petition of Minnesota, Memorandum Opinion and Order*, 14 F.C.C.R. 21697, 21704 n.26 (1999) (“Although the party seeking preemption bears the burden of proof that there is a violation of section 253(a), the burden of proving a statute, regulation, or legal requirement comes within the exemptions found in sections 253(b) and (c) falls on the party claiming the exception applies.”).

44. *City of Santa Fe*, 380 F.3d at 1269; *see also* *RT Comm., Inc. v. FCC*, 201 F.3d 1264, 1268–69 (10th Cir. 2000) (the challenged regulation need not be “insurmountable” to be preempted); *Puerto Rico Tel. Co.*, 450 F.3d at 18; *TCG New York, Inc. v. City of White Plains*, 305 F.3d 67, 76 (2d Cir. 2002) (citation omitted).

45. 8 F. Supp. 2d 582, 593 (N.D. Tex. 1998).

46. 130 F. Supp. 2d 631, 638 (D.N.J. 2001), *aff’d*, 299 F.3d 235 (3d Cir. 2002).

47. 256 F. Supp. 2d 987, 994–95 (E.D. Mo. 2003); *see also* *Qwest Comm. Corp. v. City*

these more significant decisions concerning PROW fees are discussed below.<sup>48</sup>

In *Bell Atlantic-Maryland, Inc. v. Prince George's County*,<sup>49</sup> a U.S. District Court invalidated a three percent gross revenue franchise fee requirement as an impermissible "revenue-raising measure[]." <sup>50</sup> The court began by stating that the franchise fee requirement, in combination with other nonfee provisions, was effectively prohibitive under Section 253(a) because the provisions created a substantial barrier to entry in the relevant market.<sup>51</sup> Turning to the "fair and reasonable" compensation analysis under Section 253(c), the court noted that

[i]f local governments were permitted . . . to charge franchise fees that were unrelated either to a telecommunications company's use of the public rights-of-ways or to a local government's costs of maintaining and improving its rights-of-way, then local governments could effectively thwart the FTA's<sup>52</sup> pro-competition mandate and make a nullity out of section 253(a).

The court stated that "the proper benchmark is the cost to the County of maintaining and improving the [PROW] that [the carrier] actually uses. Furthermore, to be 'fair and reasonable,' these costs must be apportioned to [the carrier] based on its degree of use, not its overall level of profitability."<sup>53</sup> The court concluded that, "[s]ince nothing in the ordinance indicates that the County set the level of its 'right-of-way charge' based on these two factors, the 'right-of-way charge' violates the FTA."<sup>54</sup>

Shortly thereafter, the Sixth Circuit issued a seemingly contradictory and much-criticized opinion in *TCG Detroit v. City of Dearborn*.<sup>55</sup> There the new entrant carrier challenged a requirement that it pay a four percent

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of Berkeley, 146 F. Supp.2d 1081, 1100 (N.D. Cal. 2001) ("Fees charged against telecommunications carriers must be directly related to the carrier's actual use of the local rights-of-way."). *But see* City of Portland v. Elec. Lightwave, Inc., 452 F. Supp. 2d 1049, 1073-75 (D. Or. 2005) (upholding five percent gross revenue fee under Section 253).

48. Although a discussion of such cases is beyond the scope of this article, it is worth noting that several state and federal courts have held that excessive franchise fees constitute taxes under state laws and must be enacted in accordance with tax legislation procedures. *See, e.g.*, Diginet, Inc. v. Western Union ATS, Inc., 958 F.2d 1388, 1400 (7th Cir. 1992); Montana-Dakota Utils. Co. v. City of Billings, 80 P.3d 1247 (Mont. 2003); City of Hawarden v. US West Comm., Inc., 590 N.W.2d 504 (Iowa 1999); AT&T Co. v. Village of Arlington Heights, 620 N.E.2d 1040 (Ill. 1993).

49. 49 F. Supp. 2d 805, 817 (D. Md. 1999), *vacated on other grounds*, 212 F.3d 863 (4th Cir. 2000).

50. *Id.*

51. *Id.* at 814-15.

52. *Id.* at 817.

53. *Id.* at 818.

54. *Id.* at 818-19.

55. 206 F.3d 618 (6th Cir. 2000).

gross revenue franchise fee in circumstances where the incumbent was immune from such fees under state law. Contrary to the consensus view that Section 253(a) provided the basis for an action with Section 253(c) being a safe harbor, the Sixth Circuit concluded that each section provided an individual cause of action.<sup>56</sup> The court, thus, started by analyzing whether the fee was “fair and reasonable” under Section 253(c). With little analysis, the Sixth Circuit held that the “totality of the circumstances” supported the district court’s conclusion that the four percent charge was fair and reasonable considering the amount of the PROW use contemplated (twenty-seven miles), the amount that other providers would be willing to pay, and what the carrier had agreed to pay in other jurisdictions.<sup>57</sup> The court further said that the immunity of the incumbent to the fee did not make it discriminatory absent proof that the incumbent was able to leverage this freedom into a competitive advantage.<sup>58</sup> The Sixth Circuit concluded that, once demonstrated to be fair, reasonable, and nondiscriminatory under Section 253(c), the fee by definition could not be prohibitive under Section 253(a).<sup>59</sup>

As noted, *City of Dearborn* was quickly criticized by other courts. In *TCG New York, Inc. v. City of White Plains*,<sup>60</sup> the Second Circuit analyzed a challenge to an LGU requirement for a five percent gross revenue requirement on new entrants, where the incumbent once again enjoyed immunity under state law. The Second Circuit adopted the FCC’s *California Payphone* “effect of prohibiting” standard, and then, contrary to the holding in *City of Dearborn*, it held that the combination of the fee and other nonfee provisions of the franchise ordinance at issue were prohibitory under Section 253(a).<sup>61</sup> With respect to Section 253(c), the Second Circuit recognized that there was not a consensus on whether PROW fees should be cost-based or viewed under the “totality of the circumstances,” so it chose to avoid that issue by analyzing the discriminatory nature of the fee.<sup>62</sup> Rejecting *City of Dearborn*, the Second Circuit held that discriminatory application of the franchise fee was per se in conflict with

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56. *Id.* at 622–24. No court has agreed with *City of Dearborn* that Section 253(c) provides an independent basis for action. *See, e.g.,* Level 3 Comm., LLC v. City of St. Louis, 477 F.3d 528 (8th Cir. 2007), *cert. denied*, 129 S. Ct. 2859 (2009); BellSouth Telecomms., Inc. v. Town of Palm Beach, 252 F.3d 1169, 1187–89 (11th Cir. 2001). The federal government, including the FCC, has similarly stated that this part of the *City of Dearborn* holding was in error. *St. Louis Amicus Brief*; *see infra* note 95, at 19.

57. *City of Dearborn*, 206 F.3d at 624–25.

58. *Id.* at 625.

59. *Id.*

60. 305 F.3d 67 (2d Cir. 2002).

61. *Id.* at 76–77.

62. *Id.* at 79.

Section 253(c). The court stated that “the Sixth Circuit’s statement [in *City of Dearborn*] that [the carrier] failed to show that [the incumbent] was undercutting its competitors and creating a barrier to entry misses the point that fees that exempt one competitor are inherently not ‘competitively neutral,’ regardless of how that competitor uses its resulting market advantage.”<sup>63</sup> Indeed, courts since *City of White Plains* have consistently struck down PROW fees that are discriminatorily applied.<sup>64</sup>

In *Qwest Corp. v. City of Santa Fe*,<sup>65</sup> the Tenth Circuit struck down an appraisal/lease fee structure that had purported to capture the PROW’s fair market value. In that case, the LGU required carriers seeking PROW permits to obtain an appraisal for the specific PROW from an LGU-approved agent and then, based on this appraisal, to pay an annual rental fee. While this method might have been consistent with Section 253 if applied using sound economic principles (as outlined below), the initial permit request yielded an appraisal of a \$6,000 annual rental rate for a single twelve-by-eighteen foot concrete pad.<sup>66</sup> Applying the *California Payphone* standard, the Tenth Circuit found that, if this fee were similarly applied throughout the LGU, the appraisal/lease system would represent a “massive increase” in PROW fees, which the court concluded was sufficient to demonstrate an effective prohibition under Section 253(a).<sup>67</sup> Analyzing the fees under Section 253(c), the Tenth Circuit noted that there was a split of authority between whether PROW fees must be cost-based or subject to the “totality of the circumstances” test in *City of Dearborn*.<sup>68</sup> The court stated that it did not have to decide the appropriate standard, because the structure failed both tests—the LGU admitted the fees were not cost-based, and the LGU failed to consider “the extent of the use contemplated, the amount other telecommunications providers would be willing to pay, and the impact on the profitability of the business.”<sup>69</sup>

In *Puerto Rico Telephone Co. v. Municipality of Guayanilla*,<sup>70</sup> the First Circuit issued a comprehensive decision in which it invalidated a five percent fee on gross revenues. In that case, the First Circuit examined both

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63. *Id.* at 80.

64. *See e.g.*, *Qwest Comm. Corp. v. City of New York*, 387 F. Supp. 2d 191, 194 (E.D.N.Y. 2005); *Montgomery Cnty. v. Metromedia Fiber Network, Inc.*, 326 B.R. 483, 494 (S.D.N.Y. 2005); *Silver Star Tel. Co., Inc., Memorandum Opinion and Order*, 13 F.C.C.R. 16356, para. 10 (1998).

65. 380 F.3d 1258 (10th Cir. 2004).

66. *Id.* at 1270–71.

67. *Id.* at 1271.

68. *Id.* at 1272.

69. *Id.* (citing *TCG Detroit v. City of Dearborn*, 206 F.3d 618, 625 (6th Cir. 2000)).

70. 450 F.3d 9 (1st Cir. 2006).

the impact that the fee would have on the carrier's operations within the municipality and the impact it would have on the operations of the carrier across the commonwealth if the fee were adopted by every other franchising authority in Puerto Rico. The court stated:

Given the interconnected nature of utility services across communities and the strain that the enactment of gross revenue fees in multiple municipalities would have on [the carrier's] provision of services, the Commonwealth-wide estimates are relevant to determining how the ordinance affects [the carrier's] "ability . . . to provide any interstate or intrastate telecommunications service."<sup>71</sup>

Applying the *California Payphone* standard, the court held that the five percent franchise fee was effectively prohibitive under Section 253(a) because it would "negatively affect [the carrier's] profitability;" give rise to "a substantial increase in costs for [the carrier];" and "place a significant burden on [the carrier]," thereby "strain[ing the carrier's] ability to provide telecommunications services."<sup>72</sup>

Turning to Section 253(c), the First Circuit recognized that courts had varied on whether Section 253(c) required fees to be limited to LGU cost recovery, but the court said it need not decide the issue because it agreed with the district court's reasoning that "fees should be, at the very least, *related* to the actual use of rights of way and that 'the costs [of maintaining those rights of way] are an essential part of the equation.'"<sup>73</sup> The First Circuit rejected the LGU's argument that the gross revenue structure was a per se appropriate measure for PROW use stating:

There are two problems with this argument. First, the appellants concede that the 5% fee applies to the entire revenue derived from calls that use *any* portion of the rights of way, regardless of whether the call traverses over one inch or 100 feet of the public rights of way. Thus, the fee charged does not directly relate to the extent of actual use of public rights of way. Second, the appellants provide no rationale for why it is "fair and reasonable" for the Municipality to charge 5%, as opposed to another percentage, of the revenue generated from these calls. The appellants provide no information or estimates regarding the amount of fees that they expect to collect through the ordinance.<sup>74</sup>

Although the First Circuit concluded that even under the "totality of the circumstances" the challenged ordinance would fail, it also rejected the *City of Dearborn* test under Section 253(c).<sup>75</sup>

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71. *Id.* at 17 (quoting Section 253(a)).

72. *Id.* at 18–19.

73. *Id.* at 22 (quoting *Puerto Rico Tel. Co.*, 354 F. Supp. 2d at 114 (brackets in original)).

74. *Id.* at 22.

75. *Id.*

C. *Eighth Circuit Decision in City of St. Louis and Ninth Circuit Decision in County of San Diego*

The Eighth and Ninth Circuits recently adopted their own standard under Section 253(a) in which they essentially required carriers to show that it is impossible to comply with the challenged requirement and still provide service. This was a stark departure from prior decisions, particularly within the Ninth Circuit. Indeed, in its very first Section 253 case, *City of Auburn v. Qwest Corp.*,<sup>76</sup> the court struck down a host of municipal regulations unrelated to management of the PROW, including excessive application fees. The court specifically held that the “fees charged under the franchise agreements are not based on the costs of maintaining the right of way, as required under the [FTA].”<sup>77</sup> The Ninth Circuit modified this holding in *Qwest Communications Inc. v. City of Berkeley*,<sup>78</sup> wherein it qualified that all non-cost-based fees were not automatically preempted but instead must be examined in the context of the regulation as a whole.<sup>79</sup> Nevertheless the court still preempted the beyond-cost permit fee at issue because the LGU’s only justification was that carriers could be excused from paying if they submitted to a comprehensive procedure to determine whether they qualified as a common carrier.<sup>80</sup>

It was not until its decision in *Sprint Telephony PCS, L.P. v. County of San Diego*<sup>81</sup> that the Ninth Circuit applied a different Section 253(a) standard. In that case, the full panel of the Ninth Circuit reversed decisions by the district court and appellate panel that had held an ordinance placing various requirements on the placement, camouflage, and maintenance of wireless transmission towers violated Section 253(a). As a precursor to its decision, the Ninth Circuit claimed that the panel in *City of Auburn* had twisted the words of Section 253(a) by improperly inserting an ellipses into the phrase, “No State or local statute or regulation, or other State or local legal requirement, may prohibit or have the effect of prohibiting the ability of any entity to provide any interstate or intrastate telecommunications service,” so that it read, “No State or local statute or regulation, or other State or local legal requirement, *may . . . have the effect of prohibiting* the ability of any entity to provide any interstate or intrastate

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76. 260 F.3d 1160 (9th Cir. 2001), *overruled by* *Sprint Telephony PCS, L.P. v. County of San Diego*, 543 F.3d 571 (9th Cir. 2008).

77. *Id.* at 1176.

78. 433 F.3d 1253 (9th Cir. 2006).

79. *Id.* at 1257.

80. *Id.* at 1257–58.

81. 543 F.3d 571 (9th Cir. 2008), *cert denied*, 129 S. Ct. 2860 (2009).



telecommunications service.”<sup>82</sup> The Ninth Circuit claimed that, by inserting this ellipses, the *City of Auburn* panel allowed for the word “may” to modify the term “have the effect of prohibiting,” and, thus, had allowed for preemption of regulations based on speculation that the regulation “might possibly” prohibit services.<sup>83</sup> The court stated that this was improper and that the phrase “effect of prohibiting” required proof of “actual or effective prohibition” of a telecommunications service.<sup>84</sup>

Up to this point, the Ninth Circuit’s analysis was not inconsistent with *California Payphone*. Indeed, the FCC in *California Payphone* had initially stated the truism that Section 253(a) required a showing of an actual or effective prohibition of service.<sup>85</sup> The FCC also had not allowed for a regulation to be preempted based on the “mere possibility” of an effective prohibition (although the Ninth Circuit’s claim that *City of Auburn* and other courts had based their holdings on the “mere possibility” of a prohibition is incorrect, as discussed below). The FCC instead held in *California Payphone* that an effective prohibition would be found if the requirement “materially inhibits or limits the ability of any competitor or potential competitor to compete in a fair and balanced legal and regulatory environment.”<sup>86</sup> The Ninth Circuit acknowledged that *California Payphone* set forth the proper Section 253(a) standard.<sup>87</sup>

For reasons unexplained, however, the Ninth Circuit in *County of San Diego* then refused to apply *California Payphone* and failed to analyze whether the ordinance at issue materially inhibited or limited the ability of the carrier to compete in a fair and balanced legal and regulatory environment. The court instead simply held that, although the ordinance heavily regulated placement and design of wireless towers, it did not specifically “prohibit[] the construction of sufficient facilities to provide wireless services to the County of San Diego.”<sup>88</sup> Because there was not an *actual prohibition* on the construction of sufficient facilities to provide services in the county, the Ninth Circuit held that the ordinance was not effectively prohibitive under Section 253(a). If its holding were not enough

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82. *Id.* at 576 (citing *City of Auburn v. Qwest Corp.*, 260 F.3d 1160, 1175 (9th Cir. 2001)) (emphasis added).

83. *Id.* at 577–78. As noted by the Ninth Circuit, the “may . . . have the effect of prohibiting” standard was initially crafted by the Maryland District Court in *Bell Atlantic-Maryland, Inc. v. Prince George’s County*. *Id.* at 576 (citing *Bell Atl.-Md., Inc. v. Prince George’s Cnty.*, 49 F. Supp. 2d 805, 814 (D. Md. 1999)).

84. *Id.* at 578.

85. *California Payphone*, *supra* note 12, at para. 38.

86. *Id.* at para. 31.

87. *County of San Diego*, 543 F.3d at 578.

88. *Id.* at 579–80.

to demonstrate that it was now requiring an actual prohibition to be shown under Section 253(a), the Ninth Circuit went on to list examples of the very limited regulations that might possibly still be prohibitive under Section 253(a):

If an ordinance required, for instance, that all facilities be underground and the plaintiff introduced evidence that, to operate, wireless facilities must be above ground, the ordinance would effectively prohibit it from providing services. Or, if an ordinance mandated that no wireless facilities be located within one mile of a road, a plaintiff could show that, because of the number and location of roads, the rule constituted an effective prohibition. We have held previously that rules effecting a “significant gap” in service coverage could amount to an effective prohibition . . . and we have no reason to question that holding today.<sup>89</sup>

The Eighth Circuit employed an almost identical analysis in applying a similarly narrow interpretation of Section 253(a) in *Level 3 Communications, LLC v. City of St. Louis*.<sup>90</sup> The challenged LGU requirement in this case was for payment of various levels of linear foot charges for use of the PROW. Like the Ninth Circuit, the Eighth Circuit stated that it considered prior decisions as having incorrectly applied a liberal interpretation of Section 253(a) based on the word “may” in the statute, which it said allowed preemption based on the “mere possibility” of a prohibition.<sup>91</sup> The court, thus, held that to demonstrate preemption a carrier “must show actual or effective prohibition, rather than the mere possibility of prohibition.”<sup>92</sup> Like the Ninth Circuit, the Eighth Circuit acknowledged that the proper test for determining an effective prohibition had been set forth in *California Payphone*. Like the Ninth Circuit, however, the Eighth Circuit then failed to actually apply the *California Payphone* analysis. Instead, the Eighth Circuit noted that the carrier had admitted that it “cannot state with specificity what additional services it might have provided had it been able to freely use the money that it was forced to pay to the City for access to the public rights-of-way.”<sup>93</sup> The

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89. *Id.* at 580 (citation omitted). The ramifications of *County of San Diego* were immediately felt. The Ninth Circuit applied the new standard to mean that the mere fact that a provider continues to operate in a locality is *conclusive* evidence that any state or local regulation, however draconian, survives review under Section 253(a). See *Time Warner Telecom v. City of Portland*, 322 Fed. Appx. 496, 498 (9th Cir. 2009) (rejecting challenge to certain in-kind requirements imposed by city because the requirements “do not have the effect of prohibiting the provision of telecommunications services, as demonstrated by [the carrier’s] continued operation.”) (emphasis added) (relying on *County of San Diego*, 543 F.3d at 578).

90. 477 F.3d 528 (8th Cir. 2007).

91. *Id.* at 532–33.

92. *Id.* at 533.

93. *Id.*

Eighth Circuit concluded that “[t]his admission establishes that [the carrier] has not carried its burden of proof on the record we have before us.”<sup>94</sup>

The FCC had an opportunity to comment on these two decisions when the Supreme Court requested that the federal government file an amicus curiae brief to address the certiorari petitions filed in these cases, which were consolidated.<sup>95</sup> Acting on behalf of both the government and the FCC,<sup>96</sup> the Solicitor General reiterated in her amicus brief that *California Payphone* set forth the proper application of Section 253(a),<sup>97</sup> and she stated that the standard had become the consensus test by the appellate courts.<sup>98</sup> The Solicitor General then acknowledged that “aspects of the Eighth and Ninth Circuits’ opinions might be read to suggest an unduly narrow understanding of Section 253(a)’s preemptive scope . . . .”<sup>99</sup> The Solicitor General noted in particular that the Eighth Circuit in *City of St. Louis* “appears to have accorded inordinate significance to [the carrier’s] inability to ‘state with specificity what additional services it might have provided’ if it were not required to pay [the LGU’s] license fee.”<sup>100</sup> The Solicitor General stated, “[t]hat specific failure of proof— which the court of appeals seems to have regarded as emblematic of broader evidentiary deficiencies in [the carrier’s] case—is not central to a proper Section 253(a) inquiry.”<sup>101</sup> With respect to *County of San Diego*, the Solicitor General noted that “[p]ortions of the Ninth Circuit’s decision . . . could be read to suggest that a Section 253 plaintiff must show effective preclusion—rather than simply material interference—in order to prevail.”<sup>102</sup> The Solicitor General said that this was plainly improper because “limiting the preemptive reach of Section 253(a) to legal requirements that completely preclude entry would frustrate the policy of open competition that Section 253 was intended to promote.”<sup>103</sup>

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94. *Id.* at 533–34.

95. See Brief for the United States as Amicus Curiae, *Level 3 Comm., LLC v. City of St. Louis*, 477 F.3d 528 (8th Cir. 2007) (No. 08-626); *Sprint Telephony PCS, L.P. v. County of San Diego*, 543 F.3d 571 (9th Cir. 2008) (No. 08-759) [hereinafter *St. Louis Amicus Brief*].

96. The *St. Louis Amicus Brief* was signed both by the Solicitor General and attorneys from the FCC. *Id.* at 22.

97. *Id.* at 9.

98. *Id.* (“The courts of appeals uniformly recognize that the FCC’s *California Payphone Order* . . . prescribes the applicable standard for determining whether a legal requirement has the effect of prohibiting the ability to provide a telecommunications service.”) (citations omitted).

99. *Id.* at 8.

100. *Id.* at 13 (quoting *Level 3 Comm., LLC*, 477 F.3d at 533).

101. *St. Louis Amicus Brief*, *supra* note 95, at 13.

102. *Id.* at 14.

103. *Id.*

While clear in its criticisms, the Solicitor General, nevertheless, advocated that the Supreme Court not review these decisions.<sup>104</sup> The Solicitor General based her recommendation on the fact that each of the courts had cited *California Payphone* as the controlling standard, even though they had not properly applied it.<sup>105</sup> The Solicitor General said that because the circuits purportedly agreed on the legal standard to be applied, the FCC could address any lack of uniformity caused by disagreements among the circuits applying the *California Payphone* decision by issuing authoritative rulings, which the Solicitor General said would govern the disposition of Section 253(a) claims brought in federal court.<sup>106</sup>

*D. Analysis of City of St. Louis and County of San Diego*

Although the Solicitor General's decision to advocate against certiorari was curious,<sup>107</sup> her concern that the Eighth and Ninth Circuits misapplied *California Payphone* was well-founded. Indeed, it should be fairly obvious that requiring "actual or effective prohibition of the provision of a telecommunications service" as mandated by the Eighth and Ninth Circuits is a more stringent standard than the *California Payphone* "materially inhibits or limits the ability of any competitor or potential competitor to compete in a fair and balanced legal and regulatory environment" standard.<sup>108</sup> The differences in language are readily apparent:

First, the *California Payphone* term "materially inhibits or limits" connotes a regulation that significantly burdens a party but does not

104. *Id.* at 17–18.

105. *Id.* at 18.

106. *Id.* (citing Nat'l Cable & Telecomms. Ass'n v. Brand X Internet Servs., 545 U.S. 967, 982–83 (2005)).

107. This recommendation reflects a questionable view of the Executive Branch and its role in making certiorari recommendations, when the Executive Branch essentially expresses concern only with the precedential impact of the decisions and not justice for the parties before it. More importantly, the recommendation reveals a shocking degree of naïveté by its implication that the precedential impact will be minimal because courts in these circuits will ignore the holdings of the circuit courts and correctly apply *California Payphone*. This implication predictably was proven wrong in the very next Ninth Circuit Section 253 case following *County of San Diego*, where the panel held that evidence of continued market operation was conclusive evidence of lack of an effective prohibition. See *Time Warner Telecom v. City of Portland*, 322 Fed. Appx. 496, 498 (9th Cir. 2009).

108. *Compare* *Sprint Telephony PCS, L.P. v. County of San Diego*, 543 F.3d 571, 578 (9th Cir. 2008) (the phrase "effect of prohibiting" requires proof of "actual or effective prohibition" of a telecommunications service) *and* *Level 3 Communs., L.L.C. v. City of St. Louis*, 477 F.3d 528, 533 (8th Cir. 2007) (to demonstrate preemption a carrier "must show actual or effective prohibition, rather than the mere possibility of prohibition") *with* *California Payphone*, *supra* note 12, para. 31 (an effective prohibition will be found if the requirement "materially inhibits or limits the ability of any competitor or potential competitor to compete in a fair and balanced legal and regulatory environment.").

necessarily rise to the level of actually prohibiting the provision of service. The Eighth and Ninth Circuits' term "actual or effective prohibition of a telecommunications service" connotes a regulation that either specifically prohibits a carrier from providing service or is so onerous as to leave little choice but to not provide service.

Second, the *California Payphone* term "materially inhibits or limits" is further relaxed when placed in front of the second clause of the *California Payphone* definition, "the ability of any competitor or potential competitor to compete." This emphasis on the "ability to compete" is much broader than the Eighth and Ninth Circuits' focus on whether services may be provided at all.

Third, the final clause in the *California Payphone* definition, "in a fair and balanced legal and regulatory environment," further broadens the scope of Section 253(a) as it describes the attributes of the market in which the carrier must be allowed to compete. This stands in contrast to a market that is unreasonable or discriminatory, which the "actual or effective prohibition" standard would appear to tolerate so long as the carrier could provide service.

That the Eighth and Ninth Circuits' rigid "actual or effective prohibition" standard is more stringent than the *California Payphone* standard is even more apparent upon reviewing the decisions issued by the FCC in which it has applied its *California Payphone* standard. The FCC consistently has preempted and/or questioned LGU requirements under the *California Payphone* standard that likely would have survived under the Eighth and Ninth Circuits' analysis. This includes:

- *Public Utility Commission of Texas*, where the FCC reviewed a state law requiring new entrants to the local market to rely at least in part on facilities not owned by the incumbent.<sup>109</sup> As with the regulations at issue in the Ninth's Circuit decision in *County of San Diego*, such requirement did not actually prohibit the provision of service, it merely regulated the types of facilities that could be used.<sup>110</sup> The FCC nevertheless preempted the requirement.<sup>111</sup>
- *Western Wireless Corporation*,<sup>112</sup> where the FCC stated that a "universal service fund mechanism that provides funding only to

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109. Pub. Util. Comm'n of Texas, *Memorandum Opinion and Order*, 13 F.C.C.R. 3460 (1997).

110. *Id.* at paras. 73–75.

111. *Id.* at paras. 74–75.

112. W. Wireless Corp. Petition, *Memorandum Opinion and Order*, 15 F.C.C.R. 16227 (2000).

[incumbents]” would likely violate Section 253(a) because it would “effectively lower the price of [incumbent]-provided service relative to competitor-provided service” and thus “give customers a strong incentive to choose service from [incumbents] rather than competitors.”<sup>113</sup> The requirement did not actually prohibit the provision of service; it merely dictated how universal service funding would be distributed, but the FCC held that the requirement likely was preempted.<sup>114</sup>

- *Federal-State Joint Board on Universal Service*,<sup>115</sup> where the FCC explained that “[s]tate designation of an unreasonably large service area could . . . violate section 253,” because “an unreasonably large service area could greatly increase the scale of operations required of new entrants.”<sup>116</sup> Again, the requirement at issue did not actually prohibit the provisions of services (and, indeed, encouraged the provision by defining a service area broadly), but the FCC nevertheless held that it likely was preempted.<sup>117</sup>
- *TCI Cablevision of Oakland County, Inc.*,<sup>118</sup> where the FCC expressed significant concern over the following:
 

[P]rovisions that . . . require franchisees to interconnect with other telecommunications systems in the City for the purpose of facilitating universal service, provide for regulation of the fees charged for interconnection, and mandate “most favored nation” treatment for the City under which a franchisee providing a “new service, facility, equipment, fee or grant to any other community . . . within the State . . .” shall provide the same to the . . . [city granting the franchise].<sup>119</sup>

Here, too, the requirement at issue did not actually prohibit the provisions of services, but the FCC nevertheless held that it likely was preempted.<sup>120</sup>
- *Petition of Minnesota*,<sup>121</sup> where the FCC expressed doubt over the lawfulness of an agreement between Minnesota and a developer

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113. *Id.* at para. 8.

114. *Id.* at paras. 9–11.

115. Fed.-State Joint Bd. on Universal Serv., *Report and Order*, 12 F.C.C.R. 8776 (1997).

116. *Id.* at para. 129.

117. *Id.*

118. TCI Cablevision of Oakland Cnty, Inc., *Memorandum Opinion and Order*, 12 F.C.C.R. 21396 (1997).

119. *Id.* at para. 105.

120. *Id.* at paras. 106–110.

that provided the developer with exclusive access to certain rights-of-ways alongside the Minnesota highway system, on the grounds that the agreement “appear[ed] to have the potential to *adversely affect* the provision of telecommunications services by facilities-based providers, in violation of the provisions of section 253(a).”<sup>122</sup> The “adversely affect” standard clearly was a lower threshold than “actual or effective prohibition,” yet the FCC applied this standard and held that the requirement likely was preempted.<sup>123</sup>

These cases stand in stark contrast to the Ninth Circuit’s list in *County of San Diego* of the narrow examples that might be preempted under its standard, which included: 1) requiring all facilities to be placed underground where such placement would render the network inoperable; 2) requiring all wireless facilities to be placed more than one mile from a road where such placement again would render the network inoperable; and 3) requiring facilities to be placed in a manner so as to cause a significant gap in service coverage.<sup>124</sup> These types of hypothetical examples obviously would actually prohibit services in that they would render all or a large part of a carrier’s network inoperable, thereby making compliance with the regulation impossible. These examples are nothing like the requirements that the FCC preempted and/or called into question in the cases discussed above.

As a final matter, it must be pointed out that the Eighth and Ninth Circuits’ purported distinguishing of the cases allegedly applying a “mere possibility” standard is really a red herring and a distraction from the failure of these courts to follow the law. First, it is irrelevant whether these prior decisions used a “mere possibility” standard, since the *California Payphone* standard is clearly acknowledged to be the proper standard and, as explained, it was clearly not followed by the Eighth and Ninth Circuits. But regardless, the Eighth and Ninth Circuits were wrong in that, although *some* courts quoted Section 253(a) with the ellipses (“may . . . have the effect of prohibiting”), none actually held that Section 253(a) was triggered by a “mere possibility” of a prohibition. Although the courts in *Prince*

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121. Petition of Minnesota, *Memorandum Opinion and Order*, 14 F.C.C.R. 21697 (1999).

122. *Id.* at para. 3 (emphasis added); *see id.* at para. 22 (“evidence in the record that utilizing rights-of-way other than the freeway rights-of-way to install telecommunications infrastructure is *substantially more expensive* than using the freeway rights-of-way”) (emphasis added).

123. *Id.* at paras. 21–22.

124. *Sprint Telephony PCS v. County of San Diego*, 490 F.3d 700 (9th Cir. 2007), *aff’d*, 543 F.3d 571, 580 (9th Cir. 2009) (*en banc*).

*George's County* and *City of Auburn* had quoted Section 253(a) with the ellipses inserted,<sup>125</sup> neither of these courts had concluded that there was a "mere possibility" of prohibition; instead, each court held that the requirement at issue *would* indeed create an effective prohibition.<sup>126</sup> Moreover, the First Circuit in *Municipality of Guayanilla*, the Tenth Circuit in *City of Santa Fe*, and the Second Circuit in *City of White Plains* did *not* cite this abbreviated quotation of Section 253(a), and each of these courts similarly held that the requirement at issue would create an effective, rather than speculative, prohibition.<sup>127</sup> Each of these three courts also cited and relied on the FCC's *California Payphone* definition of an effective prohibition.<sup>128</sup>

### III. THE FCC SHOULD CLEARLY CONFIRM THAT REVENUE-GENERATING FEES ARE EFFECTIVELY PROHIBITIVE UNDER SECTION 253(A) AND ARE TO BE APPROPRIATELY ANALYZED UNDER SECTION 253(C)

The FCC now has the opportunity in its *PROW Docket* to bring uniformity to Section 253, as it said it would do in the *St. Louis Amicus Brief* when the opportunity arose. The FCC should begin by clearly confirming that revenue-generating fees are effectively prohibitive under Section 253(a), so that the inquiry can be shifted to whether the fees are

125. *Bell Atlantic-Maryland, Inc. v. Prince George's Cnty.*, 49 F. Supp. 2d 805, 814 (D. Md. 1999); *City of Auburn v. Qwest Corp.*, 260 F.3d 1160, 1175 (9th Cir. 2001).

126. *City of Auburn*, 260 F.3d at 1176 ("Taken together, these requirements 'have the effect of prohibiting' [the carrier] and other companies from providing telecommunications services . . . and create a substantial and unlawful barrier to entry into and participation in the Counterclaim Cities' telecommunications markets.") (citation omitted); *Prince George's Cnty.*, 49 F. Supp.2d at 814 ("After reviewing the various provisions of the ordinance being challenged in this case, the court finds that the County's telecommunications franchise law unquestionably has the effect of prohibiting the provision of telecommunications services by [the carrier] and other telecommunications companies seeking to do business in Prince George's County.").

127. *Puerto Rico Tel. Co. v. Mun. of Guayanilla*, 450 F.3d 9, 19 (1st Cir. 2006) ("We agree with the district court that [the carrier] has established that Ordinance No. 40 'materially inhibits or limits the ability' of [the carrier] 'to compete in a fair and balanced legal and regulatory environment.'" (quoting *TCG New York, Inc. v. City of White Plains*, 305 F.3d 67, 76 (2d Cir. 2002)). *See also* *Qwest Corp. v. City of Santa Fe*, 380 F.3d 1258, 1271 (10th Cir. 2004) ("The City argues that a mere increase in cost cannot be prohibitive . . . As stated in *RT Communications*, however, an absolute bar on the provision of services is not required . . . . It is enough that the Ordinance would 'materially inhibit' the provision of services . . . . Given the substantial costs generated by this Ordinance, it meets that test and is prohibitive under [Section 253(a)].") (citations omitted); *TCG New York, Inc.*, 305 F.3d at 76-77 ("In light of the obstacles that the Ordinance poses to [the carrier's] ability to compete in White Plains on a fair basis, we conclude that the Ordinance violates § 253(a).")

128. *Municipality of Guayanilla*, 450 F.3d at 18; *City of Santa Fe*, 380 F.3d at 1271; *TCG New York, Inc.*, 305 F.3d at 76.



“fair and reasonable” under Section 253(c). In so doing, the FCC should clearly confirm that *County of San Diego* and *City of St. Louis* were decided incorrectly to the extent that they failed to actually apply the *California Payphone* standard.

There are several separate yet related reasons as to why Congress and the FCC intended revenue-generating fees to qualify as an effective prohibition under Section 253(a) and to be analyzed under Section 253(c).

First, it is evident from the language in the *California Payphone* standard that the FCC did not intend “effect of prohibiting” under Section 253(a) to act as a significant hurdle before the propriety of PROW fees would be considered under Section 253(c). The preemption of a requirement that “materially inhibits or limits” the ability of a carrier to compete in a “fair and balanced legal and regulatory environment” under *California Payphone* is very similar to the language of Section 253(c), which saves a requirement that requires “fair and reasonable compensation . . . on a competitively neutral and nondiscriminatory basis . . . .” It is thus difficult to imagine an unfair, unreasonable, or discriminatory fee under Section 253(c) that would *not* materially inhibit or limit the ability to compete in a fair and balanced environment under Section 253(a)—the same emphasis on fairness, reasonability, and nondiscrimination is embedded in both inquiries. Because the *California Payphone* Section 253(a) inquiry and the Section 253(c) inquiry appear nearly identical, most courts actually applying *California Payphone*’s analysis devote little time to Section 253(a) and far more time to whether fees are fair and reasonable under Section 253(c). The court in *Prince George’s County*, in fact, recognized that a finding that a fee did not meet the Section 253(c) criteria amounted to a per se effective prohibition under Section 253(a) when it noted that

[i]f local governments were permitted . . . to charge franchise fees that were unrelated either to a telecommunications company’s use of the public rights-of-ways or to a local government’s costs of maintaining and improving its rights-of-way [under Section 253(c)], then local governments could effectively thwart the FTA’s pro-competition mandate and make a nullity out of section 253(a).<sup>129</sup>

Second, it is further evident from the FCC’s application of the *California Payphone* standard that the FCC did not intend “effect of prohibiting” under Section 253(a) to act as a significant hurdle before the propriety of PROW fees would be considered under Section 253(c). Although the FCC has not had occasion to analyze the propriety of a

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129. *Prince George’s Cnty.*, 49 F. Supp. 2d at 817.

specific fee provision in a case before it,<sup>130</sup> the cases and dockets discussed immediately above demonstrate that the FCC considers Section 253(a) to present a relatively low bar by preempting regulations that not only “materially inhibit or limit” carriers, but also might “adversely affect [carriers],”<sup>131</sup> “give customers a strong incentive to choose service from [incumbents] rather than competitors,”<sup>132</sup> or “greatly increase the scale of operations required of new entrants.”<sup>133</sup> Imposing revenue-generating fees for PROW use is clearly on par with these types of prohibitive regulations. In fact, the FCC heavily implied in another amicus brief that, although the question had not arisen in a matter before it, revenue-generating fees likely would be prohibitive under Section 253.<sup>134</sup>

Third, common sense would support the notion that “effect of prohibiting” under Section 253(a) should not act as a significant hurdle before the propriety of PROW fees are considered as fair, reasonable, and discriminatory under Section 253(c). Otherwise, an LGU could seemingly charge fees in any amount, no matter how excessive or discriminatory, so long as the carrier could not show the impossibility of complying with the requirement without discontinuing or abandoning a particular service. Under such a scenario, a Fortune 15 company such as AT&T with \$124,000,000,000 in 2010 reported revenues<sup>135</sup> would have no defense against excessive or discriminatory fees imposed by a single LGU, whereas a single-market independent telephone company using the exact same PROW could show a prohibition, assuming the fees rendered the service provided by this single-market carrier unprofitable and forced the company to shut down. AT&T presumably would have to wait until it was on its

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130. A case currently pending before the FCC could provide the FCC with this opportunity. In *Level 3 Communications*, Level 3 Communications is requesting the FCC to exercise its authority under Section 253(d), which gives the FCC concurrent jurisdiction with federal courts over Section 253 claims, to invalidate several agreements signed by Level 3’s predecessors and the New York State Thruway Authority. As of the date of this Article, no decision had been issued. Level 3 Commun. LLC, Petition for Declaratory Ruling that Right-of-Way Rents Imposed by the New York State Thruway Authority Are Preempted Under Section 253, FCC WC Docket No. 09-153 (rel. July 23, 2009).

131. Petition of Minnesota, *Memorandum Opinion and Order*, 14 F.C.C.R. 21697, para. 3 (1999).

132. W. Wireless Corp. Petition, *Memorandum Opinion and Order*, 15 F.C.C.R. 16227, para. 8 (2000).

133. Fed.-State Joint Bd. on Universal Serv., *Report and Order*, 12 F.C.C.R. 8847 para. 129 (1997).

134. Brief of the FCC and United States as Amici Curiae at 14 n.7, TCG New York, Inc. v. City of White Plains, 305 F.3d 67 (2d Cir. 2002) (Nos. 01-7213, 01-7255) [hereinafter TCG Amici Brief].

135. AT&T INC., A NETWORK OF *POSSIBILITIES*: AT&T INC. 2010 ANNUAL REPORT 30 (2010), [http://www.att.com/Common/about\\_us/annual\\_report/pdfs/ATT2010\\_Full.pdf](http://www.att.com/Common/about_us/annual_report/pdfs/ATT2010_Full.pdf).

virtual death bed, having suffered the thousand cuts of excessive PROW fees across the country, before it could bring any type of action. And in that case, such an action likely would be too late to seriously challenge such fees, as it undoubtedly would be met with the LGU defense that it was just following the “group-pricing” practices of other LGUs that AT&T previously had accepted. Such a toothless preemption standard, available to only the smallest or least profitable carriers, plainly would not further Congressional interests in opening markets to competition and deploying advanced services.

Fourth, a natural reading of Section 253(a) supports the notion that revenue-generating fees are simply effectively prohibitive under Section 253(a). That is because any licensing or franchising fee requirement, even if arguably modest, quite literally “prohibits . . . the ability of an[] entity to provide” service because a carrier cannot enter the market or continue use of its network unless and until it obtains authorization from the regulatory authority and pays the demanded fees. While at first blush that might seem to be a lax standard, it must be remembered that the preemptive scope of Section 253 was intended to be “broad”<sup>136</sup> and, in particular, to prevent the establishment of a “third tier” of regulation by the LGU.<sup>137</sup> In this context, it would make sense for Congress to have intended to preempt any local fee requirement that was not otherwise specifically preserved in Section 253(b) (for states) and Section 253(c) for states and LGUs. As discussed above, when it comes to fees, the emphasis logically should be on whether the requirement at issue is “fair and reasonable” as an objective matter under Section 253(c), as opposed to whether the requirement actually prohibits a particular carrier to provide service as a subjective matter under Section 253(a).<sup>138</sup>

Fifth, revenue-generating PROW fees threaten deployment of new and advanced services and thus meet the *California Payphone* standard of “materially inhibit[ing] or limit[ing]” the ability to compete. As the First

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136. 141 CONG. REC. S8212 (daily ed. June 13, 1995) (comments of Sen. Gorton).

137. TCI Cablevision of Oakland Cty., Inc., *Memorandum Opinion and Order*, 12 F.C.C.R. 21396, para. 105 (1997).

138. It should be noted that some courts have avoided the issue of whether excessive PROW fees standing alone are prohibitive by allowing carriers to also rely on nonfee provisions to show an effective prohibition, and then analyzing the fees under Section 253(c). *See, e.g.*, TCG New York, Inc. v. City of White Plains, 305 F.3d 67, 76–77 (2d Cir. 2002); XO Missouri, Inc. v. City of Maryland Heights, 256 F. Supp. 2d 987, 992 (E.D. Mo. 2003). This process essentially allows an end-run around Section 253(a) when analyzing certain fee provisions, theoretically allowing fees to be struck down under Section 253(c) because they were ancillary to objectionable nonfee provisions, where the fees might have otherwise avoided scrutiny under Section 253(c) if enacted as stand-alone provisions. This end-run around mechanism would be unnecessary under a natural reading of Section 253(a).

Circuit recognized in *Municipality of Guayanilla*, the dollars that are required to be paid by carriers to LGUs often represent a one-for-one loss of dollars that otherwise would be used for network investment.<sup>139</sup> This diversion of investment funds is exacerbated when the excessive fee structures are adopted by LGUs in neighboring communities.<sup>140</sup> The FCC recognized the impact of excessive and obstructive LGU management practices in its NBP where it acknowledged that “[s]ecuring rights to [PROW] is often a difficult and time-consuming process that discourages private investment.”<sup>141</sup> As these authorities show, paying revenue-generating PROW fees ultimately will materially inhibit or limit a carrier’s ability to compete.<sup>142</sup>

Sixth, revenue-generating PROW fees also create competitive disparities and, thus, meet the *California Payphone* standard of materially inhibiting or limiting the ability to compete in “a fair and balanced legal and regulatory environment.” Today, wireline, wireless, and cable-based service providers employ disparate technologies and competitive strategies

139. *Puerto Rico Tel. Co. v. Municipality of Guayanilla*, 450 F.3d 9, 18–19 (1st Cir. 2006).

140. *Id.*

141. NBP, *supra* note 2, at 127.

142. Several commentators in the pending *PROW Docket* have purported to dispute the First Circuit’s common sense conclusion that excessive PROW fees inhibit broadband deployment, and they have pointed to the example that many cities already are at or close to one hundred percent broadband deployment. *See, e.g.*, Coalition of Texas Cities: Comments on the FCC’s Broadband and Rights of Way Notice of Inquiry at 22–27, Acceleration of Broadband Deployment, FCC CC Docket No. 11–59 (rel. July 18, 2011); Comments of the League of Oregon Cities at 3–5, Acceleration of Broadband Deployment, FCC CC Docket No. 11–59 (rel. July 15, 2011); Comments of the City of Eugene, Oregon at 6, Acceleration of Broadband Deployment, FCC CC Docket No. 11–59 (rel. July 18, 2011); Comments of the City of Portland, Oregon at 2, Acceleration of Broadband Deployment, FCC CC Docket No. 11–59 (rel. July 18, 2011); Comments of the City of San Antonio, Texas at 5, Acceleration of Broadband Deployment, FCC CC Docket No. 11–59 (rel. July 18, 2011); Comments of the National League of Cities et. al. at 9–16, Acceleration of Broadband Deployment, FCC CC Docket No. 11–59 (rel. July 19, 2011) [hereinafter League of Cities]. This argument suffers from several obvious weaknesses: (1) it ignores that many of these one hundred percent deployment cities are already limited to cost-based fees by state law; and (2) it fails to detail the degree to which broadband is deployed in these cities by providers not subject to PROW fees. But most importantly, the argument ignores that carrier budgeting often occurs at the regional or national level, meaning that a city’s excessive PROW fees could just as likely negatively impact resources being deployed in rural areas. Further, these commentators argue in the same breath that they are disciplined in their PROW pricing by the potential that carriers will respond by diverting resources to other cities. League of Cities at 12–13, 16. The premise for this argument—that excessive PROW charges will discourage investment in a particular city—is directly at odds with these commentators’ purported theme that PROW charges do not restrict deployment. In any event, it is common sense that the more expenses a company incurs, the less money it generally has for investment.

to compete head-to-head across a broad range of voice and nonvoice services. It is beyond expectation that any LGU could design a revenue-generating fee (i.e., a fee unrelated to the costs firms cause when they access the PROW) that is unbiased and nondiscriminatory among these different competitors. It is a near certainty, however, that unfair, biased and discriminatory fees over time will cause some existing and/or potential firm to refrain from offering a service that it would have offered otherwise. Competition is an effective means of directing efficient innovation and investment, but it is an unforgiving process that punishes firms that suffer from competitive disadvantages. As the Second Circuit recognized in *City of White Plains*, “fees that exempt one competitor are inherently not ‘competitively neutral,’ regardless of how that competitor uses its resulting market advantage.”<sup>143</sup> Indeed, it is the competitors that do not build in the PROW that are the most advantaged by inflated PROW costs, as they avoid excessive cost inputs to which their peers are subject. As one commentator has appropriately and succinctly stated:

Although competitive neutrality might seem to be satisfied so long as every carrier using any right of way were charged on the same schedule, such a limited notion ignores the presence of wireless carriers in the market. Wireless carriers do not use rights of way to provide service, but Congress expected as part of its general expectation of “convergence” that wireless carriers would begin to compete with wireline carriers for the provision of identical services. Competitive neutrality can be maintained between wireline and wireless carriers only if right of way charges to wireline carriers reflect the costs of right of way use. If wireline carriers are charged a price for right of way use that is in excess of cost, wireline service will be at an artificial cost disadvantage and wireless services will receive an implicit subsidy, resulting in inefficient demand for wireless services—and inefficient supply of them as well.<sup>144</sup>

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143. *City of White Plains*, 305 F.3d at 80. The Tenth Circuit reached a similar conclusion in *City of Santa Fe* in preempting a portion of the ordinance that required only first installers to install and reserve capacity for use by the LGU. The Tenth Circuit recognized that imposing such a cost requirement on carriers building in the PROW put them at a competitive disadvantage relative to carriers that either built later or not at all. *Qwest Corp. v. City of Santa Fe*, 380 F.3d 1258, 1273 (10th Cir. 2004).

144. James B. Speta, *Competitive Neutrality in Right of Way Regulation: A Case Study in the Consequences of Convergence*, 35 CONN. L. REV. 763, 768 (2003). In addition, although never raised as an issue in any reported case, it should be apparent that incumbent carriers cannot simply “pass-through” PROW charges in order to achieve competitive parity. Initially, many of the LGU gross revenue fees are designed to exempt the incumbent’s wholesale revenue, thus leaving no costs to pass-through to these wireline and wireless carriers. See, e.g., OR. REV. STAT. § 221.515 (2009) (limiting Oregon municipal franchise fees to retail local revenues). In these situations, only the retail revenues of the carrier with facilities in the PROW are subject to the PROW fees, thus creating a situation where customers likely would see a franchise fee on one provider’s bill but not on another’s.

For these reasons, the FCC should use the *PROW Docket* to clearly confirm that revenue-generating fees are effectively prohibitive under Section 253(a), so that the inquiry can be shifted to whether the fees are “fair and reasonable” under Section 253(c).

IV. THE FCC SHOULD CLARIFY THAT “FAIR AND REASONABLE  
COMPENSATION” UNDER SECTION 253(C) MEANS PAYMENT FOR  
MANAGEMENT COSTS PLUS A PROVEN ECONOMIC VALUE OF THE  
PROW THAT WOULD PREVAIL IN COMPETITIVE MARKETS

As described above, the interpretation of Section 253(c) has suffered from a misplaced debate over limiting fees for accessing the PROW to the costs that LGUs incur when firms place facilities in the PROW versus allowing LGUs to charge additional fees for the fair market value of the space in the PROW. Some courts have held that such fees should be cost-based;<sup>145</sup> some have held that they must at least be related to costs;<sup>146</sup> and some have analyzed whether fees are reasonable under a “totality of the circumstances” test.<sup>147</sup> Commentators have been equally divided between whether Section 253(c) was intended to be limited to costs or allow for something more.<sup>148</sup>

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Further, even if wholesale revenues were included in the PROW fee base, practical considerations would limit the ability of incumbent carrier’s to pass such fees through. Many incumbents have never had to assess city-specific fees on wholesale revenues, which revenues are generally exempt from state and local taxation, and so they lack the billing systems to track and bill the fees for these wholesale services. See JEROME R. HELLERSTEIN & WALTER HELLERSTEIN, *STATE AND LOCAL TAXATION: CASES AND MATERIALS* § 14.02 (West 2005) (1952). And even if tracking and billing were possible, these wholesale services are heavily regulated through tariffs or contracts, which may limit the charges that can be passed on to wholesale customers. This means that, whether the PROW fee is based on a gross revenue or a linear foot charge, incumbents may lack the legal or regulatory authority to pass such fees on to their wholesale customers, thus requiring the incumbents to essentially subsidize the business plans of their competitors by paying their proportional PROW fees.

145. *E.g.*, *City of Auburn v. Qwest Corp.*, 260 F.3d 1160, 1176 (9th Cir. 2001); *Bell Atlantic-Maryland, Inc. v. Prince George’s Cnty.*, 49 F. Supp. 2d 805, 817 (D. Md. 1999); *AT&T Comm. of the S.W., Inc. v. City of Dallas*, 8 F. Supp. 2d 582, 593 (N.D. Tex. 1998); *XO Missouri, Inc. v. City of Maryland Heights*, 256 F. Supp. 2d 987, 994–995 (E.D. Mo. 2003).

146. *E.g.*, *Puerto Rico Tel. Co. v. Municipality of Guayanilla*, 450 F.3d 9, 22 (1st Cir. 2006); *Qwest Comm. Inc. v. City of Berkeley*, 146 F. Supp. 2d 1081, 1100 (N.D. Cal. 2001).

147. *E.g.*, *Qwest Corp. v. City of Santa Fe*, 380 F.3d 1258, 1272 (10th Cir. 2004); *TCG Detroit v. City of Dearborn*, 206 F.3d 618, 625 (6th Cir. 2000).

148. For articles arguing that Section 253(c) limits PROW fees to costs, see Speta, *supra* note 144; see also Christopher R. Day, *The Concrete Barrier at the End of the Information Superhighway: Why Lack of Local Rights-of-Way Access Is Killing Competitive Local Exchange Carriers*, 54 *FED. COMM. L. J.* 461 (2002); Gardner F. Gillespie, *Rights-of-Way Redux: Municipal Fees on Telecommunications Companies and Cable Operators*, 107

None of these courts or commentators has focused on whether the PROW actually contains value for anyone other than telecommunications carriers and other utilities that need access to provide services. The assumption underlying the debate is that, if fees are not limited to costs, the LGU would be entitled to charge a substantially higher amount based on the PROW's fair market value. But this is a false assumption. In fact, the PROW generally has little or no fair market value. This conclusion is reached through an understanding of competitive versus monopolistic markets and the concept of economic scarcity.

A. *Competitive v. Monopolistic Pricing and the Concept of Economic Scarcity*

As the Second Circuit recognized in *City of White Plains*, “Section 253(c) requires compensation to be reasonable essentially to prevent monopolistic pricing by towns. Without access to local government rights-of-way, provision of telecommunications service using land lines is generally infeasible, creating the danger that local governments will exact artificially high rates.”<sup>149</sup> In order to avoid monopoly pricing, therefore, the PROW must exhibit aspects of a competitive market.

A competitive market is generally defined as a market in which no single entity or combination of entities can exert undue market power to control prices or the values of assets.<sup>150</sup> In competitive markets, participating firms discipline behaviors through the forces of supply and demand, and prices are driven toward the efficient firms' costs.<sup>151</sup> Scarcity is at the foundation of fair economic value in competitive markets. An asset is scarce if, at a price of zero, the demand for the asset exceeds the supply. It is closely associated with the concept of opportunity cost.<sup>152</sup> When a

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DICK. L. REV. 209 (2002). For articles arguing that Section 253(c) allows for something more (although never defined), see Jennifer A. Krebs, *Fair and Reasonable Compensation Means Just That: How § 253 of the Telecommunications Act Preserves Local Government Authority over Public Rights-of-Way*, 78 WASH. L. REV. 901 (2003); William Malone, *Access to Local Rights-of-Way: see also A Rebuttal*, 55 FED. COMM. L. J. 251 (2003); Frederick E. Ellrod III & Nicholas P. Miller, *Property Rights, Federalism, and the Public Rights-of-Way*, 26 SEATTLE U. L. REV. 475 (2003); William Malone, *Municipalities' Right to Full Compensation for Telecommunications Providers' Uses of the Public Rights-of-Way*, 107 DICK. L. REV. 623 (2003).

149. TCG New York, Inc. v. City of White Plains, 305 F.3d 67, 79 (2d Cir. 2002).

150. HAL R. VARIAN, *INTERMEDIATE MICROECONOMICS: A MODERN APPROACH* 284 (4th ed. 1996).

151. *Id.* at 391–92.

152. VARIAN, *supra* note 150, at 23, 318, 393. As observed by Dr. Varian, “[t]he economic definition of profit requires that we value all inputs and outputs at their opportunity costs.” *Id.* at 318.

scarce resource is devoted to one use, there is less of this resource available for other uses.

Sand in the desert is a classic example of something that is not scarce in an economic sense. Even though there is a finite amount of sand in the desert, if at a price of zero there is more sand available than there is demand for it, then the sand is not scarce in an economic or market value context. The sand still would have what is known as “use value” because it would be useful to those who needed it, but it would have no “exchange value” due to a lack of economic scarcity.<sup>153</sup> Under fair market conditions, the forces of supply and demand would drive the price of sand toward zero. Of course, if someone expended effort to transport the sand, clean it, and put it in bags, then the transported, cleaned, and bagged sand may command a positive price to compensate the person for this effort because it then would have exchange value.

In a monopolistic market, there are no competitors that discipline price. Accordingly, if an entity has monopoly control over sand in the desert, it can extract a positive price for the sand from those that need it, even though sand is a nonscarce asset for which there is no opportunity cost. This type of behavior is the exercise of substantial market power. If unchecked, the abuse of this power can disrupt the development of efficient and beneficial competitive markets. That is why it is often deemed necessary to impose restrictions on entities that operate without viable competitors. There are numerous antitrust and regulatory safeguards in place to guard against the creation and abuse of market power.<sup>154</sup> Generally, these restrictions set prices based upon costs, because this best mimics a competitive market. As the FCC observed in reference to setting prices for unbundled network elements under Section 251 of the FTA: “[a]dopting a pricing methodology based on forward-looking, economic costs best replicates, to the extent possible, the conditions of a competitive market.”<sup>155</sup>

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153. See Guido Montani, *Scarcity*, in 4 *THE NEW PALGRAVE: A DICTIONARY OF ECONOMICS* 253, 253–54 (John Eatwell et al. eds., 1987) (“It may happen . . . that a certain good has use-value without having exchange value. We can imagine two circumstances which give rise to such a case. The first concerns goods which are useful, but not scarce, when they are not produced by labour.”).

154. It bears noting that the problem of monopolistic behavior is a problem of relative market power. That is, the unfair aspects associated with monopolies can occur when an entity possesses substantial market power, even if the entity is not a pure monopolist, in the sense that it is the single seller in a market. See Kurt W. Rothschild, *Degree of Monopoly*, in *THE NEW PALGRAVE: A DICTIONARY OF ECONOMICS* 766, 766–68 (John Eatwell et al. eds., 1987).

155. Implementation of the Local Competition Provisions in the Telecomm. Act of 1996, *First Report and Order*, FCC Docket No. 96-98, para. 679 (1996).



*B. Where the PROW Is a Nonscarce Asset, It Should Be Priced Accordingly*

Applying the principles of competitive markets to the PROW, it would be appropriate for the LGU to assess a market rental value on a carrier if the PROW exhibits economic scarcity and the LGU incurs a corresponding positive opportunity cost when a firm occupies space in the PROW. If, however, the space in the PROW does not exhibit economic scarcity, then there is no opportunity cost associated with this space, and there is little or no fair market value related to its use.

For consideration of the role that opportunity costs play in determining fair market value of space in the PROW, it is important to separate the cost associated with directly managing rights-of-way from costs related to facilities that are lying beneath the street. Activities involved with issuing permits, inspecting construction sites, and general mapping of facilities are all directly related to managing rights-of-way. These activities engender costs that add value and should be paid. They are similar to the transporting, cleaning, and bagging of sand in the desert. Economic scarcity and opportunity costs (and, thus, exchange value) are associated with these activities.

In contrast, with respect to the actual space beneath the ground in the PROW managed by LGUs, the LGUs did not incur costs to create this space (except in rare instances), and it is unlikely that the supply of this space would exceed demand at a price of zero. That is, no entity generally wants access to slim tunnels beneath the roadway, other than utilities, and absent the utilities' occupation, the space would remain vacant. In addition, cables occupying this space beneath the street do not engender cost-causing activities by LGU employees.<sup>156</sup>

The same is true for utility poles. Once utility poles are in place, it is unlikely that demand would exceed supply if the price for using this space was eliminated, as no entity generally wants access to overhead space to string cables or other facilities along a road, other than utilities. Further,

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156. There is a debate among engineers from LGUs and carriers about whether cable installation under PROW degrades the road such that it requires additional maintenance or early replacement. See, e.g., *Pavement Degradation: How Other Cities Are Dealing With It*, AMERICAN PUBLIC WORKS ASSOCIATION (Sept. 23, 2002), [http://www2.apwa.net/documents/about/techsvcs/row/products/pavement\\_degradation-9-02.pdf](http://www2.apwa.net/documents/about/techsvcs/row/products/pavement_degradation-9-02.pdf). This was presented to the 2002 APWA International Public Works Congress and Exposition, Kansas City, Missouri on September 23, 2002. Although carriers generally deny that installations followed by proper restoration negatively impact the life or condition of the PROW, this would be a legitimate issue for consideration in a case in which an LGU actually attempted to craft its fee schedule to recover such provable costs. The general practice, however, has been for LGUs to merely assert that such degradation costs exist and to then impose a gross revenue or linear foot charge that lacks a principled relation to such alleged costs.

once a pole is in place, it is difficult to imagine what costs LGUs incur, other than the costs related to the costs of managing the PROW, when another firm places its cables on the poles. As long as there is sufficient space on the poles for all users, there is certainly no scarcity of space in the PROW, and it is difficult to imagine what diminishment of market value an LGU incurs when an additional firm places another aerial cable on pre-existing poles.

This does not exclude the possibility that there are limited areas in the PROW where the suitable space for placing facilities is scarce. Truly scarce space in certain parts of certain metro areas is conceivable. But setting a fair and reasonable fee related to these situations would first require identifying such areas in the PROW. Unless LGUs can identify areas where the demand for space suitable for placing facilities exceeds supply, or would exceed supply at a price of zero, then there is no basis for assuming a fair market value of more than zero.

Support for this valuation method is found in the comparable arena of constitutional law developed around Fifth Amendment “takings” claims, where it is government that it is seeking to use or condemn private property. In those circumstances, the Supreme Court has held that “just compensation” is properly measured by *the lost value to the property owner* rather than by the value it has to the government taking the property.<sup>157</sup> This also makes sense when measuring “value” under Section 253(c), where the government suffers little, if any, loss of value when its PROW is used for occupancy by utilities. Indeed, the case for limiting compensation is even greater in the Section 253(c) case where the government is already receiving a benefit from the occupancy of its PROW by the provision of beneficial communications services to its residents.

### *C. Scarcity Is Distinct from Negative Externalities*

Recognizing that the PROW in and of itself is a nonscarce resource, some commentators in the *PROW Docket* are nevertheless attempting to justify applying a “fair market value” element to PROW fees by blending the concepts of scarcity and negative externalities. Specifically, when addressing scarcity in the PROW, these commentators refer to “scarcity

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157. *United States v. Petty Motor Co.*, 327 U.S. 372, 377 (1946) (“The Constitution and the statutes do not define the meaning of just compensation. But it has come to be recognized that just compensation is the value of the interest taken. This is not the value to the owner for his particular purposes or to the condemnor for some special use but a so-called ‘market value.’”). *See also City of Monterrey v. Del Monte Dunes at Monterrey, Ltd.*, 526 U.S. 687, 710 (1999) (“in determining just compensation, ‘the question is what has the owner lost, not what has the taker gained.’”) (quoting *Boston Chamber of Commerce v. Boston*, 217 U.S. 189, 195 (1910)).

and the associated negative spillover effects.”<sup>158</sup> They claim that these negative effects of PROW occupation include increased excavation or construction costs, increased costs associated with design and planning, costs associated with loss-of-services, increased travel time, and lost revenues.<sup>159</sup>

In economics, such spillover effects are generally referred to as negative externalities. A negative externality exists when an action by an entity has a negative impact on others in a manner that is not addressed by market pricing.<sup>160</sup> For example, if traffic is disrupted while a carrier accesses the PROW, the interruption of smooth traffic flow is a negative externality. On the other hand, there are also positive externalities associated with communications service. For example, you experience a positive externality when people you would like to contact purchase phone service. You also experience a positive externality to your home values when broadband is deployed in your neighborhood.<sup>161</sup>

The important point is that a negative externality does not render otherwise nonscarce PROW scarce. Returning to the example of sand in the desert, if removing sand from the desert disrupts an otherwise quiet atmosphere, this could be perceived as a negative externality for those living nearby. This externality does not make sand in the desert scarce, if at a price of zero there is still more sand available than there is demand for sand. It is the quiet atmosphere, not the sand, that is the scarce commodity at issue. If some payment is deemed necessary, the appropriate amount is determined by the impact on the quiet atmosphere. In the same vein, negative externalities associated with accessing the PROW do not make space in the PROW scarce. An appropriate fee, if any, is one that addresses the costs associated with the externality, not one that treats space in the PROW as a scarce resource.

When considering PROW fees as compensation for negative externalities, it is important to consider two facts. First, externalities—both positive and negative—are endemic to the experience of living in a city, and it is neither advisable nor feasible to devise payment schedules related

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158. League of Cities, *supra* note 142, at 40.

159. *Id.*

160. See VARIAN, *supra* note 150, at 557–77.

161. See, e.g., Glenn A Worocho, *Local Network Competition*, in 1 HANDBOOK OF TELECOMMUNICATIONS ECONOMICS: STRUCTURE, REGULATION AND COMPETITION 665 (Martin Cave, Sumit Majumdar, & Ingo Vogelsang eds., 2002) (“Quite apart from any goal of distributional equity, one reason to promote widespread access to the local telephone network is to take advantage of ‘network externalities.’ These occur when each subscription confers a benefit on all existing subscribers because they can now call, and be called by, the new subscriber.”).

to all externalities. Consider the positive and negative externalities associated with well-maintained yards in a neighborhood. The pleasures we derive from our neighbors' well-maintained gardens and lawns are positive externalities, while the noise associated with lawn mowing is often experienced as a negative externality. We may support restrictions on times when mowing is permitted, but we generally do not attempt to work out payment schemes for the positive and negative externalities related to the upkeep of our yards and those of our neighbors. For the most part, we accept these as benefits and costs associated with living in a neighborhood. Second, cities are most often not the entities that endure the spillover effects described above. For example, it is perverse to claim that a city would serve the best interests of its constituents by charging fees as compensation for externalities associated with traffic disruption caused by activities reasonably performed to access the PROW. This would result in its constituents paying twice—once when in traffic and a second time when the fees are included in their utility bills.

As stated above, if there are externalities that cause LGUs to incur costs such as increased design time associated with carrier occupation of the PROW, setting fees based upon a reasonable estimation of these costs is appropriate—not because these costs make the PROW scarce, but because they represent management costs that should be compensable (and, indeed, are specifically recognized as compensable by Section 253(c)). Confusing externalities with scarcity, however, does a disservice to the process of setting fair and reasonable fees.

#### *D. Other Valuation Methods Are Economically Unsound*

Once the economics behind valuation are appreciated, it is evident that other valuation methods discussed or adopted by courts are economically unsound.

First, it is clear that fair market value is not determined by whether some carriers, under certain circumstances, might pay the demanded PROW fee. As noted by the Second Circuit in *City of White Plains*, carriers naturally need access to PROW to provide services,<sup>162</sup> and many—particularly the larger carriers—will not allow a single LGU's fee structure to prevent them from using the PROW when they can subsume the costs into a broader expense base. That willingness to redistribute costs within the carrier's business obviously does not bestow value on the particular PROW. Indeed, many LGUs will provide access to PROW with a bait-and-switch technique where a carrier may install its facilities for a five-year

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162. 305 F.3d 67, 79 (2d Cir. 2002).

term at a reduced rate but then see the rates skyrocket. These carriers are then stuck with the decision of whether to abandon sunk costs or pay the inflated fees. A carrier's decision to pay the inflated fees rather than incur greater costs of relocating their facilities can also hardly be said to bestow value on the PROW. As the court stated in *Town of West New York*, "that the Town found willing bidders does not weigh in favor of the reasonableness of the compensation scheme, and those bids are no guide to what is 'fair and reasonable' under the statute."<sup>163</sup> See also *Municipality of Guayanilla*, where the First Circuit stated that "the amount that other telecommunication providers would be willing to pay[] tells us more about telecommunications providers' resources and their desire to comply with local regulations than it does about why the fee chosen is 'fair and reasonable compensation' for the state or municipality."<sup>164</sup>

Second, it is also evident that a gross revenue fee is an inappropriate measure of value. The gross revenue formulas are faulty because they assume that each carrier occupies PROW at the same proportion relative to their overall earnings, thus ignoring that some carriers avoid installing significant facilities in the PROW by serving only large business customers or by leasing facilities from incumbents. The formulas also errantly assume that facilities that are installed are evenly used among carriers when, in truth, some carriers use less PROW by maximizing the use of their facilities, while other carriers have overbuilt and are left with under-utilized or unlit cables. Further, the formulas include revenue attributable to all services, "regardless of whether the call traverses over one inch or 100 feet of the public rights of way."<sup>165</sup> But the major problem with the formulas is that the percentages chosen have nothing to do with PROW value. No LGU in the reported cases bothered to argue or support that a three percent gross revenue fee represented an actual value of occupancy of the PROW, versus a one, five, or ten percent fee. For this reason, the First Circuit in *Municipality of Guayanilla* logically stated that it would "refuse to uphold the [five percent] fee on the off chance that it might prove to be fair and reasonable."<sup>166</sup> And the FCC noted in the *TCG Amici Brief*,

A percentage of gross revenues-based fee, even if uniformly applied, might well have no relationship to either the extent of each carrier's use of the [PROW] or the costs it imposed on the [LGU]. It therefore could be inconsistent with the competitive neutrality requirement of

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163. *New Jersey Payphone Ass'n, Inc. v. Town of West New York*, 130 F. Supp. 2d 631, 638 (D. N.J. 2001).

164. *Puerto Rico Tel. Co. v. Municipality of Guayanilla*, 450 F.3d 9, 23 (1st Cir. 2006).

165. *Id.* at 22.

166. *Id.* (quoting *Puerto Rico Tel. Co. v. Municipality of Guayanilla*, 354 F. Supp. 2d 107, 114 (D. P.R. 2005)).

Section 253(c). Although the FCC has not addressed the specific issue, there also is a serious question whether a gross revenues based fee is ‘fair and reasonable compensation . . . for use of [PROW]’ within the meaning of Section 253(c).<sup>167</sup>

Third, there are flaws in the so-called “across-the-fence” methodology, which some commentators have advocated in the *PROW Docket*.<sup>168</sup> This methodology uses appraisals of land values for properties adjacent to the PROW to assess the fair market value of the PROW.<sup>169</sup> This methodology relies on the false assumption that there is a direct relationship between the value of residential and commercial properties that border a street and the value of the PROW. First and foremost, this methodology ignores the fact that properties bordering the PROW generally exhibit economic scarcity and are valued as such, while space in the PROW generally does not exhibit economic scarcity. The positive market value for property adjacent to the PROW is a function of demand that equals supply at a positive price. As described above, where there is no demonstrated economic scarcity of space in the PROW, the supply exceeds demand even at a price of zero. This fundamental difference renders this methodology useless for the purpose of establishing a fair market value for the PROW. Second, this methodology ignores the fact that real estate value is a function of the amenities of properties (views, proximities to schools, etc.) that simply are missing from space in the PROW.

## V. CONCLUSION

The FCC should use the *PROW Docket* as an opportunity to state a uniform standard and return application of Section 253 to its original intent. In particular, it is important and necessary for the FCC to: (1) confirm that a requirement has the “effect of prohibiting” services under Section 253(a) if it conditions use of the PROW on the payment of revenue-generating fees; and (2) clarify that “fair and reasonable compensation” under Section 253(c) means payment for PROW management costs and for any other proven economic value that LGUs can demonstrate that the PROW would possess in a competitive market.

By taking these actions, the FCC can return Section 253 to its original intent, which is the development of efficient competition and, through efficient competition, the development of a world-class communications industry. The role of government as expressed through Section 253 is to ensure that competitors meet on fair and balanced playing fields so that the

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167. TCG Amici Brief, *supra* note 134, at 14 n.7.

168. League of Cities, *supra* note 142, at Ex. G 20.

169. *Id.*

best technologies and competitive strategies have the greatest opportunities to prevail. A level field of play exists when all firms pay for the actual costs they cause. Revenue-generating fees tilt the field of play and put LGUs in the positions of picking winners and losers, which is the antithesis of Section 253 and the FTA.

