



International Center
for Law & Economics

**TECH
FREEDOM**

Reply Comments of

TechFreedom¹

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In the Matter of

*Pleading Cycle Established for Comments on Electric Power Board and City of Wilson Petitions,
Pursuant to Section 706 of the Telecommunications Act of 1996, Seeking Preemption of State Laws
Restricting the Deployment of Certain Broadband Networks*

WCB Docket Nos. 14-115 and 14-116

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I. Introduction & Summary

The International Center for Law and Economics (ICLE) and TechFreedom filed initial comments in these proceedings urging the Federal Communications Commission (“FCC” or “Commission”) not to preempt the state laws at issue in North Carolina and Tennessee because (1) the Commission lacks the legal authority to do so under Section 706, (2) even if the FCC had such authority, it would be a double-edged sword, which could be used to *ban* government-owned networks in the future, so it should not be exercised in this case, (3) such a reversal in approaches could be premised on the rather obvious economic point that government provision of broadband may in fact decrease broadband deployment and investment in the aggregate by deterring private broadband competition; and (4) in general, government-run broadband, which lacks profit-driven feedback loop, is unlikely to serve consumers better in the long-run than private provision of broadband. If government is ever to enter the broadband marketplace, this should be a last resort, done only in cases where private providers will not provide broadband competition.³

Petitioners and the commenters who support them describe North Carolina’s and Tennessee’s laws (and similar laws in other states) as “bans” because doing so supports the simplistic and misleading narrative that has thus framed this discussion — and sparked confusing media coverage: Markets have failed, the story goes, either to provide broadband service at all or to provide competition for an incumbent; and municipalities are trying to cure this market failure by offering service, but are being blocked by laws passed solely to protect incumbent providers.

In fact, as discussed below, the North Carolina and Tennessee laws, like other state laws, explicitly *authorize* government-owned networks – which is essential, since municipalities, as creatures of the states, may do only those things that states authorize.⁴ At the same time,

³ See Pleading Cycle Established for Comments on Electric Power Board and City of Wilson Petitions, Pursuant to Section 706 of the Telecommunications Act of 1996, Seeking Preemption of State Laws Restricting the Deployment of Certain Broadband Networks, *Comments of International Center for Law & Economics (ICLE) & TechFreedom*, WCB Docket Nos. 14-115 & 14-116 (Aug. 29, 2014) [*ICLE & TechFreedom Comments*], available at <http://apps.fcc.gov/ecfs/document/view?id=7521826211>.

⁴ See, e.g., *City of Trenton v. State of New Jersey*, 262 U.S. 182 (1923) (“A municipality is merely a department of the state, and the state may withhold, grant or withdraw powers and privileges as it sees fit. However great or small its sphere of action, it remains the creature of the state exercising and holding powers and privileges subject to the sovereign will.”); *Hale v. Henkel*, 201 U.S. 43, 74-75 (1906) (“[T]he corporation is a creature of the state. It is presumed to be incorporated for the benefit of the public. It receives certain special privileges and franchises, and holds them subject to the laws of the state and the limitations of its charter. Its powers are limited by law. It can make no contract not authorized by its charter. Its rights to act as a corporation are only preserved to it so long as it obeys the laws of its creation. There is a reserved right in the legislature to investigate its contracts and find out

these laws (a) ensure a level playing field between government-owned networks and private networks, and (b) provide that the decision to operate such networks is made by those taxpayers who will be on the hook for the system's long-term costs, and not behind closed doors. This is essentially the right balance, although we do believe more could be done to promote deployment *without* distorting the marketplace, or burdening consumers with failed systems. Specifically, as discussed below, we urge municipalities and states to cut red tape that makes private broadband difficult and, if they have taxpayer dollars available to invest, to focus it on building broadband-ready smart infrastructure like Dig Once conduits under streets and fiber-ready poles – rather than attempting to displace the private providers that would, we believe, in the vast majority of cases, eagerly deploy faster broadband service if it were easier and cheaper to do so.

II. A Balanced Pro-Deployment Approach

If states *did* actually (or effectively) ban government-owned networks, and Congress were to pass legislation clearly authorizing preemption of such laws, the FCC would have to, in the spirit of Section 706, decide what kind of policy framework would actually “encourage the deployment on a reasonable and timely basis of advanced telecommunications capability to all Americans.” This would be done not through a petition for declaratory ruling, but through notice-and-comment rulemaking, informed by economic analysis and by commentary not merely on abstract questions, but on specific regulatory proposals. The fundamental question would be: Is it actually necessary for a municipal government to construct its own network? Or can it achieve its goal – promoting broadband competition – through cheaper means that do not involve the risks inherent in government ownership and operation of a broadband network?

Advocates of municipal broadband usually claim that government-owned networks are necessary to remedy a market failing: either no private provider will serve an area or not more than one will do so. But how do we know that a first, second or third (and so on) private provider might not enter the market to build and operate a broadband network with private

whether it has exceeded its powers.”); *City of Worcester v. Worcester Consolidated S Railroad Co.*, 196 U.S. 539, 548-49 (1905) (“A municipal corporation is simply a political subdivision of the state, and exists by virtue of the exercise of the power of the state through its legislative department. The legislature could at any time terminate the existence of the corporation itself, and provide other and different means The city is the creature of the state.”); *City of New Orleans v. New Orleans Water-Works Co.*, 142 U.S. 79, 88 (1891) (“the city, being a... creature of the state legislature, does not stand in a position to claim the benefit of the constitutional provision in question, since its charter can be amended, changed, or even abolished at the will of the legislature”).

capital instead of taxpayer dollars *if* the municipality and state made *private* deployment easier?

The right policy approach would be to:

- Ensure that cities give private providers the same access to rights of way that cities or utilities building their own networks would get — precisely as North Carolina’s law requires⁵ (although Tennessee’s apparently does not⁶);
- Cut red tape to ensure that cities make private deployment not only as easy as government deployment would be, but as easy as possible; and
- Promote public/private partnerships, like those employed in Chattanooga, TN for decades,⁷ based on having the municipality build “smart infrastructure” that private providers could lease from the city.

These are the issues the FCC should be exploring — instead of wasting its own time and that of the commenters in debating preemption that is all but certain to fail in court. If the FCC issued the Notice of Inquiry we proposed in our comments, it could build a record that would inform the drafting of legislation narrowly tailored to use preemption to promote broadband deployment overall, while respecting the interests of the states in protecting their taxpayers. With a well-developed record as to the three-fold approach we suggest, Congress could craft legislation that focuses on the roots of the alleged problem: why some broadband markets don’t have more broadband providers.

The first two issues are essentially about ensuring the right legal and regulatory framework while the third requires actual expenditure of taxpayer dollars. But the third may be where municipalities can do the most to unleash private investment. Thus far, the widespread assumption has been that cities must build and operate broadband networks themselves. But this needn’t be the case.

⁵ See N.C. Gen. Stat. § 160A-340.1(a)(5) (“Shall provide nondiscriminatory access to private communications service providers on a first-come, first-served basis to rights-of-way, poles, or conduits owned, leased, or operated by the city unless the facilities have insufficient capacity for the access and additional capacity cannot reasonably be added to the facilities. For purposes of this subdivision, the term ‘nondiscriminatory access’ means that, at a minimum, access shall be granted on the same terms and conditions as that given to a city-owned communications service provider.”).

⁶ See Tenn. Code Ann. § 7-52-601 et seq.

⁷ See David Eichenhal & Tracy Windeknecht, *Chattanooga, Tennessee: A Restoring Prosperity Case Study*, BROOKINGS 4 (Sept. 2008), available at http://www.brookings.edu/~media/research/files/papers/2008/9/17_chattanooga_eichenhal_windeknecht/200809_chattanooga.pdf (“The tide began to turn in the 1990s, with strategic investments by developing public-private partnerships — dubbed the ‘Chattanooga way.’”).

Suppose that, instead of issuing a bond to fund construction and operation of a fiber network, a city issued a much smaller bond to fund installation of “Dig Once” conduits — ideally, as part of upgrades to its other below-ground sewer, water or other utility infrastructure. Having installed such conduits, the city could lease them out to private providers. Multiple private providers, both new entrants and incumbents, could very cheaply thread fiber through those conduits, install the necessary routing and switching equipment to make their network function (including cabinets at or near the “curb”), and assume responsibility for connecting homes and businesses to their cabinets (the “last 300 feet”). Installation of conduits has been estimated to add just 1% of the cost of a road project but to reduce the cost of deployment to the curb by as much as 90%.⁸

Much the same approach could be taken with poles. In Connecticut, for example, the state has funded a long-term replacement of all utility poles in the state with taller poles capable of carrying fiber hook-ups.⁹ Additionally, Connecticut’s Department of Public Utility Control (DPUC) is also in the process of implementing a third-party statewide utility telephone pole administrator, with the intention of streamlining and expediting the pole attachment process for all broadband providers.¹⁰ Whether Connecticut’s approach is right in all its particulars, the basic thrust of encouraging the upgrading of poles and making them available to all would-be broadband companies is quite sound.

Call focusing on “smart infrastructure” the “Field of Dreams” approach — “If You Build It, They Will Come.” If it works, a municipality will have succeeded in stimulating new entry and faster broadband speeds for a fraction of the cost of building its own broadband network. It will also have escaped the long-term financial risks inherent in undertaking responsibility for maintaining and continually upgrading a constantly evolving high-tech communications system. And it will avoid the political complications that come with government operating

⁸ See Fiber to the Home Council Americas, *Becoming A Fiber-Friendly Community: Regulatory & Infrastructure Actions That Can Drive Deployments* 5 (May 2013), available at <http://www.ftthcouncil.org/d/do/1215> (“[I]nstalling conduit for fiber with enough space for additional networks . . . can reduce deployment costs along roadways by as much as 90%, while adding less than one percent to the cost of the road construction.”).

⁹ See Gregory B. Hladky, *Connecticut Cities Looking For Ultra-High Speed Internet Service*, HARTFORD COURANT (Sept. 15, 2014), available at <http://www.courant.com/politics/elections/hc-hi-speed-broadband-0916-20140915-story.html> (discussing the push for public-private partnerships in Connecticut to bring high-speed broadband to local residents and businesses, along with a bill passed in 2012 specifically addressing the usage of existing utility poles to create high-speed Internet systems).

¹⁰ See Dept. of Pub. Util. Control, *Letter to Participants Re: DPUC Investigation into the Appointment of a Third Party Statewide Utility Telephone Pole Administrator for the State of Connecticut*, Docket No. 11-03-07 (Mar. 16, 2011), available at <http://bit.ly/1vr2YoB>.

broadband networks: debates over censorship, surveillance and potential shutdowns of broadband networks when demanded by the police, without the due process that would be required when interfering with private providers.

And if the approach *doesn't* work? Cities will have lost nothing: the same conduits and poles installed to support private deployment could be used to carry a government-owned network. The cost of installing simply a conduit is far smaller than that of building an entire fiber network, and, in any event, installing the conduit is necessary in both cases: it is the only way to future-proof whatever infrastructure is eventually installed. So the municipality will have lost almost nothing — except, perhaps, the time lost while waiting for broadband providers to take advantage of newly constructed conduits and poles. But that concern could be addressed easily enough: Rather than waiting to see if broadband providers actually take advantage of smart infrastructure, reduced red tape, and equal rights for pole attachments, a municipality could solicit either expressions of interest or even preliminary commitments to provide service at levels of speed commensurate with (realistically) expected demand and at prices competitive with those available in other markets. If no such expressions or commitments are received, the city might well be justified in concluding that the market has failed and that it would be appropriate for the city to take the additional step of building its own network after (or while) it installs “dig once” conduits. But at least this way, the municipality will have tested and verified the currently untested *assumption* that private deployment will not happen, and it will have installed a smart infrastructure that will support any such private providers as might decide to deploy in the future.

Congress could, in a larger package of pro-deployment reforms, give the FCC narrow preemption authority to ensure that municipalities *can* provide service under these three prior conditions. (As we suggested in our comments, if municipalities do construct their own broadband networks, they should be required to allow private companies to offer competitive services using that network, lest the government-run network become a monopoly itself.¹¹) The FCC could set minimum standards for what municipalities and states must do to streamline the regulatory clearance process for broadband providers — both new entrants and incumbents — to build or upgrade broadband networks, such as by capping application processing times or fees. And the FCC could set rules governing what kind of process cities might go through before concluding that adequate private deployment will not be forthcoming (e.g., a methodology for determining minimum quality of service levels and how to determine comparable pricing). Or, preferably, such matters could be left to the states

¹¹ *ICLE & TechFreedom Comments*, at 31-34.

unless it could be conclusively shown that state laws are, in fact, prohibiting deployment of networks to Americans who would otherwise be adequately served — in other words, a true market failure.

Politically, a “third way” on muni broadband could pave the way for a larger set of reforms, including ensuring that federal law makes the same pole-attachment rights available for broadband networks not covered by Title II (*e.g.*, Google Fiber), that federal roads projects also include “Dig Once” conduits, and so on. Many of these ideas were proposed in the FCC’s 2010 National Broadband Plan but have yet to be implemented.¹²

Such a compromise would be a win for (almost) everyone: municipalities and their taxpayers would be spared the additional expense of building their own private networks and the risks that such networks would need to be bailed out in the future; private companies would be encouraged to enter the market, including local would-be Internet Service Providers; and broadband service could be deployed to all Americans in the most efficient way possible. The only losers from such a compromise would be the ideologues on either side of the debate.

On the radical left are those who support government-owned networks not as a last-resort measure for providing service to those whom markets would leave unserved or underserved, but out of deep-seated hostility to the very notion that private companies should run broadband networks.

On the right are two overlapping camps. First are those who might insist that government should never construct broadband networks, even when private companies have demonstrably failed to do so. While we share their skepticism of government and recognize the dangers of government-run broadband, we also recognize that markets can sometimes fail (at least, to provide service at a certain level of quality and price), especially in rural areas — although we think it unlikely that private providers would be unwilling to enter the market under the conditions we propose above.

The other potential source of opposition would be from states’ rights conservatives who object to any form of federal preemption. But there is nothing inherently wrong with federal preemption, provided that Congress *clearly* authorizes it, and that the FCC implements it only as a last resort after giving states the opportunity to weigh in on the process, as contemplated

¹² See generally, Federal Communications Commission, NATIONAL BROADBAND PLAN: CONNECTING AMERICA, Chapter 6 (2010), available at <http://www.broadband.gov/plan/6-infrastructure/>.

by President Clinton Executive Order No. 13,132.¹³ As we mentioned in our Comments, federal preemption of local zoning restrictions governing satellite dishes was essential to promoting the development of satellite television as a competitive alternative to cable.

And what of private providers? A few small operators might indeed balk at government-funded competition in the tiny percentage of markets where there is only one broadband company, even if state governments ensure that government-owned networks are not given special advantages or taxpayer subsidies. But overall, private broadband companies have applauded proposals to make broadband deployment easier, even when that might help their rivals enter the market. In 2011, for example, NCTA President Michael Powell applauded Rep. Anna Eshoo's Broadband Conduit Deployment Act of 2011, which would have provided that federally funded road projects should include Dig Once conduits.¹⁴

This alignment of incentives suggest that a legislative compromise is not merely a pipe dream, but something that could actually be enacted by Congress. But such a compromise will probably only happen after the FCC concedes that it has no preemption authority over the expansion of government-owned networks today.

III. The State Laws at Issue Are Not Bans

Numerous commenters in this proceeding have argued for preemption of the state laws in question because they "ban" municipal broadband networks, but this is simply not the case.¹⁵ These commenters apparently fail to grasp (or simply misrepresent) the fundamental purpose of the laws at issue: to enable private broadband investment to proceed alongside whatever

¹³ Exec. Order No. 13,132, 64 Fed. Reg. 153 (Aug. 4, 1999), available at <http://www.gpo.gov/fdsys/pkg/FR-1999-08-10/pdf/99-20729.pdf> ("National action limiting the policymaking discretion of the States shall be taken only where there is constitutional and statutory authority for the action and the national activity is appropriate in light of the presence of a problem of national significance. **Where there are significant uncertainties as to whether national action is authorized or appropriate, agencies shall consult with appropriate State and local officials to determine whether Federal objectives can be attained by other means.**") (emphasis added).

¹⁴ John Eggerton, *Powell Applauds Eshoo's 'Dig Once' Bill*, Broadcasting & Cable (May 3, 2011), available at <http://www.broadcastingcable.com/news/washington/powell-applauds-eshoos-dig-once-bill/58850?rssid=20065>.

¹⁵ See, e.g., *Comments of Jim Baller & James P. Cauley III, Counsel for the City of Wilson*, WCB Docket Nos. 14-115 & 14-116, at 14 (Aug. 29, 2014) [*Wilson Comments*], available at <http://apps.fcc.gov/ecfs/document/view?id=7521737310> ("Section 160A-340 is an effective prohibition on public broadband investment[.]."); *Comments of The Coalition for Local Internet Choice*, WCB Docket Nos. 14-115 & 14-116, at Attachment A p. 3 (Aug. 29, 2014), available at <http://apps.fcc.gov/ecfs/document/view?id=7521826169> ("North Carolina imposes numerous requirements that collectively have the practical effect of prohibiting public communications initiatives.").

public broadband projects might be initiated. Neither North Carolina's law¹⁶ nor Tennessee's¹⁷ can fairly be characterized as a "ban" because neither actually prohibits the build-out and operation of municipal broadband networks. In fact, both laws *authorize* municipal broadband networks while ensuring that these municipalities not compete unfairly with private providers, expose their taxpayers to undue risk by expanding beyond their borders, and that the decision to build such networks is made by the voters.

Consider North Carolina's bill, which offers a clearer, more comprehensive framework for governing muni broadband petitions than does Tennessee's. The nature of North Carolina's bill ought to be apparent from the short name of the bill that became the law at issue: "Level Playing Field/Local Gov't Competition."¹⁸ It's undeniably true that the laws at issue do impose conditions and restrictions on publicly-owned broadband networks that are not imposed on privately-owned broadband networks,¹⁹ but the reasons for this should be obvious. For one, government-owned networks have a number of inherent competitive advantages over privately-owned networks, such as tax exemptions, cross-subsidies, and various administrative efficiencies. Additionally, and perhaps most critically, publicly-owned broadband networks can have effects that are much more far-ranging than privately-owned networks: if a private network goes under, only its creditors stand to lose, whereas if a public network goes under, all local taxpayers will be left to foot the bill, regardless of whether they supported the network at its inception or were even of eligible age to vote at the time. If the network has been expanded beyond the confines of the municipality itself, the taxpayers of that municipality may be on the hook for a far larger obligation. Given the difficulty inherent in cost-accounting, it may be extremely difficult, if not impossible, for a municipal broadband network based in one municipality to attempt to require taxpayers in areas outside that area to pay for the costs of expanding and maintaining service to those areas, and thus to protect the taxpayers of its home location from paying for the cost of serving other users.

¹⁶ See Level Playing Field/Local Gov't Competition Bill, H. 129, 2011 Sess. (N.C. 2011), *available at* <http://www.ncleg.net/Sessions/2011/Bills/House/PDF/H129vo.pdf> (codified at N.C. Gen. Stat. § 160A-340 et seq.).

¹⁷ See Tenn. Code Ann. § 7-52-601 et seq.

¹⁸ See Level Playing Field/Local Gov't Competition Bill, *supra* note 16.

¹⁹ See, e.g., Fiber to the Home Council Americas, *State Resources: Tennessee* (last visited Sept. 29, 2014), *available at* <http://www.ftthcouncil.org/p/cm/ld/fid=155> ("Tennessee bans municipal provision of paging and security service but allows municipalities that operate their own electric utilities to provide cable, two-way video, video programming, Internet access, and other 'like' services *upon satisfying various public disclosure, hearing, voting and other requirements that a private provider would not have to meet.*") (emphasis added).

Thus, it seems perfectly reasonable that the North Carolina and Tennessee legislatures took precautious steps towards limiting the scope of public broadband networks. But it is unreasonable to claim that those laws represent “bans” on municipal broadband. Indeed, in the case of North Carolina, the state law in question was merely a reaction to an unexpected court ruling that overturned over 30 years of precedent.²⁰ Specifically, in *BellSouth v. City of Laurinburg*,²¹ the North Carolina Court of Appeals held that a law that previously applied only to “cable television systems” should also apply to any wired system used for any purpose, so the North Carolina legislature had to react to this change in existing law in order to ensure that every city did not suddenly invest heavily in public broadband networks — or security and home monitoring systems, enterprise broadband services or other IP-enabled services — lest these investments turn out poorly in the long run and bankrupt the entire state.²² The purpose of the law was not to “prohibit cities from entering into the business, but rather to adopt rules to make them enter more or less as a market participant should they decide to compete with services already being provided by private business.”²³ Furthermore, the North Carolina law expressly exempts those cities that were already operating networks of their own, and its competitive provisions do not apply to services operating in unserved areas.²⁴ And even where the law does apply, its provisions and restrictions are much less onerous than some commenters suggest.

Just as North Carolina’s law explicitly authorizes municipalities to offer broadband, Tennessee’s law specifically authorizes electric utilities to offer broadband service. The issue raised by Petitioner EBP is that the Tennessee law, like the North Carolina law, restricts the ability of an electric power company to offer service beyond its own territory.²⁵ Specifically, the law prevents electric companies from offering Internet and video programming services outside of their electric service territory in Tennessee.²⁶ Section 601 allows electric companies to provide telecommunications (i.e., telephone service), anywhere in the state, but it restricts

²⁰ Rep. Marilyn Avila (NC), *North Carolina’s Broadband Battle*, INSIDEALEC 12 (Nov./Dec. 2011), available at http://www.alec.org/docs/Final_NovDec2011_IA.

²¹ 168 N.C.App. 75, 606 S.E. 2d 721 (2005).

²² See Avila, *supra* note 20, at 12.

²³ *Id.* at 13.

²⁴ See N.C. Gen. Stat. § 160A-340.1(c), 340.2(b).

²⁵ See Tenn. Code Ann. § 7-52-601.

²⁶ *Id.*

the companies from providing advanced telecommunications (i.e. broadband Internet service) beyond their service area.²⁷

Further, Tennessee law authorizes pilot projects in which a municipal electric system may provide broadband service not only within its own municipal territory but beyond it to the rest of the county under certain conditions.²⁸ The 2003 amendment to Section 601 is straightforward. The General Assembly recognizes that government provision may, in fact, be necessary to cure a market failure in some areas of the state:

WHEREAS, the General Assembly recognizes that rural areas of the State are less likely to have access to state of the art technologies; and

WHEREAS, the General Assembly has previously authorized municipal electric systems to provide cable, internet, and other services within their respective service areas, subject to certain requirements; and

WHEREAS, the General Assembly finds that granting additional authorization to smaller municipal electric systems that are located in lesser populated counties will enable these electric systems to further contribute to the economic and community development of these municipalities and counties and to improve the overall quality of life for these areas.²⁹

The Tennessee law's other provisions aim primarily at preventing cross-subsidization and other unfair competitive advantages to the government-operated electric companies. For instance, Tenn. Code Ann. § 65-5-108 provides that "The [Tennessee Regulatory Authority] shall, as appropriate, also adopt other rules or issue orders to prohibit cross-subsidization, preferences to competitive services or affiliated entities, predatory pricing, price squeezing, price discrimination, tying arrangements or other anti-competitive practices."³⁰

Put simply, the state laws at issue are fiscal and procedural safeguards, not bans. As evidenced by the comments submitted by the town of Holly Springs, NC, "innovation is possible when localities are engaged[,]” and cities are still perfectly capable of deploying fiber-optic facilities

²⁷ *Id.*

²⁸ *Id.*

²⁹ See TN Senate Bill 1753 (introduced Feb. 13, 2003), available at <http://www.capitol.tn.gov/Bills/103/Bill/SB1573.pdf>.

³⁰ Tenn. Code Ann. § 65-5-108.

to the benefit their citizens and local businesses.³¹ Requiring cities to obtain popular approval and to compete on equal terms with private companies can fairly be said to be “bans” on municipal broadband networks only when the idea of government-owned networks lacks popular support — suggesting that the citizens themselves don’t want them built — or when they make no economic sense — suggesting that investors (public or private) would be foolish to throw their money away on such endeavors.

IV. Preemption Based on Section 706 Will Fail

In our initial comments, we discussed at length why we believe an effort by the FCC to preempt the state laws in question is sure to fail in court.³² Some commenters justify federal preemption by claiming that the deployment and operation of broadband networks are outside the scope of authority historically reserved to the states. In fact, however, preemption on such grounds is legally unsupported.

A. Broadband Deployment and Its Regulation Are within the Bounds of Historical State Authority

The Fiber-to-the-Home Council Americas (“FTTHC”), for example, argues that the “presumption in favor of State actions in areas where States have historically exercised their police powers ... generally has not been available when a State or local government regulates in an area ‘where there has been a history of significant federal presence.’”³³ FTTHC then argues that,

Section 706 clearly identifies such an area: removing barriers to infrastructure investment where deployment of advanced telecommunications capability is unreasonable or untimely. Here, Congress, beginning almost two decades ago, intended the Commission to have a significant presence to ensure advanced telecommunications capability is being made available in a reasonable and timely fashion to all Americans and requires that the Commission take affirmative action where that is not the case. There is an express federal presence established by Section 706, whereby the Commission has both the

³¹ See *Comments of Holly Springs, NC*, WCB Docket Nos. 14-115 & 14-116, at 2 (Aug. 29, 2014) [*Holly Springs Comments*], available at <http://apps.fcc.gov/ecfs/document/view?id=7521825037>. Holly Springs “very successfully” deployed a middle-mile fiber-optic network, and last-mile services are provided by private entities that use the Holly Springs middle-mile network for backhaul. *Id.*

³² *ICLE & TechFreedom Comments*, at 4-10.

³³ *Comments of Fiber to the Home Council Americas*, WCB Docket Nos. 14-115 & 14-116, at 18 (Aug. 29, 2014) [*FTTHC Comments*], available at <http://apps.fcc.gov/ecfs/document/view?id=7521825866>.

authority to examine broadband deployment and then, affirmatively, the obligation to take immediate action to remove barriers to infrastructure investment in locations where deployment is unreasonable and untimely and “accelerate” the availability of broadband.³⁴

This argument omits one key historical detail: the FCC did not miraculously discover that Section 706 was an independent grant of authority until December 2010, when it re-interpreted Section 706 in order to justify issuing net neutrality regulations, which the D.C. Circuit had said (earlier that year) the FCC could not base on claims in ancillary jurisdiction.³⁵ Whether or not this re-interpretation will ultimately stand, the all-new Section 706 hardly constitutes a “history of significant federal presence.”

FTTHC notes that “regulation over broadband providers is something that many States, including Tennessee and North Carolina, have declined to impose, recognizing federal preemption.”³⁶ This is besides the point. If anything, this reflects the states’ acceptance of federal preemption of state regulatory burdens upon broadband implicit in the classification of broadband as a Title I lightly regulated information service. This is entirely distinct from the purpose of laws like North Carolina’s and Tennessee’s, whose central purpose is to protect taxpayers from imprudent, long-term financial commitments by municipalities and to ensure that government-owned networks do not distort competition by receiving special privileges.

FTTHC further claims that the state laws at issue are not part of state’s historic authority because “[w]hen municipal utilities provide broadband service, they do so as a commercial or nongovernmental, proprietary actor.”³⁷ This argument — offered with no precedential support other than a general, unexplained citation to *Gregory v. Ashcroft*, 501 U.S. 452 (1991) — has absolutely no basis in law. There is no “market participation exemption” from state regulation for municipalities. In fact, the very existence of municipalities is established by state law, and

³⁴ *Id.* at 18-19.

³⁵ See *Comcast Corp. v. FCC*, 600 F.3d 642 (D.C. Cir. 2010).

³⁶ *FTTHC Comments* at 21 (citing Tenn. Code Ann. § 65-5-203) (“In order to ensure that Tennessee provides an attractive environment for investment in broadband technology by establishing certainty regarding the regulatory treatment of that technology, consistent with the decisions of the Federal Communications Commission to preempt certain state actions that are not in accordance with the policies developed by the Federal Communications Commission, the Tennessee regulatory authority shall not exercise jurisdiction of any type over or relating to broadband services, regardless of the entity providing the service.”).

³⁷ *Id.* at 20-21.

both Tennessee and North Carolina retain power over them under their state constitutions.³⁸ Regulation of municipalities thus falls squarely within the “political-function” described in *Ashcroft*.³⁹ In order to preempt in this area, the FCC needs a clear statement of authority. As we’ve argued elsewhere, Section 706 fails to provide that clear statement.⁴⁰

While we believe this should be the end of the Commission’s legal analysis, we do note that FTTHC’s argument also ignores wide range of ways Tennessee and North Carolina retain authority over municipal corporations providing goods or services⁴¹ — but it does implicitly acknowledge the purpose and intent of state laws governing government-owned networks: to create an environment where a municipality can compete with private entities in a manner which creates fair and robust competition while protecting against the particular competitive harms that result from governmental competition.

1. States Have Traditionally Regulated Government Competition with Private Companies

For instance, North Carolina’s Fair Playing Field Law clearly falls squarely within matters of historic state concern, as noted by several of the state elected representatives filing comments.⁴² As Thom Tillis, speaker of the North Carolina General Assembly and a supporter of the Level Playing Field Act in the legislature, puts it in his comments, the “Level Playing Field Law reflects North Carolina’s strong public policy of disfavoring local (and state)

³⁸ See TENN. CONST. art. XI, § 9 (“The General Assembly shall by general law provide the exclusive methods by which municipalities may be created, merged, consolidated and dissolved and by which municipal boundaries may be altered.”); N.C. CONST. art. VII, § 1 (“The General Assembly shall provide for the organization and government and the fixing of boundaries of counties, cities and towns, and other governmental subdivisions, and, except as otherwise prohibited by this Constitution, may give such powers and duties to counties, cities and towns, and other governmental subdivisions as it may deem advisable.”). See also N.C. CONST. art. V, § 10 (allows the General Assembly to vest the municipalities with authority to own and operate facilities that provide electricity).

³⁹ *Gregory v. Ashcroft*, 501 U.S. 452, 468-70 (1991). Interestingly, Department of Labor regulations include public works, which municipal broadband would surely be an example of, as among the traditional functions of state governments. See 29 C.F.R. § 510.25(b)(4).

⁴⁰ *ICLE & TechFreedom Comments*, at 4-10.

⁴¹ The State of Tennessee retains broad authority over public utilities and municipal corporations as well, but the main focus of the rest of this section will be on North Carolina’s regulatory history.

⁴² See Comments of Rep. Avila, at 1 (“the issue has moved far beyond the policy question of municipal provision of broadband services to the governing question of who has the ultimate responsibility for the oversight of local governments.”); Joint Comments of Rep. Saine and Sen. Brock, at 1 (“The Level Playing Field Law was written to address core state interests...”); Comments of Sen. Apodaca, at 1 (“North Carolina’s Level Playing Field Law was enacted to promote important public interests in the state—the protection of North Carolina taxpayers and the continued encouragement of a vibrant state economy.”).

government competition with private industry.”⁴³ That long-standing policy is set forth clearly in North Carolina law. Under North Carolina’s Umstead Act,⁴⁴ state entities are prohibited from rendering services or selling goods ordinarily and customarily offered by private enterprises.⁴⁵ This restriction dates back to 1939⁴⁶ and was enacted as an “attempt to prevent the government from competing with its taxpaying citizens.”⁴⁷

North Carolina courts have long recognized the public policy underlying the Umstead Act. The North Carolina Supreme Court has explained that “[t]he rule in North Carolina is that it is not the function of the government to engage in private business.”⁴⁸ The court elaborated that this rule is codified in the Act, “which specifically prohibits (with certain exceptions) the State of North Carolina or any agency thereof from rendering services or selling goods ordinarily and customarily rendered by *private enterprise*.”⁴⁹

While North Carolina’s legislature has granted many exemptions from this prohibition (including an exemption applicable to local governments) over the years, the general principle animating the original Act — that competition between the government and private enterprise should be discouraged — remains a fundamental aspect of North Carolina public policy, as in many states. The Level Playing Field Act’s preamble affirms explicitly draws on this principle:

as expressed in . . . the Umstead Act, it is against the public policy of this State for any unit, department, or agency of the State, or any division or subdivision of

⁴³ Comments of Speaker Tillis, at 2.

⁴⁴ N.C.G.S. § 66-58; *see also, e.g.*, David Lawrence, *Competing, Making A Profit*, Coates’ Canons: NC Local Government Law (Nov. 20, 2009), <http://canons.sog.unc.edu/?p=1274> (explaining that N.C.G.S. § 66-58 “is widely but informally known as the Umstead Act [and] generally prohibits any agency that is part of the State government from engaging ‘directly or indirectly in the sale of goods, wares or merchandise in competition with the citizens of the State’”).

⁴⁵ N.C.G.S. § 66-58(a) (“It shall be unlawful for any unit, department or agency of the State government . . . to engage directly or indirectly in the sale of goods, wares or merchandise in competition with citizens of the State . . . or to contract with any person, firm or corporation for the operation or rendering of the businesses or services on behalf of the unit, department or agency . . . in competition with private enterprise”).

⁴⁶ The Act was named for U.S. congressman and North Carolina Governor William B. Umstead.

⁴⁷ *See* Laura Young Baxley, *Umstead Act*, in *ENCYCLOPEDIA OF NORTH CAROLINA*, at 1143 (William S. Powell, ed. 2006), *available at* <http://ncpedia.org/umstead-act>.

⁴⁸ *In re Appeal of Univ. of North Carolina*, 300 N.C. 563, 577, 268 S.E.2d 472, 480 (N.C. 1980) (quotation omitted).

⁴⁹ *Id.*

a unit, department, or agency of the State, to engage directly or indirectly in the sale of goods, wares, or merchandise in competition with citizens of the State.⁵⁰

2. States Have Traditionally Regulated How Municipalities Incur Debt

Similarly, the North Carolina General Assembly has historically and comprehensively regulated how municipalities conduct their financial affairs and incur debt in support of those activities.⁵¹ These laws include detailed fiscal accounting, control and reporting requirements,⁵² and specific authorizations and requirements relating to the issuance of local debt.⁵³

While municipal authority flows from the North Carolina General Assembly, the North Carolina State Constitution also contains several provisions that constrain local authority over taxing and spending, several of which affirmatively direct the General Assembly to adopt regulations governing municipal activity. For example:

- The State Constitution prohibits cities from incurring debt secured by pledge of the local government's "faith and credit" without a vote of the people,⁵⁴ and the General Assembly is directed by this constitutional provision to adopt laws governing this activity.⁵⁵
- North Carolina's Constitution requires that the power of taxation be exercised only for a "public purpose."⁵⁶ The North Carolina Supreme Court has held that the same "public purpose" limitation applies to expenditures of governmental funds, and this restriction

⁵⁰ N.C. Sess. Laws 2011-84, available at <http://www.ncleg.net/Sessions/2011/Bills/House/PDF/H129v7.pdf>.

⁵¹ See generally Chapter 159 of the North Carolina General Statutes ("Local Government Finance Act").

⁵² See *id.* N.C.G.S. Ch. 159, art. 3, §§ 159-7, *et seq.* ("Local Government Budget and Fiscal Control Act").

⁵³ See *id.* ch. 159, art. 4, §§ 159-43, *et seq.* ("Local Government Bond Act"); *id.* art. 5, §§ 159-80, *et seq.* (revenue bonds), *id.* art. 5A, §§ 159-99, *et seq.* (capital appreciation bonds); *id.* art. 6, §§ 159-101, *et seq.* (project development financing), *id.* art. 8, §§ 159-148, *et seq.* (financing arrangements), *id.* art. 9, §§ 159-160, *et seq.* (bond anticipation, tax, revenue, and grant anticipation notes).

⁵⁴ See N.C. Const. art. V, § 4(2) ("The General Assembly shall have no power to authorize any county, city or town, special district, or other unit of local government to contract debts secured by a pledge of its faith and credit unless approved by a majority of the qualified voters of the unit who vote thereon . . .").

⁵⁵ See *id.*, art. V, § 4(1) ("The General Assembly shall enact general laws relating to the borrowing of money secured by a pledge of the faith and credit and the contracting of other debts by counties, cities and towns, special districts, and other units, authorities, and agencies of local government.").

⁵⁶ See *id.*, art. V, § 2(1) ("The power of taxation shall be exercised in a just and equitable manner, for public purposes only, and shall never be surrendered, suspended, or contracted away.").

is echoed in the statutes, which require that local government expenditures be made in order to “carry out any public purpose that the city is authorized by law to engage in.”⁵⁷

- North Carolina’s Constitution similarly directs the General Assembly to adopt laws permitting local governments to enter into private contracts and to make associated appropriations for a “public purpose.”⁵⁸
- North Carolina’s Constitution prohibits local governments from extending credit to third parties except as authorized by law and approved by the voters.⁵⁹

Each of these activities — incurring debt, entering into contracts, appropriating public funds, and securing obligations of others — is potentially implicated when and if a local government seeks to incur debt and make expenditures for the purposes of building government-owned broadband networks.

Moreover, the General Assembly has established mechanisms to ensure effective and active state oversight of local government finance. Among such mechanisms, the General Assembly has established a Local Government Commission (“LGC”) that is charged with reviewing and approving local government debt obligations.⁶⁰ The LGC was established in 1931 to help address problems in local government finance caused by the Great Depression and is focused on three areas of responsibility:

First, a unit of government must seek LGC approval before it can borrow money. In reviewing each proposed borrowing, the LGC examines whether the amount being borrowed is adequate and reasonable for the projects and is an amount the unit can reasonably afford to repay. Second, once a borrowing is approved, the LGC is responsible for selling the debt (or bonds) on the unit’s behalf. . . . Third, the LGC staff regulates annual financial reporting by oversight of the

⁵⁷ See N.C.G.S. § 160A-20.1.

⁵⁸ See N.C. Const., art. V, § 2(7) (“The General Assembly may enact laws whereby the State, any county, city or town, and any other public corporation may contract with and appropriate money to any person, association, or corporation for the accomplishment of public purposes only.”).

⁵⁹ See N.C. Const., art. V, § 4(3) (“No county, city or town, special district, or other unit of local government shall give or lend its credit in aid of any person, association, or corporation, except for public purposes as authorized by general law, and unless approved by a majority of the qualified voters of the unit who vote thereon.”).

⁶⁰ See N.C.G.S. ch. 159, art. 2, §§ 159-3, *et seq.* One of the problems addressed by the General Assembly in the Law was that the LGC’s policies and procedures were designed with governmental — not proprietary — projects in mind. The Law addresses this by concerns relevant to a competitive environment were considered by the LGC when approving loans.

annual independent auditing of local governments, by monitoring the fiscal health of local governments and by offering broad assistance in financial administration to local governments.⁶¹

Similarly, the General Assembly conducts direct oversight of local government debt through its Joint Legislative Committee on Local Government. This committee is charged with reviewing and monitoring local government capital projects that are required to go before the LGC and that require the issuance of debt of more than \$1 million.⁶² Any local project involving debt financing that fits these specified criteria must be reported to the Committee Chairs, Committee Assistant, and the Fiscal Research Division at least 45 days prior to presentation before the LGC.⁶³

Together, these oversight mechanisms and controls demonstrate the North Carolina General Assembly's longstanding, historical control of all matters pertaining to local government finance — matters which fit squarely within the issues addressed by the state's Level Playing Field Act.

This deep-dive into North Carolina's laws merely illustrates, in one state, how unremarkable it is for states to govern municipalities' decisions to compete with the private sector in certain areas. It is as "traditional" for a state to do so as it would be for a corporation to govern how its subsidiaries may spend large amounts of money. In the end, municipalities are essentially nothing more than subsidiary corporations created by states, vested with certain powers, and allowed to operate within boundaries of authority drawn by state constitutions and legislatures. This hierarchical relationship simply cannot properly be severed via federal preemption in this case.

V. Conclusion

We urge the FCC to reject the Petitions and, instead, issue a Notice of Inquiry seeking comment on ways that the FCC can enable broadband deployment within its existing legal authority, as well as comment on ways that Congress could craft legislation to promote the laudable goal of Section 706: "encourag[ing] the deployment on a reasonable and timely basis of advanced telecommunications capability to all Americans." That may well involve specific, narrow federal preemption of state laws. But if so, preemption must be clearly authorized by

⁶¹ See N.C. Dep't. of State Treasurer, *About the Local Government Commission* (last visited Sept. 29, 2014), available at <https://www.nctreasurer.com/slq/Pages/Local-Government-Commission.aspx>.

⁶² See N.C.G.S. § 120-157.2(a).

⁶³ *Id.*

our elected representatives in Congress and it must focus on ensuring that state laws do not stop municipalities from remedying *true* market failure (if it exists) by providing broadband service in areas where private deployment will not occur, even when municipalities make deployment as easy as possible. The laws at issue here do not, in fact, bar such deployment, and there is far more that municipalities can do to unleash private deployment — at a fraction of the cost. The more time and expertise the Commission squanders on this misbegotten proceeding, which will surely fail in court, the less such resources it will have to focus on actually helping to promote broadband deployment.