SB 408
Nelson (P. King)
(CSSB 408 by P. King)

SUBJECT: Continuing the Public Utility Commission and revising cable regulation

COMMITTEE: Regulated Industries — committee substitute recommended

VOTE: 4 ayes — P. King, Hunter, R. Cook, Crabb

0 nays

3 absent — Hartnett, Turner, Baxter

SENATE VOTE: On final passage, May 3 — 31-0

WITNESSES: No public hearing

BACKGROUND: Created in 1975, the Public Utility Commission of Texas (PUC) serves to ensure that Texas consumers have access to high-quality, competitive telecommunications and electric utility services. Although created to regulate the rates and services of utility monopolies, the commission now focuses primarily on oversight of those markets though rulemaking and enforcement. The PUC is governed by three full-time commissioners who represent the public and are appointed by the governor, with advice and consent of the Senate, to serve six-year terms.

The PUC underwent sunset review in 1999 and was continued by the 76th Legislature. If not continued by the 79th Legislature, the commission will be abolished September 1, 2005.

The Electric Reliability Council of Texas (ERCOT) is one of 10 regional reliability councils in North America and the Independent System Operator for the ERCOT area. ERCOT is responsible for facilitating wholesale electricity transactions among power generators and retailers, ensuring customer information is provided to retailers, maintaining the reliability of the transmission network, and ensuring open access to the network.

Federal law, in 47 U.S.C., ch. 5, subch. 5-A, regulates cable service providers. Sec. 541 authorizes a municipality to award a franchise to a cable provider authorizing construction of a cable system in the municipality's jurisdiction. It requires a provider to assure that access to cable service is not denied to any group of potential residential cable subscribers because of the income of the residents. Under sec. 542, a municipality may require a provider to pay a fee for its franchise. A municipality may regulate the services and fees of a franchised provider to the extent provided under federal law.

47 C.F.R. 76.309(c) requires cable operators to maintain certain basic customer service standards, which govern office hours, 24-hour telephone availability, installation, service calls, outages, and billing.

DIGEST: CSSB 408 would continue the PUC for six years, until September 1, 2011. The bill would add two commissioners appointed by the governor with the advice and consent of the Senate, creating a five-member governing body. The bill also would establish a statewide franchise authorizing a cable or video service provider to offer service in the state. The bill would direct the PUC to conduct a study on municipal compensation for access to rights of way.

Continuing the Public Utility Commission.

The bill would continue the PUC for six years, until September 1, 2011. The bill would add two commissioners appointed by the governor with advise and consent of the Senate, creating a five-member governing body.

Definitions. The bill would add the term "provider" – meaning service or network provider – to several areas of the statute. The bill would define "service" as basic local telecommunications service, interexchange telecommunications service, local exchange telephone service, electrical transmission service, and a service provided by an electric or telecommunications utility. The bill would exclude from the definition of "affiliate" a broker, dealer, bank, insurance company, investment adviser, or investment company. The definition also would exclude an employee benefit plan, pension fund, endowment fund, or other entity that held between 5 and 15 percent of the voting securities of a public utility, provided that the fund did not acquire the utility for the purpose or with the effect of influencing the utility.

Representation. A person representing an entity in a contested proceeding would have to be a licensed attorney. The commission could make an exception to this requirement.

Commission eligibility. To serve on the PUC, a person could not currently own stocks or bonds of $10,000 or more in a utility, provider, or affiliate upon appointment. (Under current law, a person cannot have owned such stock in the two years prior to appointment.) The bill would delete a provision preventing a person from serving on the commission if that person or the person's spouse held a 10 percent interest in an entity affected by a PUC decision in a manner other than by the setting of rates. The bill instead would prohibit a person from serving if that person or the person's spouse had a 10 percent interest in a "utility, provider, affiliate, or direct competitor."

Reporting of transactions. Provisions requiring a utility to report buying or selling a plant or merging with another utility would not apply to a provider holding a certificate of operating authority on August 31, 2005, or an incumbent local exchange carrier. Transactions that were reported to a federal agency, another state, or another agency also could go unreported.

Administrative penalties. The PUC could impose a $10,000 penalty for each violation of statute, rule, or order. A violation would not be a separate violation for each day it occurred but would count as only one violation. The PUC would have to establish a classification system for violations under which a penalty could exceed $10,000 only if it were in the highest class of violations.

The bill would institute a statute of limitations under which the commission could not initiate the process of assessing an administrative penalty later than two years after the date on which the violation occurred or the date on which the commission knew that the violation occurred.

If the PUC executive director contended that a violation occurred, the director would have to issue a report stating the facts on which the contention was based, including whether service to an end-user was the basis for the contention. An alleged violator would have 60 days, instead of the current 20, by which to accept or contest the executive director's contention. A contested hearing would be conducted by the PUC or by the State Office of Administrative Hearings. Action for civil damages could be brought against a violator but could not be brought if the PUC had acted to address the conduct as a market power violation or as a violation of ERCOT rules. A disgorgement or refund would have to be paid to ERCOT for distribution according to the PUC.

Assessment on utilities and providers. The assessment on utilities and providers to help fund the administration of Public Utilities Regulatory Act (PURA) could not exceed one-sixth of 1 percent of the gross receipts from services over which the PUC had jurisdiction, including interconnection service.

Securitization. The bill would specify that securitization financing should be used by utilities to recover regulatory assets, amounts determined under a true-up proceeding, and any amounts recovered under a competition transition charge.

Review of reporting requirements. After the bill's effective date, the PUC would review and report on its statutory and administrative reporting requirements for telecommunications providers. The report would include actions taken by the commission to amend rules after the review and recommendations for legislation necessary to change statutory reporting requirements.

Across the board recommendations. The bill would add standard sunset provisions governing conflicts of interest, grounds for removing a board member, division of responsibilities, negotiating of rulemaking, technology, and complaint procedures.

Statewide cable franchise.

An entity seeking to provide cable or video service in the state would be required to file an application for a state franchise with the PUC. The application would include an affirmation that the entity had filed all required federal forms, an agreement to comply with all applicable state and federal regulations, a description of the geographic areas to be served, and the entity's principal place of business and executive officers.

The franchise certificate issued by the PUC would grant authority for the entity to provide cable or video service and use public rights-of-way to deliver that service. This authority would be subject to a requirement that the applicant lawfully operate the service.

Municipal franchises. As of September 1, 2005, a cable service provider could terminate any municipal franchise by providing notice to the affected municipality. Such a provider would have to remit any franchise fees that had been accrued but not paid within 90 days. The provider could deduct any credit from future fees it had to pay.

A provider choosing to terminate an existing franchise or initiate service after September 1, 2005, would have to pay each municipality a fee equal to 5 percent of the provider's gross revenues. The fee would be paid quarterly and would be accompanied by a summary explaining the calculation. A provider could recover this fee from its customers.

"Gross revenues" would be defined as:

- all considerations derived by a provider from its cable or video service system in the municipality;
- all fees charged to cable or video service subscribers;
- commissions paid to a provider for exhibition of products through "home shopping" programs; and
- a portion of advertising revenue, calculated by dividing the number of subscribers in the municipality by the subscribers related to the relevant regional or national advertising compensation arrangement.

Gross revenues would not include:

- revenue billed but not received;
- revenue received by an affiliate in exchange for goods or services used by the provider for cable or video service;
- discounts provided to subscribers, leasing providers, advertisers, or a municipality;
- revenues from non-cable or non-video services, including telecommunications or Internet services;
- revenues paid by subscribers to home shopping producers;
- the sale of service for resale by another, provided that the other provider collected the 5 percent franchise fee from customers;
- any tax imposed upon the provider or its subscribers;
- service provided at no charge, as required by a municipality, including service to schools or government entities;
- revenue foregone through provision of reduced cost service;
- sales of capital assets or equipment;

- reimbursement by programmers for marketing costs incurred by the provider; or
- directory or Internet advertising revenue.

The PUC would be prohibited from preferring or discriminating against any cable or video service provider under a state franchise. A municipality only could:

- require a provider to register with the municipality and provide a point of contact;
- establish guidelines regarding the use of public access channels; and
- require a provider to submit a report addressing any failure by the provider to comply with applicable customer service standards.

If a provider did not submit customer service reports or if the reports verified non-compliance, the municipality could file a court proceeding. The PUC would compile complaints about the quality of service of cable and video providers and post the number of complaints lodged against each provider on its Web site on a quarterly basis.

A municipality could not require compensation for a provider's right or privilege to provide service or use a public right-of-way.

Quality of service. A cable or video provider could not deny access to service by a group of potential residential subscribers in an area because of the income of residents. A provider could satisfy this requirement by using an alternative technology, even if that alternative differed in terms of content or functionality. Neither the state nor a political subdivision could require a provider to build out a network, except as specifically required under federal law.

An affected person, including a municipality in which an affected person lived, could seek enforcement of this provision by initiating a proceeding with the PUC. Should a court find a provider in violation, the court would order compliance by the provider. Failure to comply would result in penalties that could include revocation of the provider's state franchise.

Federal customer service requirements under 47 C.F.R. 76.309(c) would apply until more than two providers were offering service (including direct-to-home satellite service) in an area.

Public access channels. Within 120 days after receiving a municipal request, a cable or video service provider would have to provide the municipality with capacity in its network to allow public, educational, and governmental access channels (PEGs), where technically capable. If a municipality did not have PEGs as of September 1, 2005, the provider would have to provide:

- up to three PEGs for a municipality of at least 50,000; and
- up to two PEGs for a municipality of less than 50,000.

If a municipality did have PEGs before September 1, 2005, the provider could not provide fewer PEGs than the amount that a municipality had.

A provider could place any channel used by a municipality on any tier of service, except that the municipality could designate up to three PEGs (or two for a municipality less than 50,000) for the lowest service tier for which no equipment was required to receive the channel. If the service was provided only in digital format, the PEGs would be in that format.

If a municipality had not used the three PEGs (or two for a smaller municipality) within 120 days after it had requested the PEGs, access to the additional channel capacity would be provided only if, upon 90 days written notice, the municipality met the following standards:

- if the municipality had one active PEG and desired to activate an additional PEG, the initial channel would be considered actively utilized when at least 12 hours daily were programmed on that channel and at least 40 percent of this programming was nonrepeat programming on average over each calendar quarter;
- if the municipality had two active PEGs and desired to activate an additional PEG, the two would be considered actively utilized when at least 12 hours on each channel on each day were programmed and at least 50 percent of this programming was nonrepeat programming on average over three consecutive calendar quarters.

"Nonrepeat programming" would include the first three times a program was video-cast.

A municipality would have to pay for any construction required to establish a connection between the municipality's origin point and the provider's network. The operation of a PEG would be the municipality's responsibility. Any PEG that was not utilized for at least eight hours a day no longer would be made available to the municipality and could be programmed at the provider's discretion. The PEG could be restored, but the provider would have no obligation to carry the channel on a basic or analog tier. The municipality would be responsible for ensuring that all programming over a PEG was submitted in a format capable of being transmitted by the provider.

A municipality could not require a provider to pay any fee to support PEGs.

Grandfathered services. Whether or not a cable provider chose to terminate a municipal franchise as authorized by this bill, a provider that had been operating under a municipal franchise would be required to continue certain services that it had been furnishing under its terminated franchise until the earlier of 2015 or the date on which its franchise was going to expire. This would include:

- network capacity for noncommercial use by the municipality; and
- cable services to community buildings such as municipal or public school buildings.

Applicability of other laws. Nothing in the bill would prevent a municipality or voice, cable, or video service provider from seeking clarification of its obligations under federal law or exercising any right under federal or state law.

Other provisions.

Study. The PUC would have to conduct a study and issue a report to the Legislature by September 1, 2006, with recommendations regarding municipal compensation from voice, video, and cable providers.

Repealed. The bill would repeal sections governing:

- liberal construction of Public Utilities Regulatory Act (PURA);
- recovery of attorney fees by a utility for a case brought in bad faith;
- civil penalties against utilities, pay phone providers, and affiliates;
- third-degree felony offenses;
- complaints regarding RV park owners;

- consumer protections; and
- broadcaster safeguards.

Effective date. The bill would take effect September 1, 2005. Changes related to attorney's fees, civil penalties, felony offenses, eligibility requirements of the PUC commissioners, and administrative penalties would apply only after the effective date of the bill.

SUPPORTERS SAY:

Continuing the PUC. By continuing the PUC for six years, CSSB 408 would retain this important regulatory agency. Allowing the commission to go through the sunset process again in six years is a necessary requirement for an agency governing the telecommunications and electric industries. Both of these industries involve rapidly changing technologies and regulatory requirements, and it would be appropriate to review the agency again in six years to ensure that the PUC's regulatory practices appropriately track changes in these industries.

Increasing the PUC governing body from three to five commissioners would improve representation and administration on the commission. Currently, any time two commissioners meet, that meeting is subject to open government provisions that require the meeting to be public and posted to allow for public involvement. This is an impractical arrangement that impedes the efficiency of the commission's deliberation and decision-making process.

Administrative penalties. By doubling the maximum penalty the PUC could administer from $5,000 to $10,000, the bill would strengthen the commission's enforcement authority over violations of PURA. A two-year statute of limitations on violations of PURA is necessary to provide utilities and providers with a measure of regulatory certainty in their dealings with the commission and consumers. The bill would allow the PUC to initiate the process of assessing a penalty up to two years after the commission had determined a violation had occurred, an appropriate expectation of action on the part of the commission.

Statewide video service franchise. By establishing a level playing field for competition and choice in cable and video services, CSSB 408 would put Texas at the forefront of regulatory modernization in this rapidly innovating industry. New technologies like high-speed fiber to the home and broadband provide for the convergence of voice, data, video, and other services and maximize the benefits the consumer could receive from information technology. CSSB 408 is necessary to allow deployment of integrated technologies and encourage private investment that would benefit Texas consumers.

CSSB 408 would streamline state and municipal regulation of cable service providers. Currently, before a cable provider enters a market, that provider must negotiate a franchise agreement with a municipality, an expensive and inefficient process. The result is a maze of regulations that present a barrier to entry for cable competitors. By establishing a statewide franchise, the bill would eliminate the need to negotiate individual agreements while establishing a system of stable, predictable franchise fees that have become a vital component of city budgets.

CSSB 408 would allow Texas customers to enjoy the benefits of competition in cable service that they have enjoyed in telecommunications service since the mid-1990s. Currently, incumbent cable companies generally operate as monopolies under local franchise agreements, limiting competition and consumer choice in most communities. The bill would tear down barriers to market entry and competition by ensuring that all video service providers operated under a single set of clear, equitable rules.

Federal law on cable regulation is unsettled, and Texas should provide leadership by ensuring that all companies compete on a level playing field. Municipalities and providers could seek further clarification from the courts or the FCC as to their obligations, allowing Texas to be at the vanguard of regulatory innovation.

Current safeguards that benefit cities, schools, and consumers would be affirmed under CSSB 408. The bill would provide for a base number of public access channels that many cities use for educational and civic purposes. The bill would incorporate federal requirements prohibiting discriminatory treatment of low-income citizens but would allow companies to meet this obligation through new technologies rather than archaic network build-out mandates. Federal customer service requirements would remain in place until adequate competition existed in an area.

Securitization financing. CSSB 408 would benefit consumers by allowing a utility to securitize all costs deemed recoverable under a PUC true-up proceeding. Under current law, only charges stemming from stranded costs and regulatory assets may be securitized. The bill would allow other costs related to the transition to competition, such as a utility's final fuel balance and capacity auction fees, to be securitized as well.

Through securitization, a utility can lock in its costs and sell that debt at a low rate of interest to other investors in the same way that homeowners refinance their mortgages. Thus, instead of the 10 percent or 11 percent interest rate that likely would accompany costs financed through a utility’s cost of capital, securitization would yield a lower interest rate of 4 percent to 5 percent on those costs. Consumers would see the benefit of securitization through lower utility rates.

OPPONENTS SAY:

Continuing the PUC. The PUC has worked very well as a three-member commission, and there is not a compelling reason to increase the number of commissioners to five. Consumers and regulated entities currently can be sure that all deliberations and decisions made by the commissioners will be open to public scrutiny. Small public interest organizations representing consumers could see their influence decline, as they might find their attention and limited resources stretched among five commissioners rather than three. Adding two more commissioners and their support staff would cost the state almost $1.2 million per biennium, and this money could be applied to more pressing needs elsewhere in the state budget.

Administrative penalties. Because administrative penalties no longer would be calculated on a per day, per violation basis, CSSB 408 would weaken the PUC's authority to punish entities that violate the law. If a utility or provider perpetrated a single type of violation that lasted several days, that entity would be fined only once, rather than being punished for each day a violation occurred. The longer an entity committed a violation, the more cost-effective that violation would become. Rather than weakening administrative penalties, the bill should include the sunset staff recommendation that the maximum administrative penalty be increased to $25,000 per day, per violation.

It can take months, if not years, for the PUC to determine whether an action by a regulated entity constitutes a violation. A two-year statute of limitations could deter the PUC from thoroughly proceeding with investigations to determine whether a violation occurred.

Statewide video service franchise. CSSB 408 would discriminate against existing cable providers that are subject to extensive federal, state, and local regulations governing network build out, quality of service, and public access channels, among other requirements. Cable companies that have built networks throughout entire cities would be at a disadvantage compared to new entrants, which could build only in neighborhoods with the most profit potential. SBC and other major telecommunications providers could corner the most lucrative sections of the market, harming consumers overall and providing only the illusion of true competition.

Under the guise of "intermodal competition," CSSB 408 would open the door to abusive redlining practices by new entrants in the cable market. The bill would purport to allow "alternative technologies" to satisfy nondiscrimination mandates. However, the availability of ubiquitous yet expensive direct-to-home satellite technology likely would satisfy nondiscrimination requirements while remaining an unrealistic option for low- or middle-income consumers. New providers would be free to build video networks in higher income areas while denying the cost and service benefits of new technologies to low-income Texans.

CSSB 408 would undermine local control for cities that currently can negotiate cable franchise agreements that are appropriate to the diverse needs of cities across the state. The bill would allow cable providers to opt out of negotiated agreements that often allow cities to enforce customer service standards and ensure universal service. In addition, franchise agreements provide many cities with services and grants that would be lost under the bill. The LBB estimates that Houston, Dallas, Austin, and Fort Worth all would lose from $1-2 million annually. The uniform franchise under the bill would impose a one-size-fits-all solution that simply would not work for many communities.

Securitization financing. Utilities should not be able to securitize additional transition costs. Once securitized bonds are issued, they are irrevocable. Utilities will have recovered those costs up front, rather than over time. Adjusting these costs could be difficult if it was determined upon appeal that the estimates were inaccurate.

OTHER OPPONENTS SAY:

Continuing the PUC. Given the technological innovations and regulatory changes that have occurred since the PUC was established in 1975, the Legislature should seriously consider whether a stand-alone agency is needed to oversee the electric and telecommunications markets in Texas.

Consumer protection and most other essential functions could be handled by the attorney general and relevant federal agencies. The state embarked upon a path toward full and open competition in utility markets in the 1990s, and this stand-alone agency that oversees and regulates these industries is a relic from an outmoded regulatory framework. In this era of intermodal telecommunications competition and retail electric choice, the PUC's functions no longer are necessary.

Statewide video service franchise By initiating vast policy changes while also requiring the PUC to study the issue of municipal fees from communications service providers, CSSB 408 effectively would "put the cart before the horse." While municipal cable franchising may be in need of reform, the Legislature should allow the PUC to study the issue first and then provide recommendations. The Legislature should initiate dramatic policy changes such as those in CSSB 408 only after it has a better sense of what the impact of these proposals might be.

NOTES:

According to the fiscal note, SB 408 would result in a cost of $2.7 million in general revenue in fiscal 2006-07. Adding two PUC commissioners and their support staff would cost $1.2 million in general revenue in fiscal 2006-07. Adding 17 additional positions to regulate cable and video providers would cost of $1.5 million in general revenue in fiscal 2006-07.

Under the Senate-passed version of SB 408, the PUC could have imposed a $25,000 penalty for each violation of statute, rule, or order. A violation would have been a separate violation for each day it occurred. The committee substitute added language similar to the House version of the PUC Sunset bill, HB 1779 by P. King, which was considered by the House on May 12 and left pending.

The Senate-passed version of SB 408 also would have made numerous changes to the governance, administration, and reporting requirements of ERCOT. Many of the changes in SB 408 regarding ERCOT were included in HB 1777 by P. King, which passed the House on May 6 and has been referred to the Senate Business and Commerce Committee. The ERCOT changes in HB 1777 were added to CSSB 743 by Fraser, which also is on today's Major State Calendar.

The committee substitute also includes provisions similar to HB 3179 by P. King, governing the state cable franchise. HB 3179 was placed on the General State Calendar for May 12 but was not considered by the House.

It also includes the securitization changes in CSSB 1495 by Fraser, which was set on the May 19 General State Calendar and postponed until today.

SB 408 previously was considered by the House on May 18. The bill was recommitted to the Regulated Industries Committee following a point of order. The current version of CSSB 408 removed provisions that had been in the previously considered House committee substitute, specifically those governing access to public rights-of-way by communications service providers and relocation of communication facilities located in a public right-of-way. The previous version of the House committee substitute for SB 408 was analyzed in the May 18 Daily Floor Report.