Deceptive Myths About Municipal Broadband

Disinformation about public ownership is impeding progress

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In October and November of 1906, when electrification was the must-have new technology of the era, *Moody's Magazine* invited the leading advocates and opponents of municipal electric utilities to write chapters for a special issue. The opponents contributed the following chapters: "Municipal Ownership Costly and Dangerous," "Municipal Ownership a Business Problem," "Municipal Ownership a Delusion," "Municipal Ownership Uneconomic," "Why Municipal Service is Expensive," and "Municipal Ownership Always a Failure."

With the benefit of hindsight, we know that every one of these claims was wrong. More than 2,000 municipal electric utilities have thrived over the last century, contributing greatly to the well-being of their communities and America as a whole. Another 1,000 communities established their own electric utilities and then sold them to the private sector, having achieved their goal of avoiding being left behind in obtaining the benefits of electricity. In contrast to these 3,000 successful municipalities, thousands of communities that waited for the private sector to get around to them stagnated or even became ghost towns. For an extensive comparison of the early years of the electric power industry and the broadband industry today, see http://www.baller.com/library-art-history.html.

Now, despite the lessons of history, the major telecommunications and cable providers and their retained "experts" have resurrected the same discredited arguments to oppose municipal efforts to accelerate the pace of broadband deployment in America. In this article, we take a hard look at the ten most common myths that the telephone and cable companies tell about municipal broadband and show that these canards are no more valid today than they were a century ago.

Myth #1: Municipalities want to compete with the private sector.

Municipalities rarely, if ever, go forward with a municipal broadband project for the purpose of competing with the private sector, even though that would arguably be a worthy goal. Rather, they step forward only when the public demands it, because the private sector is either not providing a service at all, or is charging excessive rates, providing poor service, or offering unduly limited consumer choice.

Contrary to the distorted image of wild-eyed, hare-brained municipalities that major telecommunications and cable companies try to paint, the vast majority of local officials are conservative, risk-averse and respectful of the business community, including the existing communications providers. After all, local officials live with the voters they serve, and they know that they will be judged harshly if they make major mistakes. Local officials may be overly optimistic when they begin to study the community's communications options, but the open processes that they must use will ensure that they are well-informed by the time that they must make decisions. Major municipal communications projects always receive intensive public scrutiny, with the private sector fully engaged. As a result, such projects rarely go forward unless there are compelling reasons for them and they have a high probability of success.

Furthermore, municipalities have significantly different goals than the private sector. Private entities must meet shareholder demands for high, short-term profits, primarily from subscriber revenues. As a result, they try to milk every last dollar of profit out of their existing copper or cable facilities, and they make investments in new technologies and facilities only if, when, and where necessary. Not surprisingly, private providers typically focus on their most lucrative, high-density markets and ignore or delay upgrading rural or poor urban areas.

In contrast, local governments typically view their primary mission as enhancing the economic vitality of their community – that is, ensuring that the community will be able to compete successfully with other communities in America and abroad in attracting, retaining, and expanding businesses and jobs. Also high on the list of municipal priorities are promoting educational and occupational opportunity, ensuring affordable access to modern health care, revitalizing urban cores, facilitating digital equity, reducing traffic congestion, street cuts, and other burdens on the en-

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vironment, strengthening public safety and homeland security, and fostering cultural enrichment and a high quality of life. While an advanced communications network will not itself enable a community to meet all of its goals, having such a network will give the community a huge advantage over those that do not.

In short, competition with the private sector is hardly ever the driving force behind a community's decision to develop an advanced communications system. Rather, it is usually a byproduct of the community's efforts to achieve its primary goals.

Myth #2: Municipalities, as regulators, favor their own service entities over the private companies they regulate.

Municipalities do not, and cannot, favor their own municipal service entities. Municipalities do not regulate telecommunications service providers or Internet access providers. Such regulation occurs at the federal and state levels, and even there, regulation is disappearing rapidly. Municipalities do issue franchises to cable operators, but cable franchising is governed by detailed federal standards, and when municipalities provide cable services themselves, they typically assume regulatory burdens that are as extensive, or more extensive, than the private sector's.

Municipalities also manage public rights of way and other public facilities. But federal and most state laws require municipalities to act in a nondiscriminatory, competitively neutral manner. In short, the premise underlying this myth – that municipalities have power to regulate in favor their own services – is simply false.

Myth #3: Municipalities have access to cheap financing.

While municipalities theoretically have the ability to obtain tax-free or tax-advantaged financing, these advantages are often illusory, particularly in the current financial market. In fact, many municipalities have found that the strings attached outweigh the few basis points they can save by using tax-advantaged financing. As a result, many municipalities now use taxable financing, just like the private sector, to fund public communications projects.

Furthermore, municipalities are much smaller and have far fewer assets to back up their borrowings than the giant incumbent private-sector communications providers that complain the loudest about the supposed advantages the municipalities enjoy. While it is true that some telecommunications and cable companies are in financial difficulty, many of the large national companies, which can back investments in particular communities with the assets and revenues of the company as a whole, have a huge advantage in obtaining favorable financing. What's more, those in financial difficulty should welcome the opportunity to provide service over a municipal system as an alternative to rebuilding their own facilities.

Myth #4: Municipalities don't have to pay taxes.

Opponents of municipal broadband maintain that municipal utilities have an unfair advantage over the private sector because they do not have to pay taxes. In fact, municipal utilities make "payments in lieu of taxes" to local governments that are usually much higher than the state and local taxes that private entities pay. For example, a survey of nationwide data by the American Public Power Association showed that municipal electric utilities pay an average of 5.8 percent of their revenues to state and local governments, while their private-sector counterparts pay an average of 4.9 percent. The survey is available at http://www.appanet.org/files/PDFs/PilotReport2002.pdf.

In some states, the disparity is much greater. For example, the Florida Municipal Electric Association recently found that, in 2003, municipal utilities in Florida paid an average of 14.6 percent of their revenues to state and local governments; whereas BellSouth paid 3.4 percent and Verizon paid 3.6 percent. The study is available at http://www.baller.com/pdfs/fmea_white_paper.pdf.

It is true that municipal entities do not pay federal or state income taxes, but that is so because they are non-profit organizations. At the same time, municipalities are not eligible for the billions of dollars of investment tax credits, accelerated depreciation, and other tax write-offs that often bring the effective income tax rates of private entities down to zero or less. Private-sector telecommunications providers were one of the most heavily tax-subsidized industries in America between 2001 and 2003. The nominal federal tax rate for corporations is 35%; private-sector telecommunications companies paid an average of only 7.5%. In particular, SBC ranked second and Verizon fourth among American companies in federal tax subsidies received during this period. The complete report is available at the Citizens for Tax Justice Web site, http://www.ctj.org/corpfed04an.pdf.

Similarly, according to data compiled by the Florida Municipal Electric Association, Florida's major local telephone companies received federal subsidies of \$83.7 million in 2004 and \$389 million in the five-year period ending in 2004 (see the Florida Municipal Electric Association article noted above for details).

Myth #5 Municipalities use public funds to cross-subsidize communications services.

The issue of cross-subsidization is full of ironies. The major telecommunications and cable companies complain bitterly that municipalities have the *potential* to cross-subsidize communications services, but for a variety of legal and political reasons, municipalities hardly ever actually do so. In contrast, the companies themselves routinely cross-subsidize their own communications services on a massive scale.

What's more, at a time when America desperately needs to accelerate the de-

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ployment of advanced communications networks, particularly in the high-cost rural and urban areas that telecommunications and cable companies are not serving adequately, it is ludicrous for these companies to insist that municipalities should be barred from taxing themselves, using surplus revenues from other utilities, or using any other means that their citizens believe to be necessary and appropriate to develop such networks.

Specifically, over the last four years, the United States has sunk to 16th in the world in per capita broadband deployment. America is also falling rapidly behind in access to high capacity broadband and cost per unit of bandwidth capacity. Given the tremendous importance of broadband to America's local, regional and global competitiveness, America should be using every tool at its disposal to stimulate investment in our broadband future.

The private sector itself has begun to make this point, at least in ways that suit its own purposes. For example, an ad of the United States Telecommunications Association takes note of America's descent in its global broadband standing and calls for removal of "outdated telecommunications laws" (see http://www.thefuturefaster.com/first/default.asp?adno=51&vndrno=9). More specifically, the major telephone companies have repeatedly insisted that their ability to invest in broadband is tied closely to relief from their *telephony*-related obligations (that is, the duty to provide their competitors Unbundled Network Elements at wholesale rates). Also, the cable companies make no apologies for using revenues from cable television subscribers to support upgrades to make their facilities capable of supporting broadband services. In neither case do the telephone or cable companies believe it necessary or appropriate to ask telephone or cable subscribers whether they would use the broadband services that their revenues are cross-subsidizing or whether they would prefer lower telephone or cable rates. Yet, the telephone and cable companies cannot complain loudly enough about the possibility of using municipal taxes or surplus municipal utility revenues to help support the development of advanced municipal communications networks.

If cross-subsidization is truly bad for consumers, as the telephone and cable companies claim, then it should be prohibited across the board, for both the public and private sectors. On the other hand, if cross-subsidization is a good thing, or at least a necessary evil, then we should encourage everyone to do it, including the public sector. There can be no rational basis for discriminating between the public and private sectors, particularly in the name of creating a "level playing field."

Myth #6: Municipal communications projects are likely to fail.

Echoing the false claims of a century ago, the major telephone and cable companies and their paid "experts" maintain that municipal communications projects today often fail or are likely to fail. This claim is flatly untrue. As Annie Collins, Mark Cooper, Harold Feld, Glenn Fleishman, John Kelly, Ben Scott, Esme Vos, and I have repeatedly shown, not a single example of a municipal "failure" stands up to analysis. Our point-by-point refutations of the industry's claims are collected at our website, at http://www.baller.com/barriers.html. The truth is that the vast majority of municipal communications projects have been successful, sometimes spectacularly so.

Myth #7: Municipalities drive investment capital out of the market.

The myth that municipal communications projects drive private capital out of the market is nonsensical on several levels. First, municipalities generally do not invest in communications projects unless the private sector has failed to do so. Thus, if municipalities did not step forward, there would be no investment at all.

Second, from the standpoint of the financial community, it makes no difference whether a project is public or private – the financial community benefits either way. If anything, the financial community benefits more from public projects, which are less risky than private projects have been.

Third, empirical evidence shows that municipal investments increase rather than decrease private investments in a community. See, for instance, Dr. George S. Ford's study, *Does Municipal Supply of Communications Crowd-Out Private Communications Investment?* An Empirical Study, Applied Economic Studies (2005), http://www.aestudies.com/library/crowdout.pdf. Dr. Ford is the Chief Economist for the Phoenix Center for Advanced Legal and Economic Public Policy Studies. His curriculum vitae is available at http://www.phoenix-center.org/FordPCVita15Apr05.pdf.

Myth #8: Municipal communications projects raise First Amendment concerns.

Municipal communications projects do not decrease the number of speakers or limit what they have to say. To the contrary, such projects *increase* the number of speakers who can reach the public. In fact, the availability of a municipal option will become increasingly important in the future if the giant telecommunications and cable incumbents succeed in their efforts to deny Internet service providers and others "open access" to their systems and, at the same time, continue to rely on copper and hybrid fiber coaxial technologies that are likely to have insufficient bandwidth capacity to meet America's projected bandwidth needs.

Myth #9: Municipalities have unfair access to poles, ducts, conduits, rights of way, and other public facilities.

True, all municipalities manage public rights of way and other public assets, and some municipalities operate utilities that own poles, ducts and conduits. As indicated above, however, federal and many state laws require municipalities to act in a non-discriminatory and competitively neutral manner. In addition, having ready access to poles, ducts, conduits, rights of way, and other public facilities cannot be unfair if municipalities allocate their costs appropriately, as they are required to do.

Myth #10. Municipalities should not invest in risky projects when the private sector is ready, willing and able to serve the community's needs.

As already discussed, municipalities are inherently risk-averse and will rarely go forward with projects unless they address critical needs and have a high likelihood of success. The rigorous open processes that municipalities go through before making decisions on major projects further diminishes risks. Most important, the intensive due diligence reviews that lenders perform before agreeing to put their money on the line in municipal broadband projects adds an especially comforting reality check on whether a municipal broadband project is viable. For these and other reasons, no major public communications project has ever failed. By contrast, hundreds of billions of dollars of investment capital have evaporated in failed private-sector projects.

Last Thoughts

As the late two-time presidential candidate Adlai Stevenson once observed, Americans "cannot read the writing on the wall until their backs are up against it."

The time has come for all Americans, including the incumbent cable and telephone companies, to open our eyes to the consequences of America's sinking global standing in broadband deployment. If America is to recover its global leadership, we must quickly pull together, recognizing that our public and private sectors have important roles to play in this endeavor. The longer we wait, the more difficult the task will be.

We owe it to ourselves and to our children to act now, with as much candor, intelligence, and courage as we can muster. ◆

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