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# SORTING THROUGH THE VISION AND THE VAGUENESS OF THE FCC'S VIDEO DIALTONE DECISION

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On July 16, 1992, the Federal Communications Commission ("FCC" or "Commission") took a major step toward implementing what has come to be known as "video dialtone" by greatly expanding the role telephone companies ("telcos") play in transmitting video services to their customers.<sup>1</sup> The *Video Dialtone Decision* is part of an extensive examination of the cable-telco cross-ownership rule,<sup>2</sup> which prohibits telcos from providing video programming and owning cable systems within their telephone service areas. Combined with a 1991 Commission decision,<sup>3</sup> the *Video Dialtone Decision* allows telcos to construct video dialtone systems without obtaining a cable franchise from local authorities. It also permits them to own up to five percent of a video programmer. The *Video Dialtone Decision* allows telcos to enter into financing arrangements, joint ventures and management or consulting agreements with a video dialtone programmer or a cable system which shares construction of the video dialtone infrastructure. Under the *Decision* the FCC claimed jurisdiction over rates charged to video dialtone customers and voted to recommend that Congress eliminate the video programming prohibition contained in the

Communications Act of 1934 ("Communications Act" or "Act").<sup>4</sup>

Describing a "typical" video dialtone system is problematic because the FCC has established only general requirements for video dialtone. Telco programmers and consumer groups have differing views of video dialtone and its capabilities. In other words, the concept of video dialtone is similar to the concept of "family values"—it means different things to different people. Understanding video dialtone, therefore, requires a little imagination. The video dialtone issue itself has become convoluted, involving the FCC, Congress and the courts.

This Article examines the latest FCC pronouncement on video dialtone, with an eye toward confronting the various legal, political and practical issues surrounding this new concept. This Article will first present the varying views on video dialtone. It will then address the regulatory framework behind the concept, and the distinctions between video dialtone, cable and traditional common carrier structures. Next, the Article reviews the FCC's recommendations to Congress regarding video dialtone and the impact the Cable Act of 1992 will have on video

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<sup>1</sup> Telephone Company-Cable Television Cross-Ownership Rules, *Second Report and Order, Recommendation to Congress and Second Further Notice of Proposed Rule Making*, 7 FCC Rcd. 5781 (1992) [hereinafter *Video Dialtone Decision*].

<sup>2</sup> 47 C.F.R. § 63.54 (1992).

<sup>3</sup> Telephone Company-Cable Television Cross-Ownership Rules, *Further Notice of Proposed Rule Making, First Report and Order, and Second Further Notice of Inquiry*, 7 FCC Rcd. 300 (1992) [hereinafter *1991 Decision*], *review petitions dock-*

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*eted sub nom.* National Cable Television Ass'n v. FCC, No. 91-1649 (D.C. Cir. filed Dec. 26, 1991); Community Antenna Television Ass'n v. FCC, No. 91-1656 (D.C. Cir. filed Dec. 31, 1991). Both NCTA and CATA again filed petitions for review (dockets 92-1529 and 92-1538, respectively) after the FCC ruled on various petitions for reconsideration. See Telephone Company-Cable Television Cross-Ownership Rules, *Memorandum Opinion and Order on Reconsideration*, 7 FCC Rcd. 5069 (1992) [hereinafter *Reconsideration Order*].

<sup>4</sup> Communications Act of 1934, as amended, § 613(b)(1), 47 U.S.C. § 533(b)(1) (1988). This section makes it unlawful for a Title II common carrier to "provide video programming directly to subscribers in its telephone service area, either directly or indirectly through an affiliate owned by, operated by, controlled by, or under common control with the common carrier." *Id.*

dialtone. After addressing the specifics of telcos providing video service to rural areas and FCC preemption of state regulatory authority over video dialtone, the Article concludes there is much to be accomplished before video dialtone becomes a reality.

### WHAT IS VIDEO DIALTONE?

Video dialtone has been described as "an enriched version of video common carriage under which [telephone companies] will offer various non-programming services in addition to the underlying video transport."<sup>5</sup> In essence, television sets would be used to connect video dialtone subscribers with video services providers in much the same way telephones are used for aural and data communication. A converter box or similar device would allow subscribers to dial up video services, via a menu, access code or some other gateway. In addition to traditional one-way video services (e.g., broadcast and cable programming), two-way video is a possibility with video dialtone. Thus, picturephones should become a reality. A video dialtone system could also transport non-video services such as voice and data.

Video dialtone is envisioned as a provider of several highly innovative services. Most of the proposed services involve viewer interaction, whereby viewers actually select information or services through the system by way of specialized equipment in the home. One such service is a video catalogue which would allow subscribers to select a product from a directory, request specific information about the product and view video demonstrations of the product. Another possibility is an electronic video newspaper which would allow subscribers to read about an event (e.g., a speech or a baseball game) and then view video clips of the action. Subscribers might also be able to view a program or sporting event and choose their own camera angles.

But the service which has gained the most attention is video-on-demand, whereby a subscriber could access a program in its entirety, at any time. This concept differs from current pay-per-view cable services in that video-on-demand subscribers would not have to wait until the next scheduled showing of the program in order to gain access. The program would

theoretically be available instantaneously. For example, a two-hour movie might be shown on pay-per-view at two-, four-, and six o'clock. Someone wanting to watch it at 4:37 would have to wait eighty-three minutes until the next showing. With video-on-demand, however, the viewer could call the service at 4:37 and start viewing the movie immediately.

The practical difference between video dialtone and traditional cable television systems would be in the manner of choice. Instead of selecting from those services that the *cable operator* chooses to carry, video dialtone subscribers would be able to pick from among the *service providers* who connect to the video dialtone system. Advocates of video dialtone see this as leading to increased choices for consumers because cable systems have limited channel capacity, and a cable operator's decisions regarding which services to carry are often based on other factors, such as whether the operator has a financial interest in a particular service or program.

### REGULATORY BACKGROUND

One concern in implementing video dialtone has been the FCC's cable-telco cross-ownership rules, which have barred telephone companies from providing cable service to their telephone subscribers since 1970.<sup>6</sup> The ban was primarily the result of Commission fears that telcos would use their control over pole and conduit space to extend their telephone monopolies to the nascent cable industry, thereby creating a strangle hold on local information distribution.<sup>7</sup> Specifically, the Commission determined that telcos must provide pole and conduit space to non-affiliated cable operators. And, because the Commission found the likelihood of telco monopolization of local cable markets so great, it completely banned telcos from providing cable service within their telephone service areas, "except where no practical alternative exists to make such service available within a particular community."<sup>8</sup> The FCC has granted several such "good cause" waivers through the years, most notably in 1988 in Cerritos, California.<sup>9</sup>

The cross-ownership prohibition was codified at section 613(b)(1) of the Communications Act by the Cable Communications Policy Act of 1984 ("1984

<sup>5</sup> 1991 *Decision*, *supra* note 3, para. 10.

<sup>6</sup> *In re Applications of Telephone Companies for Section 214 Certificates for Channel Facilities Furnished to Affiliated Community Antenna Television Systems, Final Report and Order*, 21 F.C.C.2d 307 (1970), *reconsidered in part*, 22 F.C.C.2d 746 (1970), *aff'd sub nom. General Tel. Co. of the Southwest v. United States*, 449 F.2d 846 (5th Cir. 1971).

<sup>7</sup> 21 F.C.C.2d para. 46.

<sup>8</sup> *Id.* para. 48.

<sup>9</sup> *In re General Tel. Co. of Cal., Memorandum Opinion, Order and Certificate*, 3 FCC Rcd. 2317 (1988), *rev'd by Memorandum Opinion, Order, and Authorization*, 4 FCC Rcd. 5693 (1989), *remanded sub nom. National Cable Television Ass'n v. FCC*, 914 F.2d 285 (D.C. Cir. 1990).

Cable Act").<sup>10</sup> However, the 1984 Cable Act went further than the Commission's previous decision, banning telco provision of cable services by prohibiting telcos from providing any video programming in their telephone service areas. Video programming is defined as "programming provided by, or generally considered comparable to programming provided by, a television broadcast station."<sup>11</sup> The result of this language was to bar a telco not only from providing cable service, but also from providing any video programming that was transmitted to a telco's subscribers, either directly or through an affiliate owned or controlled by the telco.<sup>12</sup> Telcos were prohibited from "providing channels of communications or pole line conduit space" to an affiliated entity in order to provide video programming within their telephone service area.<sup>13</sup> However, nothing prohibited telcos from constructing the facilities and leasing them to a nonaffiliated cable operator in what is called a "lease-back" arrangement.<sup>14</sup>

During the 1980s there was tremendous growth in the cable industry, due largely to satellite technology and in part to Congress' goal of encouraging the young cable industry. At the outset of the decade, there were 4,225 cable systems in the United States, serving 15.2 million subscribers.<sup>15</sup> By 1988, the number of cable systems had nearly doubled to 8,000, and subscribership nearly tripled to forty-five million.<sup>16</sup> In addition, the cable industry was becoming more concentrated. By 1990, the combined subscribership of two multiple system operators ("MSO")<sup>17</sup>—TCI and Time Warner—accounted for almost thirty-four percent of the nation's cable subscribers.<sup>18</sup> The top ten MSOs claimed 61.79 percent of all subscribers.<sup>19</sup> This increased concentration existed in tandem with vertical integration between MSOs and cable programmers. By the end of the decade, MSOs held equity interests in thirteen of the top twenty national basic cable services and six of the eight national pay cable services.<sup>20</sup> New services

were more likely to be vertically integrated. Sixty-four percent of the cable programming services launched since passage of the 1984 Cable Act were vertically integrated with MSOs, compared to only thirty-eight percent of those begun before 1984.<sup>21</sup> Many local cable operators became firmly entrenched monopolists, capable of preventing nonaffiliated programmers from reaching cable subscribers and precluding their few existing multichannel services competitors from carrying some of the more popular cable programming.

By the end of the decade, it was quite clear that cable was no longer an industry in need of protection. In fact, the late 1980s precipitated a call for more competition to the monopolist cable companies. As a result, the FCC initiated an inquiry in 1987 to determine whether there was still a need for the cable-telco cross-ownership restriction.<sup>22</sup> The immediate result was a tentative conclusion that, although telcos

continue to have the ability to engage in anticompetitive conduct towards cable operators, these concerns no longer justify the ban because of the growth and success of the cable industry since 1970 and because nonstructural safeguards are available which would allow the public to receive the benefits of cross-ownership between telephone companies and cable systems while preventing carrier anticompetitive conduct.<sup>23</sup>

The Commission, however, made no recommendation at the time to lift the restriction. It merely solicited comments on the tentative conclusion "for the purpose of developing the fullest possible record on which to base legislative recommendations to Congress."<sup>24</sup> Since that time, the Commission has focused on video dialtone as a competitor to cable.

The concept of video dialtone was developed by the U.S. Department of Commerce's National Telecommunications and Information Administration ("NTIA") during former FCC Chairman Alfred Sikes' tenure as NTIA Administrator.<sup>25</sup> At that

<sup>10</sup> Pub. L. No. 98-549, 98 Stat. 2780 (1984).

<sup>11</sup> 47 U.S.C. § 522(16).

<sup>12</sup> *Id.* § 533(b)(1) (1988).

<sup>13</sup> *Id.* § 522(b)(2) (1988).

<sup>14</sup> See *Final Report and Order*, *supra* note 6, para. 49.

<sup>15</sup> NATIONAL TELECOMMUNICATIONS INFO. ADMIN. REPORT 88-223. U.S. DEP'T OF COMMERCE, VIDEO PROGRAM DISTRIBUTION AND CABLE TELEVISION: CURRENT POLICY ISSUES AND RECOMMENDATIONS, 10 (1988) [hereinafter NTIA REPORT].

<sup>16</sup> *Id.*

<sup>17</sup> An MSO is a company operating more than one cable system. FCC, COMMUNICATIONS: A GLOSSARY OF COMMUNICATIONS TERMS 12 (Aug. 1991).

<sup>18</sup> *In re Competition, Rate Deregulation and the Commission's Policies Relating to the Provision of Cable Television Service*, Report, 5 FCC Rcd. 4962, para. 73 (1990).

<sup>19</sup> *Id.* at 5106 Table I.

<sup>20</sup> *Id.* para. 78.

<sup>21</sup> *Id.* paras. 79-80.

<sup>22</sup> *In re Telephone Company-Cable Television Cross-Ownership Rules*, Notice of Inquiry, 2 FCC Rcd. 5092 (1987).

<sup>23</sup> *In re Telephone Company-Cable Television Cross-Ownership Rules*, Further Notice of Inquiry and Notice of Proposed Rule Making, 3 FCC Rcd. 5849, para. 10 (1988).

<sup>24</sup> *Id.* para. 1.

<sup>25</sup> See NTIA REPORT, *supra* note 15, at 32-60.

time, NTIA concluded that telcos should continue to provide only the conduit—not the content—for video programming.<sup>26</sup> Under Sikes, the NTIA established the goal of making cable service available to unserved areas of the country as well as providing competition to monopolist cable operators.<sup>27</sup> To accomplish this goal, NTIA turned to the ubiquitous telephone companies. Local telephone companies would be the logical means to expand video programming delivery because they provided universal service—they served more than ninety percent of the nation.<sup>28</sup> However, NTIA declined to recommend telco ownership of programming because of concerns about the potential for cross-subsidization<sup>29</sup> and discrimination against competitors.<sup>30</sup> Instead, the NTIA, under Sikes, concluded that telcos should provide only the conduit by which nonaffiliated programmers could distribute their wares.<sup>31</sup>

When Sikes became FCC Chairman in 1989, one of his priorities was improving the nation's telecommunications infrastructure.<sup>32</sup> Video dialtone became part of that effort. The video dialtone concept was officially presented in the *1991 Decision*.<sup>33</sup> There, the FCC declared that the cross-ownership provision of the Communications Act did not apply to inter-exchange (i.e., long-distance) carriers because they had no control over local exchange facilities.<sup>34</sup> The Commission also ruled that the cable franchising provisions of section 621 of the Communications Act did not apply to telcos providing common carrier video dialtone services or programmers desiring to connect to telcos' systems.<sup>35</sup> Fearing that cable companies that had to obtain a franchise from local authorities before beginning construction would be placed at a disadvantage, cable interests have sought court review of the franchising decision.<sup>36</sup>

The FCC based its franchising conclusion on an interesting premise: a video dialtone system would

not be cable service as defined by the Cable Act (i.e., one-way transmission of programming with subscriber interaction necessary to select the programming)<sup>37</sup> because, with video dialtone, the telco would only provide the conduit for program delivery.<sup>38</sup> It would not own, control or provide the programming carried over its lines. Therefore, according to the Commission, telcos would not be characterized as cable operators subject to the franchising provision.<sup>39</sup> This is a fundamentally shaky argument because some video dialtone services might indeed be one-way transmissions with the telco providing merely a means for subscriber interaction. In addition, providing programming is only part of the definition of "cable operator." A cable operator can also be anyone who "is responsible for, through any arrangement, the management and operation of such a cable system."<sup>40</sup> Because a telco would be responsible for the management and operation of a system which provides one-way transmission of video programming, arguably it could be deemed a cable operator. Perhaps a better position, merely touched upon in a footnote in the *1991 Decision*,<sup>41</sup> is that video dialtone does not fit the Cable Act's definition of cable system, i.e., "a facility, consisting of a set of closed transmission paths . . . ."<sup>42</sup> Because of its common carrier nature, a video dialtone system would not have closed transmission paths. Instead, it would consist of open transmission paths available on a non-discriminatory basis to all wishing to use it.

The FCC missed a second opportunity to recognize a structural distinction between video dialtone and cable systems in its *Reconsideration Order*.<sup>43</sup> The Commission described video dialtone in that document as common carriage, but did not specifically distinguish the structural differences between video dialtone and cable systems.<sup>44</sup> Instead, the Commission focused on the definition of transmission and

<sup>26</sup> *Id.* at 54-58.

<sup>27</sup> *Id.* at 32.

<sup>28</sup> As of March 1992, 93.9 percent of the nation's households were telephone subscribers. See INDUSTRY ANALYSIS DIV., FCC, TRENDS IN TELEPHONE SERVICE, Table 1 at 2 (Sept. 1992).

<sup>29</sup> NTIA REPORT, *supra* note 15, at 51.

<sup>30</sup> *Id.* at 54.

<sup>31</sup> *Id.* at 36.

<sup>32</sup> See Statement of Alfred C. Sikes, Chairman, Federal Communications Commission, on FCC 1990-91 Re-Authorization Before the Subcommittee on Telecommunications and Finance Committee on Energy and Commerce, House of Representatives, September 14, 1989.

<sup>33</sup> See *1991 Decision*, *supra* note 3.

<sup>34</sup> *Id.* paras. 44-46.

<sup>35</sup> *Id.* paras. 50-52.

<sup>36</sup> See National Cable Television Ass'n v. FCC, No. 91-1649 (D.C. Cir. filed Dec. 26, 1991); Community Antenna Television Ass'n v. FCC, No. 91-1656 (D.C. Cir. filed Dec. 31, 1991).

<sup>37</sup> See 47 U.S.C.S. § 522(6)(A), (B) (1993).

<sup>38</sup> *1991 Decision*, *supra* note 3, para. 51.

<sup>39</sup> *Id.* para. 50.

<sup>40</sup> See 47 U.S.C. § 522(4)(B) (1988).

<sup>41</sup> *1991 Decision*, *supra* note 3, at 326 n.79 (quoting 47 U.S.C. § 522(6), which defines "cable system").

<sup>42</sup> See 47 U.S.C. § 522(6) (1988).

<sup>43</sup> See *Reconsideration Order*, *supra* note 3.

<sup>44</sup> *Id.* paras. 22-23.

the issue of programming generation.<sup>45</sup> Granted, telcos may provide some enhanced video dialtone services on a non-common carrier basis.<sup>46</sup> However, this alone should not undermine a conclusion that video dialtone is not cable service if such a determination is based solely on structural differences between cable and video dialtone systems.

#### CONDUIT VS. CONTENT: ATTEMPTING TO PRESERVE COMPETITION

As common carriers, telcos cannot unreasonably discriminate among their communications customers "in charges, practices, classifications, regulations, facilities, or services."<sup>47</sup> This prohibition could be frustrated if telcos were allowed to provide content in competition with their telephone customers.<sup>48</sup> Telcos would have greater incentives to provide their competitors with inadequate connections to the telephone system or shoddy repair service. Competitors could even face inordinate delays in the provision of service, which could impair or be fatal to their businesses. For example, in 1991 the Georgia Public Utilities Commission found that BellSouth had unnecessarily delayed the provision of a customer's voice messaging service until it was ready to establish service in competition with the customer.<sup>49</sup>

Still, the telcos argue that they need incentives beyond common carrier revenues to build video dialtone systems. Video dialtone will likely be an expensive proposition. Penn State University telecommunications professor Richard Taylor has estimated that telcos could buy the entire cable industry for less than the cost of the facilities upgrades necessary to provide video services over the telephone.<sup>50</sup> The telcos maintain that the new service fails to provide adequate justification for the necessary expense in upgrading their facilities.<sup>51</sup> The telcos are concerned that the emerging video dialtone service will not be immediately attractive to programmers.<sup>52</sup> In essence, the telcos fear that they will give a party and nobody will come. Thus, they assert that in order to ensure that the systems will not go unused, they should be allowed to provide

programming.

With the history of telco-related competition problems as a backdrop, the FCC has moved forward with video dialtone implementation. The *Video Dialtone Decision* adopted a two-tiered approach to regulating video dialtone.<sup>53</sup> The first tier would be common-carrier based, giving multiple service providers equal, nondiscriminatory access to the basic functions necessary to connect them to video dialtone subscribers.<sup>54</sup> Just as telephone users can now access a wide range of services from a wide variety of sources, so too could video dialtone customers have access to an abundant supply of video services from diverse sources.

The second tier would allow telcos to provide some video dialtone services in competition with other providers.<sup>55</sup> Telcos could provide services such as video gateways, which allow consumers to access video dialtone services; video processing functions, which would allow subscribers to store programs or replay portions of programs without a video cassette recorder; tailored menus, searches or other functions; billing and collection; order processing; video customer premises equipment; and inside wire maintenance.<sup>56</sup> The FCC adopted no standards regarding the types of services which must be offered on video dialtone systems or the actual physical components of video dialtone systems. These issues will be addressed on a case-by-case basis, as telcos apply to the FCC for permission to construct the facilities.<sup>57</sup>

The two-tiered scheme provides a carrot-and-stick approach to telco involvement in video delivery. The second, enhanced tier is the carrot in that telcos would be able to provide services free of the shackles of common carriage. But telcos that desire to provide unregulated services (such as video processing or billing and collection) would first have to provide the common carrier level on which their competitors could offer the same services.<sup>58</sup> Theoretically, telcos would not be able to impede competition because of the nondiscrimination standards of common carriage.

The Commission also stated it would rely on two common carrier nonstructural safeguards—open network architecture ("ONA") and comparably efficient

<sup>45</sup> *Id.* paras. 16-19.

<sup>46</sup> See *infra* notes 55-56 and accompanying text.

<sup>47</sup> 47 U.S.C. § 202(a) (1988).

<sup>48</sup> See National Ass'n of Regulatory Utils. Comm'rs v. FCC, 533 F.2d 601, 608-09 (D.C. Cir. 1976).

<sup>49</sup> *In re* Investigation into Southern Bell Provision of MemoryCall Services, Georgia Public Utilities Commission, Docket No. 4000-U, decided May 21, 1991.

<sup>50</sup> *Telco/Cable*, COMM. DAILY, Feb. 12, 1993, at 8.

<sup>51</sup> See *Video Dialtone Decision*, *supra* note 1, para. 122.

<sup>52</sup> *Id.*

<sup>53</sup> *Id.* para. 57.

<sup>54</sup> *Id.* para. 48.

<sup>55</sup> *Id.* para. 12.

<sup>56</sup> *Id.*

<sup>57</sup> *Id.* para. 60.

<sup>58</sup> *Id.* para. 14.

interconnection ("CEI")—to minimize telco anticompetitive behavior.<sup>59</sup> CEI was designed to ensure that common carriers provide all users with nondiscriminatory access to basic network services. It requires that information services providers be given the same access to the telephone network as is offered to their telco competitors. ONA extended CEI principles to the overall design of telco networks.<sup>60</sup>

Whether CEI and ONA requirements can be transported into the video dialtone concept in order to prevent discrimination is questionable. Having been introduced less than six years ago, these safeguard principles are still very young.<sup>61</sup> CEI and ONA have been the constant subject of legal challenge since their adoption, having been vacated by the U.S. Court of Appeals for the Ninth Circuit in 1990.<sup>62</sup> The regulations adopted by the Commission on remand from the Ninth Circuit are again under review by that same court.<sup>63</sup> The FCC's reliance on these non-deployed nonstructural safeguards is, to say the least, misguided.

#### INCREASING TELCO INVOLVEMENT: A LESSON IN CREATIVE INTERPRETATION

Even though telcos will be permitted to provide the numerous aforementioned services, they will remain prohibited from generating the content for video programming within their telephone service areas. This "content" bar is the cornerstone issue of the *Video Dialtone* proceeding. Telcos have argued that the profits generated through video programming ownership would be necessary to justify the added expenditures needed to upgrade facilities.<sup>64</sup> Telco interests contend that with program ownership, video dialtone could be operational by 2010; without it, they claim, it could take an extra twenty years.<sup>65</sup>

Those who oppose telco ownership of programming, and thus agree with the current statutory ban, challenge the telco's need to own programming. The necessity of program ownership has been disputed by several parties who noted studies and other indicators that maintained video dialtone would be sought and used by both consumers and programmers.<sup>66</sup> Telcos also argue that the prohibition on program ownership violates their First Amendment rights.<sup>67</sup> However, the courts have consistently held that the First Amendment rights of monopolists must yield in order to protect the free speech of others.<sup>68</sup>

The Commission did provide some relief to telcos in the *Video Dialtone Decision* by loosening some of the restrictions on program ownership. That relief came in the form of new interpretations of some key terms in the rules: "control" and "carrier-user relationship." The definition of "control" is essential to interpreting the statutory cross-ownership provision because a telco does not violate the provision if it does not control the entity providing video programming over its system. In addition, Note 1(a) to former section 63.54(b) of the FCC's rules allowed only carrier-user relationships between telcos and their video programmer customers.<sup>69</sup> Therefore, telcos could only provide transmission facilities and other common carriage services.

Specifically, the Commission raised from one percent to five percent the cognizable interest which a telco could have in a video programmer.<sup>70</sup> This meant that a telco which owned less than five percent of a video programmer would not be deemed to be in control of the programmer.<sup>71</sup> The FCC also permitted telcos to go beyond the "carrier-user relationship" with any video dialtone customer or an entity sharing the telco's video dialtone infrastructure.<sup>72</sup> Thus, in addition to owning up to five percent of a video programmer, a telco could finance 100 percent

<sup>59</sup> *Id.* paras. 89-96.

<sup>60</sup> See *In re Computer III Remand Proceedings: Bell Operating Company Safeguards*; and Tier 1 Local Exchange Company Safeguards, *Notice of Proposed Rule Making and Order*, 6 FCC Rcd. 174, paras. 33-40 (1990).

<sup>61</sup> Amendment of Section 64.702 of the Commission's Rules and Regulations (Third Computer Inquiry), *Report and Order*, 104 F.C.C.2d 958 (1986).

<sup>62</sup> See *California v. FCC*, 905 F.2d 1217 (9th Cir. 1990).

<sup>63</sup> See *California v. FCC*, No. 90-70083 *appeal docketed* (9th Cir. Feb. 14, 1992).

<sup>64</sup> See *Video Dialtone Decision*, *supra* note 1, para. 122.

<sup>65</sup> Anthony Gnoffo Jr., *The FCC Dials Up the Future*, PHILA. ENQUIRER, July 19, 1992, at D1, D2.

<sup>66</sup> See *Video Dialtone Decision*, *supra* note 1, para. 128.

<sup>67</sup> See *id.* para. 124.

<sup>68</sup> See, e.g., *Associated Press v. United States*, 326 U.S. 1 (1945) (holding application of Sherman Act to newspapers not First Amendment violation); *United States v. Paramount Pictures, Inc.*, 334 U.S. 131 (1948) (court determined there is the possibility of First Amendment problems if movie producers jointly blocked access to films); *Lorain Journal Co. v. United States*, 342 U.S. 143 (1951) (finding injunction under Sherman Act not a prior restraint in violation of the First Amendment). See also *United States v. Western Elec. Co.*, 673 F. Supp. 525, 585-86 (D.D.C. 1987), *aff'd in part and remanded in part*, 900 F.2d 283 (D.C. Cir. 1990), *cert. denied*, 111 S. Ct. 283 (1990).

<sup>69</sup> 47 C.F.R. § 63.54(b).

<sup>70</sup> See *Video Dialtone Decision*, *supra* note 1, paras. 35-36.

<sup>71</sup> *Id.*

<sup>72</sup> *Id.* paras. 22-31.

of the programmer's operation if the programmer were a customer of the telco's video dialtone system.<sup>73</sup> The telco could also enter into a management agreement with the programmer, and jointly venture with the programmer in non-programming aspects of the video dialtone operation, such as the manufacture and distribution of customer premises equipment.<sup>74</sup> The two new provisions combine to give a telco nearly the same rights as a cable operator.

In addition, the FCC took a dangerous step toward merging telephone and cable monopolies. The Commission permitted telcos to have all the aforementioned relationships with any entity sharing the construction and/or operation of the basic tier.<sup>75</sup> Thus, a telco could own up to five percent of, finance all or part of, and enter into other joint ventures with local cable operators who shared the video dialtone facilities. By expanding the definitions of "control" and "carrier-user relationship," the FCC has therefore attempted to circumvent the cross-ownership provision of the Communications Act.

By virtue of being in control of the distribution conduit as well as being capable of all those relationships with programmers, telcos will be in a position to exert tremendous influence over a programmer — possibly to the point of virtual control. The FCC has promised to investigate any situation in which this appears to be occurring.<sup>76</sup> However, the FCC has not provided a mechanism for telcos to report interests in programmers. Thus, the likelihood that the FCC could, on its own, discover telco control over a programmer is marginal at best. The programming ownership provision of the *Video Dialtone Decision* is already under review in several courts.<sup>77</sup> Until that issue is resolved, telcos will likely be hesitant to proceed with large-scale construction of video dialtone systems.

## CALLING CONGRESS TO ACTION

The FCC stopped short of allowing telcos to own

the types of video programming services that have come into existence since 1984.<sup>78</sup> Several telephone interests argued to the Commission that Congress, in passing the 1984 Cable Act, had intended the term "video programming" to mean programming similar to that provided by television broadcast stations in 1984. Therefore, they contend post-1984 innovative video dialtone services fell outside of the definition. Specifically, the telcos were referring to video-on-demand.

The telcos' arguments were strained. In barring telcos from providing their subscribers with video programming "similar to that provided by broadcast television stations" in 1984, Congress drew a distinction between programming and other services which television stations might offer.<sup>79</sup> For example, telcos are free to provide teletext, an information service using computer-generated text and/or graphics.<sup>80</sup> The FCC followed Congress' reasoning in delineating the telcos' role in video dialtone offerings. The Commission ruled that telcos may not generate content if the "service contains severable video images capable of being provided as independent video programs comparable to those provided by broadcast stations in 1984 . . . ."<sup>81</sup> Thus, telcos may not provide content for home shopping services which merely show products in a given time period and take orders from subscribers, but may provide content for video catalogues.<sup>82</sup> In addition, telcos may provide the equipment necessary to interact with either service.<sup>83</sup>

Although refusing to go any further in allowing telco ownership of programming, the Commission recommended that Congress repeal the 1984 Cable Act's statutory prohibition on telco-provided video programming.<sup>84</sup> In doing so, the FCC determined that eliminating the prohibition would lead to increased competition in the video marketplace and greater diversity of video services, as well as spurring investment in the telco infrastructure.<sup>85</sup> The Commission also concluded that the growth of the cable

<sup>73</sup> *Id.* para. 31.

<sup>74</sup> *Id.*

<sup>75</sup> *Id.*

<sup>76</sup> *Id.* para. 36.

<sup>77</sup> See *Mankato Citizens Tel. Co. v. FCC*, No. 92-1404 (D.C. Cir. filed Sept. 1992); *Northwestern Ind. Tel. Co., Inc. v. FCC*, No. 92-1406 (D.C. Cir. filed Sept. 1992); *National Cable Television Ass'n v. FCC*, No. 92-1530 (D.C. Cir. filed Oct. 1992); *Community Antenna Television Ass'n v. FCC*, No. 92-1539 (D.C. Cir. filed Oct. 1992). On November 17, 1992 the D.C. Circuit granted a motion to voluntarily dismiss *National Cable Television Ass'n v. FCC*, No. 92-1530 and consolidated the other cases and designated *Mankato Citizens Tel. Co. v.*

*FCC*, No. 92-1404 as the lead docket.

<sup>78</sup> See *Video Dialtone Decision*, *supra* note 1, paras. 66-76.

<sup>79</sup> See 130 CONG. REC. S14285 (daily ed. Oct. 11, 1984) (Statement by Senator Robert Packwood, Chairman of the Senate Committee on Commerce, Science and Transportation).

<sup>80</sup> See *Teletext Transmission*, 53 Rad. Reg. 2d (P & F) 1309 (1983).

<sup>81</sup> *Video Dialtone Decision*, *supra* note 1, para. 74.

<sup>82</sup> *Id.* para. 76.

<sup>83</sup> *Id.* paras. 75-77.

<sup>84</sup> *Id.* paras. 135-43.

<sup>85</sup> *Id.* para. 135.

industry had lessened the risk of anticompetitive behavior by telcos.<sup>86</sup>

Despite its claim that it had reduced the risk of anti-competitive behavior, the Commission recommended to Congress that it impose anti-competitive safeguards, including a requirement that telcos provide video programming through a separate subsidiary and on the same video dialtone platform that provides service to multiple programmers.<sup>87</sup> The Commission also recommended that the number of channels telcos could program be limited to a specified percentage of overall channel capacity.<sup>88</sup>

The implementation and effectiveness of each of these safeguards is suspect. First, the requirement that a telco provide programming through a separate subsidiary is contingent upon a Commission finding that such a requirement's benefits outweigh its costs.<sup>89</sup> This finding may already be a foregone conclusion. The Commission has stated that "any remaining risk of anticompetitive conduct by the local telephone companies is outweighed by the potential public interest benefits their entry [into video programming] would bring."<sup>90</sup> The Commission appears to have determined that the separate subsidiary requirement is not in the public interest.

Second, although telcos would be required to offer their video programming on a common carrier basis, there are means by which telcos could mask their discrimination against competitors. A federal court recently determined that some companies in the airline industry engaged in anticompetitive activities in connection with the display of flight information on computer services provided to travel agents.<sup>91</sup> The court found that the airlines engaged in a practice known as "display biasing," whereby the flights of one airline were always displayed first on the travel agents' computers. Competing airlines' flight information was oftentimes difficult to access since agents were forced to scroll past numerous flight entries in order to reach the information.<sup>92</sup> Thus, the court maintained that consumer choices were not made solely on the merits of a particular flight, and the value of the preferred airline's flights was artificially inflated.<sup>93</sup> Display biasing, the court found, resulted in a fraud upon the consumer and an unreasonable

restriction on competition.<sup>94</sup> Similarly, telcos could engage in display biasing by having their own services listed first on video dialtone menus or access directories, making it more difficult for consumers to access competitors' services.

A third problem with the recommended safeguards is that limiting the number of channels a telco could program to a percentage of overall capacity could be an exercise in futility. By the very nature of video dialtone systems there would be no "channel capacity" as typically exists in cable systems. Instead, in video dialtone, consumers would be capable of accessing numerous video services at a given moment. Because subscribers would be able to choose among a virtually infinite number of programming sources, and because it is impossible to calculate a percentage of infinity, the channel capacity safeguard is effectively meaningless.

In addition to the aforementioned problems, lifting the video programming restriction could actually *impede* development of video dialtone systems. Section 613(b) is the only provision in the Communications Act preventing telephone companies from operating cable systems in their respective telephone service areas. Eliminating that restriction, with no substitute ban in place to deal with telco delivery of cable service, would give telcos the power to purchase cable systems within their telephone service areas — something the FCC has already determined to be of "no public gain."<sup>95</sup> With the ability to *own* cable systems, telcos would have no incentive to *construct* video dialtone systems. Furthermore, the Commission has prohibited telcos from converting cable systems in their respective telephone service areas into video dialtone on the theory that cable systems provide the most likely competition to telcos for the local exchange market.<sup>96</sup> The *Video Dialtone Decision* did not recommend imposing a statutory restriction on telco-provided cable service.

The recently enacted Cable Television Consumer Protection and Competition Act of 1992 has eliminated some of the need for telco ownership of programming ("Cable Act of 1992").<sup>97</sup> The telcos have contended that vertical integration between MSOs and cable programmers would keep the most popu-

<sup>86</sup> *Id.* para. 137.

<sup>87</sup> *Id.*

<sup>88</sup> *Id.* para. 135.

<sup>89</sup> Computer III Remand Proceedings, *supra* note 60, paras. 33-40.

<sup>90</sup> *Video Dialtone Decision*, *supra* note 1, para. 138.

<sup>91</sup> *In re Air Passenger Computer Reservation Sys. Antitrust Litig.*, 694 F. Supp. 1443 (C.D. Cal. 1988).

<sup>92</sup> *Id.*

<sup>93</sup> *Id.*

<sup>94</sup> *Id.* at 1474.

<sup>95</sup> *1991 Decision*, *supra* note 3, para. 17.

<sup>96</sup> *Video Dialtone Decision*, *supra* note 1, para. 109.

<sup>97</sup> Pub. L. No. 102-358, 106 Stat. 1488 (to be codified at 47 U.S.C. § 536).



lar programming services off video dialtone.<sup>98</sup> After all, it would not be in an MSO's best interests to have its own programming available on a competing video dialtone system. However, section 12 of the new cable law prevents cable programmers from entering into exclusive agreements with cable operators for distribution of programming in the cable operator's market.<sup>99</sup> By eliminating exclusive contracts, this new legislation should increase availability of the more popular cable programs on video dialtone systems.

Although Congress has addressed telco entry in recent years<sup>100</sup> it has yet to ease the restrictions. However, change may be on the horizon. In February 1993, Representative Edward Markey (D-MA), Chairman of the Subcommittee on Telecommunications and Finance of the House Committee on Energy and Commerce, wrote the FCC concerning several telephone-related communications issues.<sup>101</sup> Markey opposed allowing telcos to purchase existing cable systems in their telephone service areas because "it denies the public a meaningful cable competitor."<sup>102</sup> While noting that the video programming restriction has served the public interest, Markey called for a reexamination of the restriction:

Witnessing the celerity, however, with which alternative providers of local exchange service are increasingly effective competitors, as well as the fact that multichannel video competitors are developing networks that have capabilities which appear virtually indistinguishable from those of the telephone network, it may be time to reexamine the prohibition on content ownership enacted through the Cable Act of 1984.<sup>103</sup>

This sentiment was echoed shortly thereafter by Acting FCC Chairman James Quello in a speech at Fordham University.<sup>104</sup>

## THE RURAL EXEMPTION: LETTING TELCOS RUN WHERE OTHERS REFUSE TO WALK

One exception to the rule against telco provision of video programming is in rural areas. When the FCC adopted the cross-ownership rules in 1970, it realized that the only practical means of bringing cable service to some rural areas might be through telco ownership of the cable system. Hence, the Commission provided for a waiver policy to allow cable-telco cross-ownership in rural areas.<sup>105</sup> In 1980, the FCC reexamined the issue and found that the waiver process often needlessly delayed cable construction in rural areas. Thus, in 1981, it created a blanket exemption to the cross-ownership rules for non-urban areas of fewer than 2,500 people.<sup>106</sup> The exemption was codified in the 1984 Cable Act without a standard. Instead, Congress left standard-setting to the FCC, stating that the prohibition "shall not apply to any common carrier to the extent such carrier provides telephone exchange service in any rural area (as defined by the Commission)."<sup>107</sup>

The Commission began a reexamination of the rural exemption in its 1988 *Further Notice of Inquiry*, seeking comment on whether the population standard should be revised or replaced with another standard, such as telco size.<sup>108</sup> Numerous parties addressed the rural exemption issue in their comments to the *Further Notice of Proposed Rulemaking* portion of the 1991 *Decision*, thus presenting the Commission with a wide variety of options.<sup>109</sup> Even though cable already exists in 91.2 percent of American households, and is expected to pass 93.2 percent by 1999, the FCC tentatively concluded that raising the rural exemption threshold to areas with a population of less than 10,000 would help speed cable service to unserved and underserved areas.<sup>110</sup> The FCC did not propose a benchmark for what constitutes "underserved," but it noted that stalled or incomplete cable systems left some areas "under-

<sup>98</sup> See, e.g., Comments of GTE Service Corporation in CC Docket No. 87-266, at 18-20 (Feb. 3, 1992); Comments of Bell Atlantic in CC Docket No. 87-266 (Feb. 3, 1992).

<sup>99</sup> Cable Act of 1992, *supra* note 97.

<sup>100</sup> See, e.g., S. 661, 102d Cong., 1st Sess. (1991); S. 1200, 102d Cong., 1st Sess. (1991).

<sup>101</sup> Letter from Representative Edward Markey, Chairman, House Subcommittee on Telecommunications and Finance, to The Honorable James Quello, Acting Chairman, FCC (Feb. 12, 1993) (on file with the *CommLaw Conspectus*) [hereinafter *Markey Letter*].

<sup>102</sup> *Id.* at 3.

<sup>103</sup> *Id.* at 4.

<sup>104</sup> See Joe Flint, *Quello: Free Telcos, Protect Local TV, BROADCASTING*, Feb. 22, 1993, at 11.

<sup>105</sup> See Section 214 Certificates, *supra* note 6, para. 51.

<sup>106</sup> *In re Elimination of the Cable Telephone Co.-Cable Television Cross-Ownership Rules, Report and Order*, 88 F.C.C.2d 564, para. 36 (1981). See also 47 C.F.R. § 63.58(a) (1992).

<sup>107</sup> 47 U.S.C. § 533(b)(3) (1988).

<sup>108</sup> See Telephone Company-Cable Television Cross-Ownership Rules, *supra* note 23, para. 84.

<sup>109</sup> See *Video Dialtone Decision*, *supra* note 1, paras. 148-49.

<sup>110</sup> *Id.* paras. 150-51.

served," citing an instance where only twenty percent of a community had received cable service by the ninth year of a fifteen-year franchise.<sup>111</sup> The *Second Further Notice of Proposed Rulemaking* portion of the *Video Dialtone Decision* sought comment on the proposed 10,000 population standard.<sup>112</sup>

An interesting aspect of this tentative conclusion is that it was based almost entirely on assertions made in the comments filed by telephone company interests. Unlike the 1980 proceeding establishing the rural exemption, the FCC had no independent data to support its tentative conclusion to raise the threshold. Instead, the Commission asked parties to supply data to affirm or rebut the conclusion.<sup>113</sup> In response to the *Second Further Notice*, the National Cable Television Association submitted an "independent" study of all communities between 2,500 and 10,000 which purported to show that there would be minimal public interest benefit in raising the standard.<sup>114</sup> On the other hand, some telephone interests, most notably GTE Service Corporation, filed data based on surveys of their own telephone coverage areas.<sup>115</sup> GTE concluded that a 10,000 population benchmark would be the *minimum* required to make a cable venture financially feasible, and it urged the FCC to adopt higher maximums (up to 25,000) or other criteria (e.g., areas outside Metropolitan Statistical Areas). This proceeding's comment period ended on November 12, 1992. No decision had been released at press time.

The absence of independent data regarding service in rural areas is due in part to the FCC's absence from the cable franchising process. Under the deregulatory theme of the 1984 Cable Act, the Commission's only franchising functions are to prescribe regulations giving franchising authorities the power to regulate basic cable rates<sup>116</sup> and to set technical standards which may be required in a franchise.<sup>117</sup> An FCC rule requires annual reporting of community and system data,<sup>118</sup> but apparently this data has not been collected since 1987. Thus, the FCC has had no real method of independently determining the extent of unserved or underserved parts of the

country.

This situation is on the verge of changing. Section 11 of the Cable Act of 1992<sup>119</sup> requires the FCC to establish "reasonable limits" on the number of subscribers an MSO may serve. This will likely cause the Commission to gather more extensive data on the communities served by cable.

## RESOLVING THE JURISDICTIONAL PROBLEMS

The Commission proposes to assert exclusive jurisdiction over video dialtone services, thereby effectively preempting the authority of state regulators over any video dialtone service provision.<sup>120</sup> The Commission premises its preemption decision largely on its interpretation of section 214 of the Communications Act,<sup>121</sup> which the agency contends gives it exclusive jurisdiction over "construction and operation" of those "facilities" utilized by "local telephone companies" to provide video dialtone service. It further asserts jurisdictional exclusivity based on a single decision of the U.S. Court of Appeals for the D.C. Circuit that is more than twenty years old. The court in *General Telephone Co. of California v. FCC*<sup>122</sup> reasoned that FCC jurisdiction over telco provision of "channel transmission service and facilities constructed to carry TV and FM Radio signals by wire between a CATV antenna (or microwave received) and subscribers," was exclusive because the local telco facility is "an integral component in an indivisible dissemination system which forms an interstate channel of communication."<sup>123</sup> The Court thus gave the FCC exclusive jurisdiction over cable television facilities constructed by telcos.

Jurisdiction over telecommunication services and providers is a joint state/federal system established under the Communications Act of 1934.<sup>124</sup> Section 152(b) of the Act provides a dual regulatory scheme by which interstate communications are subject to federal regulation by the FCC, while intrastate communication services generally are regulated solely by

<sup>111</sup> *Id.* para. 151, at 5856 (citing Warren Telephone Company Order, 6 FCC Rcd. 5286 (Common Carrier Bureau 1991)).

<sup>112</sup> *Id.* paras. 150-54.

<sup>113</sup> *See id.* para. 153.

<sup>114</sup> *See* Comments of the National Cable Television Association, Inc. in CC Docket No. 87-266 (Oct. 13, 1992).

<sup>115</sup> *See, e.g.,* Comments of GTE Service Corp. in CC Docket No. 87-266 (Oct. 13, 1992).

<sup>116</sup> *See* 47 U.S.C. § 543(b) (1988).

<sup>117</sup> *See* 47 U.S.C. § 544(e) (1988).

<sup>118</sup> 47 C.F.R. § 76.403 (1991).

<sup>119</sup> *See* Cable Act of 1992, *supra* note 97.

<sup>120</sup> *Video Dialtone Decision*, *supra* note 1, para. 72.

<sup>121</sup> 47 U.S.C. § 214 (Supp. 1990).

<sup>122</sup> *General Tel. Co. of Cal. v. FCC*, 413 F.2d 390, 401 (D.C. Cir. 1969), *cert. denied* 396 U.S. 888 (1969).

<sup>123</sup> *Video Dialtone Decision*, *supra* note 1, para. 72 (citing *General Tel. Co. of Cal. v. FCC*, 413 F.2d 390, 401 (D.C. Cir. 1969), *cert. denied* 396 U.S. 888 (1969)).

<sup>124</sup> 47 U.S.C. § 152(b) (1988).

state authorities. Federal preemption of intrastate communications service regulation by state agencies is not permitted<sup>125</sup> except in situations where the exercise of authority by state regulators negates the exercise by the FCC of its own lawful authority over interstate communications.<sup>126</sup> Moreover, in order to justify preemption of state regulation, the FCC bears the burden of demonstrating that its preemption is "narrowly tailored to preempt *only* such state regulations as would negate valid FCC regulatory goals."<sup>127</sup>

In claiming jurisdiction, the FCC appears merely to be protecting its desire to ensure unfettered implementation of video dialtone.

We are aware, however, that video dialtone facilities may be deployed in varying configurations and that we may need to address the extent of our jurisdiction depending upon the particular configuration. We believe, however, that to delay the adoption of video dialtone until all such issues are resolved would not serve the public interest, especially given the uncertain nature of how such facilities and services will develop.<sup>128</sup>

State regulators, on the other hand, are concerned that the FCC cannot adequately protect ratepayers and other local interests.

Specifically, the States should be allowed to regulate the allocation of costs between the telcos' regulated telephone service and cable television services, including the right to order structural separations where necessary. Also, the States should be allowed to determine when and if cross-ownership is permitted depending on local conditions.<sup>129</sup>

Although the FCC may claim exclusive jurisdiction whenever state regulation may thwart a national policy,<sup>130</sup> in this instance the jurisdictional claims of the two governments can be reconciled.<sup>131</sup>

The Commission's ability to withstand a preemption attack with regard to video dialtone regulation is remote. Because the signals which carry data and voice message traffic over the nation's interstate common carrier network travel through local (intrastate) telephone company facilities, the FCC must justify its preemption of state regulation of video dialtone.

Strictly speaking, these facilities are a part of that "indivisible dissemination system which forms an interstate channel of communication."<sup>132</sup> Video dialtone signals will traverse the same "interstate channel." The bifurcated jurisdictional scheme of section 152(b) repeatedly has been held applicable to this local component of the "interstate" communication pathway,<sup>133</sup> and the Commission has advanced no reason to create a separate regulatory regime purely for video transmission.

The technical factors which led the *General Telephone*<sup>134</sup> court to uphold the FCC's preemption are clearly distinguishable from the technical factors presented by the Commission's video dialtone service proposal. In *General Telephone*, the telco operated a coaxial delivery system *separate* from its local telephone exchange carriage facility. The court held that the provision of *only* "local distribution channel service to CATV operators transmitting broadcast signals from another state" to a locally franchised cable operator, or service on a one-way basis from the cable operator's headend to subscribers, was subject to exclusive FCC jurisdiction.<sup>135</sup> This narrow holding provides scant support for FCC preemption of a video dialtone service which would carry voice, data and other more traditional telephone services, in addition to video, over one wireline facility. Furthermore, the video dialtone proposal contemplates interactive programming services to be offered by multiple unfranchised operators. Accordingly, video dialtone services will differ markedly from the transmission activity found subject to exclusive FCC jurisdiction in *General Telephone*.

Full preemption is unwarranted because some, if not most, video dialtone signals are likely to be *intra*-state in character. While the precise nature of all the programming which may be transmitted over video dialtone network facilities is not clear, even services now considered interstate could become intrastate. For example, some movie distributors might choose not to offer their programs on a nationwide basis from a single origination source because the cost of long distance video transmission might be prohibi-

<sup>125</sup> Louisiana Pub. Serv. Comm'n v. FCC, 476 U.S. 355 (1986); California v. FCC, 905 F.2d 1217 (9th Cir. 1990).

<sup>126</sup> California v. FCC, 905 F.2d 1217, 1243 (9th Cir. 1990); see also National Ass'n of Util. Regulatory Comm'rs v. FCC, 880 F.2d 422, 429 (D.C. Cir. 1989).

<sup>127</sup> California, 905 F.2d at 1243 (emphasis in original).

<sup>128</sup> Video Dialtone Decision, *supra* note 1, para. 73.

<sup>129</sup> See Initial Comments of the National Association of Regulatory Utilities Commissioners in CC Docket No. 87-266 at 3 (Feb. 6, 1992).

<sup>130</sup> See, e.g., Brookhaven Cable TV, Inc. v. Kelley, 573 F.2d

765 (2nd Cir. 1978), *cert. denied*, 441 U.S. 904 (1979).

<sup>131</sup> See Louisiana Pub. Serv. Comm'n v. FCC, 476 U.S. 355, 370 (1986).

<sup>132</sup> Video Dialtone Decision, *supra* note 1, para. 72, (citing General Tel. Co. of Cal. v. FCC, 413 F.2d 390, 401 (D.C. Cir. 1969), *cert. denied* 396 U.S. 888 (1969)).

<sup>133</sup> See Louisiana Pub. Serv. Comm'n, 476 U.S. at 355.

<sup>134</sup> General Tel. Co. of Cal. v. FCC, 413 F.2d 390 (D.C. Cir. 1969).

<sup>135</sup> *Id.* at 393.

tive. Instead, such distributors may establish a network of multiple local service providers who would offer a localized video store service exclusively over local exchange facilities. The programming might be transmitted by a private carrier to a local provider, who would store it electronically and then retransmit it to subscribers. Indeed, such an arrangement may soon be in the offing—Bell Atlantic has entered into discussions with Blockbuster, the largest video store chain in the United States, to provide video-on-demand.<sup>136</sup> Of course, federal preemption of state regulation of these purely local and/or regional transmissions is contrary to the bifurcated jurisdictional scheme of section 152(b).

Finally, from a strictly technological perspective, it would be extremely costly, if not impossible, to distinguish between the voice and data traffic which pass through the local telecommunications platform and the video programming which would be transported by way of the same pathway. For example, as previously mentioned, the Commission has envisioned video dialtone as including "video catalogue" services that would combine teletext with full-motion video.<sup>137</sup> Under such a scheme, it would be difficult for accounting or strictly regulatory purposes to distinguish which portion of programming would be video, subject only to FCC jurisdiction, as opposed to data, voice and other services subject to the joint federal/state regulatory scheme.

Indeed, the Commission points out that with continued technical developments it will become "increasingly impractical to distinguish between voice, data, graphics or video transmission."<sup>138</sup> Accordingly, if the FCC acts to fully preempt video dialtone services from state regulation, there could be a complete evisceration of the currently bifurcated jurisdictional scheme mandated by the Communications Act.<sup>139</sup> It is highly unlikely that the courts would uphold such a result based on the limited preemption justification presented by the Commission.

## CONCLUSION

The FCC's recent video dialtone actions have set the stage for telephone companies to compete or combine with cable systems for local delivery of video services. Since the Commission's decision in July 1992, Bell Atlantic has received approval to build an experimental system to serve 400 of its employees in the Washington, D.C., area<sup>140</sup> and has applied to build two operating systems in New Jersey.<sup>141</sup> NYNEX is considering a joint venture with Liberty Cable in Manhattan.<sup>142</sup> In addition, U.S. West has announced plans to begin video dialtone operations in 1994.<sup>143</sup> Despite these new ventures, widespread implementation of video dialtone is likely to be at least two decades away.

There are still many obstacles to overcome. Most immediate are the twenty-two petitions for reconsideration and/or clarification of the *Video Dialtone Decision* that were filed during October 1992.<sup>144</sup> These petitions were filed by parties from all sides of the issue: telcos claimed the FCC did not go far enough in allowing their entry into video programming; broadcast and cable interests argued the Commission went too far; and state regulators were concerned that their role in rate regulation would be subrogated.

The battle is being fought in the courts as well. In addition to the review of the franchise decision, cable and telco interests have challenged the video programming decision — again from opposite perspectives. In addition, Bell Atlantic, through two of its subsidiaries, has challenged the statutory prohibition of section 533(b) of the Communications Act on First Amendment grounds.<sup>145</sup> The statute, however, would seem to pass the *O'Brien*<sup>146</sup> test. It is narrowly tailored, in that it only prohibits telcos from providing video programming within their telephone service areas, in order to further a compelling government interest, i.e., ensuring diversity of view-

<sup>136</sup> Paul Farhi, *Blockbuster, Bell Atlantic Discussing 'Video-on-Demand' Deal*, WASH. POST, Jan. 20, 1993, at G-1.

<sup>137</sup> See *supra* note 82 and accompanying text.

<sup>138</sup> *Video Dialtone Decision*, *supra* note 1, at 5828 n. 232.

<sup>139</sup> See *In re Telephone Company-Cable Television Cross-Ownership Rules*, Request for Reconsideration of the National Association of Regulatory Utility Commissioners, CC Docket No. 87-226 (Oct. 9, 1992).

<sup>140</sup> *In the Matter of the Application of the Chesapeake and Potomac Tel. Co. of Va. (Order and Authorization)*, File No. W-P-C-6834, FCC 93-160, adopted March 23, 1993, released March 25, 1993.

<sup>141</sup> Section 214 Applications of New Jersey Bell Tel. Co. filed with FCC Common Carrier Bureau. Application, W-P-C-

6838, filed Nov. 16, 1992; Application, W-P-C-6840, filed Dec. 15, 1992.

<sup>142</sup> See *Bell Atlantic Plans Video-on-Demand Trial Over Copper Wire*, COMM. DAILY, Oct. 22, 1992, at 1-2.

<sup>143</sup> *U.S. West to Roll Out VDT Network Regionwide beginning in 1994*, COMM. DAILY, Feb. 5, 1993, at 1.

<sup>144</sup> See *Petitions for Reconsideration and Clarification of Actions in Rulemaking Proceedings*, 57 Fed. Reg. 48,800-01 (Oct. 28, 1992).

<sup>145</sup> *Chesapeake and Potomac Tel. Co. of Virginia v. United States*, Civ. A. No. 92-1751 (E.D. Va. filed Dec. 17, 1992) (challenging as unconstitutional section 533(b) of the Communications Act).

<sup>146</sup> *United States v. O'Brien*, 391 U.S. 367 (1968).

points by preventing a communications monopolist from extending its monopoly power to other communications media.

The lawsuit could be rendered moot by Congress and the FCC. As noted earlier, Representative Markey has expressed an interest in easing the restriction. In addition, the *Markey Letter* also asked the FCC to consider implementing many new communications technologies on a common carrier basis.<sup>147</sup> For example, one of the cable industry's responses to the *Video Dialtone Decision* has been to step up implementation of compression technology, which allows cable systems to greatly expand their capacity. TCI has already announced plans for a 500-channel system in Florida.<sup>148</sup> The *Markey Letter* indicated that such expansion, if used to provide two-way services in competition with local telephone companies, should be allowed only on a common carriage basis.<sup>149</sup> Such a scheme would eventually lessen telcos' local exchange monopolies, thus eliminating the need for the cross-ownership restriction.

Beyond those proceedings, the Regional Bell Operating Companies ("RBOC") — which serve more than eighty percent of the nation's population — must overcome restrictions placed on them by the Modified Final Judgment ("MFJ"), which resulted in the breakup of the Bell System.<sup>150</sup> Under the MFJ, the RBOCs were prohibited from owning or generating content for information services, including video programming, both within and outside their telephone service areas. That restriction was lifted by the U.S. District Court for the District of Columbia in July 1991, but that decision has been appealed.<sup>151</sup> If the appellate court, or the Supreme

Court, reinstates the information services ban, then the FCC's video programming decision could be rendered moot for these large telephone companies. Even if the lower court decision is upheld, RBOCs will be severely limited in their activities due to an MFJ provision barring the RBOCs from providing interexchange services.

Another unknown factor will be the importance the Clinton Administration places on video dialtone. The composition of the FCC is going to change, and with that change may come a different agenda. With Al Sikes—video dialtone's most ardent supporter—gone, video dialtone's future is in question and it could take a back seat to other programs. Proponents of video dialtone may be heartened by the presence of Vice President Al Gore, who has been a supporter of increased telco involvement in video delivery. The Clinton Administration has also promised to emphasize improving the nation's telecommunications infrastructure, including increased telephone system capacity. Video dialtone could very well benefit from this commitment.

There is also the preemption issue. The Commission, and possibly the courts, will have to confront the role of state regulators in a video dialtone world. Although the FCC has claimed exclusive jurisdiction in that arena, some video services may indeed be completely local in nature. State regulators, therefore, must be accommodated. The future of video dialtone is as unclear as the structure and concepts of video dialtone. Unless the legal and practical issues are resolved, the vision of video dialtone could become little more than a pipedream.

<sup>147</sup> *Markey Letter*, *supra* note 101, at 2.

<sup>148</sup> See Mary Lu Carnevale, *Telephone Service Seems on the Brink of Huge Innovations*, WALL ST. J., Feb. 10, 1993, at A1, A9.

<sup>149</sup> *Markey Letter*, *supra* note 101, at 2.

<sup>150</sup> *United States v. American Tel. and Tel. Co.*, 552 F.

Supp. 131 (D.D.C. 1982), *aff'd sub nom. Maryland v. United States*, 460 U.S. 1001 (1983).

<sup>151</sup> *United States v. Western Elec. Co.*, 767 F. Supp. 308 (D.D.C. 1991), *appeal docketed*, No. 91-5263 (D.C. Cir. Aug. 30, 1991).