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FEDERAL COURT RULES THAT FRANCHISE FEES IMPOSED BY A MARYLAND COUNTY AGAINST A TELECOM PROVIDER VIOLATED THE TELECOMMUNICATIONS ACT OF 1996

Montgomery Cty v. Metromedia Fiber Network, 2005 WL 1469460 (S.D.N.Y. June 17, 2005)

Metromedia Fiber Network ("MFN") provides fiber optic infrastructure and high-bandwidth internet connectivity. To build its infrastructure, MFN required the use of the public right-of-way owned by Montgomery County. After a lengthy application process, MFN and Montgomery County entered into a franchise agreement that gave MFN access to the public right-of-way in Montgomery County and, in exchange, MFN was required to make semi-annual payments to Montgomery County consisting of 5% of MFN's adjusted gross revenues. The franchise agreement also required MFN to allow Montgomery County to audit its financial records, to pay expenses related to the franchise agreement up to \$2,000, to file a \$50,000 surety bond, cash deposit or letter of credit and to keep insurance policies for up to \$2 million per occurrence.

The franchise agreement expired on June 28, 2001. After it expired, MFN continued to use Montgomery County's public right-of-way but stopped paying its 5% franchise fee. MFN argued that Montgomery County's actions were discriminatory because Verizon Maryland Inc., the incumbent local exchange provider in Montgomery County, was exempt from any franchise application or fees.

In 2004, MFN filed for bankruptcy in the United States Bankruptcy Court for the Southern District of New York. Montgomery County filed claims for the unpaid franchise fees. MFN argued that the claims should be disallowed because Montgomery County's lengthy application process, fee requirement and unfettered discretion to grant the franchise violated the Federal Telecommunications Act of 1996. Additionally, MFN argued that Montgomery County's franchise process was unfair, unreasonable and discriminatory since Verizon was exempt from it entirely.

The bankruptcy court agreed with MFN and disallowed the claims as violative of the Federal Telecommunications Act of 1996. On appeal to the United States District Court for the Southern District of New York, Judge Colleen McMahon affirmed the bankruptcy court and held that Montgomery County's franchise process – based on a county ordinance governing the use of

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public right-of-ways - violated section 253 of the Federal Telecommunications Act of 1996 which forbids state and local governments from enacting laws that have the effect of prohibiting the ability of any entity to provide telecommunications service.

Judge McMahon held that although the ordinance was constitutional on its face, it was unconstitutional as applied to telecom providers, such as MFN. The lengthy application process and broad discretion to grant or deny the franchise effectively prohibited MFN from providing telecommunications service in violation of section 253. Moreover, subjecting MFN to the lengthy and discretionary application process while entirely exempting Verizon, the incumbent provider, materially limited the ability of MFN to compete in a fair and balanced legal and regulatory environment.

Judge McMahon further held that the ordinance was not saved by section 253(c) of the Federal Telecommunications Act of 1996 which allows state and local governments to require fair and reasonable compensation from telecommunications providers on a competitively neutral and nondiscriminatory basis. Judge McMahon reasoned that while precise parity of treatment was not required under section 253(c), Montgomery County could not impose "a host of compensatory provisions on one provider without placing any on another." Pointing to the disparate treatment between MFN and Verizon, Judge McMahon concluded that the franchise process was neither competitively neutral nor non-discriminatory.

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