

ECONOMIC DEVELOPMENT AND COUNTY-WIDE BROADBAND FIBER SKAGIT COUNTY WASHINGTON

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BACKGROUND

TMC Group was tasked with advising Skagit County on the most appropriate method to invest \$750,000 in economic development funds earmarked for fiber optic networking within the County. Fiber optic networks are the backbone for telecommunications services that require broadband capacity. These advanced services include high capacity networks for businesses, high speed connections to the Internet, and alternative providers of cable television or telephone service. Broadband networks may include a variety of copper wiring or wireless services for connections to users, but fiber optics are the most economical, reliable, and stable technology for the backbone.

Skagit County is one of the prime examples of why government participation is needed to deliver the benefits of broadband networks. Although the U.S. has seen a proliferation of fiber optic based network providers, most of them have concentrated on either national (long haul) carrier networks or in the high density metropolitan areas. This is market-based economics at work – there are not enough potential customers in rural areas and too few large customers. While financial markets are not willing to pour money into networks that do not show the promise of an adequate return on the investment, local governments are able to justify the cost based upon measurements other than a direct rate of return. The availability of advance network services provides an opportunity to compete for business growth and attract more affluent citizens that otherwise locate in areas that provide such services. Economic development can also be traced through the secondary effects of broadband networks installed in the local schools, businesses, and governments as the general quality of life is improved.

LOCAL FIBER OPTIC NETWORKS

The cable television (primarily Comcast) and telephone service (primarily Verizon) firms in Skagit County have installed some fiber optic capability for their backbones. As the incumbent providers, they set the market rates and limit the offerings. The difficulty in capturing a significant market share has restricted the opportunity for direct competition. This in turn creates an environment where the current providers have little outside pressure to change their business model, lower rates, or extend services beyond the current business plan.

One local company, Black Rock Cable, has started to install fiber optic cables in the Western part of Skagit County (and Whatcom County) under an Open Video System (OVS) franchise. Their current business model includes offering direct access to the fiber cables for users to install their own electronics in order to create private broadband

networks. Black Rock Cable also offers its customers connections to Internet Service Providers (ISP). However, as a for-profit business, they cannot justify installing fiber optic cables in low-density parts of the County.

The City of Mount Vernon installed fiber optic cables throughout the City to meet internal needs (networking City sites) and to produce a backbone for service providers to offer services to retail customers. This is an example of the government participation often needed to enable alternative telecommunications providers to enter an otherwise marginal but underserved market. Currently there is one primary service provider (CSS Communications) on Mount Vernon's fiber network.

The Skagit County Public Utility District plans to build an extensive fiber optic network throughout their service area, although the network is not yet started. Their requirements create a need to run fiber optic cables in some of the more sparsely populated parts of the county. The PUD will also be building a fiber optic based network in the town of Concrete under a grant that secured RUS and Skagit County funds. The PUD's goals include connecting a fiber backbone to Seattle City Light fiber at Marblemount to provide access back to the Westin Building in Seattle, an important co-location (or "meet-me") point for many carriers. With a similar connection to the Snohomish PUD at the County line, a fiber optic backbone physical ring (dual routing to the Westin) could be created. This would provide a high capacity, high reliability (redundant) service link directly to the major service providers and nationwide backbones.

INITIAL OPTIONS AND KEY ISSUES

At the beginning of this project, the major options suggested were:

- Allocate the grant money to Mount Vernon for the purpose of extending their network
- Allocate the grant money to Skagit County PUD to help them extend their planned network build
- Use some of the grant money to deliver fiber optic services to the Port of Skagit County and extend the fiber to the buildings on site
- A collaborative approach that pools the resources of all local government agencies and allocates the money to this cooperative effort

Although Skagit County wants to encourage and enable the building of fiber optic networks, the County does not want to be in the "network provider" business. In fact, there are legal restrictions on the County, covered in the next section (Legal Issues) of this report.

Some of initial discussions included:

- Mount Vernon's plans centered on extending their network, which did not address much of the rest of the County area

- Skagit County PUD's network needs mirror their core business, which follows the economic development rather than driving economic development.
- Black Rock Cable is providing some local school districts and governments with a low cost dark fiber pair (no electronics) between sites

One of the major benefits of a cooperative effort is avoiding the duplication of networks and providing the most cost-effective way to clear construction hurdles such as railroad, freeway, and waterway crossings. In general, many right of way issues can be resolved because one of the members will either control the right-of-way or already have facilities in place (such as a usable conduit).

It became apparent early in the interview process that the best use of current and future County funds is to help establish and support a united effort involving the government agencies, the PUD, and the Port of Skagit County. Properly organized and directed, this partnership style approach offers the best value for the economic development funds. However, any formal organization such as a consortium carries with it the need to review the legal "rights" and restrictions of the entity and the potential members of the group.

LEGAL ISSUES

Federal

Before we discuss the possible restrictions on members of this fiber partnership, it is important to examine the current legal environment, both on a national and on a state level. On March 24, 2004 the U.S. Supreme Court determined with finality the Federal position when they reviewed the case of *Nixon, Attorney General of the State of Missouri v. Missouri Municipal League, et al* 299 F.3d 949 (8th Cir. 2002) *rev'd* No. 02-1238 S. Ct. (2004).

The underlying case involved a statutory ban by the state of Missouri on municipal telecom services. The Attorney General of the State of Missouri did not believe that the Telecommunications Act of 1996 expressly permitted municipal telecom service. This was challenged by the Missouri Municipal league, made up of various Missouri municipalities and public power companies. Initially, the FCC ruled that power companies and municipalities have the ability to be true competitors in the telecommunications arena, but the states have the ability to determine what is permissible in their states.

On appeal to the 8th Circuit, the Federal court vacated the FCC ruling and remanded it to the Commission for further proceedings. The 8th Circuit based its decision on a discussion of what the words "any entity" meant in the Telecommunications Act of 1996 and concluded that municipalities and utility companies are included in the definition of "entity" and thus should not be prohibited from entering this business.

After agreeing to review the case, the U.S. Supreme Court decided that it is up to the states to determine whether municipalities and utilities can provide telecommunications services. The Telecommunications Act of 1996 does not specifically include municipalities in their definition of any entity.

State

This case is important to Skagit County because Washington State is one of several states with specific legislation and restrictions on public agency entry into the telecommunications business.

Currently, Washington statutes provide that first class charter cities, code cities and “home rule” counties have authority to provide telecommunications services to their residents. See AGO 2003 No. 11 for a complete discussion. In general, municipal corporations are limited to the authority granted to them by statute. However, under the Washington State Constitution (Const. art. XI sec 4, 10), a city with a population of 10,000 or more may adopt a charter which gives them broad powers to write their own laws, as long as they are consistent with the state statutes and the state Constitution. In addition, a city may be formed or reincorporate itself under the Optional Municipal Code, RCW 35A.11.020, become a “code” city, and gain powers similar to those of the state. Also, under the Constitution (Const. art. XI section 11) a county may frame a charter (“home rule” county) which gives the County the broad powers similar to state government.

Accordingly, while not specifically given the power to provide telecommunications services in the state statutes, “first class,” code cities, and “home rule” counties are also not specifically prohibited from providing these services. One of the theories for allowing them to provide telecommunications service, is that a municipal corporation exercises two types of powers, governmental and proprietary. More leeway is given when a municipal corporation is exercising proprietary powers as these powers are deemed to be akin to a business function. Providing telecommunications is a business function. The decision rendered by the AG also included a discussion of whether the statutory granting of authority to a municipality to operate an electric or gas company, water or sewer facilities was meant to be exclusive or whether implied in this was the authority to also engage in other utilities like telecommunications. In citing to *City of Issaquah v. Teleprompter Corp.*, 93 Wn.2d 567, 611 P.2d 741 (1980), the court held that code cities had the authority to operate cable television systems to serve their citizens even though there is no specific statute granting this authority.

In conclusion, the State of Washington has so far held that cities and counties that are first class, code, or “home rule” do have authority to provide telecommunications, however, second class cities and non “home rule” counties do not.

Similarly, the Washington legislature has enacted specific statutes which authorize Public Utility Districts and Rural Port Districts to provide wholesale telecommunications services. See RCW’s 54.16.330 and 53.08.370. State Representative Jeff Morris

requested an Attorney General opinion on the authority of PUD's and rural port districts to provide telecommunications services or facilities. For purposes of that opinion, the Attorney General's office answered the following questions (paraphrased): May a public utility district or rural port district sell excess capacity from internet telecommunications systems directly to end users; do the statutes preclude PUD and rural port districts from providing telecommunications services or facilities to end users; because RCW 39.34.080 provides that public agencies can contract with other public agencies to perform governmental service activities or other undertakings that each is authorized by law to perform, is a PUD or rural port district authorized to provide telecommunications services or facilities to another public agency as an end user. See AG 2001 No. 3.

The legislature in 2000 enacted, RCW 54.16.330 and RCW 53.03.370(1). These statutes state the express purposes for owning telecommunications facilities by either a PUD or a rural port district are for their own internal telecommunications needs, or to provide wholesale telecommunications services within the district and by contract with another public utility district. The authority of the PUD and rural port districts to provide these services is determined by the fact that they are municipal corporations authorized by statute in RCW 54.04 and RCW 53.04.060. As discussed above, the powers of a municipal corporation are as defined in the statutes and may be broader to the extent the activity is proprietary rather than governmental. Even then, the authority is limited by statute in that they may not act beyond the scope of the grant of power or contrary to express limitations. While providing wholesale telecommunications is proprietary (the same function as that of a business enterprise), it does not automatically grant the right to operate an ancillary business to the authorized purpose. An important distinction between PUD's, port districts, and code cities is that the first two are restricted by statute and the latter have broader powers by statute and the state constitution.

In order to determine the PUD and Port District authority, the first thing that must be decided is "what is an end user?" Wholesale service means to provide for resale to someone else, in this case an entity authorized to provide telecommunications services to the general public. An "end user" would be a retail customer who purchases from an authorized company. Because the public agency would be a user, the PUD or port district cannot sell directly to the public agency. The AG stated that the statute was explicit as to their authority and thus they were not authorized to enter this ancillary business.

The next question to be answered is whether because of RCW 39.34.080, otherwise known as the Interlocal Cooperation Act, the PUD or Port could sell directly to other public agencies. Under this statute public agencies are allowed to contract with each other to perform any governmental service activity or undertaking they are otherwise authorized to perform. However, they are not allowed to act beyond their powers just because they have entered into an Interlocal Cooperation agreement. AGO 1969 No. 8 However, they are not prevented from acting jointly with a government agency to secure telecommunications services from a retail provider. Thus, the government agencies, PUD, and Port District can use an Interlocal Agreement to procure services.

The environment in Washington is not necessarily stable in that there was an attempt in 2003 to have the definition of “end user” added to the statute as well as language to restrict a PUD or port authority’s ability to market their telecommunication services and language that clarifies that wholesale telecommunications services could not be sold to a public agency. While this bill did not pass in 2003, in 2004 the legislature did approve adding language to RCW 54.16 to clarify how funds received from wholesale telecommunications services must be kept and how they can be spent.

With the recent U.S. Supreme Court decision, it leaves it up to the states to draft their own laws relating to the issue of public agencies’ entering the telecommunications business. It is almost certain that the incumbent carriers will continue their lobbying to restrict public agency entry into their field of business as it has the potential to reduce their income.

Interlocal Cooperation Act

Before the public agencies in Skagit County can enter into an Interlocal Cooperation Agreement, each entity’s legal authority needs to be reviewed and the goals of the group should be defined. As stated above, a public entity may not enter into an Interlocal Agreement in order to expand the authority it already has by law. See RCW 39.34.080 which states “Any one or more public agencies may contract with any one or more other public agencies to perform any governmental service, activity, or undertaking which **each public agency entering into the contract is authorized by law to perform:** PROVIDED. That such contract shall be authorized by the governing body of each party to the contract. Such contract shall set forth fully the purposes, powers, rights, objectives and responsibilities of the contracting parties.” (emphasis added)

Although Mount Vernon would qualify to offer telecommunications services to its citizens (“end users”) because it is a code city, no other member of the proposed group has such broad authority. Therefore, the group cannot use an Interlocal agreement for the purpose of entering the telecommunications business. Similarly, the PUD and the Port District are authorized to offer telecommunications wholesale services and no other member, other than Mount Vernon, would have such authority. Thus, before the group is established, the goals must be clearly stated and fall within the realm of what each member could achieve on its own.

Public Agencies have entered into Interlocal Agreements to set up a group to share ideas which would increase efficiencies in Government. (Southwest Washington GEM). They have also joined forces to service parks (Vancouver and Clark County Interlocal Parks Agreement) and to coordinate building codes and permitting (Eastside Building Services Outreach Program) among others.

But when a proposed member oversteps its authority such as the situation in 1967 when Benton and Franklin Counties as well as Kennewick and Pasco tried to enter into a Interlocal Agreement to build a bridge over the Columbia River, it was deemed by the Attorney General’s office to be outside the authority of the two cities to build a bridge

outside their territorial limits. The situation was different in 1976 when the City of Seattle, The State Highway Commission, King County, the Port of Seattle and Metro tried to enter an Interlocal agreement in order to build a bridge cross the Duwamish River in West Seattle. All of the parties to this agreement had some authority within the geographic area in question. The opinion (AG 1976 No. 74), however, stated that each member of the consortium could only participate to the extent of their authority. In other words, the state highway commission would only be involved to the extent that the bridge would connect to state highways and the county could only participate to the extent county roads were expanded or because they are a “home rule “ county, they could participate to the extent the county council gives them authority through county ordinances.

While the laws regarding the joint construction of transportation projects have changed and now allow these groups to join for purposes of transportation projects, a comparison of individual agency authority would be necessary to determine if each member of the Skagit County consortium had authority to do what the consortium as a whole is doing. For example, as a “second class” city, Sedro Woolley would have no authority to build a fiber network to offer retail or wholesale telecom services. At the same time, although Mount Vernon is authorized to provide telecommunications services to the citizens of Mount Vernon, a question still exists as to how far beyond their city limits their authorization extends, especially within the boundaries of another city. Although sometimes a city can go outside city limits to provide underserved areas with utilities such a water, sewer, garbage, etc., it is uncertain how telecommunications services (previously provided by private enterprises) would be viewed.

By contrast, each City could cooperate to build an extensive network, by establishing the guidelines and specifications for the network and participate as to where the network would run what streets, poles, etc. In this setup, however, no city would have control over or ownership of the network within the limits of the other city. However, the use of the network outside of internal requirements, i.e., providing wholesale or retail services, would be limited as discussed previously.

The County, PUD and Port District would have the broadest powers with respect to where the network could be built, but none of them can provide service directly to the “end users,” and the County can not even provide wholesale services.

CONCEPTUAL RECOMMENDATION

Based upon the discussions and analysis of options, it is recommended Skagit County use their economic funds, political will, and technical resources to help create a county-wide unified approach to public fiber optic broadband networks. Without exception, the local public agencies supported this concept in preliminary discussions. Each of the following sub-elements should be considered starting points for the group to discuss.

1. Entity Format: Although it is hoped the current climate of political cooperation and harmonious technical needs will last indefinitely, it is a fact that each participant will have different internal goals, resources, and requirements. The best way to remove the future uncertainties is a formal separate entity controlled by group-set policies. This produces structure for funding, technical coordination, ongoing management, and resolution of disputes. Thus, a consortium appears to be preferred, but the concern over individual limitations may dictate everything from who can be a legal member to what type of activities the consortium can perform or what service may be offered.
2. Asset Ownership: Another key element because of legal restrictions; it is likely that the consortium should not own any of the physical assets, which include everything from conduits and fibers to the electronics where the networks will intersect. Where networks will be constructed by participating members, it is likely that ownership should remain with the entity, rather than transferring assets to the consortium or to another member. With any ownership scenario, it will be necessary to consider the issues of facilities maintenance, repair, and response/recovery interval commitments.
3. Funding: The County's current economic development funds can be used to initially fund activities and services not provided through the internal resources of the participating agencies. However, the group will have some ongoing expenses and needs to either collect a small annual assessment or will need to retain fees collected from service providers using the backbone network.
4. Policies and Management: Regardless of the legal structure, the consensus is the elected officials should officially set policies and provide high-level oversight. They in turn would each assign management tasks to a trusted representative from each member to execute the group's duties according to the agreed policies.
5. Technical Coordination: The group has several competent technical people in internal staff positions that can provide technical guidance and help coordinate their individual agency's needs. When necessary or appropriate, the group can elect to bring in an unbiased technical resource for either mediation or for assistance when the work load exceeds a reasonable level for otherwise busy professionals. Many critical elements need to be coordinated, including the basic design, route planning, electronics, local drops, and splice points.
6. Additional Grants: To complete the eventual vision of county-wide broadband networks will require substantial sums beyond the current builds and plan of the members and identified grant funds. Therefore, one of the best roles the group entity can undertake is the pursuit of additional grant funds. The Port of Skagit County, with its primary mission to foster economic development, can qualify to apply for funds not otherwise available – grant applications can be filed with the Port as the requesting agency on behalf of the group. Additional grants may be available through farm bills, rural development, etc.
7. Other Group Activities: Normally, each member will individually contract with any outside firms needed for physical construction since the facilities will likely be built and owned by specific members. However, at times the group entity will act on behalf of the group's interest, especially when negotiating with potential service providers (wholesale agreements).

ORGANIZATIONAL ISSUES

Selecting an organizational structure that will not need to be revised due to legislative changes or changing legal restrictions is one of the main goals. This philosophy is one reason why it makes sense for the consortium to avoid attempting to become an owner and operator of complete network services. If the consortium takes on roles that its potential members are restricted from, then those members could not be formally part of the group. A conservative approach will consider the following:

- The consortium can formally include only those agencies with authority to provide telecommunications services in the County (the PUD, the Port, Mount Vernon, and Anacortes). In this scenario, other key players, such as Skagit County, would be merely advisors to the consortium.
- Since the consortium can not easily own the shared network, each entity will need to build and own a portion of the network. Then it is necessary to decide how the fibers needed for county-wide service providers or for inter-governmental networks will be assigned and managed. Although it was suggested at one point that fiber ownership could be traded between agencies, it is more likely that the assignment will be via a formal right-to-use agreement.
- The internal networking needs of the government and public agencies can be contracted through a contract Service Provider. This helps to avoid the problems with the “End User” definition that restricts both the PUD and the Port from directly providing facilities or services to others. The agreements with the service providers can be established during the selection phase that ensures the public entities are provided preferential (minimal cost) pricing.
- The consortium may be able to designate one of its members (Mount Vernon is the only logical choice) as the service provider for inter-agency and intra-agency networking requirements. An outside service provider would be used for carrier services, including ISP access, and for all non-public users. There is a need to verify if the City has the authority to provide this service throughout the county. Although examples can be found where cities provide services outside of their city limits, it is usually to extend critical utilities to underserved areas. It is not clear what is required to allow the City of Mount Vernon to provide services within another city’s boundaries, even if the telecommunications network is labeled a utility. (See discussion of Interlocal agreements on page 6)
- The consortium can be organized to merely act as a coordinator and to provide general services such as technical advice, procurement activities, legal advice, and contract coordination. This helps work around the limitations the consortium would encounter by avoiding all ownership and construction activities. This “oversight committee” would not be a party to actual service provider agreements – parallel agreements would be negotiated for each wholesale network.

There are a few additional issues that the consortium and its members should address. One of these is the option to negotiate with private providers such as Black Rock Cable

for the sale or exchange of right to use fiber or pathways. Contracts with such providers must allow for the wholesaling of the fiber since some current contracts limit the use of the fiber to public agency networking needs. The contracts must also provide long term stability, clear maintenance and access provisions, and a cost effective alternative to the costs of constructing directly owned facilities. However, if the providers are willing to enter into favorable contracts, it makes sense to maximize the fiber optic resources in the County rather than building completely separate and competing network facilities.

The other main issue the consortium members should address is the use of wireless technologies for access to the fiber broadband network where it is cost effective. One example of that is the previous estimate of the cost to run fiber to all buildings at the Port represents a large cost relative to the number of potential users. It may make more sense to run fiber to a couple of buildings and use advanced wireless techniques to extend service to other buildings and users on site. The wireless portion could be obtained through one of the service providers to help keep the capital costs down, or the wireless electronics could become part of the consortium controlled wholesale backbone network.

SUMMARY

Skagit County should use its economic development funds to help create a consortium that will be similar to the approach used with E911 services. The consortium will direct efforts and coordinate between members, but it will not supercede members' authority or rights. Rather than assigning the funds to a single entity for additional fiber builds, the County should use the funds to:

- Establish the consortium
- Obtain additional legal and technical assistance as required
- Pursue federal, state, and private foundation grants
- Begin targeted fiber builds with a high economic development return, as agreed to by the consortium participants. The best initial use of funds would be to link the Port of Skagit County to the existing Mount Vernon fiber network, especially since the Port's primary mission includes encouraging economic development.

The networks should be owned and operated by organizations specifically empowered to construct fiber networks and enter into wholesale agreements. The consortium and its members should avoid the legal and administrative problems of retail services by contracting with outside service providers. The wholesale agreements can be crafted to ensure an opportunity for success with retail customers while providing minimal costs for consortium members to obtain services.

The consortium should be created to avoid legal entanglements, with its role limited to the appropriate tasks. Once organizational issues are settled, it is strongly recommended that a formal legal opinion be obtained, preferably from the State's Attorney General's office.