Lorraine

SACRAMENTO METROPOLITAN CABLE TELEVISION COMMISSION
IN JOINT MEETING WITH
THE CITY COUNCIL
AND
BOARD OF SUPERVISORS
RELATING TO CABLE TELEVISION
700 "H" STREET - BOARD CHAMBERS
SACRAMENTO, CALIFORNIA 95814

WEDNESDAY JULY 6, 1983 2:30 P.M.

Members: Bill Bryan; Illa Collin; Orvell Fletcher; Toby Johnson; Terry Kastanis; Lynn Robie; Joe Serna; Ted Sheedy; Sandy Smoley

ITEM NO. 1: Report Back - Anti-Trust Issue and Rebidding

ITEM NO. 2: Staff Report - Rebidding the Franchise

CABLE COMMISSION ONLY

ITEM NO. 3: Staff Report - Information Only - Commission Budget

ITEM NO. 4: Commission Action - Final Approval - PERS Contract

ITEM NO. 5: Special Counsel Report - Information Only

ITEM NO. 1

SACRAMENTO METROPOLITAN
Cable Television Commission
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ROBERT E. SMITH
EXECUTIVE DIRECTOR

June 28, 1983

To: Members, Sacramento Metropolitan Cable Television Commission

From: Bob Smith, Executive Director
Sacramento Metropolitan Cable Television Commission

Subject: REPORT BACK - ANTI-TRUST ISSUES AND REBIDDING

INTRODUCTION

On June 9, 1983, the Board of Supervisors and City Council delayed consideration of a staff recommendation to begin in the refranchising process to allow United-Tribune Cable of Sacramento ("UTC") an additional thirty (30) days, to July 6, 1983, to submit a proposal for the Sacramento Cable Television Franchise. Additionally, at that time, the Board and Council authorized staff to retain an attorney specializing in anti-trust matters to review several possible approaches to franchising from an anti-trust standpoint.

As of this date, UTC has not submitted a proposal for staff review. However, upon the recommendations of City Attorney James Jackson, staff contacted Attorney Ronald S. Katz of Palo Alto regarding the Commission's anti-trust concerns.

ANTI-TRUST ADVICE

Ronald S. Katz, Esq., of Gaston Snow & Ely Bartlett is a specialist in anti-trust matters with three years experience in the anti-trust division of the U.S. Department of Justice. Mr. Katz will be present at your July 6, 1983 joint meeting to answer possible questions.

Attorney Katz has advised staff by the attached letter that:

1. Any form of a consortium bid, with or without United Cable Television as a participant, would expose the Commission to anti-trust liability unless such a bid was generated through a public proposal process.

2. Negotiating with the former unsuccessful bidders is a viable alternative if the prior applications remain unadjusted and as originally submitted. Any adjustments in the prior proposals could result in anti-trust liability, the magnitude of which is dependent upon the significance of such adjustments. (Staff contacted all the unsuccessful bidders and all are unwilling to accept this alternative.)

3. The most prudent method of selecting a new cable franchisee for Sacramento, from an anti-trust liability standpoint, is to refranchise in an open and competitive atmosphere as set forth in the Ordinance.

CURRENT POLICY ISSUES

I believe that UTC failed to accept the franchise which the Commission offered because the proposed contract terms would have prevented a reduction in inflated promises, thereby increasing the business risk and reducing the profitability of the system. I believe this problem reflects a fundamental dilemma in the process. An enforceable contract creates a problem for any cable company which attempts to satisfy perceived political desires for a high level of nonrevenue generating community services and at the same time, contend with the business risk associated with constructing and operating a new cable system.

This community has embarked upon a process in which it has requested competitive proposals which it has then sought to recast in contractually enforceable language.

On many occasions, the applicants were warned by the elected officials that the City and County were serious about enforcing whatever promises were made by the applicants.

And yet, some applicants have even now indicated their reluctance to submit a proposal unless the Commission abandons its efforts to enforce promises which are made in the process. In my view, this would permit an applicant to propose whatever the applicant felt was necessary to secure the franchise and then allow the applicant to deliver only those items which it desired to do. In examining this dichotomy, there seem to be four options available to the City and County:

1. Abandon the Process.
   As demonstrated by the experience of our neighboring City of Auburn, unenforceable promises can indeed be worse than no promises at all. If, in fact, there were a demonstrated lack of interest to bid on an enforceable basis, the Commission could simply defer the issuance of any franchise until there was demonstrated demand from potential subscribers in this community for cable television and until the potential applicants were willing to front for all of the costs of the franchising process.

1. (continued)

The staff believes that this position is an over-reaction. The staff believes that there are potential applicants that are willing to bid only those items to which they intend to be contractually bound.

2. Public Ownership.
The City and County could avoid the overbidding dilemma by developing a system under public control. Public ownership or partnership of the cable system offers the benefits of public participation in the monopoly profits collected by the operator from the subscribers, the ability to control subscriber rates in a monopolistic enterprise (otherwise denied us as a franchisor in California) and additional enforcement tools in which we would otherwise be deprived by federal legislation such as S.66.

However, the financing, building and operating of a cable system includes a substantial business risk which could, to some degree, impact the City and County, depending upon the form of ownership participation utilized. Careful planning and study would have to be undertaken before the feasability of public ownership could be accurately assessed for a system such as Sacramento. The time required for such a study could delay the entire process for up to an additional six months, during which time the expense of the Commission would be underwritten solely by the City and County.

Finally, it is unlikely that a publicly owned system could commit, at the outset, to the degree of nonrevenue generating services and facilities which were promised by competing private concerns. While a publicly owned or controlled system would generate the same degree of revenue as the privately owned system, the nonrevenue generating services and facilities could conceivably be made only as the profits were actually realized and received, probably in the seventh to tenth years of operation.

Another alternative short of outright public ownership is that of a public/private partnership. This approach would tend to minimize the risk and yet offer, at least to some degree, many of the advantages. The revised RFP which we have prepared already contains questions for those applicants wishing to propose such a public/private partnership.

In view of the expense and time delay involved in consideration of the public ownership option, it is my recommendation that you defer exploring this option until you have exhausted all private sector opportunities.

3. Franchising Without Enforceability.
Clearly, it is possible to concede to the desires of these cable companies and reduce the enforceability of their promises. Such an approach would likely result in a high level of "promises" to the Commission and to the Community in the refranchising process. However, without enforceability, there will be no assurance whatever that any company would actually deliver these promises to the community. In fact, the historic experience of communities in dealing with cable television companies as well as the recent efforts of the industry to secure federal legislation usurping local control and removing local remedies would suggest that few of such "promises" would ever be implemented.

The staff believes that the adoption of this approach at this time is inconsistent with the pain-staking development of the Ordinance proposal process in Sacramento. Further, I believe that such a process is fundamentally lacking in candor.

4. Franchising With Enforceability.
The temptation to promise more than one can reasonably deliver will continue to tempt franchise applicants to inflate their promises. However, the likely result of continuing the current process and utilizing the draft resolution as part of the RFP will be more modest including more realistic promises of community commitments. It may well be that some or all of such commitments will be conditioned upon certain levels of profitability of the franchise. In this way, the community could share in the business success of the system while not burdening the system or endangering its financing or survival.

The staff believes that the level of public participation in the profitability of the system could also be increased by changing the buyout provisions of the Ordinance, or lengthening the franchise term from fifteen to twenty or twenty-five years.

The staff recommends modification of the buyout provisions of the Ordinance only to the extent previously recommended (the greater of replacement cost or "market value" as defined in the event of purchase upon change of law or expiration and no renewal). Further, the staff recommends lengthening the franchise period to at least twenty years. The staff believes that these changes, along with retaining the option of accepting a nonselected bid if a satisfactory resolution cannot be achieved with a tentative selectee, will significantly increase the likli-hood of a high level of public participation in the profits of the system and the award of a franchise in the next round of bids.

CONCLUSION AND RECOMMENDATION

Based upon the advice from Attorney Katz, as set forth above and the staff analysis outlined above, staff would reaffirm its recommendation of June 1, 1983, to reject UTC's application as well as its subsequent proposals and proceed with an open and competitive refranchising process as set forth in the ordinance on the basis of the revised RFP including the draft resolution.

Respectfully submitted,

BOB SMITH, Executive Director
Sacramento Metropolitan Cable
Television Commission

RES:jc

Attachment

JUN 27 1983

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June 24, 1983

Mr. Brenton A. Bleier
1001 G Street, Suite 101
Sacramento, California 95814

PRIVILEGED AND CONFIDENTIAL

Re: Sacramento Metropolitan Cable Television Commission

Dear Mr. Bleier:

Thank you for your letter of June 20, 1983. In this letter I will first make a general statement in response to your letter and then will respond to each of your questions. Pursuant to your request, I will also make myself available for the July 6, 1983, meeting of the Sacramento Metropolitan Cable Television Commission ("the Commission").

I. Introductory Comments

As I understand the cable television situation in Sacramento now, you find yourself faced with the practical problem that you have gone through an extremely expensive bidding process, do not have a live bidder at this point, and wish to continue the bidding process without incurring antitrust liability. One approach has been used to date--the original bidding process--and another approach has been suggested--what you refer to as a "consortium" type of arrangement.

The above two approaches stake out the two opposite ends of the antitrust spectrum. The original bidding process is the safest possible process that the Commission could use from an antitrust point of view. The consortium approach is extremely hazardous from an antitrust point of view because of its dangerous parallels with the fact situation in the recent case of Affiliated Capital Corporation v. City of Houston, No. 81-2335 (5th Cir., Mar. 17, 1983). That

case involved a verdict of $2.1 million (which will be trebled to $6.3 million under the antitrust laws) against the City of Houston, its mayor and a cable tv company based on the following facts cited in the court's opinion:

> "Mayor McConn had let it be known that that he did not want to choose between competing applicants. He wanted the applicants to work together, resolve any overlaps in their territories and present him with a finished product. He abdicated his responsibility in the franchising process to a group of powerful Houston businessmen. In turn, these businessmen became 'friendly competitors' in an effort to segment the city among themselves and prevent any outsiders from competing with them."

Therefore, it is my opinion (1) that, from an antitrust viewpoint, the safest course for the Commission is to restart the bidding process and (2) that, if the Commission chooses the consortium approach, it would have unacceptable antitrust exposure. Insofar as there are courses of action between the two mentioned above (such as amending the original ordinance or letting an RFP based on the Commission's offer of franchise to UTC) the closer that these courses of action approximate the restarting of the bidding process, the safer they are from an antitrust point of view, and vice versa.

I believe that there are valid governmental reasons for the Commission to choose a course of action less ideal from an antitrust point of view than restarting the bidding process. If such a course of action is chosen, it is important that these governmental reasons be emphasized as the basis for that choice. In that way the Commission can both act in a practical manner and minimize its antitrust exposure.

II. Response to the Numbered Questions In Your 6/20/83 Letter

Revival of the Earlier Proposals

1. Before specifically answering your first question in this category, it is important to make two general points which the question brings up. The first is that the question asks whether the commission would "incur liability" by acting in a certain way. This question seems to assume that

the important thing in an antitrust case is whether at the end of the judicial process there would be a finding against the city.

Although that question is an extremely important one, in antitrust cases it is rarely answered because those cases are so time-consuming and expensive that well over 90% of them are settled. The more relevant question in my mind is whether the Commission has acted in such a way as to attract an antitrust plaintiff's attention. If it has and if an antitrust suit is begun, the painful reality of having to deal with that suit over a period of years far overshadows its final result. The "nuisance value" of an antitrust suit is high because expensive discovery procedures call into question virtually every action of the defendants and those connected with them. Plaintiffs use this extensive discovery both as a tactic of attrition and as a vehicle for creating unfavorable inferences against defendants.

The other general point which this question brings up is that the question seems to assume that there is an absolute answer to it. There are rarely absolute answers to antitrust problems because most antitrust cases are decided on the facts. The reason for this is that antitrust law itself is very simple--it merely prevents unreasonable restraints of trade. The difficult thing is to determine what is "unreasonable". Since that determination always depends on the facts, which are almost always unique, an antitrust practitioner must look to analogous cases (which in the relatively new field of municipal antitrust are few) and draw on his own experience in order to give an opinion. I believe that most reputable antitrust practitioners will give similar advice on similar fact situations, but obviously reasonable practitioners can differ on close calls.

Given the above general comments, my response to your first question in this category is that I believe that the Commission would be likely to attract an antitrust plaintiff if it accepted a proposal of a prior applicant without further public solicitation of proposals and without amendment of the ordinance. What you would have in that situation is a case where an ordinance was set up, in part, to avoid antitrust problems and then that ordinance was ignored. A potential antitrust plaintiff might well try to get a jury to infer that there were improper reasons for such conduct, and the discovery process might well turn up events which could support such an inference.

On the other hand, if the ordinance were properly amended in such a way as to emphasize the governmental reasons for the amendment, then revival of the earlier proposals would more closely approximate the original bidding process and would therefore be less risky from an antitrust point of view. The obvious governmental reasons for amending the original ordinance are that a substantial amount of time and money has been consumed by the original bidding process, the original bidding process did not produce the anticipated results, the original bidding process was open and fair, and it would be a waste of resources to repeat that process if there were acceptable candidates who were willing to reinstate their prior bids.

2. Allowing prior applicants to make material adjustments to their earlier proposals substantially increases the Commission's exposure from an antitrust point of view. It is further from the original bidding process (and therefore less safe from an antitrust point of view) than the course of conduct suggested in question one above. Furthermore, it gives a plaintiff the opportunity to create the inference that the original bidding process was just a sham because, although it seemed open and fair, the rules of the game later changed in a way favorable only to those who got into the process.

If changes in the original proposals came not from the applicants but, rather, out of the offer of franchise from the Commission, then antitrust exposure would be lessened. On the other hand, if the Commission's offer reduced what the applicant offered in its bid, antitrust exposure would increase. Such conduct would give an opportunity to those companies who did not participate in the process to create an inference of collusion between the city and the applicant who succeeded on a basis less costly to it than its original bid.

3. As indicated above, I believe that the best way to handle enhancements is in the offer of franchise by the Commission. I believe that it increases antitrust exposure unacceptably if any "assurances" are given (or even discussed) prior to selection.

4. I believe that the course of conduct suggested in question 4 would increase the Commission's antitrust exposure

unacceptably. Once applicants are allowed to change their prior bids or to try to approximate the UTC bid, I see no convincing reason why the bidding should be restricted to any given group of applicants.

Post Selection Bid Enrichment

1. I believe that the same policies underlying the laws to which County Counsel Elem has referred also underlie the antitrust laws. An inference of collusion could surely be raised if an applicant succeeds on the basis of a bid offering certain significant provisions and then ends up making a contract which does not include all of those significant provisions.

The "Consortium"

1. This would be a very dangerous course of action from an antitrust point of view.

2. The answer to the first question posed in question two is that would be a very dangerous course of action. The answer to the second question is that I do not believe that it would make a difference from an antitrust point of view if one applicant, say the X Company, had partners A, B and C when it originally made the bid but only partners A and B remained at a later time.

3. No.

4. Yes, although I believe that both the Commission and the members of the consortium have unacceptable antitrust exposure in such a case.

5. I believe that the course of action suggested in this question would create unacceptable antitrust exposure.

6. Standing would be conferred on anyone who was hurt by the action of the Commission. The concept of standing in antitrust laws has recently been broadened and can include cable tv companies which did not get a chance to bid, suppliers of those companies, and consumers. It is also conceivable that a class action could be brought.

Public Financing of Previous Selectee

1. I believe that this question suggests a course of conduct which would create unacceptable antitrust exposure. An inference of collusion could certainly be created from a

situation in which a company makes a bid in which it seems to undertake a large financial risk and then makes a contract in which that risk disappears.

2. No.

3. No.

* * * * *

In the above letter I have tried to walk the line between being too cryptic and too expansive. If I have crossed that line one way or the other, I hope that I will be able to remedy that with my oral presentation on July 6, 1983. I look forward to meeting with you at that time.

Sincerely,

Ronald S. Katz

RSK/cwg