

Franchise Fees

Background¹

The topic of franchise fees for local governments was not included on the research agenda approved by the panel in May 2015. As a result, no research paper was prepared on this topic. The issue of franchise fees was raised during the panel meetings and this brief background note was prepared in response to that discussion.

Local governments typically charge private utility companies for the use of public rights-of-way. It is a legislatively mandated method of compensating municipalities for the use of public rights-of-way by telecommunications providers.

U.S. municipalities are often granted authority to levy franchise fees and taxes, though not all do so. For example, in a survey of 216 large cities, municipalities were authorized to apply fees or taxes on local telephone service, telecommunications, wireless telephones, rights-of-way, long distance telephoning, access lines, and internet access. In addition, surveyors found that 72% of the municipal governments surveyed were authorized to impose cable franchise fees. In some responding cities cable franchise fees made up 6.31% of the general revenue fund and local telephone taxes/fees accounted for up to 3.51% (Wu and Pagano 2008).

Although cable and telecommunication franchise fees are common, some issues exist regarding the proper design of the fees. In an extensive legal review Colton and Sheehan assert that the revenues that are legally collectible through the fees depend on how the fees are applied. For example, if the fee is part of a “licensing” program designed to “exert some local regulatory authority over the utility,” the fees must reflect the local costs of regulating the utility. Or, if the fee is designed as an “inspection fee,” the charge may not exceed the costs of inspection. In other words, a city may not directly seek to raise revenue from a public utility through such fees. (Colton and Sheehan 1989). A determination of how these issues are resolved in Connecticut needs to be worked out.

Rents on public right-of-ways, however, may be used for such a purpose. Colton and Sheehan claim, “Cities hold public property in trust for their citizens and for the use by the general public. The grant of property rights to a utility is incompatible with the use of that property by the general public. Accordingly, public utilities should pay to gain that portion of the property right.” (Colton and Sheehan 1989). Thus, in the view of Colton and Sheehan if a municipality would seek to include revenue raising measures in new franchise contracts for public utilities, it is important that such provisions be structured as rental fees. By doing thus, “limitations on the city’s taxing power are avoided as are limitations on the right of a city to charge fees in excess of actual costs” (Colton and Sheehan 1989).

¹ Prepared for the Connecticut Tax Study Panel. This note draws on *Special Report: Franchise Fees*, Utah City Managers Association Benchmarking Project, November 5, 2010.

Generally, such franchise fees are added to the customer's bill, listed as a separate item, an amount equal to the fee imposed by local legislative authorities, whether by ordinance, franchise or other means, which fee is based on the gross receipts collected by the Company from the sale of gas to customers within the boundaries of the particular legislative authority. Such amount shall be added exclusively to bills of customers receiving service within the territorial limits of the authority imposing the fee. An example of such a franchise fee is described in the text box here.

Tennessee Natural Gas Franchise Revenue

Class: Local Taxes

Description: Municipalities can impose a franchise fee and other conditions upon the operation of a gas company within their corporate limits

Requirements or Restrictions: The franchise agreement is subject to the approval of the Tennessee Regulatory Authority (T.C.A. 65-4-107). The franchise agreement is passed by municipal ordinance.

Current Rate: Variable; there is no maximum franchise fee.

Frequency of Payment: Annually.

References

Colton, R. D. and M. F. Sheehan (1989). "Raising Local Government Revenue Through Utility Franchise Charges: If the Fee Fits, Foot It." *The Urban Lawyer* **21**(1): 55-84.

Gillespie, G. F. (2002). "Rights-of-Way Redux: Municipal Fees on Telecommunications Companies and Cable Operators." *Dickinson Law Review* **107**(2): 209-252.

Peacock, B. (2010). *A Tale of Two Markets: Telecommunications and Electricity*. Texas, Center for Economic Freedom: 25-26.

Wu, Y. and M. A. Pagano (2008). "Municipal Communications Tax Revenue Reliance and Fiscal Impact of Possible Federal Preemption." *Public Budgeting & Finance* **2008** (Spring): 82-100.