Statement of Randall O. Fraser
Revenue Laws Study Committee
January 11, 2006

Good afternoon. My name is Randy Fraser. I am currently the Vice President for Government Affairs for Time Warner Cable in North Carolina and have served two terms as the President of the North Carolina Cable Telecommunications Association. I've worked in the cable industry for 32 years, and I've had the pleasure of working with many of you over the past years. It is a privilege to speak with you again today on behalf of Time Warner Cable.

You have asked for our views on tax and regulatory policy affecting our industry. Our position is simple: Like services should be treated alike. Whether it is called "tax equity," "regulatory parity," or "leveling the playing field" the fundamental goal is the same. The State should not pick winners and losers among competitors.

You have, in recent years, successfully achieved sales tax parity for North Carolina citizens receiving television services from cable and satellite companies. You reinforced that parity last year when you brought the State's sales tax into compliance with the Streamlined Sales Tax Initiative. You may well have a similar opportunity in the coming session to ensure regulatory parity if you consider legislation to help define the rules for the telephone companies' entry into the cable television business.

My colleague Tom Adams will speak more about these issues on behalf of the cable association. But first, I thought it would be helpful to give you a brief snapshot of the origins of cable television, the competitive environment in which cable currently operates, and the current tax structure applicable to cable service.

Cable Investment and Innovation

Cable television is a testament to free enterprise. It traces its roots to Community Antenna Television (or "CATV") systems that were built in rural areas where reception of television broadcast signals was spotty or totally unavailable because of mountains or other obstructions in the terrain.

Consumer demand for television service in these areas led to the birth of cable television. Private individuals and entities, using risk capital, without any guaranteed rate of return, constructed facilities beginning in the 1960s to serve these rural consumers. Soon, the demand for cable television grew beyond rural areas to cities and towns throughout the nation.

Over the past ten years, cable service has been transformed by advances in technology. Just ten years ago, cable was a one-way analog video service. Today, cable provides an interactive broadband platform that offers a variety of voice, video, and data services.

The cable industry has spent approximately $100 billion nationwide -- yes, $100 billion -- to upgrade its facilities so that it can offer these services. We didn't come to the government seeking hand-outs or subsidies for this upgrade, and we didn't ask for special regulatory favors to support this effort. We did it because that's how the free enterprise system works—you make an investment with the hope of earning a return.

With the additional capacity and digital capability provided by this investment, cable operators now offer tiers of digital programming, along with video-on-demand and digital video recording capability. Cable also increased the quality and diversity of its programming and pioneered commercial high-speed Internet service as well as Voice-Over-Internet Protocol (or "Digital Phone") telephone service.

The result of this investment has been that cable has driven much of the technical innovation in video and digital services that consumers enjoy today. Cable is the leader in broadband deployment; it is leading in facilities-based digital phone deployment; and it will, in the years to come, continue to bring new and innovative services and products to its customers.

To give you a snapshot of the extent of this service in North Carolina, cable has over 1.8 million video subscribers in this State. It also has over 600,000 broadband customers, and more than 150,000 Digital Phone customers. And we don't just serve high population metropolitan areas, we also serve rural communities in the state—communities like Pikeville (population 714) and Fremont (population 1,400) in Wayne County and Boiling Springs (population 3,800) in Cleveland County.

Competitive Environment

While cable has been a leader in bringing technical innovation and new communications services to its customers, it does face stiff competition for all its products.

Today, cable faces vigorous competition from two satellite companies—DishNetwork and DirecTV—as well as free, over-the-air broadcasting companies. The satellite companies, who also include local broadcast signals in their service packages, now enjoy a share of the video market that is approximately 27%. Nationwide, DirecTV and DishNetwork are the 2nd and 4th largest providers of video services in terms of total subscribers. The practical effect of this is that in every location that my company, Time Warner, provides service, it faces at least two competitors that typically take more than 1 out of every 4 customers.

Of course this is in addition to competition from other sources of video programming like over-the-air television—which has about 10% of the market—other competitors like Internet video, the sale and rental of DVDs and videotapes, and movies.

Also, new competition in the multichannel video industry is increasingly coming from the telephone companies. All the major telephone companies like BellSouth and Verizon have announced that they intend to provide video services and have, in fact, begun offering services in other states.

I would also point out that other competitors are emerging on an almost daily basis. Recent competitive announcements include Apple's statement that it is providing video downloads of television programming to its iPods; and Google has stated that it is launching an Internet-based service ("Google Video Store") to allow consumers to pay to download shows and movies. As these new services take root and duplicate standard video services, the legislature may well need to consider how these new services should be treated, from a tax and regulatory perspective, consistent with the treatment of other similar services.

But the bottom line is undeniable—today cable faces vigorous and increasing competition in the market for video subscribers.

Recent Tax Increases

Cable pays its fair share of taxes. And this share just went up in the last legislative session.

As this next slide shows, by virtue of tax increases in the last legislative session, cable operators are now subject to a 7% gross receipts tax imposed by the State. This tax was imposed on cable service in the last legislative session and was effective

January 1, 2006. However, to preserve overall tax equity between cable and satellite subscribers, the legislature allowed cable operators to take a credit against this new tax in an amount equal to local franchise taxes paid. As Tom Adams will talk about in more detail, local governments are authorized by the State to impose a franchise tax on cable operators in an amount up to 5% of gross receipts. This money goes directly to the bottom line of local government operations and is used for general welfare purposes. The vast majority of local governments do impose this tax at the maximum rate of 5%. In any event, the effect of this credit is that, regardless of what rate of tax is imposed by local governments, cable customers pay a total rate of 7% in combined tax to state and local government.

In addition to the new state gross receipts tax, in the last legislative session the tax on the purchase of the "cable" we put in the ground and on poles was raised from 1% to 7%. This is obviously a significant tax increase on essential cable facilities.

Current Taxation of Cable Video Service

This next slide summarizes the current taxes paid by cable operators in North Carolina.

* As mentioned, cable is subject to the new 7% state gross receipts tax as well as a local franchise tax—typically in the amount of 5%—with a credit given against the state tax for local taxes paid.
* In addition to these gross receipts taxes, cable pays up to a 12% tax on rental of cable boxes or converters and remote control devices. This includes the 7% state tax plus an up to 5% local franchise tax.

* Cable operators also pay a 7% tax on its purchase of fiber and other cable used in its network.
* Of course, cable operators are also subject to general state business taxes like corporate income and franchise taxes.
* Cable operators also pay property tax at the local level.

Speaking just for my company, Time Warner, we pay more than $63 million a year in state and local taxes. With the new 7% state gross receipts tax, obviously this number will go up in 2006.

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I hope this brief overview has helped to put cable in its appropriate context. As the cable industry has been built entirely through the use of private, risk capital, I hope you can appreciate how important it is to preserve a level-playing field where competitors can fairly compete without the government picking winners and losers based on technology or other factors.

Again, I appreciate the opportunity to speak to you today.

Let me now turn the podium over to my colleague, Tom Adams.