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Risks Posed by Government-Owned Networks Justify State Law Limits

by

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In late May, Minnesota’s Governor Tim Walz signed into law a bill that eliminates the necessity for voter approval for local governments to enter the broadband Internet services market and compete against private providers. Minnesota’s new statute – and others like Minnesota’s – may prove costly to local taxpayers and harmful to consumers of broadband services.

State laws that limit local government ownership of broadband networks sometimes are misleadingly labeled “barriers” or “roadblocks” to “community broadband.” But those laws serve important public purposes. Some of those laws secure the right of the people to vote on whether to approve their local government’s entry into the broadband business. Others provide express protections for local taxpayers from risky local government-owned broadband projects.

State law limits on government-owned networks are justified because of the high risk local governments will unfairly privilege their own networks over private market competitors. Such laws also protect against public indebtedness from struggling government-owned networks that often burden local taxpayers and take funds from other government services. Ongoing buildout by cable and fiber providers as well as new access options enabled by fixed wireless access

(FWA) and satellite broadband significantly continue to shrink the number of truly unserved areas. These deployment trends of private market providers make new government-owned networks all but unnecessary. States are better served by encouraging private market investment to expand access.

Minnesota's old law permitted local governments to "own and operate a telephone exchange within its own borders," subject to approval by 65% of local residents in a public vote. The state's old law had been interpreted to limit local government ownership and operation of broadband networks. [Minnesota Senate File 4097](#) eliminates the right of the people to vote on the matter.¹ However, the new law does retain jurisdictional border limits and it includes limits on the use of local government condemnation power to seize and acquire private networks. Some supporters of government-owned networks deem it a victory for "community broadband" to eliminate community vote by referenda.

Following Minnesota's repeal of its local voter approval requirement, about fifteen states have laws that limit the authority of their local governments to become broadband Internet service providers. Laws limit government broadband networks in states such as Alabama, Florida, Louisiana, Missouri, North Carolina, Tennessee, and Wisconsin. Their requirements vary. Some laws require a local vote of the people to approve the networks or public hearings before approval. Some laws ban the use of local taxes, fees, or bond issues to fund government-owned networks to protect taxpayers from the financial risk of network losses and to ensure thereby the financial stability of core government services such as police, fire, emergency services, garbage collection, and more. Also, some state laws expressly prohibit government-owned networks from operating outside the geographic boundaries of the local jurisdiction.

State laws regarding public hearings, the right to vote, taxpayers' protections, and the like rest on constitutional principles. A core attribute of states' sovereignty is their power to bestow, define, alter, and remove the powers of local governments. The Court's pronouncement in *Trenton v. New Jersey* that "[a] municipality is merely a department of the state, and the state may withhold, grant, or withdraw powers and privileges as it sees fit" reflected longstanding jurisprudence and it remains good law today.² In *Nixon v. Missouri Municipal League* (2004),³ the Supreme Court reaffirmed the principle that local governments may act only when authorized by their respective states and thereby rejected a claim that Section 253(a) of the Communications Act preempted a Missouri law that prohibited the state and any of its subdivisions from offering telecommunications services for sale to the public. And in *Tennessee v. FCC* (2016), the Sixth Circuit applied *Nixon* and observed that the decision-making structure of states and their discretionary determinations for their political subdivisions implicated "core attributes of state sovereignty."⁴ The Sixth Circuit vacated the FCC's 2015 order that attempted to preempt Tennessee and North Carolina laws limiting their respective local governments from offering broadband Internet services.

¹ Minnesota Senate File 4097, 93rd Legislature (2023-2024), at: <https://www.revisor.mn.gov/bills/bill.php?b=senate&f=Sf4097&ssn=0&y=2024>.

² 262 U.S. 182, 187 (1923).

³ 541 U.S. 125 (2004).

⁴ 832 F.3d 597, 612 (6th Cir. 2016).

Thus, states are responsible for ensuring that local governments act within the confines of their delegated authority and that they can carry out traditional functions. In fulfilling that responsibility, states should establish and retain safeguards in place when their local governments seek to act outside of traditional roles and in ways that pose dangers to the integrity of primary government services and the well-being of local residents.

When local governments own broadband networks there are inherent conflicts of interest. It creates the danger that the local government will exercise its powers to privilege the government-owned network over private market competitors. By becoming a competing provider in the markets over which they have regulatory power, there is a real risk that local governments will give preferences to their own network over private competitors in local permitting processes and charging fees. For example, in July 2020, the city council of Des Moines, Iowa, voted to create a \$50 million “open access network” within public rights-of-way designed exclusively for fiber broadband providers and that at least initially favored one anchor tenant over the incumbent cable broadband provider.⁵ The cable provider filed a petition with the FCC challenging the city council’s action, and the parties later settled.⁶

The potential for government favoritism of government-owned networks discourages competitive entry by private market providers as well as investment in existing networks in the same locality. Research by former FCC Chief Economist and member of the FSF Board of Academic Advisors Michelle Connolly and Tianjiu Zuo – summarized in a November 2022 *Perspectives from FSF Scholars*, “[The Adverse Impact of Municipal and Cooperative Internet Service on Entry and Competition](#),” – indicates that “municipal and cooperative participation in the broadband marketplace had a disproportionately negative impact on additional Internet service provider (ISP) entry.⁷ Based on analysis of 2015-2020 FCC Form 477 data for Illinois, Professor Connolly and her co-author found that “when two private firms provide ISP service in a census block, the average predicted probability of entry is 46.4 percent... [I]f one of these is a municipality, the predicted probability falls to 31.7 percent.”⁸ As Professor Connolly explained, “concerns over inherent municipal regulatory conflicts of interest are strongly dissuasive to private ISPs when they consider entering a market.”⁹

State laws limiting government-owned networks are strongly justified because broadband networks are expensive and financially risky. An empirical study published in June 2022 titled

⁵ For background, see Andrew Long, “City’s Preferential Treatment of Fiber-Based Broadband Raises Competition Concerns,” *FSF Blog* (October 28, 2021), at: <https://freestatefoundation.blogspot.com/2021/10/citys-preferential-treatment-of-fiber.html>.

⁶ See Petition of MCC Iowa LLC for Expedited Declaratory Ruling Pursuant to Section 253(d) of the Communications Act, WC Docket No. 21-217, Order (released January 2022), at: <https://docs.fcc.gov/public/attachments/DA-22-85A1.pdf>.

⁷ Michelle P. Connolly, “[The Adverse Impact of Municipal and Cooperative Internet Service on Entry and Competition](#),” *Perspectives from FSF Scholars*, Vol. 17, No. 57 (November 4, 2022), at: <https://freestatefoundation.org/wp-content/uploads/2022/11/The-Adverse-Impact-of-Municipal-and-Cooperative-Internet-Service-on-Entry-and-Competition-110422.pdf> (summarizing Tianjiu Zuo and Michelle Connolly, “Impact of Municipal and Cooperative Internet Provision on Broadband Entry and Competition” (September 29, 2022), at: <https://ssrn.com/abstract=4178663>).

⁸ *Id.* at 3.

⁹ *Id.* at 1.

“[Municipal Fiber in the United States: A Financial Assessment](#)” offers insight.¹⁰ The study’s co-authors, FSF Academic Advisor Board member Christopher C. Yoo, Jesse Lambert, and Timothy P. Pfenniger, reviewed official reports by municipalities and examined fifteen different projects. In the study, they found that none of those projects generated sufficient cash flow to stay solvent in the short run without outside infusions of financial support. Additionally, “87% have not actually generated sufficient nominal cash flow to put them on track to achieve long-run solvency.”¹¹ The study’s co-authors projected that about half of those networks “would not be on track to breakeven even assuming the theoretical best-case performance in terms of capital expenditures and debt service.”¹²

For example, based on an analysis of initial investment and net present cash flow of operations as of 2019, the study’s co-authors found that Wisdom, Minnesota’s government-owned network would take 20 years to break even, that Salisbury, North Carolina’s government-owned network would break even in 355 years, and that the UTOPIA network owned by local governments in Utah would never break even.¹³ And three of the government-owned networks analyzed in the paper by Professor Yoo and his co-authors – in Burlington, Vermont, Dunnellon, Florida, and Provo, Utah – were sold at steep financial losses.¹⁴ Perhaps the most notable of those failures was the iProvo network that reportedly was sold to Google for \$1.00 in 2013.¹⁵

Debts from struggling government-owned networks pose a significant financial risk to local government treasuries. Drawing from general tax revenues, imposing surcharges on different government-provided services, or issuing municipal bonds to keep struggling networks afloat can burden local taxpayers and hamper the financial stability of traditional government services like police, fire, emergency medical care, and road maintenance.

Furthermore, government ownership of broadband networks runs against the basic norm of American constitutionalism favoring the acquisition, use, and protection of *private* property. U.S. broadband networks are the product of \$2.1 trillion in private capital investment since 1996, including over \$100 billion in private investment annually.¹⁶ States reasonably ought to consider safeguards against any local government actions that could have the consequence of dissuading private investment in network buildout and upgrades within their jurisdictions.

The best case for government-owned networks is when an area is unserved by any private market provider. But the percentage of the population that is unserved is small and continues to shrink. Aside from ongoing buildouts to rural areas by cable broadband providers and fiber providers, 5G-enabled fixed wireless access (FWA) services offer significantly improved means to reach

¹⁰ Christopher C. Yoo, Jesse Lambert, and Timothy P. Pfenniger, “Municipal Fiber in the United States: A Financial Assessment,” *Telecomm. Pol.*, Vol 46, Iss. 5 (Jun. 2022), at: https://scholarship.law.upenn.edu/cgi/viewcontent.cgi?article=3448&context=faculty_scholarship.

¹¹ *Id.*

¹² *Id.*

¹³ *Id.* at 26 (Table 6).

¹⁴ *Id.* at 29.

¹⁵ See Randolph J. May, “Google Goes to a Dollar Store,” *FSF Blog* (April 22, 2013), at: <https://freestatefoundation.blogspot.com/2013/04/google-goes-to-dollar-store.html>.

¹⁶ See USTelecom, “2022 Broadband CapEx Report” (September 8, 2023), at: <https://ustelecom.org/wp-content/uploads/2023/09/2022-Broadband-Capex-Report-final.pdf>.

unserved Americans in hard-to-reach areas without the high costs of digging trenches and attaching to poles to reach small pockets of unserved Americans. And competing satellite broadband providers Starlink and EchoStar offer nearly ubiquitous broadband access, with speeds and latency that are improved significantly compared to earlier generations of satellite services. The number of subscribers to FWA and satellite broadband services is growing fast. Expensive new government-owned broadband projects are overwhelmingly unnecessary given those access alternatives. And any such projects are likely to encounter difficulty in successfully competing against private market providers.

Promoting broadband access to all of a community's residents is a commendable goal. But labeling local votes of the people or taxpayer protections "barriers" or "roadblocks" effectively dismisses other important goals such as preserving local government integrity, respecting the will of local residents, and safeguarding taxpayers and beneficiaries of traditional government services. State laws limiting government-owned networks help ensure that local governments take a balanced approach to achieving all of those goals. States that have such laws in place should keep them.

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Further Readings

Seth L. Cooper, "[Preemption Bill on Government-Owned Networks Rests on Shaky Legal Ground](#)," *FSF Blog* (May 3, 2023).

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