

# Advice for Developers: Preempt Disaster

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No developer wants to think a relationship with a service provider will go wrong, but planning ahead of time to be able to efficiently terminate a contract and substitute an alternative provider is always a good idea.

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**I**magine the following scenario: You are a developer whose company spent several million dollars building a mixed-use community that includes an apartment complex, a planned unit development of single-family homes and buildings for commercial lease.

For several years, the development flourished. Most of the apartments were leased, and home sales were active. Then the economy slowed, and so did business at the development. At that point, the community's television and broadband service provider seemed to lose interest. The television programming, provided in bulk to all residents of the development, is expensive and inadequate. The Internet access service, also purchased in bulk, is expensive and measurably slower than what is available from other ISPs in the same geographic area.

Worst of all, services are unreliable, and outages are frequent. When customers call the service provider's "hotline," they are placed on hold for extended periods, and those who are willing to wait for a human voice on the line are treated rudely and unresponsively. Service appointments are missed, and often the attempted fixes do not work. When customers give up calling the service provider, they call your office to complain about the service provider and demand that something – anything – be done.

Meanwhile, the service provider's poor performance is affecting the marketability of the development. Irate residents and commercial tenants have plastered the Internet's social media platforms with complaints, some legitimate, others not. Several complaints have been lodged with the Better Business Bureau, not only against the service provider but also against your company. Leasing and sales activities at the development have slowed to a crawl. Low occupancy, now chronic, plagues the development while costs remain constant. Because the service provider's bulk service fee must be paid on all rentable units and salable lots, including those that are unoccupied, a significant portion of that fee must come from your company's pocket. Rumors fly, investors are unhappy and there's no end in sight. What to do?

After making multiple phone calls and sending numerous letters to the service provider and receiving apologies and promises but no meaningful action, you inform the service provider CEO that you are preparing a notice of default. The CEO says he is in discussions with a large cable operator concerning the sale of his assets at the development, and a default notice would kill any prospect of a sale. You wait, but when time passes and nothing changes, you eventually deliver a default notice alleging that the provider's Internet service is uncompetitive

and that that the provider repeatedly failed to repair service-related problems within the deadlines specified in the service-level agreement (SLA).

The service provider responds with a letter from a law firm denying that any breach of contract occurred and threatening litigation should you take any action to evict or replace the company as the sole provider at the development. Litigation will be expensive and require years to resolve, during which time the provider would have little incentive to invest any resources in improving the quality of services.

As exaggerated as this scenario may seem, both authors of this article encounter variations of it with some frequency in our practices. However, some relatively simple measures can effectively preempt the worst effects of a service provider's substandard performance.

### PREEMPTING DISASTER

The first line of defense in preempting disaster is to exercise great care in selecting a reliable, well-funded bulk service provider whose long-term strategy involves growth as a provider of services rather than, say, maximizing its subscriber count to inflate its sale price. This need not imply excluding smaller, independent operators from consideration. Indeed, a growing number of such independent service providers specialize in fiber-to-the-premises deployments and are willing and able to tailor their technologies and services to a developer's specific vision for a community.

However, even the best due diligence cannot guarantee a service provider's success. Therefore, responsible planning includes consideration of what will happen if the provider fails and how to deal with that eventuality.

There are two components to this planning: A community should have the ability to efficiently terminate a nonperforming service provider without incurring prohibitive costs in time, resources and money, and it should have the ability to replace the terminated provider with minimal disruption of services to its members.

## Developers must insist on contractual language that eliminates any ambiguity surrounding the provider's obligations under the agreement.

The first point is a matter of contract; the second is a matter of infrastructure.

### CONTRACTING TO AVOID DISASTER

Terminating a nonperforming service provider efficiently means minimizing the likelihood of litigation in the event the service agreement is terminated for breach. Securing the ability to enforce without litigation is, or should be, a central goal in negotiating a contract.

One way to avoid litigation in enforcing a contract is to negotiate a buyout clause under which the provider agrees to vacate if the property owner pays the provider a specific sum of money, usually based on the provider's initial investment in the property, discounted by an agreed-upon rate reflecting the depreciating value of equipment over time.

However, this strategy doesn't always work. Sometimes the parties cannot agree on a buyout fee that is fair to both sides. In addition, an owner should not be obligated to pay a buyout fee when its decision to terminate the relationship is based on the provider's failure to perform as promised.

Assuming that the owner must enforce the agreement, tying the service provider's access to private property to its right to actually deliver services to customers is of paramount importance. The service provider should not retain an easement or other right to remain on the property after the provider is no longer actually providing services pursuant to the agreement. Accordingly, the agreement should clearly specify that upon termination, unless the parties reach a new agreement, the provider must promptly remove or abandon any movable

equipment, cooperate in the transition of customers to the new provider and then vacate the premises.

Another obstacle to efficient termination is ambiguity surrounding the provider's obligations under the agreement. One party issues a notice of breach to the other party; the other party denies that a breach has occurred. Generally, the defense asserts that the facts alleged in the notice of breach either did not occur or do not clearly and unequivocally constitute a breach of the contract. The question is how to write a contract so as to preempt these defenses to the maximum extent possible.

Owners typically want to terminate contracts when a broadband service provider fails to provide high-quality competitive services or to provide responsive customer service. Though contractual commitments relating to competitive services and responsive customer service are less crucial when customers have a choice among providers, such commitments are of paramount importance in bulk arrangements, in which only one service provider is operating at the property. In this circumstance, precise drafting of contractual provisions describing a service provider's stay-competitive commitment and customer service obligations can minimize the likelihood of litigation in the event the provider breaches either of these obligations.

Here are a few examples of typical contractual provisions that make determining whether the facts constitute a breach of the agreement difficult:

- The service provider promises to "use commercially reasonable efforts" to ensure that the services provided remain "competitive with"

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similar services available from other providers in the “same geographical area.”

- The service provider is obligated to upgrade the on-site facilities such that the technology used to provide the services is at all times “similar to” that used by competing providers in the same area. Although this and similar language *seem* to impose a real obligation on the service provider, that appearance is for the most part illusory and usually inadequate to deter litigation in the event that the provider stumbles.
- The provider is obligated to deliver connectivity speeds of “up to 30 Mbps” or “burstable to 50 Mbps.” Although the apparent purpose of these provisions is to establish a floor on the bandwidth to be delivered to each home, the effect is exactly the opposite: “Up to 30 Mbps” means that anything less than 30 Mbps is acceptable. What does “burstable” mean? That occasionally a lucky resident might be able to download a 50-megabit file in the span of one second?

Another reason contractual provisions may be unenforceable is that the developer has no access to evidence proving a breach of contract. Suppose the provider’s customer service performance is clearly substandard; service interruptions are common and the provider takes forever to respond to complaints, let alone actually fix the problems. Thus, the provider is obviously in breach of the contract’s SLA standards, which require that service interruptions be repaired within strict deadlines and that the deadlines be met 95 percent of the time during any calendar quarter. However, the service provider responds to the

developer’s notice of breach by flatly denying that any breach occurred.

How many property owners generate and maintain records documenting the provider’s compliance with SLA standards – records that are sufficiently detailed to prove a breach of contract by a service provider? Although detailed SLA standards look impressive in a service agreement, those standards don’t mean much if the provider is not also obligated to maintain records demonstrating compliance and to turn those records over to the developer upon request.

In summary, ambiguous language in a contract is sometimes useful because it offers the only way to reach agreement. But in the most important provisions in a contract – those provisions most likely to be breached and to require enforcement – ambiguity is an invitation to litigation. In the real world, in which a developer or an HOA must decide how to allocate limited resources, the mere threat of litigation is often enough to persuade an owner to tolerate substandard performance by a service provider. Tolerating substandard performance in turn erodes the value of the asset. Furthermore, though finding the right words to establish a strict legal standard is important, considering how in the real world the standard would actually be enforced in a courtroom, should the need arise, is equally important.

### PLANNING INFRASTRUCTURE TO AVOID DISASTER

Even if a developer can efficiently terminate a service agreement, what happens next? The developer must have a plan for bringing in an alternative provider without extended delays and

interruptions in customer service. This is primarily a matter of infrastructure design and control.

The key to effective planning is to ensure that the developer, to the extent possible, retains control over the telecommunications infrastructure installed within the development. The importance of developer control is obvious when one considers the implications of allowing the incumbent carrier to build and own or otherwise control that infrastructure: When preserving the value of the asset requires replacing the incumbent carrier (or adding a second provider to compete), the incumbent carrier’s ownership or control over bottleneck infrastructure can function only as an obstacle to achievement of that goal.

By “telecommunications infrastructure,” we mean the on-site physical facilities required to deliver broadband services to customers within the development, including fiber plant, wireless mesh networks, backbone and lateral conduit to and between buildings and common areas, handholes, telecom huts and closets, floor-to-floor chases, ceiling pathways, above-ground access points such as light poles, and in-building wiring. “Bottleneck” components of the telecommunications infrastructure are those components that cannot be cost-effectively replicated for the purpose of accommodating an alternative service provider, including especially underground conduit and fiber plant and inside wiring.

An incumbent service provider that owns or is granted exclusive access to bottleneck facilities understands that control over essential infrastructure gives the provider leverage against the developer. Accordingly, the incumbent has less incentive to perform at a high level because of the practical difficulties associated with altering the status quo.

A developer should avoid conveying to a service provider any right to directly or indirectly monopolize bottleneck infrastructure, particularly after a service agreement has been breached or terminated for nonperformance. In addition, a developer can

design infrastructure to preclude monopolization of bottleneck facilities.

The obvious and best way is for a developer to install redundant bottleneck facilities. For example, the authors recommend that our developer clients install “shadow conduit” systems throughout their developments, reserving one run of conduit for the developer, who can then use the excess capacity to leverage future opportunities as they become available. The same goes for fiber optic wiring located within underground and in-building conduit. Because most of the sunk cost of infrastructure placement stems from trenching, laying more than one run of pipe in each trench makes financial sense. The incremental cost of placing duplicate conduit in a trench is more than outweighed by the benefits of having multiple pipes rather than one. Whether the developer wants to offer residents the services of

an alternative provider or entirely new services that have suddenly become available, those services can be easily and cheaply installed in preexisting reserve conduit extending from the street all the way to customer premises.

Even where redundant infrastructure was not installed, a developer can retain control over bottleneck facilities by ensuring that the incumbent carrier understands and agrees that those facilities are a shared resource. Thus, whenever possible, the service agreement should clearly state that essential facilities are owned by the developer and not by the service provider, that the incumbent service provider’s right to access and use those facilities is nonexclusive and that the incumbent’s right of access terminates once the incumbent has ceased providing services to customers within the development.

In summary, when circumstances conspire to persuade a property owner

that tolerating substandard services is better than replacing the service provider, it is usually because, during the early planning and contracting phases of development, the owner did not give adequate thought to preparing for the worst. Even though nobody heading into an ambitious project wants to dwell on what could go wrong later, the best course is to take affirmative steps early on to avoid regrets down the line. ♦

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