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## PHOENIX CENTER POLICY BULLETIN NO. 42

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### USTELECOM AND ITS AFTERMATH

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*Abstract:* In 2015, the Federal Communications Commission made the controversial decision to reclassify broadband Internet access as a common carrier “telecommunications” service under Title II of the Communications Act. While much of the debate has focused on the legality of reclassification, little attention has been paid to actual implementation. As detailed in this BULLETIN, a proper implementation of Title II precluded the Commission’s approach, forcing the Agency to ignore the “vast majority of rules adopted under Title II” and “tailor[] [Title II] for the 21st Century.” Surprisingly, the D.C. Circuit found in *United States Telecom Association v. FCC* that the agency had wide latitude to interpret the Communications Act and not only upheld the agency’s decision to reclassify but also its gross distortion of Title II. In so doing, the D.C. Circuit has extended *Chevron* deference beyond any reasonable limit, greatly expanding the Commission’s authority well beyond its statutory mandate. This BULLETIN first presents several examples of how the 2015 *Open Internet Order* ignores both the plain language of Title II and the extensive case law to achieve select political objectives, followed by a discussion of the D.C. Circuit’s acceptance of such legal perversions. Next, this BULLETIN discusses how the FCC attempted to use the same theory of the case found in *USTelecom* to regulate the prices of Business Data Services. Conclusions and policy recommendations are at the end.

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## I. Background

For over a decade, the thorny issue of net neutrality has loomed over the telecom debate. What started with the simple notion that the Federal Communications Commission should stop broadband service providers (“BSPs”) from engaging in strategic anticompetitive conduct eventually morphed into the Obama Administration subjecting the Internet to legacy common carrier regulation under Title II of the Communications Act designed for the old Ma Bell telephone monopoly of the last century.<sup>1</sup> While much of the debate to date has revolved around the threshold legal question of whether the Commission has the authority to reclassify in the first instance, the purpose of this BULLETIN is to focus on perhaps the more substantive (yet notably neglected) legal problem: the Commission’s actual implementation of Title II, in particular the ratemaking provisions of Sections 201 and 202 and its forbearance authority in Section 10.

As explained in detail below, a proper application of these provisions should have prevented the Commission from doing what it wanted to do in its *2015 Open Internet Order* – in particular, the Commission wanted (1) to force BSPs to provide edge providers with terminating access without compensation (i.e., a regulated price of zero) in direct contradiction of Section 201; (2) to impose a blanket ban on reasonable discrimination in direct contradiction to Section 202; but yet (3) to give the patina of a “light touch” approach, to forbear from the tariffing requirements of Section 203 despite directly imposing price regulation. The Commission’s solution to its legal pickle? To ignore the “vast majority of rules adopted under Title II”<sup>2</sup> by selectively picking and choosing whatever provisions of Title II it found convenient to achieve a results-driven outcome, so that it could, in the Commission’s own words, “tailor[] [Title II] ... for the 21st Century.”<sup>3</sup> In effect, since the statute prohibited the rules the Commission wished to impose, the Agency simply rewrote the statute. Respect for precedent at the Commission, it seemed, was officially dead.<sup>4</sup>

Which brings us to the point of the pencil: properly viewed, the current iteration of the net neutrality debate is not really about an “Open Internet,” free speech or even who has the biggest Reese’s Peanut Butter mug; it’s about *power*.<sup>5</sup> That is, should an administrative agency be

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<sup>1</sup> *Protecting and Promoting the Open Internet*, REPORT AND ORDER ON REMAND, DECLARATORY RULING, AND ORDER, FCC 15-24, 30 FCC Rcd 5601, 80 Fed. Reg. 19738 (rel. Mar. 12, 2015) (hereinafter “*2015 Open Internet Order*”).

<sup>2</sup> *Id.* at ¶ 51.

<sup>3</sup> *Id.* at ¶ 5.

<sup>4</sup> C.f., T.R. Beard, G.S. Ford, L.J. Spiwak, and M. Stern, *Eroding the Rule of Law: Regulation as Cooperative Bargaining at the FCC*, PHOENIX CENTER POLICY PAPER NO. 49 (October 2015) (available at: <http://www.phoenix-center.org/pcpp/PCPP49Final.pdf>).

<sup>5</sup> J. Eggerton, *John Oliver Takes on FCC's Pai, Net Neutrality*, BROADCASTING & CABLE (May 8, 2017) (available at: <http://www.broadcastingcable.com/news/washington/john-oliver-takes-fccs-pai-net-neutrality/165586>).

permitted on its own initiative to expand its power beyond its statutory mandate at the expense of private actors' Fifth Amendment due process protections? Indeed, if an administrative agency, by its own admission, is free to interpret selectively its own enabling statute to fit the times, then what is the role of Congress? At stake, in other words, is whether an administrative agency should be permitted to re-write the law – especially when it does so simply to fit a political agenda.<sup>6</sup>

According to the D.C. Circuit in *United States Telecom v. FCC*, the answer appears to be “yes.”<sup>7</sup> Citing the Supreme Court’s seminal case in *Brand X*,<sup>8</sup> the D.C. Circuit found in *USTelecom* that the FCC had wide – nearly unbounded – latitude to interpret the Communications Act and not only upheld the agency’s decision to reclassify, but also upheld the agency’s ability to “tailor” how it chose to implement Title II. In so doing, the D.C. Circuit – rather by design or by omission – has taken *Chevron* deference to the extreme.<sup>9</sup> As demonstrated below, *USTelecom* has greatly expanded the Commission’s authority to set the rates, terms and conditions of private actors well beyond its statutory mandate. Accordingly, the statutory construct of “Title II” now has no meaning; it is some bizarre legal hybrid that the FCC made up and the D.C. Circuit has sanctioned. For those who care deeply about due process and the rule of law, the precedent set by the D.C. Circuit in *USTelecom* is deeply troubling and is a case that we will likely have to deal with its aftermath for years to come.

This paper is organized as follows: In the next section, I present several examples how the Commission in its 2015 *Open Internet Order* ignored both the plain language of Title II and extensive case law to achieve select political objectives, followed by a discussion of the D.C. Circuit’s review of such legal manipulations. In Section III, I demonstrate how former FCC Chairman Tom Wheeler attempted (but, due to the clock running out by the Presidential election in 2016, ultimately did not succeed) to use the same theory of the case found in *USTelecom* to regulate the prices of Business Data Services. Conclusions and policy recommendations are at the end.

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<sup>6</sup> The Obama White House’s interference in the FCC’s deliberations regarding the 2015 *Open Internet Order* is well-documented. See, e.g., G. Nagesh & B. Mullins, *Net Neutrality: How White House Thwarted FCC Chief*, WALL STREET JOURNAL (February 4, 2015) (available at: <https://www.wsj.com/articles/how-white-house-thwarted-fcc-chief-on-internet-rules-1423097522>); L.J. Spiwak, *The “Clicktivist” In Chief*, THE HILL (November 12, 2014)(available at: <http://thehill.com/blogs/pundits-blog/technology/223744-the-clicktivist-in-chief>).

<sup>7</sup> *United States Telecom Association v. FCC*, 825 F.3d 674 (D.C. Cir. 2016), *pet. for rehearing en banc denied*, 855 F.3d 381 (2017) (hereinafter “*USTelecom*”).

<sup>8</sup> *National Cable & Telecommunications Ass’n v. Brand X Internet Servs.*, 545 U.S. 967 (2005).

<sup>9</sup> *Chevron U.S.A. Inc. v. Natural Resources Defense Council, Inc.*, 467 U.S. 837, 104 S.Ct. 2778, 81 L.Ed.2d 694 (1984).

## II. 2015 Open Internet Order and the D.C. Circuit's Response

When the FCC was contemplating its current *2015 Open Internet Rules*, it had a choice of two legal theories under which it could proceed. Under the first theory, the Commission could have followed the guide path set forth by the D.C. Circuit in *Verizon* and enacted its rules using the authority provided by Section 706 of the Telecommunications Act of 1996.<sup>10</sup> The advantage of this approach is that because this was a relatively “greenfield” area of the law, the Commission would have had a great deal of latitude to determine its own path under a “commercially reasonable” standard.<sup>11</sup> The other option (which the Commission ultimately chose) was a reclassification of broadband Internet access as a Title II common carrier telecommunications service. The downside of a Title II approach is that when you choose to apply a law designed for the old Ma Bell monopoly to the Internet, however, is that you presumably also get the nearly eighty years of established case law that goes along with it.<sup>12</sup>

By its own admission, the Commission in its *2015 Open Internet Order* imposed a “no paid prioritization” rule that was specifically designed to “prohibit broadband providers from charging edge providers a fee...”<sup>13</sup> As the D.C. Circuit expressly recognized in *Verizon v. FCC*, this rule was intended to “bar providers from charging edge providers for using their service, thus forcing them to sell this service to all who ask at a price of \$0.”<sup>14</sup> With intent, the Commission’s rule establishes “a regulated price of zero.”<sup>15</sup> Thus, despite the Commission’s protestations to the contrary,<sup>16</sup> because net neutrality is unambiguously price regulation (albeit “zero-price” regulation), the reclassification dictated by the FCC’s Commission’s *2015 Open*

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<sup>10</sup> L.J. Spiwak, *What Are the Bounds of the FCC’s Authority over Broadband Service Providers? – A Review of the Recent Case Law*, 18 JOURNAL OF INTERNET LAW 1 (2015).

<sup>11</sup> *Id.*; see also *Protecting and Promoting the Open Internet*, FCC 14-61, NOTICE OF PROPOSED RULEMAKING, 29 FCC Rcd 5561 (2014) at ¶ 10 (hereinafter “2014 Open Internet NPRM”).

<sup>12</sup> *Id.*

<sup>13</sup> See *2015 Open Internet Order*, *supra* n. 1 at ¶ 113.

<sup>14</sup> See *Verizon v. FCC*, 740 F.3d 623, 657 (D.C. Cir. 2014).

<sup>15</sup> *Id.*, 740 F.3d at 668 (D.C. Cir. 2014) (Silberman J. Dissenting).

<sup>16</sup> See, e.g., *2015 Open Internet Order*, *supra* n. 1 at ¶ 37 (our “light-touch approach for the use of Title II” means “no rate regulation”); *id.* at ¶ 382 (“... there will be no rate regulation...”); see also T. Wheeler, *This is How We Will Ensure Net Neutrality*, WIRED (February 4, 2015) (“... there will be no rate regulation...”) (available at: <https://www.wired.com/2015/02/fcc-chairman-wheeler-net-neutrality/>);

*Internet Order* must satisfy the relevant rate-making provisions of Title II of the Communications Act.<sup>17</sup> These provisions include:

- Section 201, which mandates that rates must be “just and reasonable”;<sup>18</sup>
- Section 202, which prohibits “unreasonable” discrimination;<sup>19</sup> and
- Section 203, which provides the enforcement mechanism for Sections 201 and 202 – i.e., tariffs.<sup>20</sup>

If, however, the Commission wants to refrain from imposing direct price regulation and surrender this function to the market, then Section 10 allows the FCC to forbear from the tariffing requirements of Section 203 under a delineated set of circumstances.<sup>21</sup>

What is important to understand is that the ratemaking and forbearance provisions of Title II are not solely designed to govern the conduct of the regulated firm (the Commission’s rules serve that function), but to govern the conduct of the *regulator*. Indeed, whenever the government intervenes into the market – particularly when it seeks to set the price, terms and conditions of service of private actors – a myriad of Constitutional due process concerns come to the fore that must be respected to avoid an undue takings under the Fifth Amendment. For this reason, courts have provided detailed guidance on how the Commission is supposed to interpret these various statutory provisions. As explained in detail below, the Commission’s problem in its *2015 Open Internet Order* was that both the plain terms of the statute and this extensive precedent prohibited them from doing what they wanted to do.<sup>22</sup> The Commission’s solution? Ignore the plain language of the statute and the case law in order to make up both a new theory of rate regulation and forbearance under Title II *de novo*. Let’s look at a few examples.

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<sup>17</sup> See generally, G.S. Ford and L.J. Spiwak, *Tariffing Internet Termination: Pricing Implications of Classifying Broadband as a Title II Telecommunications Service*, 67 FEDERAL COMMUNICATIONS LAW JOURNAL 1 (2015) (available at: <http://www.fclj.org/wp-content/uploads/2015/02/Tariffing-Internet-Termination.pdf>).

<sup>18</sup> 47 U.S.C. § 201.

<sup>19</sup> 47 U.S.C. § 202.

<sup>20</sup> 47 U.S.C. § 203.

<sup>21</sup> 47 U.S.C. § 160. Indeed, in case where the Commission has opted to pursue this route in the past, it has relied upon the complaint process contained in Section 208 (47 U.S.C. § 208) as a regulatory backstop. See *In re Policy and Rules Concerning the Interstate, Interexchange Marketplace*, FCC 96-424, SECOND REPORT AND ORDER, 11 FCC Rcd 20730 (rel. October 31, 1996) (hereinafter “IXC Detariffing Order”).

<sup>22</sup> Ford and Spiwak, *Tariffing Internet Termination*, *supra* n. 17.

## A. "Just and Reasonable Rates"

1. *The Commission's Approach*

Under Section 201 of the Communications Act, all rates must be "just and reasonable." However, as the D.C. Circuit remarked over thirty years ago, the phrase "just and reasonable" is not "a mere vessel into which meaning must be poured."<sup>23</sup> The problem, of course, is that ratemaking is "far from an exact science."<sup>24</sup> For this reason, courts simply require that in order to satisfy the just and reasonable standard, the Commission must set a regulated rate that falls within the *zone of reasonableness*. As illustrated in Figure 1, this zone of reasonableness lies between rates that are *confiscatory* at the low end (that is, below cost and a "takings" under the Fifth Amendment) and rates that are *excessive* at the high end (that is, "creamy returns", the limit of which is defined by the markup R).<sup>25</sup> As the Supreme Court held in its seminal *Permian Area Rate Cases*, the zone of reasonableness is such that the rate "may reasonably be expected to maintain financial integrity, attract necessary capital, and fairly compensate investors for the risks they have assumed, and yet provide appropriate protection to the relevant public interest, both existing and foreseeable."<sup>26</sup> So, in attempting to set a just and reasonable rate, the Commission must set a rate that exceeds cost, but not by too much.<sup>27</sup>

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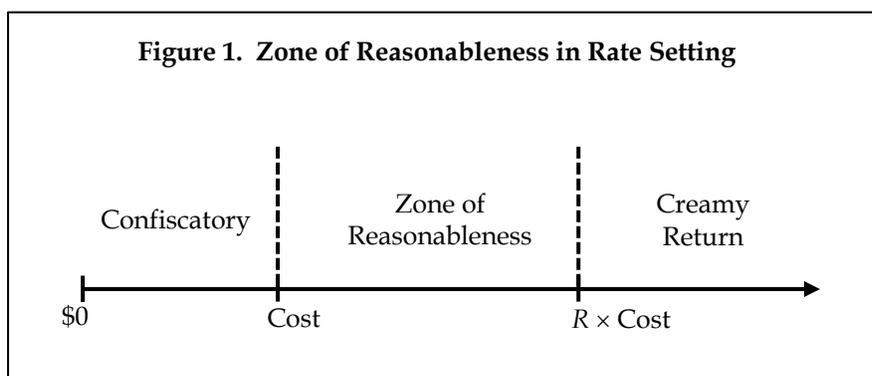
<sup>23</sup> See, e.g., *Farmers Union Central Exchange v. FERC*, 734 F.2d 1486, 1504 (D.C. Cir.), *cert denied sub nom.*, 469 U.S. 1034 (1984) (emphasis supplied). It is important to recognize that the "just and reasonable" standard is not exclusive to the Communications Act. This standard can also be found, for example, in the Federal Power Act and in the Natural Gas Act, all of which were enacted during the same time period.

<sup>24</sup> See, e.g., *Fed. Power Comm'n. v. Conway Corp.*, 426 U.S. 271, 278 (1976); *WorldCom v. FCC*, 238 F.3d 449, 457 (D.C. Cir. 2001); *Sw. Bell Telephone Co. v. FCC*, 168 F.3d 1344, 1352 (D.C. Cir. 1999); *Time Warner Entm't Co. v. FCC*, 56 F.3d 151, 163 (D.C. Cir. 1995); *United States v. FCC*, 707 F.2d 610, 618 (D.C. Cir. 1983); see also *In the Matter of Access Charge Reform; Price Cap Performance Review for Local Exchange Carriers; Interexchange Carrier Purchases of Switched Access Services Offered By Competitive Local Exchange Carriers; Petition Of US West Communications, Inc. For Forbearance from Regulation as a Dominant Carrier in the Phoenix, Arizona MSA*, FCC 99-206, FIFTH REPORT AND ORDER AND FURTHER NOTICE OF PROPOSED RULEMAKING, 14 FCC Rcd 14221 (rel. August 27, 1999) at ¶¶ 96, 144.

<sup>25</sup> See, e.g., *Farmers Union*, *supra* n. 23, 734 F.2d at 1502.

<sup>26</sup> *In re Permian Basin Area Rate Cases*, 390 U.S. 747, 792 (1968).

<sup>27</sup> I would like to thank Phoenix Center Chief Economist Dr. George S. Ford for his graphic rendering of the "zone of reasonableness."



As noted above, in its *2015 Open Internet Order*, the Commission imposed a “no paid prioritization” rule that was specifically designed to “prohibit broadband providers from charging edge providers a fee....”<sup>28</sup> This rule is intended to “bar providers from charging edge providers for using their service, thus forcing them to sell this service to all who ask at a price of \$0.”<sup>29</sup> Thus, the Commission’s rule establishes “a regulated price of zero.”<sup>30</sup> Accordingly, if edge providers are “customers” of BSPs as the D.C. Circuit found in *Verizon*, then the Commission’s *2015 Open Internet Order* has the unambiguous effect of requiring BSPs to provide carriage to edge providers without any compensation.<sup>31</sup>

By directly setting a “zero-price,” the Commission’s actions violated many basic principles of ratemaking. For example, under the plain terms of the Communications Act, if edge providers are in fact customers of a BSP as the D.C. Circuit found in *Verizon* and Title II applies to this service as the *Order* plainly states, then a BSP must be allowed to charge a positive “fee” for this termination service because a common carrier is “for hire.”<sup>32</sup> Indeed, the statute defines a service regulated under Title II as an “offering [] for a fee directly to the public.”<sup>33</sup> Equally as important, this positive fee must also satisfy the “just and reasonable” ratemaking standard contained in Section 201. However, the Commission may not set a rate arbitrarily. Instead, the Commission

<sup>28</sup> See *2015 Open Internet Order*, *supra* n. 1 at ¶ 113.

<sup>29</sup> See *Verizon v. FCC*, *supra* n. 14, 740 F.3d at 657.

<sup>30</sup> *Id.*, Silberman J. Dissenting, 740 F.3d at 668.

<sup>31</sup> *Id.*, 740 F.3d at 654 (Commission seeks to “compel[] an entity to continue furnishing service at no cost.”)

<sup>32</sup> 47 U.S.C. § 153(11); see also 47 U.S.C. §151(53).

<sup>33</sup> *Id.* (Emphasis supplied).

must provide its whys and wherefores on how it derived the rate.<sup>34</sup> The Commission provided no such analysis in its *2015 Open Internet Order*.

Formulating termination rates is likely to be a complex and arduous task, but drudgery is no excuse for the Commission's avoidance of the requirements of its own choice to apply Title II. Unquestionably, the cost of a service is not zero – there are no free lunches. In fact, it could be argued that most of the costs of the broadband network are attributable to edge providers, since the bulk of traffic is downstream rather than upstream (a ratio of about 6:1).<sup>35</sup> Under a fully-distributed cost formula, it is feasible that much of the costs would be assigned to the edge providers.<sup>36</sup> As such, it may be that the revenues from edge providers eventually make up a lion's share of BSP revenue from the sale of broadband service. In such a world, the consumer would benefit greatly. Economic theory predicts that as the edge providers' price rises, the end-users' price falls.<sup>37</sup> A more balanced rate structure across the two sides of the market may be beneficial to both network deployment and service adoption.

Unfortunately, the Commission failed to even consider such inquiry in its *2015 Open Internet Order*. In fact, it did nothing.<sup>38</sup> What cost standard was used to establish this zero price? Historical cost? Forward-looking cost? Marginal cost? Average cost? Total Element Long Run Incremental Cost? We cannot know, because the Commission arbitrarily set a price of zero without a shred of analysis.<sup>39</sup> Instead, the Agency bluntly told BSPs that they are prohibited from charging edge providers a fee for terminating access (despite the fact that edge providers impose a cost on the network). Absent some cost analysis indicating otherwise, therefore, the

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<sup>34</sup> See, e.g. *Century Communications Corp. v. Federal Communications Comm'n*, 835 F.2d 292, 300–02 (D.C. Cir. 1987) (rejecting FCC's judgment where supported by "scant" evidence), *cert. denied*, 486 U.S. 1032, 108 S.Ct. 2014, 2015, 100 L.Ed.2d 602 (1988); *Cincinnati Bell Telephone Company v. FCC*, 69 F.3d 752, 760, (6th Cir. 1995) (overturning Commission's judgment when FCC "provide[d] to this Court nothing, no statistical data or even a general economic theory, to support its argument.").

<sup>35</sup> *Global Internet Phenomena Report*, 1H 2014, SANDVINE (2014) at p. 5.

<sup>36</sup> S. Brown and D. Sibley, *THE THEORY OF PUBLIC UTILITY PRICING* (1986) at pp. 44-9.

<sup>37</sup> See G.E. Weyl, *The Price Theory of Two-sided Markets* (2006) at p. 17-8; J.P. Choi & B-C. Kim, *Net Neutrality and Investment Incentives*, 41 RAND J. OF ECONOMICS 446-465 (2010) at pp. 453-7.

<sup>38</sup> Despite having this wealth of case law brought to its attention, the Commission summarily proceeded to ignore it. See *2015 Open Internet Order*, *supra* n. 1 at fn. 1519.

<sup>39</sup> Indeed, even in the case of TELRIC—a methodology many argued produced a confiscatory rate—the Commission demonstrated its whys and wherefores to the satisfaction of the courts. See generally, *AT&T v. Iowa Utilities Board*, 525 U.S. 366 (1999); *Verizon v. FCC*, 535 U.S. 467 (2002) (finding FCC had provided sufficient detail in establishing TELRIC rate for unbundled network elements).

Commission – by definition – arbitrarily established a “confiscatory” (i.e., below cost) rate for the service BSPs offer to edge providers under Section 201.<sup>40</sup>

## 2. *The D.C. Circuit’s Response*

When the Commission first attempted to impose a “no blocking” and “no paid prioritization” rule in 2010, the D.C. Circuit in *Verizon* repeatedly pointed out that the Commission was imposing zero-price regulation on BSPs under Title I. (In fact, it was the crux of the court’s reversal of the FCC’s 2010 *Open Internet Rules*, finding that the Commission was improperly attempting to regulate Title I “information” services” as “common carriers” under Title II.<sup>41</sup>) Yet, when essentially the same rules came before the court again in *USTelecom*, the D.C. Circuit accepted this zero-price regulation at face value in the context of Title II. In fact, they made no mention of it at all.

This lack of attention to the Commission’s attempt to force BSPs to carry edge providers’ traffic without any compensation was a serious omission by the court. Indeed, throughout the 2015 *Open Internet Order*, the FCC made great hay out of using the “just and reasonable” standard in Section 201 to justify its rules, yet the court never once stopped to consider whether the actual rate imposed by the FCC’s rules – i.e., zero – passed muster under that standard. By giving the Commission a free pass to set a regulated rate without conducting an underlying cost analysis, the court has established a dangerous precedent. Under an expansive reading of *USTelecom*, the Commission now has wide latitude to set the rates, terms and conditions of broadband service providers with little regard to their guaranteed due process protections under the Fifth Amendment. Such a result is particularly curious given that the court has not hesitated to reprimand the Commission in the past for its failure to engage in the requisite due diligence when

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<sup>40</sup> Ford and Spiwak, *Tariffing Internet Termination*, *supra* n. 17.

<sup>41</sup> See, e.g., *Verizon*, *supra* n. 14, 740 F.3d at 655-56 (“We have little hesitation in concluding that the anti-discrimination obligation imposed on fixed broad-band providers has ‘relegated [those providers], *pro tanto*, to common carrier status.’ In requiring broadband providers to serve all edge providers without ‘unreasonable discrimination,’ this rule by its very terms compels those providers to hold them-selves out ‘to serve the public indiscriminately.’”)

reviewing rate cases.<sup>42</sup> Even though ratemaking is a complex problem, complexity is no excuse for the court to give the Commission a pass in this instance.<sup>43</sup>

## B. *Undue Discrimination*

### 1. *The Commission's Approach*

Under the express terms of Section 202(a), carriers are allowed to engage in *reasonable* discrimination.<sup>44</sup> In fact, the Commission conceded this very point before the D.C. Circuit in *Orloff v. FCC*.<sup>45</sup> But how to define “unreasonable” discrimination? According to well-established case law, any charge that a carrier has unreasonably discriminated must satisfy a three-step inquiry (in sequence): (1) whether the services offered are “like”; (2) if they are “like,” whether there is a price difference among the offered services; and (3) if there is a price difference, whether it is reasonable.<sup>46</sup> If the services are not “like,” or not “functionally equivalent” in the legal parlance, then discrimination is not an issue and the investigation ends. There is no valid discrimination claim for *different* prices or price-cost ratios for *different* goods.

Notably, a determination of whether services are “like” is based upon neither cost differences nor competitive necessity. Cost differentials are excluded from the likeness determination and introduced only to determine “whether the discrimination is unreasonable or unjust.” Likeness

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<sup>42</sup> As a classic case, take the example of payphone rates. While the Commission was charged with a simple task—setting a single rate—it took three separate attempts before the court finally found that the Commission acted correctly. See *In re Implementation of the Pay Telephone Reclassification and Compensation Provisions of the Telecommunications Act of 1996*, FCC 96-386, REPORT AND ORDER, 11 FCC Rcd 20541 (rel. September 20, 1996) (“First Order”); *Illinois Pub. Telecomms. Ass’n v. FCC*, 117 F.3d 555 (D.C. Cir. 1997) (“Payphones I”); *In re Implementation of the Pay Telephone Reclassification and Compensation Provisions of the Telecommunications Act of 1996*, FCC 97-371, SECOND REPORT AND ORDER, 13 FCC Rcd 1778 (rel. October 9, 1997); *MCI Telecomms. Corp. v. FCC*, 143 F.3d 606 (D.C. Cir. 1998) (“Payphones II”); *In re Implementation of the Pay Telephone Reclassification and Compensation Provisions of the Telecommunications Act of 1996*, FCC 99-7, THIRD REPORT AND ORDER AND ORDER ON RECONSIDERATION OF THE SECOND REPORT AND ORDER, 14 FCC Rcd 2545 (rel. February 4, 1999); *American Public Communications Council v. FCC*, 215 F.3d 51 (D.C. Cir. 2000) (“Payphones III”).

<sup>43</sup> On potential explanation may lie with the author of the majority’s opinion—Judge Tatel—who has shown a reluctance in the past to focus on the FCC’s violation of basic ratemaking principles. See, e.g., L.J. Spiwak, *From International Competitive Carrier to the WTO: A Survey of the FCC’s International Telecommunications Policy Initiatives 1985-1997*, 51 FEDERAL COMMUNICATIONS LAW JOURNAL 111 (1998); *Addendum*, 51 FEDERAL COMMUNICATIONS LAW JOURNAL 519 (1999).

<sup>44</sup> 47 U.S.C. § 202(a).

<sup>45</sup> *Orloff v. FCC*, 352 F.3d 415, 420 (D.C. Cir. 2003), *cert denied*, 542 U.S. 937 (2004) (“the Commission emphasizes that § 202 prohibits only *unjust* and *unreasonable* discrimination in charges and service.”) (Emphasis in original.)

<sup>46</sup> See, e.g., *MCI Telecommunications Corp. v. FCC*, 917 F.2d 30, 39 (D.C. Cir. 1990) and citations therein.

is based solely on functional equivalence.<sup>47</sup> If the services are determined to be “like” or “functionally equivalent,” then the carrier offering them has the burden of justifying any price disparity as reasonable, such as a difference in cost.<sup>48</sup> If a price difference is not justified, then the price difference is deemed unlawful. A price difference cannot be arbitrarily presumed unlawful, yet that is exactly what the Commission proceeded to do in its *2015 Open Internet Order*.

One usual measure to determine reasonableness is an inquiry as to whether the different rates are offered to “similarly situated” customers.<sup>49</sup> That is, are the customers roughly the same size and exchange similar levels of traffic, or, for example, is one customer a wholesale customer while the other only buys at retail? In the standard course of regulating telecommunications rates, such distinctions permit different rates. A prioritized termination service is not the functional equivalent of the typical termination service so there is no claim of unreasonable discrimination under Section 202 across the two services. Nor does Netflix.com place the same demands on the network as does craigslist.org. To the extent the Open Internet is about slow-and-fast lanes and Title II about “just and reasonable” and “not unreasonably discriminatory” rates, Title II offers no barrier to different services with different rates. In fact, it seems more likely that Title II facilitates rather than impedes the creation of prioritized termination.<sup>50</sup>

Clearly, a “no paid prioritization” rule violates both the letter and the spirit of Section 202. As was its expansive interpretation of Section 201, however, the Commission’s response was to ignore the law. In this particular case, the Commission side-stepped the law by promulgating its “no paid prioritization” rule—not under Section 202(a), the statute which is eponymously charged with regulating all issues of discrimination—but under the “public interest” catchall of Section 201(b) and Section 706.<sup>51</sup>

## 2. *The D.C. Circuit’s Response*

Similar to its blessing of the Commission’s tortured approach to the “just and reasonable” standard of Section 201, the court was just as accommodating to the Commission’s disregard of the plain language of Section 202. Rather than the blind neglect the court engaged in towards the

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<sup>47</sup> *Id.*

<sup>48</sup> *Id.*

<sup>49</sup> See, e.g., *In the Matter of Competition in the Interstate Interexchange Marketplace*, FCC 90-90, 5 FCC Rcd. 2627, NOTICE OF PROPOSED RULEMAKING (rel. April 13, 1990) at ¶¶ 131-139 (citing *Associated Gas Distributors v. FERC*, 824 F. 2d 981, 1007-1013 (D.C. Cir. 1987); but c.f. *Orloff*, *supra* n. 45 (allowing a mobile CMRS carrier to charge different promotional rates to similarly situated retail customers under *competitive* market conditions in the absence of tariffs).

<sup>50</sup> See Ford and Spiwak, *Tariffing Internet Termination*, *supra* n. 17.

<sup>51</sup> See *2015 Open Internet Order*, *supra* n. 1 at ¶ 292.

Commission's use of Section 201, however, this time the court decided to engage in a bit of legal gymnastics.

As noted in the previous section, rather than confront the plain language of Section 202(a) that expressly permits reasonable discrimination, the Commission adopted its "no paid prioritization" rule under the "public interest" catchall of Section 201(b) and Section 706—an explicit recognition that the Agency was skirting the plain language of the statute.<sup>52</sup> In so doing, this use of Section 706 apparently provided a sufficient legal hook for the court. Citing its ruling in *Verizon*, the court held that not only does the Commission have independent rulemaking authority under Section 706 but that such authority "extends to rules 'governing broadband providers' treatment of internet traffic'—including the anti-paid-prioritization rule—in reliance of the virtuous cycle theory."<sup>53</sup> In other words, once Section 706 is invoked, Section 202's express allowance of reasonable discrimination becomes irrelevant.

The majority's willingness to give the FCC a pass on basic ratemaking principles did not escape the dissent's watchful eye, however. As Judge Williams noted,

... I can find no indication—and the Commission presents none—that any of the agencies regulating natural monopolies, such as the Interstate Commerce Commission, Federal Energy Regulatory Commission, or Federal Communications Commission—has ever attempted to use its mandate to assure that rates are "just and reasonable" to invalidate a rate distinction that was not

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<sup>52</sup> Section 706 is comprised of two relevant sections. Under Section 706(a),

The Commission and each State commission with regulatory jurisdiction over telecommunications services shall encourage the deployment on a reasonable and timely basis of advanced telecommunications capability to all Americans (including, in particular, elementary and secondary schools and classrooms) by utilizing, in a manner consistent with the public interest, convenience, and necessity, price cap regulation, regulatory forbearance, measures that promote competition in the local telecommunications market, or other regulating methods that remove barriers to infrastructure investment. 47 U.S.C. §1302(a).

Section 706(b), in turn, requires the Commission to conduct a regular inquiry "concerning the availability of advanced telecommunications capability." 47 U.S.C. §1302(b). It further provides that should the Commission find that if "advanced telecommunications capability is [not] being deployed to all Americans in a reasonable and timely fashion," then it "shall take immediate action to accelerate deployment of such capability by removing barriers to infrastructure investment and by promoting competition in the telecommunications market." *Id.* The statute defines "advanced telecommunications capability" to include "broadband telecommunications capability." 47 U.S.C. §1302(d)(1).

<sup>53</sup> *USTelecom*, *supra* n. 7, 825 F.3d at 734.

unreasonably discriminatory. To uproot over a century of interpretation – and with so little explanation – is truly extraordinary.<sup>54</sup>

Yet, because Judge Williams was in the minority, the majority's blessing of the Commission's abject failure to adhere to basic principles of ratemaking remains the law of the land.

Putting aside both the FCC's and the court's tortured interpretation of the "virtuous cycle" theory for the moment<sup>55</sup> as well as its deliberate dismissal of both the plain terms of the statute and established case law, it is important to recognize that *USTelecom* represents a significant expansion of the D.C. Circuit's interpretation of Section 706. First, while the court had previously recognized Section 706 as an independent source of authority, prior to *USTelecom* the D.C. Circuit was quite adamant that the Commission's use of its Section 706 authority was not unfettered. As the court made plain in *Verizon*, "any regulatory action authorized by Section 706(a) [must] fall within the Commission's subject matter jurisdiction over such communications – a limitation whose importance this court has recognized in delineating the reach of the Commission's ancillary jurisdiction."<sup>56</sup> Reading this case in conjunction with the court's earlier holding in *Comcast v. FCC*, this language means that any use of Section 706 must be tied directly to a specific delegation of authority in "Title II, Title III, or Title VI..."<sup>57</sup> In other words, prior to *USTelecom*, precedent dictated that one should read Section 706 as some sort of "enhanced" ancillary authority to the Communications Act – subject to appropriate constraints – which would provide sufficient legal jurisdiction for the Commission to oversee the activities of BSPs providing Title I "information" services.<sup>58</sup> Under the pre-*USTelecom* reading of Section 706, therefore, precedent would seem to dictate that if the Commission wants to control the rates, terms and conditions of BSPs under Section 706, then the agency needs to look exclusively at ratemaking portions of the Communications Act – namely, Sections 201 and 202.

Significantly, this reading of Section 706 was nothing new to the court. In fact, the D.C. Circuit's 2009 ruling in *Ad Hoc Telecommunications Users Committee v. FCC* – a case the Commission cited with approval several times in its 2015 *Open Internet Order* – is directly on

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<sup>54</sup> *USTelecom*, *supra* n. 7, 825 F.3d at 759-760.

<sup>55</sup> For a thorough dismantling of the FCC's mis-application of the "virtuous cycle" theory, see G.S. Ford, *Bait-and-Switch – Or Why the FCC's "Virtuous Circle" Theory is Nonsense*, BLOOMBERG BNA (May 18, 2015) (available at: <http://www.phoenix-center.org/oped/BloombergBNAVirtuousCircle18May2015.pdf>).

<sup>56</sup> *Verizon*, *supra* n. 14, 740 F.3d 623 at 639-40 (emphasis supplied). It is interesting to note that when the Commission cited this exact passage from *Verizon* in its *Order*, the agency specifically omitted the italicized language above. See 2015 *Open Internet Order*, *supra* n. 1 at ¶ 138.

<sup>57</sup> *Comcast v. FCC*, 600 F.3d 642, 654 (D.C. Cir. 2010) (emphasis supplied).

<sup>58</sup> See Spiwak, *Bounds of the FCC's Authority*, *supra* n. 10.

point.<sup>59</sup> In *Ad Hoc*, the court was asked to rule on the FCC's decision to use its Section 10 authority to forbear from dominant carrier price regulation for special access services. To support its decision to forbear, the Commission also argued that its actions would further Section 706's goals of promoting broadband deployment. After review, the court held that the

general and generous phrasing of § 706 means that the FCC possesses significant, albeit not unfettered, authority and discretion to settle on the best regulatory or deregulatory approach to broadband—a statutory reality that assumes great importance when parties implore courts to overrule FCC decisions on this topic.<sup>60</sup>

However, the court made it crystal clear that the Commission's forbearance authority did not lie in Section 706 itself, but exclusively in Section 10. As the court stated bluntly, "As contemplated by § 706 . . . [f]orbearance decisions are governed by the Communications Act's § 10...."<sup>61</sup> Under this reasonable reading of the statute, therefore, even if the Commission un-reclassifies and returns broadband Internet access service to a Title I "information service," then the Commission—should it so chose—can implement adequate safeguards to protect an "Open Internet" because the Commission's use of Section 706 is constrained by the relevant provisions of the Communications Act via the doctrine of ancillary jurisdiction.

The problem with the D.C. Circuit's ruling in *USTelecom* is that this decision marks a significant expansion of the Commission's Section 706 authority not only from the court's 2009 ruling in *Ad Hoc*, but from its rulings in *Comcast* and *Verizon* as well. Indeed, the majority's ruling in *USTelecom* does not just elevate Section 706 to same level of 201 and 202; *USTelecom* essentially holds that Section 706 now *supersedes* Sections 201 and 202. The problem with such an expansive reading is that at least under Section 201 and 202, the Commission must comply with basic ratemaking principles to ensure, for example, that the Commission does not establish a confiscatory rate. Under *USTelecom*, however, the D.C. Circuit has told the Commission that if it wants to regulate directly BSPs rates, terms and conditions under Section 706, then it need not first determine that rates are "just and reasonable." Instead, the agency is now free to pick a rate out of thin air so long as it can claim that this rate will lead to increased broadband deployment.<sup>62</sup>

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<sup>59</sup> *Ad Hoc Telecommunications Users Committee v. FCC*, 572 F.3d 903, 907 (D.C. Cir. 2009).

<sup>60</sup> *Id.* at 906-07.

<sup>61</sup> *Id.* at 907.

<sup>62</sup> The preceding discussion raise an interesting academic question: what if FCC had adopted a "commercially reasonable" standard similar to one D.C. Circuit approved in *Cellco* as originally contemplated in the Commission's 2014 *Open Internet NPRM*. See 2014 *Open Internet NPRM*, *supra* n. 11 at ¶ 10. Most likely the Commission would not have run into the problem of whether it violated the just and reasonable standard because Commission would not be

### C. Forbearance of Tariffing Requirements

#### 1. The Commission's Approach

Finally, we come to the FCC's forbearance decision. In its *2015 Open Internet Order*, the Commission used its authority under Section 10 to forbear from the tariffing requirements of Section 203 when it reclassified broadband Internet access as a Title II common carrier telecommunications service.<sup>63</sup> Prior to the *2015 Open Internet Order*, the FCC had never granted forbearance of tariffing requirements in the total absence of competition – either competition was present or at least imminent.<sup>64</sup> The reason is because under the plain language of Section 10 of the Communications Act, the FCC may only forbear when the

enforcement of such regulation or provision is not necessary to ensure that the charges, practices, classifications, or regulations by, for, or in connection with that telecommunications carrier or telecommunications service are just and reasonable and are not unjustly or unreasonably discriminatory.<sup>65</sup>

Stated another way, the Commission needs to ensure that the market will ensure that rates continue to fall under the just and reasonable standard before it can eliminate tariffs.<sup>66</sup> The problem for the Commission, however, is that its entire Open Internet paradigm up to 2015 rested on the proposition that each individual BSP is a “terminating monopoly” (subsequently changed to the more innocuous term “gatekeeper” in the *2015 Open Internet Order*) which, by the Commission's own terms, has the ability to raise price and restrict output.<sup>67</sup>

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directly setting a rate. Instead, companies would have privately negotiated rate and then the Commission would have evaluated that rate under a defined set of parameters. See *Spiwak, Bounds of the FCC's Authority*, *supra* n. 10.

<sup>63</sup> *2015 Open Internet Order*, *supra* n. 1.

<sup>64</sup> For a detailed discussion of the FCC's forbearance authority, see G.S. Ford and L.J. Spiwak, *Section 10 Forbearance: Asking The Right Questions To Get The Right Answers*, 23 *COMMLAW CONSPPECTUS* 126 (2014).

<sup>65</sup> 47 U.S.C. §160(a)(1).

<sup>66</sup> See *Orloff*, *supra* n. 45, 352 F.3d at 420 (In the case of Section 203 forbearance, “[r]ates are determined by the market, not the Commission, as are the level of profits.”).

<sup>67</sup> In its *2015 Open Internet Order*, in response to comments from the dissent in *Verizon* that “because terminating monopolies are not largely discussed outside of Commission jurisprudence, and ‘[t]he gatekeeper effect is a tool that facilitates the exercise of market power over sellers; it is not market power itself’”, the Commission elected to substitute the phrase “gatekeeper” for “terminating monopoly.” For all intents and purposes, the Commission essentially uses these terms to mean the same thing. See *2015 Open Internet Order*, *supra* n. 1 at n. 130 (“However, our reliance on these terms for our determinations today focuses on how this unique “gatekeeper” position of broadband providers in combination with other realities about broadband availability and access affects broadband providers’ incentives and abilities to harm the open nature of the Internet. As explained further below, the Commission’s discussion of these

In the *2015 Open Internet Order*, the Commission rejected the obvious logic of the statute, holding that it was free to surrender ratemaking to the market even in the presence of a “gatekeeper” because “nothing in the language of Section 10 precludes the Commission from proceeding in that basis where warranted.”<sup>68</sup> The problem is that the Commission’s legal logic for its new forbearance standard is circular. Let’s walk through it step-by-step:

- (1) All BSPs are “gatekeepers” – i.e., they are dominant over themselves and competition is irrelevant.
- (2) Under Title II, “dominant” firms (i.e., those firms with market power) have traditionally been subject to rate regulation under Section 201 and 202.<sup>69</sup>
- (3) Rate regulation is enforced by the tariffing provisions of Section 203.
- (4) Under the plain terms of Section 10, the Commission may only forbear from the requirements of Section 203 when “enforcement of such regulation or provision is not necessary to ensure that the charges, practices, classifications, or regulations by, for, or in connection with that telecommunications carrier or telecommunications service are just and reasonable and are not unjustly or unreasonably discriminatory.”<sup>70</sup>
- (5) But because BSPs are subject to the “no paid prioritization” rule and “no blocking rule,” the presence of competition was not warranted as a prerequisite for forbearance in this particular case. Instead, the Commission can forbear from the tariffing requirements of Section 203 because enforcement of the “no paid prioritization” and “no blocking” rules are sufficient to ensure that rates will remain just and reasonable as required by Section 10.<sup>71</sup>

The logical flaw in the Commission’s argument is readily apparent: *The Commission is not surrendering ratemaking to the market because it does not trust the market to ensure that rates will remain just and reasonable.* Instead, the Commission claimed it was forbearing from price regulation but nonetheless imposed a regulated price without the due process protections of a tariff. This it

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terms is especially important in combination with switching costs and limited retail broadband competition for fixed broadband. With respect to mobile, the presence of some additional retail competition is not enough to alter our conclusion here.”)

<sup>68</sup> *2015 Open Internet Order*, *supra* n. 1 at ¶ 439.

<sup>69</sup> See, e.g., *In re Motion of AT&T Corp. to Be Reclassified as a Non-Dominant Carrier*, FCC 95-427, ORDER, 11 FCC Rcd 3271 (rel. 23 Oct. 1995).

<sup>70</sup> 47 U.S.C. § 160.

<sup>71</sup> *2015 Open Internet Order*, *supra* n. 1 at ¶¶ 441-452.

cannot do: Again, either the Commission may regulate prices via tariffs (subject to the due process contours of established law), or it may forbear from the tariff requirements and rely upon the market to ensure that rates remain “just and reasonable.” The Agency cannot directly set a regulated price in a de-tariffed market, but that is precisely what it did in the *2015 Open Internet Order*.<sup>72</sup>

These legal shenanigans did not go un-noticed. As then-Commissioner Pai warned in his lengthy dissent,

What I cannot find—and what our precedent does not countenance—is any instance where the FCC eliminated economic regulations without first performing any market analysis or finding competition sufficient to constrain anticompetitive pricing and behavior. \*\*\* [T]he FCC has not and, under the statute, cannot forbear from any economic regulation on a whim or a lark. Instead, it must identify something else that will constrain pricing, and that something else has always been—and can only be—competition.

But in forbearing from economic regulations in today’s *Order*, the Commission doesn’t just fail to find sufficient competition. It goes so far as to find that competition is lacking in the market for broadband Internet access service: Competition “appears to be limited in key respects,” with consumers facing “high switching costs . . . when seeking a new service,” and “broadband providers hav[ing] significant bargaining power in negotiations with edge providers and end users.” \*\*\* If that’s truly how the FCC sees the market, it should go ahead and use the m-word—monopoly—and rely on the economic regulations of the Communications Act that Congress designed to prevent a monopolist (back in 1934, it was Ma Bell) from exercising market power to the detriment of consumers. I do not see how the Commission could possibly forbear from economic regulations while at the same time finding that competition is so limited or nonexistent. Yet the *Order* does just that.<sup>73</sup>

For these reasons, Commissioner Pai pointed out that the Commission essentially invented “out of whole cloth a new method of conducting a forbearance analysis that bears little resemblance to either the terms of the Act or the Commission’s precedents.”<sup>74</sup> Instead, as Commissioner Pai explained, the “forbearance section of the Order most clearly reveals that the Commission’s

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<sup>72</sup> *C.f.*, Orloff, *supra* n. 45.

<sup>73</sup> See Dissent of Commissioner Pai to *2015 Open Internet Order*, *supra* n. 1, slip op. at p. 378.

<sup>74</sup> *Id.*

decision today is driven neither by the law nor the facts but rather by the need to reach certain predetermined policy outcomes.”<sup>75</sup> Commissioner Pai had a valid point: when it comes to the Agency’s new forbearance standard, it is readily apparent that the Commission did not forbear from tariffing requirements to relieve constraints on the regulated. Quite to the contrary, the Commission acted to relieve constraints on itself as the regulator.

## 2. *The D.C. Circuit’s Response*

Once again, the court upheld the Commission’s tortured application of the plain terms of the Communications Act. To be clear, however, this result was not due to superior legal acumen by the Commission, but the consequence of litigation tactics. First, counsel for the appellants actively supported the FCC’s new forbearance standard. Certainly, a regulated firm cannot be expected to challenge a relaxed standard for setting aside regulation (ignoring, unfortunately in this case, the fact that the relaxed standard was being used *to expand* regulation.) Second, the court found that for the one intervenor who did challenge the FCC’s forbearance standard – Full Service Network – their counsel failed to make the requisite statutory arguments outlined above. As the court noted,

Notably ... Full Service Network has never claimed that the Commission misapplied any of the Section 10(a) factors, failed to analyze competitive effect as required by Section 10(b), or acted contrary to its forbearance precedent. Indeed, when pressed at oral argument, Full Service Network disclaimed any intent to make these arguments.”<sup>76</sup>

Facing no meaningful opposition to the Commission’s perversion of the plain language of Section 10, the court therefore upheld the FCC’s new forbearance standard.

This perversion of Section 10 by both the Commission and the majority in *USTelecom* proved to be a bridge too far for Judge Brown. In her scathing dissent to the court’s denial of a rehearing *en banc*, Judge Brown argued that both the FCC and the majority in *USTelecom* “disregard[ed] the nature of forbearance.” As Judge Brown observed,

Forbearance permits the FCC *to reduce* common carriage regulation over telecommunications, *not expand* common carriage regulation by reclassifying an information service and shaping common carriage regulations around it. The FCC has consistently understood this, invoking forbearance toward one of “Congress’s

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<sup>75</sup> *Id.*

<sup>76</sup> *See USTelecom, supra* n. 7, 825 F.3d at 732

primary aims in the 1996 Act:" "deregulate telecommunications markets to the extent possible." \*\*\*

There is a sad irony here. Both this Court and the Supreme Court admonished the FCC for asserting forbearance authority without congressional authorization when the Commission's aim was *deregulatory*. Now, when the Commission's aim is to *increase regulation*, this Court is willing to bless the Commission using forbearance without any satisfaction of the statutory requirements, and at odds with the nature of forbearance itself.<sup>77</sup>

In Judge's Brown's view, if "the FCC is to possess statutory forbearance authority, it should conform to forbearance's statutory conditions and the overall statutory scheme. Neither is the case here."<sup>78</sup> Given such a perversion of the plain terms of Section 10, therefore, Judge Brown concluded that the "FCC's abuse of forbearance amounts to rewriting the 1996 Act in the bowels of the administrative state, when it should petition Congress for these purportedly-necessary changes."<sup>79</sup>

Judge Brown's dissent vindicates FCC Commissioner Michael O'Reilly concerns about the Agency's 2015 *Open Internet Order*. As Commissioner O'Reilly presciently noted in his dissent to the 2015 *Open Internet Order*,

... the most surprising—and troubling—aspect of the item is that it promises forbearance from most of Title II but does not actually forbear from the substance of those provisions. Instead, the item intends to provide the same protections using a few of the "core" Title II provisions that are retained: chiefly, sections 201, 202, and 706. I call this maneuver *fauxbearance*.<sup>80</sup>

And that is precisely the point: either the Commission can directly impose price regulation (and follow the rules thereto) under Title II or it can deregulate surrender to the market. It cannot do both (except—apparently according to the D.C. Circuit—it can do so now).

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<sup>77</sup> *USTelecom, petition for rehearing en banc denied*, Judge Brown dissenting, *supra* n. 7, 855 F.3d at 409 (emphasis in original and citations omitted).

<sup>78</sup> *Id.*

<sup>79</sup> *Id.*

<sup>80</sup> Dissent of Commissioner Michael O'Reilly, 2015 *Open Internet Order*, *supra* n. 1, slip op. at p. 396.

### III. USTelecom and its Aftermath: The FCC Attempts to Regulate Business Data Services

Facing no opposition from the D.C. Circuit to their reinvention of Title II jurisprudence in the 2015 *Open Internet Order*, the Commission under FCC Chairman Tom Wheeler wasted no time to push the edge of the legal envelope. For example, in 2016, the Agency launched a *Further Notice of Proposed Rulemaking* (“FNPRM”) to develop a new policy framework for “Business Data Services” or “BDS” (formally known as “Special Access” services).<sup>81</sup> Without belaboring the details, the Commission essentially sought to divide the BDS world into two segments based upon a simple head-count: markets that are “competitive” and markets that are “not.” According to the FNPRM, if a market is competitive, then the FCC will remove price regulation; but if the FCC finds that a market is not competitive, then the Agency intends to impose price cap regulation on “dominant” carriers. Significantly, however, the Commission did not seek to enforce this rate regulation via the process outlined in the Commutations Act—i.e., a tariff. Instead, the Commission proposed to forbear from the tariffing requirements of Section 203 and instead exclusively rely upon the general catch-all rate provisions of Sections 201 and 202 of the Communications Act.<sup>82</sup>

If this legal theory sounds familiar, it should. It was the same theory of ratemaking and forbearance that the Commission used in its 2015 *Open Internet Order*. And, just as in the BDS case, the Commission actions bore no bearing to established Title II jurisprudence. By the FCC’s own admission, the detariffed BDS market was *not competitive*—i.e., firms have market power and, therefore, have both the incentive and ability to raise price and restrict output. Thus, by definition, the Commission cannot surrender enforcement of the “just and reasonable” standard to the market, yet that is exactly what it purported to do in the BDS context. But, just as in the 2015 *Open Internet Order*, despite this alleged forbearance, the FCC was fully prepared to impose a regulated rate on “detariffed” providers without any cost justification (other than the fact that the Commission believed them to be “too damn high”).<sup>83</sup>

Given the case law outlined above, the problems with the Commission’s proposed approach in the *BDS Further Notice* become apparent: if the government wants to set a regulated price (i.e.,

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<sup>81</sup> *In the Matter of Business Data Services in an Internet Protocol Environment, Investigation of Certain Price Cap Local Exchange Carrier Business Data Services Tariff Pricing Plans, Special Access for Price Cap Local Exchange Carriers, AT&T Corporation Petition for Rulemaking to Reform Regulation of Incumbent Local Exchange Carrier Rates for Interstate Special Access Service*, FCC 16-54, TARIFF INVESTIGATION ORDER AND FURTHER NOTICE OF PROPOSED RULEMAKING, \_\_ FCC Rcd \_\_ (rel. May 2, 2016) (available at: [http://transition.fcc.gov/Daily\\_Releases/Daily\\_Business/2016/db0602/FCC-16-54A1.pdf](http://transition.fcc.gov/Daily_Releases/Daily_Business/2016/db0602/FCC-16-54A1.pdf)) (hereinafter “BDS Further Notice”).

<sup>82</sup> *Id.* at ¶ 263.

<sup>83</sup> See G.S. Ford, *How (and How Not) to Measure Market Power Over Business Data Services*, PHOENIX CENTER POLICY PAPER NO. 50 (September 2016) (available at: <http://www.phoenix-center.org/pcpp/PCPP50Final.pdf>).

a rate), then tariffing provides an important constraint on the FCC's behavior. For example, tariffing forces the Commission to engage in a serious analysis to see if a rate is "just and reasonable" – a task the Commission never attempted to do.<sup>84</sup> Indeed, in the absence of a full-fledged review of a tariff in a rate case, how is a carrier protected from the Commission setting a confiscatory (i.e., below-cost) rate in violation of the just and reasonable standard contained in Section 201? Short answer: it's not. Similarly, under Section 202, firms are allowed to engage in *reasonable* discrimination so long as they provide the same product at the same price to a "similarly situated" customer. In the absence of a formal tariff where price terms and conditions are public to all, litigation of alleged "unreasonable" price discrimination will run rampant. As with its *2015 Open Internet Rules*, the Commission was not attempting to use its forbearance authority to relieve constraints on the regulated; quite to the contrary, the Commission was seeking to relieve the constraints on itself as the regulator.

With last year's election, political pressure forced then-FCC Chairman Tom Wheeler to pull his proposed *BDS Further Notice* on the eve of the Commission vote (something Mr. Wheeler was not particularly happy about).<sup>85</sup> Mr. Wheeler's successor—current FCC Chairman Ajit Pai—subsequently formally withdrew Mr. Wheeler's approach and replaced it with an approach more in line with the established Title II jurisprudence outlined above: namely, where there is sufficient competition, the Commission would forbear from regulation, and in markets still served by only one firm, it would impose price regulation via mandatory tariffs under Section 203.<sup>86</sup> As the Commission correctly observed, "we conclude it is not practical to detariff carriers that are now subject to—and will remain subject to—price cap regulation, *where the tariff is the tool the Commission has used – and will continue to use – to enforce that regulation.*"<sup>87</sup> Still, with USTelecom still on the books, despite the restraint shown by the Pai-led Commission the risk that a subsequent Commission with activist regulatory proclivities could again set a rate without the due process protections that tariffs afford remains a very legitimate possibility.

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<sup>84</sup> *Id.*

<sup>85</sup> L.J. Spiwak, *A Political Temper Tantrum at the FCC*, THE HILL (December 1, 2016) (available at: <http://thehill.com/blogs/pundits-blog/technology/308187-a-political-temper-tantrum-at-the-fcc>).

<sup>86</sup> *In the Matter of Business Data Services in an Internet Protocol Environment; Technology Transitions; Special Access for Price Cap Local Exchange Carriers; AT&T Corporation Petition for Rulemaking to Reform Regulation of Incumbent Local Exchange Carrier Rates for Interstate Special Access Services*, FCC 17-43, REPORT & ORDER, \_\_ FCC Rcd \_\_ (rel. April 28, 2017).

<sup>87</sup> *Id.* at ¶ 165 (emphasis supplied).

#### IV. Conclusion

*USTelecom* has established a troubling precedent. As noted above, the statutory construct of “Title II” now has no meaning; it is some bizarre legal hybrid that the FCC made up and the D.C. Circuit has sanctioned. The big question is what happens next? As of this writing, the D.C. Circuit has denied petitions for rehearing *en banc* review,<sup>88</sup> and whether the Supreme Court will grant *certiorari* is a crapshoot—particularly as the Republican-led FCC has announced plans to reverse its 2015 *Open Internet Order*.<sup>89</sup> While removing the Internet out from under the thumb of such a bizarre legal construct certainly is a step in the right direction, *USTelecom*—for the foreseeable future—remains the law of the land and can provide powerful ammunition for a future Commission who does not share Chairman Pai’s respect for due process.

If anything, *USTelecom* proves the old adage that “bad facts make bad law.” While the Commission certainly has great latitude to interpret the Communications Act, the Agency must nonetheless operate “within the bounds of reasonable interpretation”<sup>90</sup> and it is not at liberty to pick and choose select provisions of the statute to govern for the sake of expediency. Or does it? With the D.C. Circuit’s decision in *USTelecom*, the FCC apparently now has *carte blanche* to tailor its enabling statute to fit a results-driven outcome and trample on key due process concerns so long as it can sprinkle some pixie dust about promoting broadband deployment.

And if that unbridled expansion of regulatory power doesn’t scare you, then it damn well should.

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<sup>88</sup> *USTelecom*, petition for rehearing *en banc* denied, *supra* n. 7.

<sup>89</sup> *C.f.*, Editorial: *Defining Deference Down: A Chance for the Supreme Court to Revisit its Chevron Doctrine*, WALL STREET JOURNAL (May 11, 2017) (available at: <https://www.wsj.com/articles/defining-deference-down-1494544427>); *In re Restoring Internet Freedom*, FCC 17-60, NOTICE OF PROPOSED RULEMAKING, \_\_ FCC Rcd \_\_, (rel. May 23, 2017) (available at: [https://apps.fcc.gov/edocs\\_public/attachmatch/FCC-17-60A1.pdf](https://apps.fcc.gov/edocs_public/attachmatch/FCC-17-60A1.pdf)).

<sup>90</sup> See, e.g., *Utility Air Regulatory Group v. Environmental Protection Agency*, \_\_ U.S. \_\_; 134 S.Ct. 2427, 2431 (2014); *City Of Arlington, Texas v. Federal Communications Commission*, \_\_ U.S. \_\_, 133 S.Ct. 1863, 1864 (2013)).