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Net Neutrality

In the wake of the D.C. Circuit Court's decision in *Verizon v. FCC*, net neutrality advocates have called upon the Federal Communications Commission to reclassify broadband Internet service as a common carrier "telecommunications service" under Title II of the Communications Act. This, they argue, will prevent a situation where broadband providers can give themselves and others willing to pay a fee a "fast lane" on the Internet, while slowing other businesses so that their services seem less attractive. But the fact of the matter, writes Lawrence J. Spiwak, president of the Phoenix Center for Advanced Legal & Economic Public Policy Studies, is that the FCC has ample legal authority to draft new enforceable net neutrality rules—without having to reclassify. Besides, Spiwak explains, so-called Internet fast lanes are perfectly legal under Title II.

Understanding the Net Neutrality Debate: A Basic Legal Primer

BY LAWRENCE J. SPIWAK

There is an old saying that "ignorance of the law is no excuse." Unfortunately, when it comes to the net neutrality debate, we may have found the exception to the rule.

As a prime example, one needs only to look at the growing cacophony from those who are urging the Fed-

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eral Communications Commission to reclassify broadband Internet access from being an "information service" under Title I of the Communications Act to a traditional "common carrier" telephone service under Title II of the Communications Act.¹ As support for this draconian change in approach to regulating broadband services, proponents of reclassification claim that the FCC lacks sufficient regulatory authority to police the Internet under Title I and, therefore, only Title II reclassification will prevent Broadband Service Providers (BSPs) from engaging in anticompetitive conduct.

Once the law is properly understood, however, this argument does not hold up.

Background. Hard to believe, but the FCC actually has a long and distinguished history of applying a light regulatory touch to nascent technologies that can, and often do, disrupt the status quo (see, e.g., the FCC's successful *Competitive Carrier* paradigm for long distance service).² Consistent with this precedent, as the Internet began to emerge as an alternative platform to tradi-

¹ See <http://www.markey.senate.gov/news/press-releases/to-protect-net-neutrality-markey-leads-senate-dems-in-call-to-reclassify-broadband-as-a-utility>.

tional telecommunications services in the early 1990s, the agency had the foresight to apply a light regulatory touch.

What is interesting to note is the FCC's choice of legal theories under which it decided to pursue its deregulatory strategy for broadband. The Telecommunications Act of 1996 offered the FCC two broad paths.³

The agency could have regulated broadband Internet access by classifying the service as a Title II common carrier telecom service but use its authority under Section 10 of the 1996 Act to forbear from select portions of the Communications Act.⁴ This path was specifically rejected by both Democrat and Republican administrations, however. As the Clinton-era FCC observed in 1998, "classifying Internet access services as telecommunications services could have significant consequences for the global development of the Internet. We recognize the unique qualities of the Internet, and do not presume that legacy regulatory frameworks are appropriately applied to it."⁵

The decision to eschew Title II was sound in light of the fundamental legal and policy problems with such an approach, and these reasons are still valid today. As the FCC itself noted, this Title II approach would foist a host of legacy regulations designed for a monopoly telephone world (including state regulation) immediately upon the Internet—a policy which on its face makes little sense, not to mention its inconsistency with FCC precedent of applying *de minimis* regulation on nascent technologies.⁶ Second, the agency's use of its Section 10 forbearance authority has a sordid past, and the agency's latest theory of forbearance—set forth in its *Phoenix Forbearance Order*⁷—effectively neuters Section 10 as a plausible deregulatory tool.⁸ More importantly, for such a "light touch" common carrier approach to work effectively, the FCC must maintain a sufficient level of credibility for "regulatory self-restraint" with both the industry and financial markets

² See, e.g., *In re Motion of AT&T Corp. to Be Reclassified as a NonDominant Carrier*, FCC 95-427, 11 FCC Rcd. 3271 (1995) and citations therein.

³ Indeed, it should be noted that prior to the enactment of the 1996 Act, the Communications Act did not contain any provisions that would expressly allow the agency to forbear lawfully from applying portions of the Act. Thus, for example, when the FCC tried to eliminate tariff requirements for non-dominant long-distance carriers, the Supreme Court held that the agency lacked this authority. See *MCI v. AT&T*, 512 U.S. 218 (1994).

⁴ 47 U.S.C. § 160.

⁵ *In the Matter of Federal-State Joint Board on Universal Services*, Federal Communications Commission, FCC 98-67, 13 FCC Rcd 11,830, REPORT TO CONGRESS (rel. April 20, 1998) (available at: http://www.fcc.gov/Bureaus/Common_Carrier/Reports/fcc98067.pdf) at ¶ 82.

⁶ For a detailed list of potential regulatory obligations that would be triggered by reclassification, see, e.g., *AT&T Ex Parte*, FCC GN Docket No. 14-28 (May 9, 2014) (available at: <http://apps.fcc.gov/ecfs/document/view?id=7521120564>).

⁷ *In the Matter of Petition of Qwest Corporation for Forbearance Pursuant to 47 U.S.C. § 160(c) in the Phoenix, Arizona Metropolitan Statistical Area*, FCC 10-113, MEMORANDUM AND ORDER, 25 FCC Rcd 8622 (rel. June 22, 2010), *aff'd*, *Qwest v. FCC*, 689 F.3d 1214 (10th Cir. 2012).

⁸ See, e.g., G.S. Ford and L.J. Spiwak, *The Impossible Dream: Forbearance After the Phoenix Order*, PHOENIX CENTER POLICY PERSPECTIVE No. 10-08 (December 16, 2010) (available at: <http://www.phoenix-center.org/perspectives/Perspective10-08Final.pdf>).

to preserve investment incentives—a credibility which is tenuous at best.⁹

Instead of choosing a Title II approach for broadband Internet access services, the FCC opted to classify broadband Internet access as an "information service"¹⁰ under Title I and imposed regulation (as necessary) under its long-standing "ancillary authority."¹¹ Not only did such an approach avoid applying legacy regulations to the Internet, but had the added benefit of effectively preempting state public utility commissions from regulating broadband.¹² The FCC eventually classified cable broadband,¹³ wireline broadband,¹⁴ wireless broadband¹⁵ and even broadband over powerline¹⁶ as a Title I information service, and the agency's deregulatory approach is widely credited with the rapid pace of deployment, adoption, and innovation in the broadband ecosystem.¹⁷

The FCC Has Ample Authority Under Existing Law. That said, given the numerous novel legal questions raised by the net neutrality debate, the FCC has had a bit of

⁹ See G.S. Ford, L.J. Spiwak and M. Stern, *The Broadband Credibility Gap*, 19 COMM'LAW CONSP'CTUS 75 (2010) (available at: <http://www.phoenix-center.org/papers/CommLawConsp'ctusBroadbandCredibilityGap.pdf>); G.S. Ford and L.J. Spiwak, *What is the Effect of Regulation on Broadband Investment? Regulatory Certainty and the Expectation of Returns*, PHOENIX CENTER POLICY PERSPECTIVE No. 12-05: (September 19, 2012) (available at: <http://www.phoenix-center.org/perspectives/Perspective12-05Final.pdf>).

¹⁰ 47 U.S.C. § 153(24) defines an "information service" as "the offering of a capability for generating, acquiring, storing, transforming, processing, retrieving, utilizing, or making available information via telecommunications, and includes electronic publishing, but does not include any use of any such capability for the management, control, or operation of a telecommunications system or the management of a telecommunications service." This definition is a near-perfect description of Internet access services.

¹¹ See Communications Act Section 4(i), 47 U.S.C. 154(i), which provides that the FCC "may perform any and all acts, make such rules and regulations, and issue such orders, not inconsistent with this chapter, as may be necessary in the execution of its functions." For a good summary of the FCC's ancillary authority, see B. Esbin and A. Marcus, "The Law Is Whatever the Nobles Do": *Undue Process at The FCC*, 17 COMM'LAW CONSP'CTUS 1 (2009) (available at: <http://commlaw.cua.edu/res/docs/Esbin-Marcus-Revised-2.pdf>).

¹² See, e.g., *In re Petition for Declaratory Ruling that Pulver.com's Free World Dialup is Neither Telecommunications Nor a Telecommunications Service*, FCC 04-27, 19 FCC Rcd 3307, MEMORANDUM AND ORDER (rel. February 19, 2004).

¹³ *National Cable & Telecommunications Ass'n v. Brand X Internet Services*, 545 U.S. 967 (2005).

¹⁴ See *In re Appropriate Framework for Broadband Access to the Internet Over Wireline Facilities*, FCC 05-150, 20 FCC Rcd 14853, 14862, REPORT AND ORDER AND NOTICE OF PROPOSED RULEMAKING (rel. September 23, 2005), *aff'd* *Time Warner Telecom, Inc. v. FCC*, 507 F.3d 205 (3rd Cir. 2007).

¹⁵ *In re Appropriate Regulatory Treatment for Broadband Access to the Internet Over Wireless Networks*, FCC 07-30, 22 FCC Rcd 5901, DECLARATORY RULING (rel. March 23, 2007).

¹⁶ *In re United Power Line Council's Petition for Declaratory Ruling Regarding the Classification of Broadband over Power Line Internet Access Service as an Information Service*, FCC 06-165, 21 FCC Rcd 13281, 13281, MEMORANDUM OPINION AND ORDER (November 7, 2006).

¹⁷ See, e.g., K. High, *Digital Pioneers Remember Past, Forecast Future of the Internet*, POLITICS365 (December 6, 2013) (available at: <http://politic365.com/2013/12/06/digital-pioneers-remember-past-forecast-future-of-the-internet/v>).

difficulty in drafting legally sustainable *Open Internet* rules. Last May, the FCC issued a new notice of proposed rulemaking to take another bite at the apple.¹⁸ Significantly, once again, the FCC did not propose to reclassify broadband as a Title II common carrier telecommunications service; rather, it found that it had sufficient legal authority under existing law to draft such rules and that reclassification was unnecessary. Is the FCC correct?

Three recent cases from the D.C. Circuit—*Comcast v. FCC*,¹⁹ *Cellco Partnership v. FCC*²⁰ and *Verizon v. FCC*²¹—shed light on the current state of the law.²² These cases hold that the FCC has ample authority over BSPs going forward under the current legal regime and, as such, reclassification of broadband Internet access as a Title II common carrier telecommunications service is unwarranted. In particular, these cases hold the following:

First, where applicable, Broadband Service Providers are still subject to direct jurisdiction under certain sections of Title II (telephone service), Title III (wireless service) and Title VI (cable service) of the Communications Act; hence, the FCC’s decision to classify broadband Internet access as a Title I information service does not *a fortiori* mean that the FCC has abdicated its oversight of Broadband Service Providers. To the contrary, to the extent BSPs continue to engage in activities which fall within the agency’s direct subject matter jurisdiction, the FCC’s ability to carry out its traditional core mandate (e.g., spectrum allocation, consumer protection, public safety, universal service, etc.) remains very much intact.²³

Second, the FCC’s ancillary jurisdiction over Broadband Service Providers remains alive and well, provided that the FCC ties the use of that jurisdiction to a specific delegation of authority under Title II, Title III, or Title VI. In this sense, nothing has changed as a matter of administrative law. So, while ancillary authority remains a potent and legally-sound tool in the FCC’s regulatory arsenal to remedy policy-relevant harms, especially on a case-by-case basis, the agency must provide its whys-and-wherefores to the court.

Third, with the D.C. Circuit’s ruling in *Verizon*, the FCC now has an *additional hook for ancillary authority* under Section 706 of the Communications Act²⁴ to

regulate Broadband Service Providers, subject to two important limitations: (1) like the FCC’s use of its traditional ancillary authority, in order to invoke Section 706, the FCC must tie its actions back to a specific delegation of authority in Title II, Title III, or Title IV; and (2) the FCC must also demonstrate that any use of Section 706 is designed to promote infrastructure investment and deployment on a reasonable and timely basis. As it turns out, these limitations can be meaningful. For example, because the FCC must tie its invocation of Section 706 to a specific delegation of authority, this requirement probably prevents the FCC from extending regulation to stand-alone edge providers who are not otherwise engaged in jurisdictional activities as some fear. Similarly, because the FCC must tie its use of Section 706 to a specific delegation of authority in the Communications Act, Section 706 probably does not expand the FCC’s authority to preempt state laws restricting municipal broadband deployment.²⁵

Finally, these cases make clear that although the FCC retains jurisdiction over Broadband Service Providers, the nature of the type of regulation it may impose has changed. Specifically, because the FCC classified broadband Internet access as a Title I information service, the FCC is prohibited by statute from imposing traditional Title II common carrier obligations on BSPs.²⁶ This means that the agency may not, among other things, regulate broadband Internet access using the traditional “unjust and unreasonable” or “undue discrimination” common carrier standards of Title II. However, these cases also hold that the FCC may regulate the conduct of BSPs under a “commercially reasonable” standard, which, the courts reasoned, permits individualized transactions and is thus sufficiently different from common carrier regulation to be lawful. Thus, in a way, the FCC’s regulatory authority over Broadband Service Providers may actually be *broader* than what it previously had under the traditional Title II common carrier regime. That said, the D.C. Circuit has

“The FCC 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.”

Section 706(b), in turn, requires the FCC to conduct a regular inquiry “concerning the availability of advanced telecommunications capability.” It further provides that should the FCC find that “advanced telecommunications capability is [not] being deployed to all Americans in a reasonable and timely fashion,” 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.” The statute defines “advanced telecommunications capability” to include “broadband telecommunications capability.”

²⁵ For a full explanation of this point, see, L. Spiwak, *The FCC Can’t Use Section 706 to Preempt State Laws Prohibiting Municipal Broadband*, @LAWANDECONOMICS (May 1, 2014) (available at: <http://phoenix-center.org/blog/archives/1901>).

²⁶ See 47 U.S.C. § 153(51) (“A telecommunications carrier shall be treated as a common carrier under this chapter only to the extent that it is engaged in providing telecommunications services. . .”)

¹⁸ *In the Matter of Protecting and Promoting the Open Internet*, FCC 14-61, __ FCC Rcd __, NOTICE OF PROPOSED RULEMAKING (rel. May 15, 2014).

¹⁹ *Comcast v. FCC*, 600 F.3d 642 (D.C. Cir. 2010).

²⁰ *Cellco Partnership v. Verizon*, 700 F.3d 534 (D.C. Cir. 2012).

²¹ *Verizon v. FCC*, 740 F.3d 623 (D.C. Cir. 2014).

²² For a detailed examination of these cases, see L.J. Spiwak, *What Are the Bounds of the FCC’s Authority Over Broadband Service Providers? A Review of the Recent Case Law*, PHOENIX CENTER POLICY BULLETIN No. 35 (June 2014) (available at: <http://www.phoenix-center.org/PolicyBulletin/PCPB35Final.pdf>).

²³ Given that national security and law enforcement issues are often governed by other statutes (e.g., CALEA) which have a “wholly distinct legislative history and Congressional purpose” from that of the Communications Act, see, e.g., *Time Warner Telecom v. FCC*, 507 F.3d 205, 119-220 (3rd Cir. 2007), any discussion about how the FCC’s decision to classify broadband Internet access as an information service impacts the FCC’s authority to comply with these type of statutes is beyond the scope of this piece.

²⁴ See 47 U.S.C. § 1302(a)-(b). Section 706(a) provides:

made it clear that any appellate court evaluation of any new “commercially reasonable” standard will be contingent on “how the common carrier reasonableness standard applies in . . . context, not *whether* the standard is actually the same as the common carrier standard.”²⁷

Title II is No Panacea. Despite the reality that current law gives the FCC ample oversight authority over Broadband Service Providers, there are many who argue that the FCC needs to reclassify broadband Internet service as a Title II common carrier telecommunications service. To justify such a heavy-handed regulatory intervention, one popular argument is that only reclassification will prevent Broadband Service Providers from creating “fast lanes.” While I hate to be the bearer of bad news, the cold fact of the matter is that “fast lanes” are perfectly legal under Title II.

As a common carrier, a Broadband Service Provider would be subject to rate regulation. A regulated rate is not a commercially set price; rather, it is a price set by the government to approximate competitive market conditions plus provide for a reasonable rate of return. Moreover, the FCC may not set this rate in an arbitrary manner. To the contrary, the standard set forth in the Communications Act requires that any rate must be both “just and reasonable”²⁸ and not “unduly discriminatory.”²⁹

Regarding the first prong of the test (“just and reasonable”), it is well established that a rate must fall into what is referred to as the “zone of reasonableness”—i.e., it cannot be “confiscatory” (below cost) on the bottom end and “excessive” on the high end.³⁰ As a result, while regulated rates cannot allow a monopoly return, at the same time a rate generally must have a “positive” price (i.e., it cannot be set at “zero”).³¹ Both the courts and the FCC itself have consistently recognized that ratemaking is “far from an exact science,”³² so this “zone of reasonableness” can be quite wide.

²⁷ *Verizon*, *supra* n. 21, 740 F.3d at 657.

²⁸ Section 201 of the Communications Act, 47 U.S.C. § 201(b) provides in relevant part that “All charges, practices, classifications, and regulations for and in connection with such communication service, shall be just and reasonable, and any such charge, practice, classification, or regulation that is unjust or unreasonable is declared to be unlawful. . . .”

²⁹ Section 202 of the Communications Act, 47 U.S.C. § 202(a), states:

“It shall be unlawful for any common carrier to make any unjust or unreasonable discrimination in charges, practices, classifications, regulations, facilities, or services for or in connection with like communication service, directly or indirectly, by any means or device, or to make or give any undue or unreasonable preference or advantage to any particular person, class of persons, or locality, or to subject any particular person, class of persons, or locality to any undue or unreasonable prejudice or disadvantage.”

³⁰ For a good primer on basic ratemaking, see G.S. Ford and L.J. Spiwak, *The Need for Better Analysis of High Capacity Services*, 28 JOHN MARSHALL JOURNAL OF COMPUTER AND INFORMATION LAW 343 (2011).

³¹ Indeed, one of the reasons the D.C. Circuit struck down the FCC’s last set of *Open Internet* rules is because the FCC forced Broadband Service Providers to charge a “zero” price to all comers for broadband Internet access. See *Verizon*, *supra* n. 21.

³² 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

Regarding the second prong of the test (i.e., that any rate must also not be “unduly discriminatory”), note that the operative word here is “*undue*”—i.e., reasonable discrimination in service offerings is perfectly acceptable. Thus, according to well-established case law, any claim that a carrier has unduly 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.³³ 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 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 is based solely on functional equivalence.³⁴ 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.³⁵ If a price difference is not justified, then the price difference is deemed unlawful. One usual measure to determine reasonableness is an inquiry as to whether the different rates are offered to “similarly situated” customers.³⁶ 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.³⁷ Since edge providers place different demands on last mile broadband networks, differences in rates are easily justified, and it would be difficult for the FCC, under Title II regulation, to block such rate differentials.

Conclusion. Trying to formulate enforceable *Open Internet* rules is no easy task. On the one hand, it is important to have an expert agency available as a “cop on the beat” that can act swiftly to protect consumers against potential anticompetitive conduct. At the same time, we need to make sure that these rules are not so draconian that this government intervention will stymie

(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 *Access Charge Reform*, FIFTH REPORT AND ORDER AND FURTHER NOTICE OF PROPOSED RULEMAKING, 14 FCC Rcd 14221 (1999) at ¶¶ 96, 144 (FCC justified its deregulatory triggers by noting that “regulation is not an exact science”).

³³ See, e.g., *MCI Telecommunications Corp. v. FCC*, 917 F.2d 30, 39 (D.C. Cir. 1990) and citations therein.

³⁴ *Id.*

³⁵ *Id.*

³⁶ 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)).

³⁷ For a deeper exploration of this topic, see, e.g., G.S. Ford and L.J. Spiwak, *Non-Discrimination or Just Non-Sense: A Law and Economics Review of the FCC’s New Net Neutrality Principle* PHOENIX CENTER POLICY PERSPECTIVE No. 10-03 (March 24, 2010) (available at: <http://www.phoenix-center.org/perspectives/Perspective10-03Final.pdf>).

innovation and retard further broadband deployment.³⁸ While I certainly have my policy differences with many

³⁸ For example, one significant risk of over-regulation would be the “commoditization” of broadband networks which would, in turn, lead to significant concentration, if not outright monopolization, of the industry. See T.R. Beard, G.S. Ford, T.M. Koutsky & L.J. Spiwak, *Network Neutrality and Industry Structure*, 29 HASTINGS COMMUNICATIONS & ENTERTAINMENT LAW JOURNAL 149 (2007); L.J. Spiwak, *Professor Susan Crawford and the Looming “Cable Monopoly,”* @LAWANDECONOMICS

of the FCC’s current proposed rules, I give kudos to the FCC for recognizing that it has ample authority under current law to issue these proposed rules without having to push the “nuclear” option of reclassification.

Hopefully, the FCC—working with stakeholders—will use this ample legal authority to craft a set of rules that, while perhaps not giving everyone what they want, will at least give them what they need.

(November 16, 2012) (available at: <http://phoenix-center.org/blog/archives/899>).