CENTER FOR BUSINESS & PUBLIC POLICY
GEORGETOWN UNIVERSITY McDonough SCHOOL of BUSINESS

April 10, 2015

Charlotte Savercool
Legislative Clerk
Committee on Energy and Commerce
2125 Rayburn House Office Building
Washington, D.C. 20515

Re: Questions for the Record, Subcommittee on Communications and Technology, Heading on "The Uncertain Future of the Internet," Feb. 25, 2015

Dear Ms. Savercool:

Attached are my responses to questions for the record from members of the Subcommittee.

It was an honor once again to appear before the Subcommittee, and I greatly appreciate the opportunity to supplement my testimony with answers to these questions.

Sincerely,

Larry Downes, Project Director
Evolution of Regulation and Innovation Project
Georgetown Center for Business and Public Policy
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Responses to Questions for the Record of

Larry Downes

Project Director, Georgetown Center for Business and Public Policy

The Evolution of Regulation and Innovation Project

U.S. House of Representatives

Committee on Energy and Commerce

Subcommittee on Communications and Technology

"The Uncertain Future of the Internet"

February 25, 2015

The Honorable Brett Guthrie

1. **Small, rural carriers are important to my district, so I would ask you to provide your further thoughts on how they in particular might be affected if Title II regulations are challenged in court. What are some of the effects of protracted litigation that you would expect to affect these small, rural carriers both indirectly and directly, especially given that many of them will not have the resources to spend a significant amount of time or money in court, even though we expect a legal challenge to be initiated by some of the larger carriers?**

It is virtually certain that the order will be challenged in court, and indeed, two lawsuits have already been filed prior to the publication of the order in the Federal Register.

Given the enormous complexity of the final order, its many controversial rulings and changes to existing FCC regulations, and the unusual manner in which the final document differed from the Notice of Proposed Rulemaking issued in May, 2014, we can expect not only multiple petitions to be filed but that the briefing, argument, and opinion-writing activities associated with these lawsuits will take as long, if not longer, than Verizon's challenge to the 2010 order. The case was not decided until early 2014.

It is also worth noting that because the holding in an important U.S. Supreme Court case, ***NCTA. v. Brand X Internet Services***,[1] is challenged if not overruled *sub silencio* by multiple sections of the FCC's Report and Order, this case also has the potential to be appealed to the Supreme Court. ***Brand X*** upheld the FCC's interpretation of the definition of "telecommunications services" in the 1996 Telecommunications Act, which was that it did not include broadband Internet Access services and that,

[1] *NCTA v. Brand X Internet Services*, 545 U.S. 967 (2005).

therefore, such services were not subject to Title II public utility regulation. If the Court agrees to review any of the petitions that will be filed in response to the FCC's "reclassification," that could easily add another year to the process.

All of this translates to considerable uncertainty for all participants in the broadband ecosystem, including rural carriers and small ISPs serving rural communities. And that problem is particularly acute to rural providers, in that, to the surprise of many, the FCC's order extended the full scope of its many new regulations and Open Internet rules to all Internet access providers large and small.

As I wrote in a recent article reviewing some of the strongest legal arguments that will likely be raised against the order:

> Though the FCC, for now at least, is still leaving out of the scope of the order private networks run by universities and limited Internet access provided by airlines, coffee shops and other public locations, the new rules will apply the public utility treatment to every one of thousands of small ISPs, including small mom-and-pop companies offering service using fixed wireless antennae and unlicensed spectrum.
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> But the agency's justification of potential anti-competitive behavior fits even worse here than it does with larger ISPs. Small ISPs have no market power with which to behave anti-competitively.
> Complying with the new rules—and answering complaints filed with the agency against them—will likely drive many out of business. Yet the FCC ignored pleas from the Small Business Administration and municipal broadband providers (in a separate order voted on the same day, ironically, the agency moved to free them from state restrictions–more litigation to follow) to leave them alone.
>
> A letter from 43 muni broadband operators predicted that "Title II regulation will undermine the business model that supports our network, raises our costs and hinders our ability to further deploy broadband." Denied.[2]

Even if rural providers do not participate directly in the litigation, or indirectly through their trade associations or by filing amicus briefs, I would expect many rural carriers will respond to the uncertainty of the protracted challenges by reducing future investments in new or expanded services or in new technologies that could improve the price and performance of their existing coverage.

Why? If the order is not significantly or even completely overturned, as noted, rural providers will be subject to a vast sweep of new rules and requirements, with which many will find it difficult if not

[2] Larry Downes, *On Net Neutrality, the Six Ways the FCC's Public Utility Order Will Lose in Court,* FORBES, April 8, 2015, *available at* http://www.forbes.com/sites/larrydownes/2015/04/08/on-net-neutrality-six-ways-the-fccs-public-utility-order-will-lose-in-court/.

impossibly expensive to comply. That's because, as you note, many smaller providers run on a very lean business model, focusing all of their budget and human resources on building and servicing equipment and on working closely with customers.

Few are likely to have full-time legal counsel or even much experience or need to work with outside counsel, and even then not the kind of specialized regulatory lawyers familiar with the ins and outs of Title II compliance on the one hand and FCC complaint processing and administrative adjudications on the other.

Thus a victory for the FCC could have devastating impact on the budgets if not the viability of smaller and more entrepreneurial providers servicing geographically sparse rural populations—an essential piece of the puzzle in improving both the availability and adoption of broadband technology in the U.S.

Given both the uncertainty and the potentially disastrous outcome, privately-owned rural providers will therefore be understandably hesitant starting now to make significant new investments in their businesses. Investors large and small who are aware of the litigation will likewise be less likely to invest in rural providers while the litigation is pending.[3]

And, if the FCC prevails, investment in rural providers is likely to become even more unattractive as the full impact of the evolving Title II regime becomes clearer. Given that the order agrees to forbear from some of the most onerous requirements of Title II only "for now" or "at this time," even after the litigation concludes the scope and cost of new regulatory oversight will still remain uncertain, perhaps indefinitely.

From start to finish, the FCC's decision to "reclassify" broadband and subject it to Title II will have a long-lasting chilling effect on rural providers until such time as the courts nullify the order or Congress legislates to rein in the agency.

2. You note that many of the commercial activities that the White House and their supporters at the FCC appear to be worried about, and that are ostensibly driving Title II regulation, are already subject to FTC anti-trust and anti-competition law, but that the FCC's enforcement power under Title II would preempt the FTC from taking further enforcement action. In addition, as a result of preemption the FCC would lack access to the FTC's "legal toolkit," as you term it.

[3] Even before the order was issued, at least one leading Wall Street analyst, Craig Moffett, had already downgraded the stocks of even the largest ISPs on the prospect of Title II regulation. See Georg Szalai, *Cord Cutting, Comcast Deal Risks Cause Cable Stock Downgrades*, THE HOLLYWOOD REPORTER, Feb. 17, 2015, *available at* http://www.hollywoodreporter.com/news/analyst-downgrades-cable-stocks-comcast-774297 ("On that Title II regulation, Moffett said he was 'far less sanguine' than investors seem to have been. 'At its core, Title II is about price regulation,' he said. 'It would be naive to believe that the imposition of a regime that is fundamentally about price regulation, in an industry that the FCC has now repeatedly declared to be non-competitive, wouldn't introduce risk to future pricing power.')

What do you expect the practical effect of this to be, especially in the context of forbearance—if the FCC forbears from only some provisions of Title II and not others, how might that affect the overlap of the two agencies' enforcement powers? Put another way, to what extent will the FTC be preempted from acting under Title II regulation if only some provisions of Title II apply in any given situation?

Section 5 of the Federal Trade Act categorically exempts from its authority any enterprise classified as a "common carrier." The FTC cannot enforce Congress's longstanding prohibition of "[u]nfair methods of competition in or affecting commerce, and unfair or deceptive acts or practices in or affecting commerce" against such entities.[4]

The extent (or not) of current or future forbearance has no bearing on the extent to which a Title II reclassification cuts off the jurisdiction of the Federal Trade Commission. If the FCC's effort to reclassify all broadband Internet access providers as common carriers subject to any part of Title II survives legal challenge and is left uncorrected by Congress, the FTC will be completely foreclosed from its continued enforcement of Section 5 and other important provisions of federal law, including consumer privacy protections.[5]

As FTC Commissioner Joshua Wright put it succinctly in his recent testimony before the House Committee on the Judiciary:

> Reclassifying broadband internet services as common carrier services under Title II will create further obstacles to protecting consumers and fostering competition by depriving the FTC of its long-standing jurisdiction in this area and threatening the robust consumer protection efforts that the agency has engaged in over the last two decades.[6]

This understanding of the common carrier classification is neither controversial nor partisan. FTC Commissioner Ohlhausen has said, for example, that "[i]f an entity is a common carrier providing common carrier services, we can't bring actions against them."[7] In recent testimony before the House Committee on the Judiciary, likewise, Commissioner McSweeny called for "repeal of the common carrier

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[4] *See* 15 U.S.C. 45(A) (2).

[5] Paul J. Feldman, *A First Look Inside the Net Neutrality Order*, CommLaw Blog, April 2, 2015, *available at* http://www.commlawblog.com/2015/04/articles/internet/a-first-look-inside-the-net-neutrality-order/ ("unless the courts overturn the FCC's reclassification of broadband access service, or Congress deletes the common carrier exemption, the FTC may be out of the business of enforcing privacy against broadband Internet access providers").

[6] Prepared statement of Commissioner Joshua D. Wright, Federal Trade Commission on *Wrecking the Internet to Save It? The FCC's Net Neutrality Rule*, before the United States House of Representatives, Committee on the Judiciary, March 25, 2015, *available at* https://www.ftc.gov/system/files/documents/public_statements/632771/150325wreckinginternet.pdf.

[7] See Brian Fung, *The FTC Doubles Down on its Net Neutrality Ambitions*, THE WASHINGTON POST, Sept. 29, 2014, *available at* http://www.washingtonpost.com/blogs/the-switch/wp/2014/09/29/the-ftc-doubles-down-on-its-net-neutrality-ambitions/.

exemption," which she acknowledged would otherwise "hinder the FTC from protecting consumers against unfair and deceptive common carrier activities."[8]

The practical effect of reclassification, to put it plainly, is that the FTC will no longer be empowered to police ISP practices it deems unfair or deceptive, a power many believe has been the real if implicit source of open Internet protections all along.

The FTC, as I noted in my testimony, has more experience and expertise in policing anti-competitive and anti-consumer practices, with a more flexible set of tools with which to correct market failures with a minimum of inefficient and potentially unintended negative consequences.

As Commissioner Wright said in his testimony, the FTC has until now been active in policing a number of ISP practices it considers unfair or deceptive within the context of its long history of adjudicating such complaints, utilizing a variety of regulatory and adjudicatory methods:

> The FTC has used its full range of law enforcement authority to protect consumers in the broadband sector, including obtaining injunctive relief and consumer redress where appropriate, and engaging in consumer and business education. The FTC has also pursued policy initiatives to address important consumer protection issues relating to broadband and Internet service, including requiring truthful, clear, and conspicuous disclosure of material terms of service, data security, and privacy.
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> Importantly, the FTC has certain enforcement tools at its disposal that are not available to the FCC. Unlike the FCC, the FTC can bring enforcement cases in federal district court and can obtain equitable remedies such as consumer redress. The FCC has only administrative proceedings at its disposal, and rather than obtain court-ordered consumer redress, the FCC can require only a "forfeiture" payment.
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> In addition, the FTC is not bound by a one-year statute of limitations as is the FCC. The FTC's ability to proceed in federal district court to obtain equitable remedies that fully redress consumers for the entirety of their injuries provides comprehensive consumer protection and can play an important role in deterring consumer protection violations.

[8] Prepared statement of Commissioner Terrell P. McSweeny, Federal Trade Commission on *Wrecking the Internet to Save It? The FCC's Net Neutrality Rule*, before the United States House of Representatives, Committee on the Judiciary, March 25, 2015, *available at* https://www.ftc.gov/system/files/documents/public_statements/632781/mcsweeny_-_prepared_statement_us_house_judiciary_committee_-_3-25-15.pdf. *See also* Brendan Sasso, *Net Neutrality Has Sparked an Interagency Squabble Over Internet Privacy*, THE NATIONAL JOURNAL, March 9, 2015, *available at* http://www.nationaljournal.com/tech/the-future-of-broadband/net-neutrality-has-sparked-an-interagency-squabble-over-internet-privacy-20150309.

The FTC has done some remarkable consumer protection work in the broadband sector and, since the advent of the Internet, the FTC has been the primary federal agency identifying problematic practices relating to deceptive advertising, privacy and data security, as well as enforcement actions designed to stop these practice sand to deter others from adopting similar practices that harm consumers.

Before reclassifying broadband services under Title II, and thereby outside the reach of the FTC, it is important to consider the ramifications of depriving broadband consumers of the FTC's specialized enforcement abilities as well as its accompanying decades of expertise.

A few recent enforcement efforts illuminate the types of protections consumers would lose with reclassification.

For example, the FTC recently filed an action against AT&T in federal district court, charging that AT&T failed to adequately disclose to its customers on unlimited data plans that, if they reach a certain amount of data use in a given billing cycle, AT&T reduces –or "throttles"–their data speeds to the point that many common mobile phone applications –like web browsing, GPS navigation and watching streaming video –become difficult or nearly impossible to use.

The FTC complaint further alleges that, even as unlimited plan consumers renewed their contracts, the company still failed to inform them of the throttling program. When customers canceled their contracts after being throttled, AT&T charged those customers early termination fees, which typically amount to hundreds of dollars.

The FTC also brought and settled a nearly identical case against Tracfone, the largest prepaid mobile-provider in the U.S. In that case, Tracfone agreed to pay $40 million to the FTC for consumer redress to settle charges that it deceived millions of consumers with its promises of "unlimited" data service.[9]

As Commissioner Wright noted in his testimony above, as a result of the FCC's categorical ban on blocking, throttling, and paid prioritization, the FTC will also be precluded from continuing its application of antitrust law based on standards and practices developed over the last century. As Commissioner Wright warns, the FCC's categorical bans will introduce "false positives"—that is, bans on practices that actually result in consumer benefit.[10]

[9] Prepared statement of Commissioner Joshua D. Wright, Federal Trade Commission on *Wrecking the Internet to Save It? The FCC's Net Neutrality Rule*, before the United States House of Representatives, Committee on the Judiciary, March 25, 2015, *available at* https://www.ftc.gov/system/files/documents/public_statements/632771/150325wreckinginternet.pdf.

[10] *Id.*

It is ironic that in urging the Title II approach, the FCC not only introduced considerable legal uncertainty but effectively cut off the authority of the agency best suited to ensure continued protection of the open Internet, as it had been doing all along. The practices that inspired reclassification were already subject to enforcement by the FTC, and the FTC had been doing an efficient and effective job, if only too modestly to be recognized as such by the FCC and the White House[11].

The Honorable Gus Bilirakis

1. **Mr. Downes, as an advisor to start-ups and new entries in this space, can you explain how the agility of the market could change under Title II?**

   What will small or budding internet based businesses have to worry about or comply with next week under Title II that you don't have to today?

As I noted in my recent article analyzing the legal case against the Title II order, its scope is breathtaking, encompassing not just large facilities-based ISPs but potentially every participant in the Internet ecosystem, including small ISPs, municipal broadband providers, equipment providers, content delivery networks, backbone providers, transit providers, and even Internet content and other service providers.[12]

The reach of this radical transformation of U.S. communications law, done entirely without Congress's input, has the potential to remake every relationship in the ecosystem today.

The FCC, to use Chairman Wheeler's own words, has appointed itself the "referee on the field" for the Internet.[13] But even with the best of intentions, it should be obvious that a slow-moving federal agency, applying rules and procedures leftover from the beginning of the Industrial Revolution, will at the very least slow down the pace of innovation for this remarkable engine of disruption, vastly reducing its agility—the source to date of unquestioned U.S. competitive advantage in the information revolution.

A few examples of how this new regime will interfere with what has long been the bastion of "permissionless innovation" should make clear just how intrusive the FCC's "refereeing" will be:

> **Revised definition of PSTN now includes every service that utilizes an IP address** - Since the Communications Act explicitly prohibited the FCC from applying Title II to mobile broadband services, the order cynically gets around that hard stop by "redefining" the Public Switched Telephone Network, which is subject to Title II, to include a second network—the Internet. As a

[11] The FCC's Title II Report and Order makes no reference to the FTC's common carrier exemption and the impact of "reclassification" on on-going efforts at its sister agency, for example.

[12] *See* Larry Downes, *On Net Neutrality, the Six Ways the FCC's Public Utility Order Will Lose in Court,* FORBES, April 8, 2015, *available at* http://www.forbes.com/sites/larrydownes/2015/04/08/on-net-neutrality-six-ways-the-fccs-public-utility-order-will-lose-in-court/.

[13] Statement of Chairman Tom Wheeler, *Protecting and Promoting the Open Internet*, GN Docket No. 14-28, REPORT AND ORDER ON REMAND, DECLARATORY RULING, AND ORDER, FCC 15-24, March 12, 2015.

result of this audacious maneuver, any "service" that "uses" IP addresses is now subject to Title II. Every component from one end of the Internet to another has now been transformed into a telephone service, subject to any or all of the old rules at the whim of the FCC.

General Conduct rule - One of many sweeping changes not mentioned in the initial Notice of Proposed Rulemaking was the introduction of a "flexible" general conduct rule, which states:

> Any person engaged in the provision of broadband Internet access service, insofar as such person is so engaged, shall not unreasonably interfere with or unreasonably disadvantage (i) end users' ability to select, access, and use broadband Internet access service or the lawful Internet content, applications, services, or devices of their choice, or (ii) edge providers' ability to make lawful content, applications, services, or devices available to end users. Reasonable network management shall not be considered a violation of this rule.

The meaning of this vague new conduct standard will be developed through adjudication, based on complaints filed by any party who believes themselves to be a victim of unreasonable interference or disadvantage. To aid its enforcement bureau, however, the Report and Order provides multiple factors to consider in evaluating complaints. But these factors clarify nothing—instead, they add to the uncertainty.

Even the Electronic Frontier Foundation, which strongly encouraged the FCC to pursue the Title II path, was deeply disturbed by the ambiguity and uncertainty this new rule would introduce:

> Unfortunately…the general conduct rule will be anything but clear. The FCC will evaluate "harm" based on consideration of seven factors: impact on competition; impact on innovation; impact on free expression; impact on broadband deployment and investments; whether the actions in question are specific to some applications and not others; whether they comply with industry best standards and practices; and whether they take place without the awareness of the end-user, the Internet subscriber.
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> There are several problems with this approach. First, it suggests that the FCC believes it has broad authority to pursue any number of practices—hardly the narrow, light-touch approach we need to protect the open Internet. Second, we worry that this rule will be extremely expensive in practice, because anyone wanting to bring a complaint will be hard-pressed to predict whether they will succeed. For example, how will the Commission determine "industry best standards and practices"? As a practical matter, it is likely that only companies that can afford years of litigation to answer these questions will be able to rely on the rule at all. Third, a multi-factor test gives the FCC an awful lot of discretion, potentially giving an unfair advantage to parties with insider influence.[14]

[14] Electronic Frontier Foundation, *Dear FCC: Rethink the Vague 'General Conduct' Rule*, Feb. 24, 2015, *available at* https://www.eff.org/deeplinks/2015/02/dear-fcc-rethink-those-vague-general-conduct-rules.

Interconnection - Despite the fact that Chairman Wheeler had repeatedly insisted the order would have nothing to do with the backend ("peering is not a net neutrality issue") the order includes new regulation for every node in the Internet's architecture. As the order notes at Paragraph 29:

> As discussed below, we find that broadband Internet access service is a "telecommunications service" and subject to sections 201, 202, and 208 (along with key enforcement provisions). As a result, commercial arrangements for the exchange of traffic with a broadband Internet access provider are within the scope of Title II, and the Commission will be available to hear disputes raised under sections 201 and 202 on a case-by-case basis: an appropriate vehicle for enforcement where disputes are primarily over commercial terms and that involve some very large corporations, including companies like transit providers and Content Delivery Networks (CDNs), that act on behalf of smaller edge providers.

Yet when it comes to interconnection, peering, and other backend traffic management in particular, the order acknowledges that the agency has no experience or expertise "refereeing" the thousands of private agreements that networks make with each other to exchange traffic. That is no surprise—as I noted in my testimony, according to the OECD, over 99% of such agreements are so straightforward they aren't even reduced to writing.[15]

To overcome its lack of experience, the agency simply announces it will work out the details of its newly self-granted powers over time, as complaints come in. One can imagine in the future that any time traffic exchange negotiations between two parties—a CDN and an ISP, or a dominant edge provider and an ISP—become stuck or break down, one of the parties will simply file a complaint with the FCC, or threaten to do so, rather than continue negotiating.

"The best approach," the FCC says, "is to watch, learn, and act as required, but not intervene now, especially not with prescriptive rules." That's a process "that is sure to bring greater understanding to the Commission." But that "greater understanding" will come at a profound price to the Internet ecosystem, leaving every provider of Internet services unsure as to whether or not its commercial arrangements old and new with other providers does or does not satisfy the FCC's evolving understanding of "just and reasonable" practices.

Advisory Opinions - If a service provider is uncertain whether or not a new service will satisfy the FCC's evolving standards, the FCC notes at Paragraph 36, they may apply for an advisory opinion or seek guidance from a newly-created open Internet ombudsperson. But the order "declines to establish any firm deadlines to rule on them or issue response letters." The

[15] Rudolf Van Der Berg, *Internet Exchange Traffic: Two Billion Users and it's Done on a Handshake*, OECD, Oct. 22, 2012, *available at* http://oecdinsights.org/2012/10/22/internet-traffic-exchange-2-billion-users-and-its-done-on-a-handshake/

advisory opinions, moreover, are simply that—advisory. They are not binding on the enforcement of any future complaint, and may be withdrawn at any time.

Again, these are just some of the new delays, expenses, and uncertainties that will be introduced into what has been until now a model for efficient entrepreneurship. It is not clear to whom the new rules apply or how they will be enforced. The FCC makes no promises about the speed with which its already over-burdened enforcement staff will process complaints, and leaves open to any aggrieved party—including disappointed business partners, consumers, and class action lawyers—the opportunity to bring a complaint to enforce any of the rules.

Given the heavy reliance on forbearance, entities with no previous experience operating under Title II or any other public utility law will suffer a steep learning curve and an expensive legal bill, with specialized counsel being required. And the agency's frequent reminder that multiple provisions of Title II and 700 existing Title II rules are being forbeared from only "at this time" or "for now" leaves open the very real possibility that the agency will, at any point in the future, change its mind about its cynically-described "light touch" approach to "modernizing" public utility law.

In short, new start-ups will have to worry about all of this, and more—they will have to worry about every aspect of Title II that is currently not being applied but which could be, and which could extend to any enterprise offering a "service" that utilizes IP addresses—in short, to any participant in the Internet ecosystem.

They won't know what new rules or practices they will have to comply with until the agency decides through its complaint what behaviors are and are not acceptable and by whom. Even then, the general conduct rule is there to adapt to changing conditions, rendering the possibility that practices adjudicated as acceptable today will not be tomorrow.

And the possibility of shifting policy goals leading to changing forbearance decisions leaves open the possibility that everything will change, at any time, based only on the FCC's unstated view of changing conditions—a view that is not supported, as in the Report and Order, by any form of cost-benefit analysis.

And all of this on the FCC's timetable, subject to limited budget, intentionally slow-moving administrative processes, and the availability of multiple levels of appeal.

In effect, the order has for no particular reason changed the speed limit on the Internet from 55 to 5, but has yet to hire highway patrol officers to police its arbitrary new rule or establish how, when or where they will be enforced.

That leaves start-ups—who are by definition companies that are bent on breaking the existing rules of business—with little choice but to continue driving at the same speed, now looking over their shoulder

at every moment for the more-or-less random chance of being caught and possibly having their licensed permanently revoked.