NEW "UNBUNDLING" RULES: WILL THE FCC FINALLY OPEN UP CABLE BROADBAND?

This iBrief discusses a recent Court of Appeals decision remanding FCC rules on the "unbundling" of Internet services by telephone exchange carriers. These rules ordered many Internet service providers to share their equipment with competitors, so that consumers could choose their providers instead of having to accept all services from the company who installed the physical Internet connection. Cable Internet providers are not included in these rules. This iBrief predicts that cable broadband operators will soon be governed by the same "unbundling" provisions as other ISPs.

The Federal Communications Commission ("FCC") has been sent back to the drawing board to rewrite its open access rules for the companies whose wires, loops and switches carry the Internet across the country and into the homes and offices of America. What the Commission decides will have major implications for the future of the Internet. The FCC rules, which granted new competitors access to incumbent companies' equipment, were supposed to increase competition and prevent telephone monopolies from becoming Internet monopolies. But the FCC ignored more than half the problem, disregarding the competitive impact of cable companies who provide Internet service. The D.C. Circuit Court finally took note of the glaring disparity and ordered the FCC to reconsider.[1]

Hometown, USA v. FCC

Municipalities around the country have been trying to make one of the FCC's orders make sense by requiring cable carriers (who also provide Internet service) to share their hardware with competitive Internet Service Providers ("ISPs").[2] Local telephone exchange carriers already have to share their equipment with incoming local exchange carriers who want to provide Internet service.[3] But courts are not drawing this analogy; instead, they keep striking down requirements that would force cable providers to share hardware.[4]

At least two Circuit Courts have denied municipalities the ability to provide a level playing field for all incoming competitors seeking to provide Internet services.[5] Incumbent local telephone exchange carriers ("ILECs") – those companies who own the equipment over which

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[1] *See* United States Telecom Ass'n v. FCC, 290 F.3d 415 (D.C. Cir. 2002).
[2] *See*, *e.g.,* MediaOne Group Inc. v. County of Henrico, 257 F.3d 356 (4th Cir. 2001); AT&T Corp. v. City of Portland, 216 F.3d 871 (9th Cir. 2000).
[3] Telecommunications Act of 1996, 47 U.S.C. § 251(c)(3)(2002).
[4] *See MediaOne*, 257 F.3d at 365; *Portland*, 216 F.3d at 880.

telecommunications service travels – are required to share their equipment with competitors (Competitive Local Telephone Exchange Carriers, or "CLECs") seeking to provide Internet services to consumers.[6] In contrast, cable companies providing Internet service along with cable services over their broadband systems are exempt from this rule.[7] Henrico County, Virginia tried to condition one company's transfer of a cable franchise to AT&T, after a merger, on that company providing "open access" to competitors.[8] In *MediaOne Group Inc. v. County of Henrico*, the cable company offered a "bundled" service to customers, which combined its cable service with Internet services over its cable modem platform.[9] Customers who wanted cable television had to take both services together, meaning those customers who wanted a different Internet service provider would have a strong disincentive to acquire that redundant service.[10] Henrico County's "open access" condition required MediaOne to open its broadband pipeline to unaffiliated ISPs at the same rates, terms and conditions as it provides to itself and its affiliates.[11] The district court held that the County violated the Communications Act because it required MediaOne to provide telecommunications facilities as a condition of transfer, a condition that "cable operators" escape under the Telecommunications Act of 1996.[12] Various telephone companies joined Henrico County in the suit, since those companies providing DSL services, regulated as telecommunications services, were required to share their equipment with competitors.[13] These companies chafed at the regulatory disparity created by the imbalance in the rules.[14]

The City of Portland attempted to enforce a similar franchise transfer condition on AT&T's "@home" service, after AT&T's merger with TCI Cable.[15] Portland-area ILECs called for open access to TCI's cable broadband network to create a "level playing field" with the ILECs.[16] The court in *Portland* recognized that the parties wanted them to consider what national policy on open access to the Internet was appropriate, but they flatly declined.[17] The court showed deference to the FCC and determined that @home was outside the scope of the FCC

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[5] *E.g., MediaOne*, 257 F.3d at 365; *Portland*, 216 F.3d at 871.
[6] 47 U.S.C. § 251(c)(3).
[7] Portland, 216 F.3d at 879.
[8] *MediaOne*, 257 F.3d at 360.
[9] *Id*. at 359-60.
[10] *Id*. at 360.
[11] *Id*.
[12] *Id*. at 361.
[13] *Id*. at 364.
[14] *MediaOne,* 257 F.3d at 364.
[15] *Portland*, 216 F.3d at 875.
[16] *Id*.

because it was a cable operator providing an information service and a cable telecommunications service (distinctions discussed infra).[18] These classifications meant Portland was prohibited from regulating cable broadband Internet access.[19] The result was that Henrico County, Virginia and Portland, Oregon failed in their efforts to increase competition and decrease monopolization of Internet service in their region.

Defining Cable Broadband Internet Service

A major foundation of both of these decisions is the classification placed around these companies.[20] Both courts decided the plaintiff was, at least in part, a cable service providing telecommunications services, and therefore fell outside the bounds of the Telecommunications Act.[21] This classification removes them from the requirements of the Act, because the Act specifically states, "if a cable operator or affiliate thereof is engaged in the provision of telecommunications service … the provisions of this title shall not apply to such cable operator or affiliate for the provision of telecommunications services."[22] The Act defines "telecommunications" as the "transmission, between or among points specified by the user, of information of the user's choosing, without change in the form or content of the information as sent and received."[23] This definition is not sufficiently keyed to the reality of the Internet. Consumers search or surf the Internet and interact with information, which surprises them at every turn. The familiar experience of being bombarded with pop-up ads while traversing a website is just one example of how the Internet is often not "transmission … of information of the user's choosing." Also, Internet users do not tend to specify the points to and from which information is being transmitted. Communicating on the Internet is not like placing a phone call, where the caller enters a number of his or her choosing and, thereby, specifies the points between which information is transmitted. It is often more like casting a wide net, into uncharted seas, with no idea where the catch will come from.

The problem lies in determining what cable operators are providing if it cannot be classified as a telecommunications service. The FCC has invited "comments on alternative approaches to classifying cable modem service and the cable modem platform under the

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[17] *Id*. at 876.
[18] *Id*. at 878.
[19] *Id*. at 880.
[20] *See generally MediaOne*, 257 F.3d at 365; *Portland*, 216 F.3d at 880.
[21] *See generally MediaOne*, 257 F.3d at 365; *Portland*, 216 F.3d at 880.
[22] 47 U.S.C. § 541(b)(3)(A)(ii).
[23] 47 U.S.C. § 153(43).

Communications Act" to answer this very question.[24] Courts have rejected, and rightly so, the suggestion that cable operators are providing a cable service.[25] The Act defines "cable services" as "(A) the one-way transmission to subscribers of (i) video programming, or (ii) other programming service, and (B) subscriber interaction, if any, which is required for the selection or use of such video programming or other programming service."[26] The Ninth Circuit described the "essence of cable service [as the] … one-way transmission of programming to subscribers generally."[27] Clearly, this does not describe the Internet, which users transform through their input, and which is a two-way medium, as any frequenter of 'chat rooms' could attest.

Cable operators may be providing "Internet access service," formerly called "information services," defined as "a service that enables users to access content, information, electronic mail, or other services offered over the Internet, and may also include access to proprietary content, information and other services as part of a package of services offered to consumers."[28] However, the term does not include user input into that definition, a key part of the Internet for many who create their own web pages and even operate businesses over those web pages. "Information services" are not, and have never been, subject to regulation under the Act, so that classification would do little to help the FCC resolve the access quandary.[29] A new classification could settle the issue, but whatever the means, the FCC has been ordered to reconsider their access rules.

An Order for New Rules

The D.C. Circuit Court of Appeals finally noted and challenged the disparity between those who are and those who are not regulated in this area.[30] The court sent the FCC back to the drawing board on two of its orders – the Local Competition Order and the Line Sharing Order.[31] Incumbent local carriers sought review of the two rules, the second of which related to cable broadband operators.[32] The court pointed out that the second rule, the 'Line Sharing Order,' ignored the market force of cable broadband operators.[33] The rule required that these ILECs

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[24] *See* Inquiry Concerning High-Speed Access to the Internet Over Cable and Other Facilities, 65 Fed. Reg. 60, 441 (2000).
[25] *E.g., Portland*, 216 F.3d at 876.
[26] 47 U.S.C. § 522(6).
[27] *Portland*, 216 F.3d at 876.
[28] 47 U.S.C. § 231(e)(4).
[29] *Portland*, 216 F.3d at 878.
[30] *United States Telecom*, 290 F.3d at 415.
[31] *Id*. at 42.
[32] *Id*. at 4.
[33] *Id*. at 37-8.

"unbundle" the high frequency portion of copper loops, which transmit information ranging from analog telephone service to DSL, to allow new local carriers to provide telephone service and DSL access at the same time.[34] ILECs also had to remove voice-band enhancing equipment on the loops, which tends to interfere with DSL service.[35]

The major flaw the court found in this rule was that by requiring ILECs to share loops with CLECs, the FCC had "completely failed to consider the relevance of competition in broadband services coming from cable."[36] The FCC itself had confirmed the dominance of cable in the Internet market.[37] Cable companies have 54% of existing high-speed lines, almost double the 28% held by DSL.[38] With access comes popularity, since broadband allows users to access the Internet at speeds 50 to several hundred times faster than through conventional modems.[39] It is an unfortunate oversight, considering the FCC expected its unbundling plan to lead to "rapid introduction of competition in all markets" and promote "facilities-based competition, investment, and innovation."[40]

Real competition and growth in this industry requires making the cable companies, which provide bundled Internet and cable access, a part of the regulated class. The court noted that mandatory unbundling comes at a high cost, including "disincentives to research and development by both ILECs and CLECs and the tangled management inherent in shared use of a common resource," which are particularly large burdens, if the purported goals are not being achieved.[41] The court remanded the rule to the FCC, because the non-inclusion of cable meant there was no reason to think its unbundling requirement would bring on a significant enhancement of competition.[42] Therefore, it seems these communications requirements cannot survive without the inclusion of cable broadband operators.

The court likened the FCC's misstep in this area to their error regarding the Local Competition Order, which required ILECs to unbundle network elements and provide them to CLECs.[43] Although their own rules require unbundling only if "lack of access to that element materially diminishes a requesting carrier's ability to provide the services it seeks to offer," the

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[34] *Id*. at 14.
[35] *U.S. Telecom*, 290 F.3d at 16.
[36] *Id*. at 37.
[37] *Id.* at 38.
[38] *Id*.
[39] *See Portland*, 216 F.3d at 873.
[40] Local Competition Order, 47 C.F.R. § 51.317(b)(3)(ii)(2002).
[41] *U.S. Telecom*, 290 F.3d at 40.
[42] *Id*. at 41-2.
[43] *Id*. at 41.

FCC ordered this unbundling across the board, in every "geographic or customer market."[44] The court questioned the FCC's decision to disregard the state of competition in any particular market.[45] The court pointed out that subsidization by state regulatory commissions in the name of universal service means rural and/or residential subscribers are usually undercharged while urban and business markets are overcharged.[46] Common sense tells us that incoming competition will not go to markets where customers are charged below cost.[47] So it is no surprise that CLECs have invested heavily in the overcharging markets.[48] The result is a situation in which the rules do little to further the goals they are meant to achieve. Once it noted this, the D.C. Circuit was consistent in its message for the FCC – rewrite your rules to fit their purpose.

The Struggle Continues

The court noted the "extraordinary complexity of the Commission's task" but provided the FCC with no further guidance.[49] The task is complicated by the ambiguity of the Telecommunications Act. The Supreme Court has said it is "a gross understatement to say that the 1996 Act is not a model of clarity."[50] In fact, the FCC was already forced to rewrite the unbundling access rules; the Supreme Court decided the Commission had exceeded the scope of the Act by giving competitors "blanket access" to unbundled network elements without compelling those competitors to prove the level of need required in the Act.[51] The Court stated that the FCC's low bar created a situation where it was "hard to imagine when the incumbent's failure to give access to the element would not constitute an impairment."[52] As a result of that ruling, the FCC revised its standards for unbundling and created the 'Local Competition Order' and the 'Line Sharing Order.'[53] Now both have been remanded to the Commission for review.[54]

All of this toil would have been unnecessary had a bill introduced in the House of Representatives passed. The "Internet Freedom Act" (IFA) stated that "broadband access transport providers" had to give fair, "anticompetitive" contracts to ISPs, who want to use the

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[44] *Id*. at 9.
[45] *Id*. at 19.
[46] *Id*. at 17-8.
[47] *See id*. at 18.
[48] *Id*. at 18.
[49] *Id*. at 17.
[50] AT&T Corp. v. Iowa Utilities Board, 525 U.S. 366, 397 (1999).
[51] *Id*. at 388-9.
[52] *Id*. at 389.
[53] *U.S. Telecom*, 290 F.3d at 7-8, 14.
[54] *Id*. at 42.

pre-existing broadband hardware for their service.[55] The IFA would provide unaffiliated service providers the same deal cable broadband operators give themselves and their affiliates.[56] A violation of the IFA would be considered a breach of the antitrust prohibitions in the Sherman Act.[57] However, the last committee hearing on the bill took place in July 2000, so it looks doubtful that Congress will resolve this issue and take the pressure off of the FCC.

Conclusion

It is time for the FCC to get the rules right. Cable broadband operators providing Internet service have been free riders in this arena for too long. The inevitable result of the FCC's Line Sharing Order would be that cable broadband operators are ushered into the 'favorite son' position, with regards to providing Internet service, while non-cable exchange carriers are forced to offer their hardware to competitors at cheap rates. Such favoritism works against the stated goals of the Telecommunications Act of 1996, which are "promot[ing] competition and … encourag[ing] the rapid deployment of new telecommunications technologies."[58] If cable broadband operators are allowed to automatically include Internet service into their cable offering without giving competitors the opportunity to lease their facilities, alternatives to an Internet provided by the major cable operators will cease to exist. Competition would be nil. Also, a company, or oligarchy of companies, dominating a market in this way has no incentive to develop new technology, when their customers are bound to use their systems regardless of the quality.

After the D.C. Circuit Court of Appeal's recent decision, the FCC will likely finally include cable broadband operators into the fold of these "open access" requirements. It is where they belonged all along.

But you don't have to tell Henrico County and Portland – they already knew that.

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[55] *See* Internet Freedom Act, H.R. 1686, 106th Cong. § 1 (1999).
[56] *Id*.
[57] *Id*.
[58] Telecommunications Act of 1996, Preamble, Pub. L. No. 104-104, 110 Stat. 56, 56 (1996).