

Firm Advisory

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FCC Issues Tariff Investigation Order and FNPRM to Reform Regulation of Business Data Services (f/k/a Special Access Services)

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On May 2, 2016, the Federal Communications Commission (“FCC”) released an Order and Further Notice of Proposed Rulemaking (“FNPRM”) that (a) resolve a 2015 investigation into the terms and conditions of tariffed pricing plans of certain large ILECs associated with special access services, which the FCC now refers to as Business Data Services (“BDS”), and (b) seek comment on a proposal to replace the existing fragmented BDS regulatory regime with a new technology-neutral regulatory framework. The FCC’s stated primary objectives in adopting the Order and FNPRM are to promote competition in the BDS marketplace and help the technological revolutions underway as the telecommunications industry transitions from TDM copper networks to all-IP multi-media networks. The Order and FNPRM are summarized in turn below.

I. Tariff Investigation Order

The Order is the result of an FCC-initiated investigation into a wide range of terms and conditions in 18 BDS tariff pricing plans offered by AT&T, CenturyLink, Frontier and Verizon, which all are subject to the FCC’s price cap regulations. The Order finds that certain terms and conditions are unreasonable practices under section 201(b) of the Act, and directs the relevant ILECs to remove these provisions from their BDS tariffs.

Specifically, the Order concludes that the following three types of contractual provisions have the effect of decreasing facilities-based competition and the transition to newer technologies, and therefore constitute unjust and unreasonable practices:

- All-or-nothing provisions that require customers to commit all their relevant in-service purchases to a single pricing plan are anti-competitive because they unreasonably restrict purchase options and have not otherwise been justified by reasonable business concerns. The FCC found that the all-or-nothing provisions in certain AT&T, CenturyLink, Frontier, and Verizon tariffs unreasonably restrict purchase options and have not otherwise been justified by reasonable business concerns. The FCC declined, however, to apply corrective action to existing agreements under these plans. Rather, it keeps the investigation open with regard to this issue and seek a further comment on how its finding that these provisions are unlawful should be applied to existing agreements without disrupting the market for these services unnecessarily.

- Shortfall penalties that impose penalties greater than the amount a purchaser would have paid had it met its minimum commitment level for the service. The FCC held that certain AT&T (i.e., Southwestern Bell and Pacific Bell), Frontier, and Verizon BDS tariffs contained shortfall provisions in excess of a reasonable measure of damages and were therefore unjust and unreasonable.
- Early termination fees (“ETFs”) that assess a fee that exceeds the opportunity cost an ILEC would incur as a result of an early termination. The FCC found that certain AT&T (i.e., Pacific Bell and Southwestern Bell) and Frontier tariffs contained such unreasonable ETFs.

The FCC directs the applicable ILECs to remove such unjust and unreasonable provisions from their tariffs and submit revised tariffs within 60 days from the release date of the Order. As to shortfall provisions, Southwestern Bell, Pacific Bell, Frontier and Verizon may elect to include in their revised tariffs shortfall penalties or fees that are no greater than the amount of revenue that a customer would have paid had the minimum commitment been met, which would be applicable to both existing and future customers. With respect to ETFs, AT&T and Frontier may elect to file tariff revisions with early termination fee provisions that result in fees that are not in excess of the ILEC’s expectation damages, with such revisions also applying to both existing and future customers.

II. Further Notice of Proposed Rulemaking

In the FNPRM, the FCC provides analysis of “dedicated service” data collected in 2015, and seeks public comment on the FCC’s proposal for a new BDS regulatory regime. The goal of the FCC’s new regulatory framework is the large scale de-regulation of BDS products and markets where competition exists, and new tailored rules designed to protect commercial customers and the consumers who rely on them where competition does not exist.

The FCC’s new regulatory framework is based on four guiding principles:

- (1) Competition is best, and where competition exists there should be little government intervention;
- (2) Any new regulatory framework should be technology-neutral;
- (3) Barriers inhibiting the transition from TDM to IP-based services should be removed, and
- (4) New regulations should meet the needs of both today’s and tomorrow’s marketplaces.

Based on these four guideposts, the FCC proposes and seeks comment on the regulatory changes summarized below.

A. New Technology-Neutral Regulatory Framework for Business Data Services. The FCC recognizes that the BDS market has changed substantially, both in terms of technology and providers, and proposes replacing the existing, fragmented regulatory BDS structure with a new technology-neutral framework that classifies markets as either competitive—in which all providers are subject to minimal oversight—or as non-competitive—in which providers are subject to a new set of tailored rules. By establishing a new technology-neutral regime, the FCC hopes to facilitate the continued evolution of robust competition that will result in ever-improving services for American businesses and consumers.

B. Statutory Authority. The FCC proposes that sections 201 and 202 of the Act serve as an adequate basis of statutory authority for actions that the FCC would take to create and implement its proposed technology-neutral framework for BDS services. Some key issues the FCC seeks comment on are whether the FCC has the statutory authority under sections 201 and 202 of the Act to:

- Place certain limits on terms and conditions of BDS to ensure they are offered on just, reasonable and not unreasonably discriminatory terms, especially in non-competitive markets.
- Require price cap filings for TDM services and benchmarked prices for non-TDM services.
- Use benchmarked prices to ensure that non-TDM services in non-competitive markets are offered on just and reasonable prices.
- Adopt new triggers for determining whether markets are competitive or non-competitive.

The FNPRM also asks whether forbearance from tariffing provisions for ILEC TDM services in competitive markets would prevent the FCC from requiring price cap filings for ILEC TDM services in non-competitive markets based solely on the statutory authority in section 201(b). In addition, the FNPRM seeks comment on whether any transitional or incremental policy actions should be adopted while the FCC considers and moves to comprehensively reform the BDS regulatory framework.

C. Competitive Market Test. Under the new framework, the FNPRM proposes identifying markets where de-regulation is possible based on a Competitive Market Test, which will determine the markets where the current and potential competition is bringing material competitive effects to customers. The Competitive Market Test focuses on multiple factors, such as bandwidth, customer classes, business density, and the number of providers in a designated geographic area. The FCC seeks comments on a number of issues relating to the proposed test, including:

- The criteria for the Competitive Market Test and the appropriate weight to assign to the various factors in applying the test.
- How to ensure the accuracy of data and how often the FCC should reapply the test.
- The extent to which and how the FCC should give providers and purchasers an opportunity to challenge determinations rendered by the test.
- Whether the FCC should apply the Competitive Market Test based on different BDS customer classes at varying bandwidths to capture different levels of demand and competition, and if so, how the FCC should separate the product market by customer type and bandwidth.
- Whether census blocks should be used as the geographic area for applying the Competitive Market Test.

D. Definition of Business Data Services. The FNPRM proposes and seeks comment on the following definition of BDS:

A telecommunications service that transports data between two or more designated points at a rate of at least 1.5 Mbps in both directions (upstream/downstream) with prescribed performance requirements that typically include bandwidth, reliability, latency, jitter, and/or packet loss. BDS would not include “best effort” services, e.g., mass market BIAS such as DSL and cable modem broadband access.

E. New Regulations for All Markets. The FNPRM proposes and seeks comment on several new regulations that would apply to BDS providers in competitive and non-competitive markets.

- *Non-Disclosure Agreements (NDAs)*. The FCC found that some NDAs could prohibit CLECs from providing information to the FCC and inhibit the FCC’s oversight of the BDS market going forward. For this reason, the FCC proposes and seeks comment on a rule prohibiting the use of NDAs that restrict providers’ and purchasers’ ability to disclose information to the FCC.
- *Scope of terms and conditions requirements adopted in the Order*. The FNPRM seeks comment on whether the three requirements adopted in the accompanying Order should be applied to other tariff pricing plans that were not subject to the tariff investigation and to commercial agreements for IP-based BDS. The FCC also seeks comment on other issues, including whether the Order’s requirements should be applied in noncompetitive markets or, more generally, in all markets.

F. Rules for Non-Competitive Markets. Under the proposed regulatory framework, after the Competitive Market Test is applied, the BDS markets designated as non-competitive would be subject to new regulatory requirements. Some fundamental issues the FCC seeks comment on include:

- The scope of regulation in a non-competitive market, and whether the rules should apply to all or some providers and, if some, which ones and on what basis (such as market power).
- Whether the new regulations should only apply to the largest BDS provider in the non-competitive market as measured by network coverage, locations served, revenues or some other metric or metric combination.

The rules proposed for non-competitive markets are intended to constrain potentially anti-competitive conduct while also providing the flexibility to allow all providers to respond to competition. The types of requirements the FCC is considering include price-cap regulations, anchor or benchmark pricing, wholesale pricing, and restrictions on terms and conditions. The FNPRM seeks detailed input and comment on all of these proposed regulations, including, among others:

- *Price cap regulation*. The continued use of price caps on BDS that are now subject to price cap regulation in non-competitive markets, the structure of the price-cap system, other potential cap components, baseline price cap level adjustments, the proposed

methods for calculating and adjusting the X-factor and price cap index, and moving services in non-competitive areas into price-cap regulation.

- *Anchor or benchmark pricing for Ethernet.* Currently, an interim rule is used to ensure that ILEC providers, that are discontinuing legacy TDM services used as wholesale inputs by competitive carriers, offer Ethernet services at reasonably comparable rates, terms and conditions. This interim rule applies to two categories of services: (1) BDS services at DS1 speed and above; and (2) commercial wholesale platform services such as AT&T's Local Service Complete and Verizon's Wholesale Advantage. The FNPRM proposes to replace the interim rule with an anchor or benchmark pricing approach, and seeks comment on three different options.
 - Option 1: Rely on regulated TDM service prices to anchor the prices of similar packet services.
 - Option 2: Establish one regulated price for packet-based BDS to serve as an anchor for nearby-bandwidth packet-based BDS (such as a 10 Mbps Ethernet service).
 - Option 3: Initially use reasonably comparable prices for regulated TDM services as a benchmark to help the FCC determine whether rates for various packet-based BDS are just and reasonable, but over time, use the packet-based BDS prices as a benchmark.
- *Wholesale pricing.* The FCC seeks comments on how frequently BDS providers charge wholesale customers rates that exceed the corresponding retail rate, and is also interested in proposals for adopting rules, under sections 201 and 202(a), that ensure just and reasonable wholesale rates in non-competitive markets.
- *Terms and conditions.* The FNPRM proposes and seeks comment on regulations addressing certain ILEC terms and conditions that disadvantage CLECs, such as: restrictions on tying arrangement, percentage commitments, term commitments, upper percentage thresholds, overage penalties, and automatic renewal and evergreen provisions.

G. Deregulation of the Pricing Process. The FCC proposes replacing the current pricing flexibility regime with rules based on the results of the Competitive Market Test. The FNPRM seeks comment on proposed changes that would:

- Move competitive services out of price caps;
- Move non-competitive services into a structure that provides the protections of price caps while allowing providers to negotiate individual contracts, and
- Create a path to detariff TDM BDS while maintaining price caps on a detariffed basis.

H. Verizon Forbearance Action. In 2006, Verizon's Enterprise Broadband Forbearance Petition, which sought to exclude TDM special access services from certain Title II regulations, was deemed granted by operation of law after the FCC did not act on the petition within the statutory time limit. In order for the new regulatory framework to apply in a technology-neutral manner, the FCC proposes eliminating the current exemption for certain Verizon services from the basic provisions of the Act that govern just and reasonable offerings of telecommunications

services. The FCC also proposes extending the decision to eliminate forbearance to Hawaiian Tel and the legacy Verizon portions of FairPoint and Frontier, which were “Verizon telephone companies” at the time of the deemed grant.

I. Periodic Data Collection Requirements. The FNPRM proposes a periodic data collection to allow the FCC to update identification of competitive and non-competitive markets.

If you would like further information concerning this NPRM or assistance in preparing comments, please let us know.

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