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The Georgetown Center for Business and Public Policy is pleased to announce a new policy paper, "The Losing Case for Special Access Regulation" by Senior Industry and Innovation Fellow Larry Downes.

While not a visible market to those outside the telecommunications industry, the market for dedicated transmission (namely, special access) services is a large and critical component of the vibrant telecommunications ecosystem. In this policy paper, Larry Downes contrasts the lethargic pace of the evolution of regulatory oversight of special access services with the rapid changes in the supply and technology associated with special access. Additionally, he delves into potential explanations for this discontinuity, arguing that much of the incongruity can be explained by successful political rent seeking by consumers and competitors in this market.

True to the spirit of the Center's work generating ideas, convening leaders, and shaping policy, this paper is a timely and important contribution to inform the policy debate.

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The Losing Case for Special Access Regulation

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In 2005, the Federal Communications Commission (FCC) initiated a Notice of Proposed Rulemaking aimed at revisiting its longstanding price regulation of wholesale enterprise communications services, also known as "special access."

In response to growing signs of competitive discipline, the FCC had largely deregulated that market in 1999. The 2005 proceeding was aimed at adjusting the speed and specifics of its continued withdrawal. But the Commission never completed its investigation, and appears no closer to doing so now than it did a decade ago.

Since 2012, however, the agency has increasingly rattled its saber in the direction of re-regulating special access. Though there has been little in the way of definitive action, over fifty filings by the Commission in the proceeding, most of them recent, have introduced considerable uncertainty for both regulated and unregulated competitors.

The timing for the agency's frustrating behavior couldn't be worse. In sharp contrast to the FCC's shifting and often retrograde agenda, the special access market has moved dramatically forward since 2005, and at a pace that is accelerating. New competitors and new Internet-based technologies have dramatically increased speed and capacity, putting tremendous downward pressure on price. Even as the Commission threatens renewed oversight, the relatively slow analog offerings of the remaining regulated providers have become more and more marginalized.

This paper briefly reviews the history of the special access proceeding and argues that while the FCC appears increasingly eager to expand the scope of its control over this dynamic market, the case for regulation is actually growing weaker.

While the FCC's stated goal in this proceeding is to regulate toward competitive outcomes, doing so by artificially elevating one set of competitors over another is a strategy that has regularly backfired.[1] That is a particularly high risk in markets, such as special access, that are in the process of complete transformation thanks to better and cheaper technology drivers that, if left alone, create superior competitive outcomes, and do so in a neutral manner.[2]

[1] To take recent examples, the agency's efforts to placate some potential bidders in both the 700 MHz C and D block auctions in 2008 and the more recent H block auction in 2013, in hopes of stimulating more bidding from new entrants or smaller mobile operators, all ended disastrously, with greatly reduced prices and failure to secure a reserve price in some cases and with fewer rather than more bidders in all three. *See* Gerald R. Faulhaber and David J. Farber, THE OPEN INTERNET: A CUSTOMER CENTRIC FRAMEWORK, 4 *International Journal of Communications* 302 (2010), *available at* http://ijoc.org/index.php/ijoc/article/viewFile/727/411; Larry Downes, FORGET THE FAST LANES, HERE'S WHAT REALLY MATTERS AT THE FCC THIS WEEK, *The Washington Post*, May 12, 2014, *available at* https://www.washingtonpost.com/news/innovations/wp/2014/05/12/forget-the-fast-lanes-heres-what-really-matters-at-the-fcc-this-week/.

[2] *See generally* Larry Downes and Paul Nunes, BIG BANG DISRUPTION: STRATEGY IN THE AGE OF DEVASTATING INNOVATION (Portfolio 2014). *See also* Paul F. Nunes and Larry Downes, WHAT COMPANIES MUST DO NOW THAT BETTER IS ALSO CHEAPER, ***European Business Review***, Nov-Dec 2015, pp. 46-49, *available at* http://www.europeanbusinessreview.com/?p=8422.

In particular, I address three specific dangers arising from the FCC's renewed interest in a market it first deregulated in 1999 and which has, since that time, become exponentially more competitive:

(1) The market for special access services delivered on analog networks, which has until now encompassed the legal limit of the FCC's authority, is rapidly disappearing. Faster and cheaper digital technologies are taking over even as incumbents are slowed from adopting the new technologies by regulatory overhang and the impact of rent-seeking behavior by enterprise customers and competitors. Those working the hardest to encourage FCC re-regulation are customers who have recently become competitors for the incumbents, with unregulated offerings of their own they are eager to protect.

(2) The proceeding increasingly exhibits worrisome signs of mutating into another extension of the Commission's fast-expanding effort to insert itself deeply into digital broadband markets, particularly for Internet access, not only for enterprise users but for mass market consumer access, mobile broadband, and interconnection—in essence into broadband regulation from end to end.

(3) The embarrassing delays in this now decade-old proceeding provide the best proof possible of the folly of the FCC's threats to re-regulate special access services offered by legacy providers, new entrants, or both. The proceeding's meandering path, easily hijacked by special interests, acutely though unintentionally highlights the Commission's inability to develop a 21st century regulatory toolkit that would provide effective oversight of any market characterized by the regular deployment of faster and cheaper technologies and the dynamic competition that results.

What is Special Access?

Special access refers to business arrangements between network operators and other enterprises to transmit voice and data traffic on a wholesale basis. Historically, competitive local exchange carriers (CLECs) relied on special access leased from incumbents to supply or supplement capacity for resale to their own business customers. Businesses also use special access to manage internal communications. And special access is an essential component of mobile networks, where it provides backhaul for mobile voice and data traffic, reducing the strain on over-taxed wireless networks. Special access connections are increasingly the middle mile of the broadband Internet.

As the FCC defines it, "Special access…encompasses dedicated transmission services for voice and data traffic that do not use local switches. This service is used by 'businesses and competitive providers to connect customer locations and networks with dedicated, high-capacity links.' As

recognized in the Commission's National Broadband Plan, '[s]pecial access circuits play a significant role in the availability and pricing of broadband service.'"[3]

Like other aspects of the communications industry being transformed by the broadband revolution, however, the special access market is evolving rapidly. Cable, fiber-optic and high-speed Ethernet loops deployed by a growing range of companies are quickly displacing the legacy analog technologies of traditional phone companies. Copper simply can't handle the speeds necessary for exploding Internet traffic, especially for mobile backhaul. Gigabit Internet will never run on these circuits, which average speeds of only 1.5 Megabits per second.

New competitors with new technologies have long since arrived. Already, wholesale special access services offered by companies including Level 3, Time Warner Cable, Comcast, and Cogent have taken significant market share. Even Google is getting into the special access business. CLECs, who once relied almost exclusively on incumbents for special access connections to fill gaps in their own resale offerings, are increasingly self-sufficient.[4]

Today, the agency estimates that the provision of special access is a $40 billion market. Of that, the rapidly dwindling share for regulated incumbent phone companies offering analog service is less than 40%, with IP-based special access now commanding a roughly equivalent percentage of the market. In the 1980s, by comparison, incumbent phone companies controlled 92% of the market.[5]

The Special Access Proceeding

Beginning in 1999, the FCC exercised discretion to exert minimal oversight on the regulated part of the special access business, letting the market determine price and terms in areas where there

[3] Federal Communications Commission, IN THE MATTER OF SPECIAL ACCESS FOR PRICE CAP LOCAL EXCHANGE CARRIERS, WC Docket No. 05-25, RM-10593, ORDER ON RECONSIDERATION. September 15, 2014, ¶2, *available at* http://apps.fcc.gov/ecfs/comment/view?id=6019368263.

[4] For details on the emerging competitive landscape of the special access market, *see* Ex Parte Letter from Verizon, SPECIAL ACCESS RATES FOR PRICE CAP LOCAL EXCHANGE CARRIERS, WC DOCKET NO. 05-25 AND RM-10593, September 24, 2015, *available at* http://apps.fcc.gov/ecfs/comment/view?id=60001300162. *See also* Fred Campbell, HOW CABLE INDUSTRY GROWTH COULD BENEFIT FROM FCC SPECIAL ACCESS INVESTIGATION, ***Forbes***, Oct. 28, 2015, *available at* http://www.forbes.com/sites/fredcampbell/2015/10/28/how-cable-industry-growth-could-benefit-from-fcc-special-access-investigation/.

[5] Federal Communications Commission, IN THE MATTER OF INVESTIGATION OF CERTAIN PRICE CAP LOCAL EXCHANGE CARRIER BUSINESS DATA SERVICES TARIFF PRICING PLANS, WC Docket No. 15-247, ORDER INITIATING INVESTIGATION AND DESIGNATING ISSUES FOR INVESTIGATION, October 16, 2015, ¶2-14, *available at* *http://transition.fcc.gov/Daily_Releases/Daily_Business/2015/db1016/DA-15-1194A1.pdf*. *See also* Fred Campbell, FCC DECLARES INTELLECTUAL BANKRUPTCY IN BUSINESS DATA SERVICES INVESTIGATION, ***Forbes***, Nov. 2, 2015, *available at* *http://www.forbes.com/sites/fredcampbell/2015/11/02/fcc-declares-intellectual-bankruptcy-in-business-data-services-investigation/*.

was clear competition.[6] The 1999 order, approved under FCC Chairman William Kennard, was aimed at giving "the nation's largest telephone companies progressively greater flexibility in setting interstate access rates as competition develops, gradually replacing regulation with competition as the primary means of setting prices."[7]

The 1999 order recognized "the development of competition in the marketplace," and aimed to free ILECs to "compete more efficiently" in local markets where competitive providers had already emerged, particularly since passage of the 1996 Telecommunications Act.[8]

By 2005, however, the FCC came to doubt the specifics of its light-touch regime. Noting complaints from both ILECs and their customers that the formulae the agency used to evaluate the reasonableness of prices was overly complicated and failed to reflect the true dynamics of the changing market, the Commission initiated a review of its "pricing flexibility rules" for special access.[9]

Now, after ten years and over fifty filings by the FCC alone swelling the proceeding's docket, the agency has yet to complete that review. If anything, it is has moved backwards, even as the market has moved forward with increasing velocity. Reading through the chronology on the Commission's "Special Access Data Collection Overview" website,[10] the sad story of the agency's efforts to conclude the 2005 proceeding emerges.

After years of relatively little activity, the FCC's Wireline Competition Bureau suddenly re-imposed price regulations in 2012. That abrupt change came largely in response to pressure from two special interests: CLECs who resold special access circuits leased from the ILECs and mobile carriers, who had grown to rely heavily on incumbent phone networks for wireless backhaul as

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[6] *See* Federal Communications Commission, COMMISSION ADOPTS PRICING FLEXIBILITY AND OTHER ACCESS CHARGE REFORMS, August 5, 1999, *available at* http://transition.fcc.gov/Bureaus/Common_Carrier/News_Releases/1999/nrcc9054.html.

[7] *See* Federal Communications Commission, Report 99-206, IN THE MATTER OF ACCESS CHARGE REFORM, FIFTH REPORT AND ORDER AND FURTHER NOTICE OF PROPOSED RULEMAKING, August 27, 1999, *available at* https://apps.fcc.gov/edocs_public/attachmatch/FCC-99-206A1.pdf.

[8] *Id.*

[9] "After decades of regulations, rulemakings, and hundreds of "pricing flexibility grants," piecemeal tinkering with special access had become a dangerous hobby. Consider just one part of the current calculation, the Price Cap Index, which limits how much incumbent phone companies (or "local exchange carriers") can charge for special access. Here's the *simplified* explanation from the FCC:

> The PCI has three basic components: (1) a measure of inflation, i.e., the Gross Domestic Product (chain weighted) Price Index (GDP-PI); (2) a productivity factor or "X-Factor," that represents the amount by which LECs can be expected to outperform economy-wide productivity gains; and (3) adjustments to account for "exogenous" cost changes that LEC's [sic] control and not otherwise reflected in the PIC."

Larry Downes, THE FCC SCORES A HAT TRICK OF ERRORS ON INTERNET REGULATION, ***Forbes***, August 27, 2012, *available at* http://www.forbes.com/sites/larrydownes/2012/08/27/the-fcc-scores-a-hat-trick-of-errors-on-internet-regulation/.

[10] Federal Communications Commission, SPECIAL ACCESS DATA COLLECTION OVERVIEW, *available at* https://www.fcc.gov/encyclopedia/special-access-data-collection-overview-0.

consumer demand for mobile broadband services exploded with the rapid adoption of smartphones by consumers.

Both groups had taken advantage of the improving price and performance of broadband technology to build their own network capabilities. At the same time, these users found they could more easily acquire supplemental capacity from new and unregulated broadband providers. That increased competition was putting downward pressure on prices in some local markets, leading some resellers and mobile operators to regret having entered into long-term contracts with ILECs.

Those contracts were, of course, aimed at locking in regulated prices and other terms that seemed attractive at the time but which were becoming a less attractive option for the users, at least in some geographies. The two groups implored the FCC to free them from their contractual obligations or otherwise rewrite the agreements on their behalf before their expiration.

The suspension of pricing flexibility signaled at least a partial victory for the special interests. Meanwhile, the agency initiated a vast data collection effort aimed at determining the "true" competitive dynamics of the special access market.

The decision to reimpose price regulations flew in the face of acknowledged market realities, bowing instead to rent-seeking and anti-competitive behavior of the resellers and mobile operators. At the very least, suspending longstanding pricing flexibility before collecting and analyzing current market data to determine if the policy was still working seemed to many at the time to be putting the cart before the horse.[11] But the FCC promised to complete its review quickly, and to replace the suspended price flexibility rules with a more enlightened regulatory regime.

That, however, didn't happen. Following nearly two years of negotiations, notably with the Office of Management and Budget, the agency was finally given permission in late 2014 to proceed with data collection, and then only in a limited capacity. The agency's initial preference for two separate years' worth of data was cut back by OMB to one specific year—2013. For that year, the FCC mandated that both purchasers and suppliers of special access services submit data they hoped would provide a snapshot of the state of the market.

The data collection effort was not completed until mid-2015. But despite complex safeguards established for review of the proprietary information submitted, even authorized parties were unable to see the information until recently. Even then there was considerable doubt as to the

[11] *See* Larry Downes, THE FCC SCORES A HAT TRICK OF ERRORS ON INTERNET REGULATION, *supra note 9.* ("As Commissioner Ajit Pai points out in his dissent, however, that just means that under the fastest possible timetable, new rules can't be put in place until at least sometime in 2015. In the 'interim,' the existing process, flawed as it might be, is now suspended."). That was in 2012. At the end of 2015, as it turned out, the FCC had only begun its review of data that was, by design, certain to be both incomplete and obsolete in any case.

usability of the databases the FCC had created.[12] These continued problems forced the agency to once again extend the comment period, now pushed well into 2016.

Meanwhile, efforts by special interests to turn the proceeding to their own advantage continues to wreak havoc on this essential market. In October, the agency announced an investigation into a key subset of long-term special access contracts between incumbent providers and their customers.[13] This despite the fact that, again, the agency had yet to perform any analysis of its limited view of the market as it stood in 2013, nor provided effective access to the data to anyone else.

The inescapable implication of this provocative act was that the agency was bowing to pleas from long-sheltered CLECs and mobile operators, some of whom are now increasingly self-sufficient and/or relying on their own equipment to offer special access services themselves. Given the rapid changes in the market, these enterprises apparently regret making long-term contractual commitments. Now they want the FCC to rewrite terms and prices on their behalf, to the detriment of the incumbents, who are both their suppliers and competitors in the emerging market.

Three Reasons to Worry About the Special Access Proceeding

As even this very brief review makes clear, the special access proceeding has hardly been a shining example of regulatory efficiency. It has been fraught with delay, negative unintended consequences and growing signs of regulatory arbitrage from long-time industry insiders.

The FCC's active inaction since 2012 has also introduced considerable and unhelpful confusion into the special access market, imposing direct and indirect costs for all market participants with no offsetting benefits whatsoever. As the National Cable & Telecommunications Association presciently noted in late 2013:

> The Commission is farther than ever from reaching any sort of meaningful conclusion. In 2012, the Commission both suspended its old pricing flexibility triggers and authorized a highly detailed, extremely onerous data collection that it views as a prerequisite to adopting new triggers. However well-intentioned, this combination of decisions has left

[12] *See* IN THE MATTER OF SPECIAL ACCESS FOR PRICE CAP LOCAL EXCHANGE CARRIERS, WC Docket WC Docket 05-25, JOINT REQUEST FOR FURTHER EXTENSION OF TIME OF THE UNITED STATES TELECOM ASSOCIATION AND ITTA, Nov. 10, 2015, *available at* https://www.ustelecom.org/sites/default/files/documents/Special-Access-Revised-Motion-for-Extension-of-Time-11102015-final.pdf.

[13] Federal Communications Commission, IN THE MATTER OF INVESTIGATION OF CERTAIN PRICE CAP LOCAL EXCHANGE CARRIER BUSINESS DATA SERVICES TARIFF PRICING PLANS, WC Docket No. 15-247, ORDER INITIATING INVESTIGATION AND DESIGNATING ISSUES FOR INVESTIGATION, Oct. 16, 2015, *available at* http://transition.fcc.gov/Daily_Releases/Daily_Business/2015/db1016/DA-15-1194A1.pdf.

> the Commission completely adrift, with no meaningful ability to regulate or deregulate in a critically important sector of the communications marketplace.[14]

As time continues to pass, the case for any regulatory intervention becomes weaker by the minute. Since 2005, and particularly in the last five years, the special access market has fundamentally transformed from one served predominantly by incumbent telephone companies using relatively slow copper-based analog networks to one where nearly 40% of the market is served by high-speed Internet based technologies offered by multiple new competitors, including cable companies and other new entrants along with the CLECs. That percentage is growing fast.[15]

Yet despite the fact that the agency has only just completed a mandated collection of data that at best will only reveal the state of the market in 2013 and has yet to analyze that data, the FCC, as the recently-announced investigation makes clear, is determined to take some action to re-regulate some or all special access providers and their dealings.

Doing so would almost certainly do more harm than good. Despite the FCC's wildly mixed signals to market participants over the last ten years, the special access market has clearly become more competitive, offering enterprise customers better and cheaper technologies from a widening range of competitive providers large and small, national and local. The unregulated part of the market is growing and innovating, offering faster speeds at lower prices, with providers committing substantial capital investments for future growth.

The agency's 2012 decision to suspend pricing flexibility over the fading analog part of the market, on the other hand, has likely accelerated its decline. The light touch regime had long served both the FCC's policy goals and the market well, but the increasingly unprincipled and directionless review of those policies is having the opposite effect.

The agency has failed to pursue a fact-based review as promised, or in any case has failed to conduct such a review either quickly or comprehensively. Its process, especially since 2012, has been neither open nor transparent. And even so it seems clear the Commission has failed to ask the right questions or collect the right data.

In short, what was intended as a rational sanity check on longstanding deregulation, one designed with clearly defined parameters and timeframes, has devolved into a general review of an undefined but fast-changing subset of the broadband market.

Beyond general harm to the market caused by the FCC's withering scrutiny, there are three particular sources of concerns worth noting:

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[14] IN THE MATTER OF SPECIAL ACCESS FOR PRICE CAP LOCAL EXCHANGE, WC Docket No. 05-25, APPLICATION FOR REVIEW OF THE NATIONAL CABLE & TELECOMMUNICATIONS ASSOCIATION, Dec 9, 2013, *available at* http://apps.fcc.gov/ecfs/comment/view?id=6017479333.

[15] *Supra* notes 4 and 5.

1. Rent-seeking behavior in the declining analog market

The 2012 announcement of a new and extensive data collection effort, followed-up with the late 2015 announcement of a new investigation of some still-active special access agreements between incumbent phone companies and their customers, are strong indications that the FCC has fallen victim to rent-seeking behavior by CLECs, mobile operators and others hoping to squeeze a small set of incumbent providers in the waning days of existing long-term contracts.

The Commission's stated goal in opening its investigation, for example, has nothing to do with revisiting its 1999 pricing formula, but rather to determine whether certain contract terms constitute "reasonable practices" and, if not, how the agency should rewrite them. (As is typical for agreements between large businesses, the specific terms and conditions are not publically disclosed at the insistence of both buyers and sellers.)

Not surprisingly, the Broadband Coalition, a trade group of companies who traditionally resold analog services under the protection of the FCC, cheered the investigation.

"Consumers and business customers are demanding more broadband choices," the group said in a statement. "They want the freedom to choose their own service provider. But in markets controlled by large incumbent providers who charge monopoly-era rents, archaic lock up tactics in the terms and conditions to which their customers are subject are hurting competitors who want to bring new affordable options to the marketplace."[16]

How so? The Broadband Coalition and other potential beneficiaries of the FCC's renewed interest in special access regulation argue that exclusive contracts and contracts that require pre-defined levels of committed purchase, negotiated some time ago, are inherently "bad for competition" and somehow negatively impact consumer choice for broadband.[17]

But there is no basis in either law or economics for such sweeping claims. Output or requirements contracts, as they are known, have been standard forms of merchant-based commerce since the beginnings of capitalism. Their formation and interpretation are one of the first subjects taught to law students in first-year contracts courses. Their origins may be old, but their mechanics are hardly "archaic."[18]

In effect, such contracts represent a hedge by both buyers and sellers against an uncertain future, where supply and demand may change in ways that impact each contracting party's interests. Entering into such contracts allows both parties to invest long-term resources in their respective

[16] Editor, ***The Broadband Coalition***, BELL 'LOCK UPS' LOCK OUT COMPETITION, Oct. 16, 2015, *available at* http://thebroadbandcoalition.com/inthenews/2015/10/16/broadband-coalition-bell-lock-ups-lock-out-competition.html.

[17] *Id.*

[18] See, e.g., ***Black's Law Dictionary***, 6th Ed. at 324 (West Publishing 1990); see also ***Uniform Commercial Code*** ¶ 2-306, which governs OUTPUT, REQUIREMENTS, AND EXCLUSIVE DEALINGS.

production and sale of the goods subject to such contracts, secure in both price and quantity over a defined period of time.

Over the course of such agreements one or likely both parties' predictions of price changes will invariably prove inaccurate. But that hardly means all such contracts are inherently unfair. Indeed, the formation of any contract presumes that one party has made a better prediction of value than the other.

In the fast-changing special access market, it now seems, enterprise customers who committed to long-term requirements and exclusive purchase when the negotiated terms were attractive to them now regret their decision in light of better and perhaps cheaper alternatives from a growing list of providers offering high-speed, IP-based special access using newer network technologies.

That one party's prediction of supply and demand proved inaccurate has never been understood to be the basis for a court to modify or rescind such agreements; nor should it be for a regulator long absent from the field. In any case, no serious economic analysis of the costs and benefits of such agreements would simply begin and end by comparing contract price to market price in the final years. Over the full period of the agreements now being reviewed, and taking into account opportunity costs of investment decisions made in connection with them, the buyers may well come out ahead—perhaps far ahead—of the sellers.

Given the lack of serious analysis and the secrecy typical of business-to-business commercial arrangements, it's hard to know precisely how many crocodile tears are really being shed here. But the invocation of consumer harms from such agreements, it's worth highlighting, is both unsupported and entirely gratuitous.

As with all such agreements, existing output contracts will naturally expire on their own terms. Meanwhile, the business prospects for non-IP services are decaying as fast as the old copper networks. Cable and fiber-based services, everyone agrees, are the future of the market, especially as broadband traffic continues to explode and higher speeds are demanded by businesses and consumers alike.

And that future is coming up fast in the rear-view mirror of the regulated providers. Perhaps as much as half of the special access market has already moved to a growing set of competitors (including companies in the Broadband Coalition) offering faster connections and IP-based solutions.

In particular, mobile operators including Sprint and T-Mobile have dramatically reduced their dependence on the incumbents, deploying fiber-based backhaul to the vast majority of their cell sites. T-Mobile claims, for example, to have fiber at 50,000 of its 54,000 locations.[19] And middle mile providers including Windstream, Level 3 and XO Communications, who once depended on

[19] Phil Goldstein, T-MOBILE'S CARTER: WE'D BE A 'VERY INTERESTING' PARTNER FOR DISH, ***FierceWireless,*** March 5, 2015, *available at* http://www.fiercewireless.com/story/t-mobiles-carter-wed-be-very-interesting-partner-dish/2015-03-05.

capacity leased from incumbent phone companies at rates overseen by the FCC, are investing in their own faster connections, cherry-picking the most attractive markets.[20]

Even absent the increasingly competitive offerings of non-regulated providers, sophisticated enterprise resellers buying wholesale special access services do not need more mothering. Strip away all the rhetoric about "locking out competition" and the "freedom a customer has to take their business elsewhere," and this is rent-seeking pure and simple. The complaining companies are asking the FCC to rewrite contracts only now that they apparently feel they should have negotiated different deals or shorter terms. This is classic regulatory arbitrage.

Whatever the motivation of the complainants, the FCC's decision to investigate could prove a pyrrhic victory. While one FCC official told ***The Wall Street Journal*** that this new proceeding "will take at least a few months,"[21] the likely reality, given the history of the 2005 special access review, is that it will drag on for years. By then, the current set of "tariff pricing plans" subject to the review will have expired or become irrelevant, or both.

If anything, the expanded review will simply slow down rather than speed up the transition of their former suppliers to more competitive offerings. The Broadband Coalition claims to want the latter, but given their own entry into the IP-based middle mile market, presumably what they really want is the former. Which is perhaps what was really behind their complaints all along.

2. Extending monopoly-era regulation to competitive broadband markets

The 2013 data collection effort hints at a more worrisome problem. Beyond proving once again how easy it is for the FCC's agenda—and taxpayer resources—to be hijacked by quarrelling industry insiders, the Commission's continued tilting at the special access windmill reveals just how determined the agency is to insert itself deep inside largely unregulated broadband markets, both enterprise and consumer. And how dangerous that misguided decision may prove to be.

The FCC, like the market's current participants, knows that special access is rapidly moving from regulated rate capped analog circuits to all-IP technologies offered by a wide range of high-speed competitors--competitors that are outside of its jurisdiction.

Though the agency claimed to be reviving the special access proceeding in part to speed up the transition away from what's left of the analog phone network toward an all-IP infrastructure, the Commission is actually pursuing a very different agenda: creating a role for itself in the fast-approaching digital future . Leveraging the momentum of its decision to vastly expand its public

[20] Sean Buckley, XO INVADES CENTURYLINK'S TURF BY EXTENDING FIBER INTO 100 SALT LAKE CITY BUILDINGS, ***FierceTelecom***, August 28, 2015, *available at* http://www.fiercetelecom.com/story/xo-invades-centurylinks-turf-extending-fiber-100-salt-lake-city-buildings/2015-08-28.

[21] Ryan Knutson, FCC OPENS PROBE INTO 'SPECIAL ACCESS' MARKET, ***The Wall Street Journal***, Oct. 18, 2015, *available at* http://www.wsj.com/articles/fcc-opens-probe-into-special-access-market-1445029101.

utility authority,[22] under cover of saving "net neutrality," to include the entire Internet, the agency is putting all service providers on notice. The Commission intends to remain an active participant even in markets that are unarguably competitive and growing more so.

These latest moves, in other words, have little to do with the "lawfulness of certain terms and conditions contained in certain special access tariff pricing plans" offered by incumbent phone companies. That is largely pretext to advance the FCC's expanding efforts to appoint itself the official global governance body for the Internet, in spite of an explicit and prescient decision by a bi-partisan Congress to deny it that authority as early as 1996.[23]

The link between cause and effect here can be found in February's misnamed "Open Internet" order. Since Congress had denied the agency jurisdiction over the Internet, the Commissioners reasoned, the only way they could enforce the net neutrality rules was to redefine "the Internet."

Which is just what the Commission did. In a little-understood provision, the Open Internet order brazenly changes the plain meaning of "the public switched telephone network," over which the agency maintains vast regulatory power through Title II of the Communications Act, to include both that network ***and*** the Internet.

"The public switched telephone network," the Commission decided, meant both the public switched telephone network and the Internet, including any "service" that "uses" IP addresses.[24] A term the agency and the courts had long understood to distinguish old analog technology from new digital replacements was suddenly and implausibly redefined to erase that distinction. With

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[22] Gautham Nagesh and Brody Mullins, NET NEUTRALITY: HOW THE WHITE HOUSE THWARTED FCC CHIEF, ***The Wall Street Journal***, Feb. 4, 2015, *available at* http://www.wsj.com/articles/how-white-house-thwarted-fcc-chief-on-internet-rules-1423097522.

[23] *See* The Telecommunications Act of 1996, 47 U.S.C. § 230(b)(2) (The policy of the United States is "to preserve the vibrant and competitive free market ... for the Internet and other interactive computer services unfettered by Federal or State regulation."). *See also* NCTA V BRAND X INTERNET, 545 U.S. 967 (2005) (agreeing with the FCC that broadband Internet access is an "information service" not subject to Title II of the Communications Act of 1934). In the last decade, the FCC, through the Open Internet proceeding and other proceedings, has attempted to extend its broadband authority into, among others, mobile data roaming, interconnection, and the shutdown of the increasingly obsolete analog telephone network. *See* Larry Downes, THE FCC NOSES UNDER THE BROADBAND INTERNET TENT, ***Forbes***, June 6, 2012, *available at* http://www.forbes.com/sites/larrydownes/2012/06/06/the-fcc-noses-under-the-broadband-internet-tent/ and Larry Downes, THE FCC SCORES A HAT TRICK OF ERRORS ON INTERNET REGULATION, ***Forbes***, August 27, 2012, *available at* http://www.forbes.com/sites/larrydownes/2012/08/27/the-fcc-scores-a-hat-trick-of-errors-on-internet-regulation/.

[24] Federal Communications Commission**,** IN THE MATTER OF PROTECTING AND PROMOTING THE OPEN INTERNET, GN Docket No. 14-28, REPORT AND ORDER ON REMAND, DECLARATORY RULING, AND ORDER, March 12, 2015, ¶395, *available at* https://transition.fcc.gov/Daily_Releases/Daily_Business/2015/db0312/FCC-15-24A1.pdf. *Cf.* CELLCO PARTNERSHIP V. FCC, 700 F.3d 534, 538 (D.C. Cir. 2012) ("section 332 specifies that providers of 'commercial mobile services,' such as wireless voice-telephone service, are common carriers, whereas providers of other mobile services are exempt from common carrier status.") This this framework erects a "statutory exclusion of mobile-Internet providers from common carrier status." Id.at 544.

the stroke of a pen, the 21st century digital network turned out all along be the same thing as the 20th century analog network, simply because the agency needed it to be.

The "reclassification" of Internet-based information services in the 2015 Open Internet Order as "telecommunications services," subject to any and all of the public utility provisions of Title II, potentially opens the door to full rate regulation of all special access providers--large and small, old and new, national and local.[25]

If the FCC's legal and linguistic gambit survives the on-going court challenge, it magically extends the FCC's full Title II public utility jurisdiction from fast-fading analog services to broadband ISPs, mobile networks, and most anyone with a website or Internet service. Including, of course, IP-based special access services.[26]

Thus the endgame of the 2005 special access proceeding may be not only the re-regulation of legacy wholesale services, but new regulations aimed at the emerging IP-based broadband special access market. Such regulation would simply supplement the rest of the FCC's new Title II agenda, giving it complete authority over all forms of broadband access.

So where the agency felt constrained in 2005 and again in 2012 to limit its special access oversight to the former Bell companies whose analog services it continued to regulate under Title II, that constraint has now been removed. The FCC's renewed tinkering with the regulated special access market seems to be little more than a dress rehearsal for future regulation of new cable and fiber-based competitors, all of it considered and applied at the same leisurely pace we've seen with the 2005 order.

3. Mismatched pace of FCC proceedings and market dynamics

The third area of concern is more straightforward than the first two, albeit equally dangerous. Simply put, in markets undergoing dramatic change in response to disruptive technological innovation, the ability of industrial-era regulatory institutions to solve even legitimate market failures is highly limited and fraught with potential and unintended harm. That is largely because even as the pace of change in the market accelerates, regulatory change remains at a constant or declining speed. Even with the best of intentions, the regulators simply can't keep up.

The special access market is changing, with the FCC's 2005 proceeding falling farther behind. As I have noted in related contexts, "Substantive public policy challenges arise because rules and rulemaking processes fashioned in the monopoly era of telephony contemplate a set of

[25] The 2015 Open Internet Order makes only passing reference to special access, but notably does not explicitly exclude currently unregulated broadband enterprise services from the FCC's new definition of "public switched telephone network."

[26] The 2015 Order is currently being challenged in an all-inclusive legal battle pending before the D.C. Circuit. See Larry Downes, JUDGMENT DAY FOR THE FCC'S LATEST NET NEUTRALITY FOLLY, ***Forbes***, Sept. 9, 2015, *available at* http://www.forbes.com/sites/larrydownes/2015/09/09/judgment-day-for-the-fccs-latest-net-neutrality-folly/.

regulatory trade-offs and consumer choices that are no longer accurate, or in many cases necessary."[27]

Worse, as the pace of market transformations accelerate and new forms of competition emerge, the regulatory process remains static at best, with regulators experiencing drag coefficients both from obsolete legal levers and from industry insiders using their influence to slow down rather than speed up proceedings for self-interested reasons.

The evolving special access market and the FCC's 20th century regulatory toolkit, originally designed to micromanage the former telephone monopoly, is a textbook case of this kind of mismatch.

On the one hand, as noted, the market is changing rapidly. New technologies exhibiting the faster and cheaper characteristics I have elsewhere described as "big bang disruptions"[28] are inspiring new special access innovations from a variety of market participants, including existing CLECs, cable providers, and new entrants such as Google. Competition is robust and expanding, and prices are falling.

At the same time, the FCC, with no Congressional authority—and therefore no legal tools--to regulate broadband Internet markets, is trying to shoehorn itself into the role of Internet "cop on the beat."[29] And it is doing so using the worst possible regulatory mechanism: its increasingly obsolete common carrier authority under Title II.

All the while, the agency is being manipulated by special access customers-cum-competitors into using that authority to slow the deployment by incumbents of the new technologies and to rewrite existing contracts to further reduce the incumbents' ability to compete.

No more compelling evidence of the danger of that folly is needed than the history of the special access proceeding itself, which has dragged on for over a decade, failing at every stage to demonstrate either relevance or an ability for the FCC to conclude it in a way that would enhance, rather than damage, both emerging and legacy services.

Indeed, even if new technologies and new competitors were not providing sufficient market discipline to maintain effective competition in special access, the agency's failure to collect and analyze the data it needs even to understand the dynamics of that market makes clear the danger of expanding or even maintaining the agency's role in regulating special access.

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[27] Larry Downes and John M. Mayo, THE EVOLUTION OF INNOVATION AND THE EVOLUTION OF REGULATION, 23 ***CommLaw Conspectus*** 10, 11-12 (2014), *available at* http://papers.ssrn.com/sol3/papers.cfm?abstract_id=2542362.

[28] Larry Downes and Paul Nunes, BIG BANG DISRUPTION: STRATEGY IN AN AGE OF DEVASTATING INNOVATION (Portfolio 2014).

[29] Statement of Tom Wheeler, Chairman, Federal Communications Commission, Before the Subcommittee on Communications and Technology, Committee on Energy and Commerce, U.S. House of Representatives, Hearing on FCC REAUTHORIZATION: OVERSIGHT OF THE COMMISSION, March 19, 2015, *available at* http://docs.house.gov/meetings/IF/IF16/20150319/103182/HHRG-114-IF16-Wstate-WheelerT-20150319.pdf.

Conclusion

The special access proceeding has become a deeply cynical enterprise, with layer upon layer of subterfuge and misdirection. What appeared in 2005 to be a simple course correction from the agency's sensible deregulation of the enterprise market in 1999 has morphed into yet another front in the agency's battle to seize regulation of the Internet from the engineering-driven multistakeholder process that has ably guided its explosive development up until now.

CLECs, mobile network operators and other buyers of incumbent special access services see the renewed proceeding as an opportunity to improve their own competitive position as both buyer and now seller (rather than reseller) of enterprise wholesale services. But in the process, they have aligned themselves, knowingly or otherwise, with the agency's self-interested effort to carve out a leading role for itself as sole regulator for the entire broadband ecosystem.

The special interests are playing with fire. While the agency may be supportive for now of their efforts to hamstring the incumbents, it may only be to enhance the Commission's larger agenda of establishing regulatory primacy of broadband access from end to end—a goal that could intentionally or otherwise harm the continued growth of competitive markets.

The agency has become adept at playing one set of interests off another, even as those interests in turn play the agency for short-term advantages. In the long run, every participant in the Internet ecosystem seems destined to feel the withering scrutiny of the FCC. That is the real danger inchoate in the special access proceeding.

Ironically, self-styled consumer advocates cheered loudly when the Commission tried to assert its authority to "prophylactically" protect the Open Internet from hypothetical dangers in 2008, 2010, and again this year.[30]

But it should at last be clear to even the most naïve Internet activist that the FCC is hardly a benign occupying force, one that will efficiently and unobtrusively ensure corporate interests don't somehow ruin the greatest engine of innovation of this century, leaving everyone else—consumers, edge providers, smaller carriers--in peace.

The special access proceeding, unfortunately, has become the latest indication of the kind of policing the Commission has in mind as the Internet's regulatory cop on the beat. In sharp contrast to the engineering-driven multistakeholder process that has so far driven the unprecedented success of digital technology, the Chairman's approach is neither enlightened nor modern. Nor, it seems, is it based on sound economic principles or analytic practices.

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[30] *See* Larry Downes, UNSCRAMBLING THE FCC'S NET NEUTRALITY ORDER: PRESERVING THE OPEN INTERNET, BUT WHICH ONE? *20* ***Comm Law Conspectus*** *83 (2011), available at* http://papers.ssrn.com/sol3/papers.cfm?abstract_id=2164985.