



THE FREE STATE FOUNDATION

A Free Market Think Tank for Maryland.....Because Ideas Matter

Perspectives from FSF Scholars
July 15, 2016
Vol. 11, No. 26

The FCC's Special Access Proposal Is Infected With Special Pleading

by

Randolph J. May * and Seth L. Cooper **

Critical investment in next-generation broadband technologies is now threatened by new rate controls on special access services proposed by the Federal Communications Commission. “Business data services” (BDS) has replaced “special access” as the Commission’s new term for the broad class of advanced services targeted by its rate regulation proposal.

It’s no wonder the Commission opted to change the terminology. This whole decades-long proceeding has been driven in large part by “special access.” That is, special access to the Commission’s administrative processes by some favored parties engaging in special pleading to obtain special rent-seeking treatment. While Chairman Wheeler may be smart to ditch the “special access” label, a name change isn’t going to alter what is fundamentally wrong with the agency’s proposal.

Here’s what is really going on in the newly-denominated BDS proceeding. Special rent-seeking privileges are sought primarily by a segment of BDS competitors who serve business enterprises, not everyday residential or retail consumers. New rate controls would give these special interest pleaders price cuts on wholesale access to their competitors’ facilities, including advanced IP-based broadband networks.

The Free State Foundation
P.O. Box 60680, Potomac, MD 20859
info@freestatefoundation.org
www.freestatefoundation.org

Prompted by the continued special interest pleading, the Commission is proposing rate controls based on problematic analyses that disregard existing competitive forces. And by virtue of a last minute data dump, the Commission, in effect, curtailed the opportunity to prevent useful public comment on critical peer reviews that supposedly support its preferred analysis.

It is true that special interest pleading is nothing new at the Commission, and we freely acknowledge that no company or market segment has a monopoly on it. But the long, tortured history of the “special access” proceeding, in the face of ever increasing facilities-based competition in most places, is stupefying. This tortuous history is attributable, in significant part, to the Commission’s responsiveness to rent-seeking pleas from those who see more to gain from using the regulatory process to achieve their objectives than from expending resources to build out network facilities. Awash in special interest pleading, problematic analyses, and questionable agency processes, the best course would be for the Commission to close the BDS proceeding.

Unlike everyday services involving voice, cable, or Internet networks, special access or BDS services use private or dedicated facilities to serve specific high-volume users, typically business enterprises, with quality performance guarantees. Thus, BDS services are almost always business-to-business arrangements involving sophisticated parties. BDS services are not used by ordinary residential consumers.

Historically, special access lines were provided almost exclusively by incumbent local exchange carriers (ILEC) using TDM technology. Recognizing the presence of market competition that had emerged following the breakup of the old Ma Bell telephone monopoly, in 1999 the Commission relaxed some of its rate regulation controls for special access services. In the years that followed, telephone company providers rolled out new types of services using advanced technologies, including packet-switched broadband.

Pursuant to a series of *Broadband Enterprise Orders* issued by the Commission, certain advanced BDS technologies – such as Ethernet – have been exempt from dominant carrier and tariff requirements designed for legacy telephone services. Section 10 regulatory forbearance relief has encouraged investment in network upgrades and transition to all-IP based broadband network technologies offering faster, superior service. Significantly, market entry and expansion by cable operators has also reshaped the competitive landscape, providing business enterprise customers additional price and service options. Cable investments in business data facilities were made, to a significant degree, in reliance on the Commission’s deregulatory policy. And 4G LTE network capabilities now offer even more additional alternatives to business enterprise customers.

Despite the undeniably increasingly competitive landscape for BDS, a narrow segment of providers has continuously called on the FCC to impose new BDS regulations. These special pleaders seek to use the regulatory process to obtain favored treatment for themselves at the expense of their market rivals. Rate controls would restrict the ability of their market rivals to seek returns on their facilities investments through contractual bargaining and market-based pricing.

Again, no individual or company or set of companies has a corner on the special pleading market at the FCC. But in this particular instance, after a decade-long clamor for special access regulation, the FCC unwisely appears ready to capitulate to the incessant calls for new regulatory controls. Under its proposal, the Commission will broadly impose rate controls on BDS services, based on the Commission's own determination about what constitutes "reasonable" prices, even down to service provided to individual buildings. If adopted, the Commission's BDS proposal effectively re-regulates broadband enterprise services that use advanced technologies like Ethernet and, for the first time, bring into the agency's regulatory grip the new competitive enterprise services offered by cable operators.

By imposing rate controls, the Commission necessarily will curb financial returns on investment for business data facilities. This will discourage infrastructure deployment by both incumbents and by new facilities-based entrants like the cable operators. Rate regulation also discourages facilities-deployment and market entry by competitors who, given a choice, prefer regulatory arbitrage to facilities-based competition. Common sense recognition of the economic incentives involved was supplied by the D.C. Circuit in *Ad Hoc Telecommunications v. FCC* (2009): "Perhaps an obvious point, but a decision that gives owners of telecommunications lines more control over access to those lines tends to increase the incentive for competitors to build competing lines."

If adopted by the Commission, the new BDS regulation would be especially favorable to Sprint, which previously owned considerably more special access facilities. In 2006, it spun off many of its facilities to a separate entity – Embarq – now owned by CenturyLink. By imposing new rate regulations on ILECs and cable operator entrants, the Commission's proposal effectively subsidizes Sprint's business decision to sell its own facilities and lease its rivals' facilities at government-dictated prices.

The Commission has tried to prop up its problematic BDS proposal with a suspect analysis. In its scramble to find a purported rational basis for ascertaining BDS rates it considers "reasonable," the Commission's rulemaking proposal suggests it's appropriate to define the relevant BDS market by discrete "location." In essence, each building with a BDS connection can be considered its own "market." Under this novel market-definition approach, a competitor serving a building 100 feet away would be irrelevant to the market analysis. This extremely narrow market definition approach tracks with special interest claims that competition is impossible in any place where only ILEC connections presently exist. This wrong-headed approach ignores the potential for competition and runs against accepted market analysis principles.

As bad, the Commission's eagerness to serve special interests apparently prompted it to undertake problematic procedures. For nearly two months, the Commission declined to publicly release critical peer reviews of the analysis upon which its regulatory proposal is based. The Commission finally released these reviews on the same day public comments were due. Of course, this irregular procedure ensured that the work of its hand picked analyst would avoid careful scrutiny in the initial round of public comments.

Unfortunately, special access is an apt description for what is going on – and has been going on for a long time – in the Commission's formerly-named special access proceeding. To protect its

institutional integrity, and uphold rule of law norms, the Commission must guard against granting unjustified regulatory favors to special interests in this or any other proceeding. The BDS proceeding ought to be closed now. Instead, the Commission should seek new ways to promote additional facilities-based investment and deployment in all-IP network technologies by all market participants, incumbents and new entrants alike.

* Randolph J. May is President of the Free State Foundation, an independent, free market-oriented think tank located in Rockville, Maryland.

** Seth L. Cooper is a Senior Fellow of the Free State Foundation.

Special Access

Comments of the Free State Foundation, [Regarding Business Data Services in an Internet Protocol Environment](#) (June 28, 2016).

Michael J. Horney, "[The FCC Cannot Proceed in the BDS Proceeding with a Flawed Analysis](#)," *Perspectives from FSF Scholars*, Vol. 11, No. 17 (June 6, 2016).

Randolph J. May, "[The FCC's Flawed Understanding of Competition](#)," *Real Clear Markets* (March 11, 2016).

Randolph J. May, "[The IP Transition: Focus on Consumers, Not Propping Up Competitors](#)," *FSF Blog* (July 23, 2015).

Seth L. Cooper, "[FCC Should Finally Grant CenturyLink Forbearance on Broadband Enterprise Services](#)," *FSF Blog* (July 22, 2014).

Randolph J. May, "[Special Access: A Special FCC Debacle in the Making](#)," *FSF Blog* (December 17, 2013).

Seth L. Cooper, "[FCC Inviting An Especially Big Mess On Special Access](#)," *FSF Blog* (October 31, 2012).

Randolph J. May, "[Fresh Thinking on Special Access](#)," *Perspectives from FSF Scholars*, Vol. 4, No. 1 (February 12, 2009).

Randolph J. May, "[Special Access and Sound Regulatory Principles: The Market-Oriented Case Against Going Backwards](#)," *Perspectives from FSF Scholars*, Vol. 2, No. 16 (June 4, 2007).