



# THE FREE STATE FOUNDATION

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## *Perspectives from FSF Scholars*

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### **Free State Foundation Scholars React to the D.C. Circuit's Decision on the Open Internet Order**

by

**Seth Cooper, Gus Hurwitz, Daniel Lyons, and Richard Epstein \***

Below are quick reactions from Free State Foundation Scholars – Seth Cooper, Gus Hurwitz, Daniel Lyons, and Richard Epstein – to yesterday's D.C. Circuit decision in *US Telecom v. FCC*. The Court's decision upheld the FCC's *Open Internet Order*.

Here are the reactions:

#### **SETH COOPER:**

##### **D.C. Circuit Upholds FCC's Nearly Open-Ended Power to Regulate Broadband**

By upholding the FCC's *Open Internet Order* in its entirety, the D.C. Circuit is really upholding almost open-ended power by the FCC to regulate broadband Internet services. This includes rate regulation of broadband services, regulation of when and how broadband networks exchange traffic, and "general conduct" regulation of network management decisions by broadband providers. The Court's decision upholding of Title II reclassification also paves the way for the FCC to subject consumers of broadband services to universal service surcharges – in effect, Internet taxes.

The FCC never made any finding of broadband market failure – a point the Court's majority was unconcerned with but which dissenting Senior Judge Stephen Williams was rightly troubled by. So consumers won't experience any benefits from the Internet regulations that were just upheld. Rather, the FCC's public utility-style regulation of broadband networks threatens innovation and

financial investment that are critical drivers of Internet growth. Evidence of decreased investment has already surfaced in the time since the FCC adopted the *Open Internet Order*. Unless the Court's decision is reversed or the FCC's regulatory policy is overturned, further diminishment of innovation and investment will reduce consumer choices for new broadband services and offerings.

Among critics of Internet regulation it was expected that some or perhaps several aspects of the FCC's *Open Internet Order* would be upheld in Court. Indeed, the Court's upholding of Title II reclassification of wireline broadband services is less than surprising – although unthinkable from a public policy standpoint. But what is surprising is the manner in which the Court's majority accepted so completely and without slightest reservation the agency's rationalizations for the entirety of the *Open Internet Order*. Even the most legally and factually problematic aspects of the *Open Internet Order* – including Title II reclassification of mobile broadband services, FCC authority over network interconnection, and the vague "general conduct" standard for network management – received easy judicial endorsement. Among other things, the D.C. Circuit's majority failed to hold the FCC to Supreme Court precedents that required the agency to identify new facts or supply a reasonable explanation for its abrupt change of policy.

The dynamic Internet ecosystem that we enjoy today emerged from a lightly regulated environment. The *Open Internet Order* marked the start of a highly regulated future for the Internet. Regrettably, *US Telecom v. FCC* gives the FCC judicial sanction to regulate competitive broadband services in a similar manner to how it regulated the 20th Century monopoly telephone services. The FCC's regulations threaten innovation, financial investment, and consumer choice in next-generation broadband Internet services. And as indicated, in the very near future the FCC may insert USF surcharges on the monthly bills of broadband consumers.

There is nothing left to lose by appealing the decision in *US Telecom v. FCC* to the D.C. Circuit *en banc* or to the U.S. Supreme Court. The decision heightens the urgency in Congress passing a new Communications Act that can restore a lightly regulated environment and also allow targeted regulatory remedies in proven instances of market failure.

## **GUS HURWITZ:**

Yesterday's D.C. Circuit opinion rejecting challenges to the FCC's *Open Internet Order* was complicated and dense. For that reason, its conclusion was also relatively unsurprising. In administrative law, courts are in the first instance substantially deferential to agency decisions. When courts reviewing complex agency orders get "into the weeds," debating the details of the agency's conclusions as the D.C. Circuit did in this case, they are likely to find in favor of the agency. This is true as a matter of law, as captured in the deferential *Chevron* standard. But it is also true in less visible ways. If the best case to be made against a regulation is disagreement with the agency's policy conclusion backed by a smorgasbord of technical arguments – nit-picking minor procedural points, dissecting the finer points of earlier binding precedent, and the like – judges are unlikely to be impressed. And if they are unimpressed, between procedural

tools and affording the agency deference, judges can easily dismiss these arguments to find in favor of the agency.

And that's what we saw in this case. The court was uninterested in petitioners' efforts to relitigate *Brand X* and *Verizon* – opinions themselves buttressed in principles of deference. The notice issues were decided on “logical outgrowth” grounds – an analysis that can easily go whatever way judges' whims carry it. And in several cases, the majority dismissed arguments as having not been sufficiently raised by petitioners. Here, too, in realist terms the judges could have engaged these arguments had they been so inclined – but lacking interest they could simply brush them aside. This is perhaps most illustratively seen where the majority rejects the argument that reclassification was arbitrary and capricious – an argument the dissent embraces – because, although the point was raised in the introduction to one of the petitioners' briefs, that brief “provide[d] no further elaboration on this point.” The court was not wrong to reject this argument on procedural grounds – though no one would have batted an eye had it instead embraced the argument, as there was surely sufficient fact and argument in the record to support the court's consideration. But this maneuver is interesting for how it illustratively parallels the “logical outgrowth” analysis: the court finds the barest mention of reclassification in the NPRM sufficient to have preserved the issue before the FCC, but also finds a comparable discussion by petitioners insufficient to have preserved the issue before the court.

Judge Williams's dissenting opinion tells the story of what might have been had the case been framed differently. Rather than focusing on what the Commission said or did that was “wrong” – that is, rather than disagreeing with its conclusions or the steps taken to get to them – Judge Williams focuses his dissent on the myriad inconsistencies surrounding the Commission's adoption of the *Open Internet Order*. He points to the substantial evidence in the record contradicting the Commission's analysis, and the Commission's lack of response to those critiques. He points to the thin evidence that the Commission was able to cite to in the record to show support for its analysis – a lack of evidence that Judge Williams says shows the Commission's theory of paid prioritization “is, to put it simply, false.” He cites to examples of “analysis” underlying the Commission's Order that were mere conclusory statements, or supported by mere anecdotes. He points to the insufficient explanations offered by the Commission for its retreat from previously strongly-held policy positions. He compares the relative sophistication of past Commission decisions with the sparse analysis underlying the new Order. He highlights that the Commission's theories are asserted “without bothering to conduct an economic analysis!” He discusses contradictions in the Commission's own theories: its need to disclaim market analysis in some cases and to rely on it in others; its assertion that Sections 201 and 202 map onto the Internet yet also require forbearance in order to be logically consistent with the structure of the statute. He lambasts the Commission for relying on studies to support its conclusions when those studies' authors submitted comments repudiating the conclusions that the Commission drew from them.

In other words, Judge Williams's opinion would have seen the Commission hoisted by its own petard. The frontal assault taken by petitioners, arguing that the Commission was wrong in every way imaginable, was easily parried by a court disinclined to second guess a federal agency. But the argument that the Commission was inconsistent and incoherent is – or would have been – harder for the court to ignore. It would have forced the court to grapple with the arbitrary and

capricious decisionmaking underlying the *Open Internet Order*, and this would have required the court to either reject the Order for the incoherent farce that it is, or give that farce the court's own stamp of approval. But the approach taken allowed the judges to sweep the inconsistencies and contradictions under the carpet of deference.

### **DANIEL LYONS:**

The D.C. Circuit's decision is perhaps unsurprising given the current state of American administrative law. But it is nonetheless astonishing to see on paper the ease with which the agency completely reversed course regarding broadband regulation and cast aside a half-century of well-developed law regarding unjust and unreasonable discrimination by common carriers, solely to secure a legal hook sufficient to support its paid prioritization ban. Indeed, the motif uniting the 115 pages of the majority's opinion is deference – to the agency's policy judgments, its factual findings and hypotheses, its legal interpretations, and its exercise of the substantial authority delegated to it by Congress. This repeated deference, and the court's casual observation that it is “forbidden” from considering “whether the agency's decision is wise as a policy matter,” helps explain why both academia and the Supreme Court are beginning to question the wisdom of our three-decade experiment with doctrines like *Chevron*.

Judge Williams was the only judge honest enough to cry that the Chairman has no clothes. His partial dissent exposes in convincing fashion the extent to which the agency departed from its past precedent without adequate explanation, and the almost complete lack of facts underpinning its conclusion that broadband providers pose a threat to the free flow of information or that a ban on paid prioritization would promote a virtuous cycle of innovation. Judge Williams' dissent represents a strain of opinion once prominent on the D.C. Circuit – particularly in FCC cases – but waning in recent years, one that takes the APA's arbitrary and capricious standard seriously and requires the agency to support its claims and respond meaningfully to comments that challenge its assertions.

It remains to be seen whether the deficiencies the dissent cites will be sufficient to support *en banc* review. And while the likelihood of a *certiorari* grant is always small, particularly absent a circuit split, there are nonetheless a few nuggets in his opinion that could interest the Supreme Court. Primary among these is the “major questions” exception to *Chevron*, articulated most clearly in the 2015 *King v Burwell* opinion, in which the Court announced that *Chevron* deference is inappropriate in certain cases of economic and political significance. The D.C. Circuit seemingly found that its hands were tied by the Supreme Court's earlier decision in *Brand X*. But that decision predated *Burwell*, and the Supreme Court would not necessarily be similarly bound. If the Court were interested in expounding upon the doctrine announced so cryptically last year, this case provides an excellent vehicle to do so.

### **RICHARD EPSTEIN:**

Regrettably Correct: The FCC Wins On Its Net Neutrality Rules

On June 14, 2016, the United States Court of Appeals for the District of Columbia by a divided [decision](#) came out foursquare in favor of the Federal Communications Commission decision to switch the classification of broadband services, including broadband for mobile applications, from an “information service” to “telecommunication service.” To the unpracticed eye, this statutory distinction doubtless looks like another instance of the mind-boggling word-play that so often brings modern regulatory law into disrepute. But in this instance, the choice of terms is really critical, because it indicates the reach of the regulatory powers of the FCC. Call broadband the source of information services, and they are largely unregulated by the FCC. Call them telecommunications services and they are subject to the full scheme of common carrier regulation that dates back to the Federal Communications Act of 1934, which was intended to deal with the problems posed in the days when AT&T had an end-to-end monopoly over telephone services.

On the merits, I have little doubt that the decision of the FCC represents a form of regulatory adventurism that this nation will long regret. The stated purpose of the new system of regulation is to make sure that the dominant carriers do not engage in one of three practices – blocking, throttling, and paid prioritization. Of these, only the third matters in practice. Nobody in the Internet business is going to adopt a rule that keeps the so-called edge providers – think Netflix, Google, and Amazon – from providing content and services over the internet. Why else would anyone want to subscribe in the first place? It is also not likely that they would engage in any practice to slow down transmission just to frustrate its user base.

So the real debate is over what Judge Williams in his dissent called the “jewel of the crown,” paid prioritization. And here it is simply baffling why the FCC should think that this practice, which allows people to pay more in order to get better service, should be somehow inconsistent with the sound operation of the Internet. Paid prioritization exists in every walk of life, and it is an efficient way to sort demand by intensity in every market, no matter what the level of competition. There are people who have life and death problems who need immediate communications and others who can wait. Long before the Internet the Post Office charged different rates for air and ground mail. Why anyone would want to stop this in the name of equality of access is a total mystery to me. It reminds me of [the foolish efforts](#) to make sure that cruise ships, hotels and apartment houses provide roughly equal service to customers with very different demands.

Nonetheless, the merits of the order were not much discussed in these opinions. To be sure, Judge Williams noted that the FCC did not examine competitive conditions before imposing the net neutrality order. But his argument only went to the level of review needed to work the FCC’s switch in position, not its ultimate merits. But as the majority answered on that point, there was no statutory obligation for the agency to do so.

But that one sally aside, the remainder of the joint opinion of Judges Tatel and Srinivasen delved into the inner recesses of American administrative law, whose dominant trope is that of judicial deference to administrative expertise. That manifested itself in two ways in the joint opinion. The first was a long cautionary note that judges are not “a panel of referees on a professional economics journal,” but ordinary judges whose sole task is to ask whether the rule falls within the outer limits of the statute. On that question, moreover, they are guided by principles of

deference when a statute is unclear, and on these issues they must let the agency change its views, without bearing a special burden of explanation, under the Supreme Court's 2005 decision in [National Cable & Telecommunications Association v. Brand X Internet Services](#).

*Brand X* invoked the presumption of deference in favor of a decision that allowed the FCC to classify broadband as information services. A quick look at the two definitions shows that *Brand X* needed all the deference that the Supreme Court could muster. In dealing with information services, the provider allows the user "a capability" for processing information. In contrast, telecommunications services involve the transmission of information generated by others. These days most of what anyone uses on the Internet are services supplied by those "edge providers," which makes the broadband companies telecommunications providers in my book. The irony therefore is that the Supreme Court got to the right substantive result in *Brand X*, by using a mode of deferential reasoning that poses a serious risk to the rule of law.

The reason why this case will be so hard when and if it goes before the Supreme Court is that the FCC wins, pretty cleanly in my book, even if, as is decidedly not the case, it has to defend its rule under an interpretive regime that affords it no deference at all. This sad conclusion shows just how important it is to have meaningful legislative reform in this area, so that government regulation is tied to the control of monopoly power, and not to the provision of services in an ever more competitive market. Yet given the low estate to which competition has fallen in these populist times, that result is most unlikely until the level of investment in Internet services starts to fall. And even then there will always be doubts as to the reasons for the decline. So while it is hard indeed to fault the majority opinion on its application of established administrative law, there is much reason to despair over the intellectual climate that prompted the FCC to flex its regulatory muscles in so counterproductive a fashion.

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