US Federal Communications Commission Suspends Special Access Pricing Flexibility Rules

The Federal Communications Commission recently adopted an order suspending "on an interim basis" its special access pricing flexibility rules.[1] The Order states that parties adversely affected by the suspension may seek relief through the forbearance process, and the Commission promised to issue a mandatory data request within 60 days, which will help it subsequently conduct a detailed market analysis of the special access market. The two Republican Commissioners, Robert McDowell and Ajit Pai, dissented.

The actions taken in the Order are unlikely to have any immediate effect on special access prices. However, the analytic framework articulated in the order suggests that it may take significant time for the Commission to adopt permanent replacement rules, and that these replacement rules are likely to be significantly more complex and administratively burdensome than the suspended rules.

Special access services are telecommunications services that employ a dedicated link between two points. They are purchased by business customers that, for example, seek to connect multiple offices, and by other carriers that seek to provide service in areas where they lack their own facilities. Both voice and data may be carried using special access services. Special access services offered by incumbent local exchange carriers (ILECs) traditionally have been rate regulated, either through rate of return or price-cap regulation.

In 1999, the Commission adopted the *Pricing Flexibility Order*,[2] which gave ILECs subject to price-cap regulation greater flexibility to set special access prices as competition developed. First, the Commission allowed all ILECs greater flexibility to adopt density zone pricing plans, under which they could charge different prices in different zones within a study area.[3] Second, the Commission established certain competitive triggers that were designed to "measure the extent to which competitors had made irreversible sunk investment."[4] If ILECs demonstrated that they met the trigger, they could receive greater pricing flexibility.

The Commission established two phases for pricing flexibility. Under Phase I, the ILEC would be able to offer contract tariffs and volume and term discounts, while remaining subject to price cap regulation. Under Phase II, the ILECs would be freed from price-cap regulation. In part to ensure "administrative workability," the Commission adopted the metropolitan statistical area (MSA) as the geographic area for granting relief.[5] And as a proxy for competitive sunk investment, the Commission adopted collocations in ILEC wire centers in part because it found that a collocation "provides an administratively simple and readily verifiable mechanism."[6] An additional advantage of collocations was that the ILECs possessed the necessary data which they could submit with their application.

The *Pricing Flexibility* rules do not apply to high-capacity, packetized transmission services sold to enterprise customers, however. As the result series of forbearance petitions filed by price-cap LECs, which were either granted by the Commission or deemed granted, these "enterprise broadband special access" services were removed from dominant carrier regulation.[7]

In its recent Order, the Commission reconsidered and rejected many of the assumptions and conclusions of the 1999 Order. First, it criticized the use of MSAs as the geographical area for relief, finding, among other things, that "MSAs have generally failed to reflect the scope of competitive entry,"[8] that "business demand varies significantly within MSAs"[9] and that "MSAs "do not have 'reasonably similar' competitive conditions across their geographic areas."[10]

Second, the Order criticizes the use of collocations as a proxy for competitive investment in channel terminations[11] both because competitors may not invest in channel terminations after they collocate and because collocations fail to take account of non-collocated competitors, such as cable companies.[12] The Commission found that the collocations proxies were "both over- and under-inclusive, resulting in inaccurate assessments of whether actual and potential competition is sufficient to constrain special access prices in the areas granted relief."[13] Based on these conclusions, the Order suspends the pricing flexibility rules on an interim basis. The Order notes that ILECs may still request pricing relief through forbearance or waiver petitions.[14]

The Order states that the Commission will issue a mandatory data request within 60 days, and, after the data is collected, will perform a market or competition analysis that it will use in developing new rules. The Order predicts that new rules will be adopted in 2013.[15]

In their dissents, Commissioner McDowell and Commissioner Pai, among other things, criticized the majority for suspending the existing rules "without an adequate evidentiary record or market analysis," and expressed concern that the "interim solution" may turn into a long-term change.[16] In addition, Commissioner Pai criticized the Commission's suggestion that "a market-power/non-dominance analysis should be the test for any regulatory relief, and argued that the majority discounted "the value of administrative simplicity in favor of analysis on a more granular level."[17]

This decision, together with the 2010 decision in *Qwest/Phoenix,*[18] in which the Commission adopted a market-power framework for analyzing forbearance petitions, suggests that the Commission may be turning to a market-power analysis when evaluating requests for deregulation or forbearance. While such an approach is useful in identifying whether a particular firm possesses market power, it is extremely fact-intensive and administratively burdensome, both for parties and for Commission staff.[19] And, if the Commission intends to do an in-depth market analysis, it is likely to require highly disaggregated data, which means that the request likely will be detailed and burdensome. If this turns out to be the case, the Commission will have to allow parties sufficient time to gather the data, and then allow Commission staff time to clean the data and analyze it, which could push adoption of new rules past 2013.

The Commission is also likely to face several challenges in adopting new rules. First, the Commission may find it difficult to identify a geographic area for granting relief that reflects similar competition conditions throughout such area, since business demand and the level of competition may vary from one building to the next. Similarly, the Commission may have difficulty identifying relatively simple and verifiable metrics that accurately estimate the extent of competition and competitive investment within that area. There clearly is a tradeoff between analytical precision and administrative burden,[20] and achieving an appropriate balance will delay final resolution of this issue. If the Commission insists too much on

analytical precision, it may make the process so burdensome that no ILEC will attempt to seek relief.

Second, for MSAs where relief has already been granted, the Commission will face a significant challenge in transitioning from the old rules to the new, particularly since many competitors and enterprise customers currently enjoy significant discounts under contract tariffs or under volume or term discount plans. Finally, some might question whether it makes sense to invest all the resources necessary to complete this proceeding, when carriers and customers alike are increasingly turning to packetized transmission services that currently are not subject to these rules.

For more information about the Suspension Order, or any other matter raised in this Legal Update, please contact the following lawyer.

Donald K. Stockdale Jr.
+1 202 263 3366
dstockdalejr@mayerbrown.com

Endnotes

[1] *In the Matter of Special Access for Price Cap Local Exchange Carriers, WC Docket 05-26*, Report and Order (Released August 22, 2012) (*Special Access Suspension Order*).

[2] *In the Matter of Access Charge Reform*, CC Docket No. 96-262, Fifth Report and Order and Further Notice of Proposed Rulemaking, 14 FCC Rcd 14221 (1999) (*Pricing Flexibility Order*).

[3] *Id.* 14 FCC Rcd at 14233, para. 21.

[4] *Special Access Suspension Order* at 7, para. 11.

[5] *Pricing Flexibility Order*, 14 FCC Rcd at 1259-1261, paras. 71-76

[6] *Id.*, at 14267, para. 84.

[7] *Special Access Suspension Order*, at 11 & n.64.

[8] *Id.* at 17, para. 35.

[9] *Id.* at 19, para. 38.

[10] *Id.* at 23, para. 41.

[11] Channel terminations are basically the dedicated lines connecting end user locations.

[12] *Special Access Suspension Order* at 38 & 42-43, paras. 65, 72-75.

[13] *Id.* at 57, para. 103.

[14] *Id.* at 48, para. 84.

[15] *Id.* at 5, n.16.

[16] *Dissenting Statement of Commissioner Robert M. McDowell* at 88-89; *see also Dissenting Statement of Commissioner Aijit Pai* at 94-95, 97-98.

[17] *Id.* at 104-105.

[18] *In the Matter of Petition of Qwest Corp. for Forbearance Pursuant to 47 U.S.C. § 160© in the Phoenix, AZ. Metro. Statistical Area*, 25 FCC Rcd 8622 (2020), *aff'd Qwest Corp. v. FCC*, No. 10-9543 (10th Cir. Aug. 6, 2010). The Tenth Circuit decision, the Commission's *Qwest/Phoenix Order*, and the market-power framework were previously discussed in our August 16, 2012 Legal Update available at http://www.mayerbrown.com/US-Tenth-Circuit-Court-of-Appeals-Upholds-FCCs-Market-Power-Framework-08-15-2012/.

[19] *Cf. In the Matter of Verizon Communications Inc. and MCI, Inc. Applications for Approval of Transfer of Control*, WC Docket 05-75, 20 FCC Rcd 18433, paras.28 & 37 (2005) (finding that the relevant geographic market for wholesale special access services is a particular customer's location).

[20] *See,e.g.*, Donald K. Stockdale, Jr., *Geographically Segmented Regulation: Lessons from the FCC for European Communications Markets*, 82 Communications & Strategies: Digiworld Econ. J. 85 (2011)

0912