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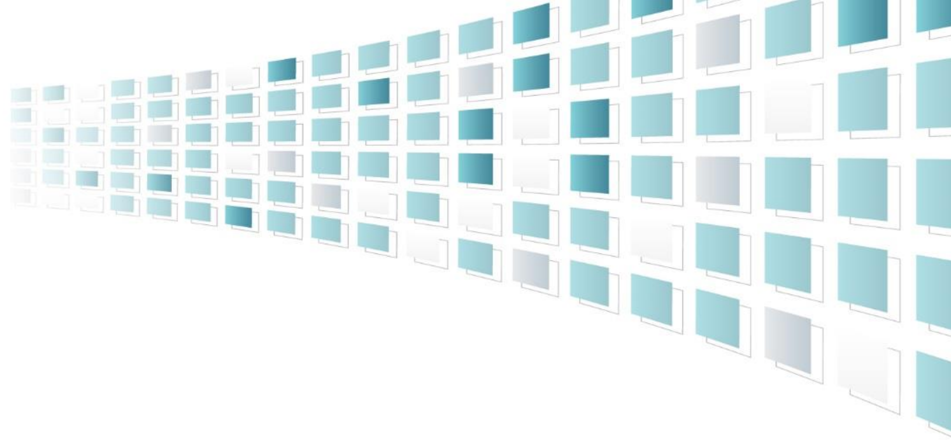

The Private Carriage Path to a Less Regulatory, More Market-Based Telecommunications Future

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Introduction

President Donald Trump campaigned on a promise to reduce federal regulations by at least 70 percent.[1] Underlying this politically salient goal is the administration's view that public interest aims are best served when the regulatory atmosphere supports and does not undermine job creation, innovation, and investment incentives. In other words, the President's views are a clarion call for government to reinvent itself, following decades of excessive regulatory encroachment into private enterprise. The current administration continues to support government involvement to promote and protect public interest aims, but in a manner that defers to free market and economically sound principles.

The question before the Federal Communications Commission ("FCC" or "Commission"), and indeed the entire telecommunications industry, is how to recognize these laudable deregulatory goals while at the same time sustaining the Commission's core mission.[2] Of course, the Commission can look critically at its existing rules and walk back those it concludes are imposing unreasonable burdens without clear, corresponding benefits. Conversely, Congress could take the lead by re-calibrating the regulatory structures instituted in the 1996 revision of the Communications Act. These solutions promise to be effective, if pursued, but will take time and require expenditure of political capital.

This White Paper proposes an alternate opportunity for the Commission to realize the deregulatory aims of the Trump administration and Republican-led Congress by using tools that the FCC already has at its disposal.[3] This is the "**Private Carriage Path to a Less Regulatory, More Market-Based Telecommunications Future**."

The private carriage legal classification is a game-changer for many businesses. Private carriers negotiate deals on an individualized basis with other companies. This allows private carriers to customize contract terms and offerings to meet the unique needs of their customers.

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[1] Chris Kaufman, *Republican Trump says 70 percent of federal regulations 'can go,'* REUTERS (Oct. 7, 2016), http://www.reuters.com/article/us-usa-election-trump-regulations-idUSKCN12629R.

[2] *See* 47 U.S.C. § 151.

[3] This approach is consistent with recent views expressed by Chairman Ajit Pai: "Going forward, I hope that the commission will do a much better job of respecting the rule of law. If we have a good idea that we don't have the power to put into practice, then we should ask Congress to give us that power." Ajit Pai, *Remarks of FCC Commissioner Ajit Pai Before the Free State Foundation's Tenth Anniversary Gala Luncheon* (Dec. 7, 2016); *see also* Jenna Ebersole, *FCC Republicans Want Course Correction, Process Fix*, LAW360 (Dec. 7, 2016), https://www.law360.com/articles/870242/fcc-republicans-want-course-correction-process-fix.

Because private carriers are subject to limited regulatory oversight, the market – and not the regulatory agency – is the final arbiter of the private carrier's actions and business opportunities. But private carriers do not enjoy an unencumbered regulatory landscape. Currently, there is a significant level of guess work and associated uncertainty involved when invoking the private carriage legal classification for a variety of reasons described in this White Paper. And for those companies taking advantage of private carrier exemptions, complications arise at every turn that hamper the benefits of private carriage status while unnecessarily exposing businesses to risks of financial and reputational harm at the hands of the Commission and administrators of various FCC programs.

With private carriage, the Commission is faced with a stark deregulatory opportunity available now, without procedural or political hoops. This White Paper describes the opportunity in detail. First, this White Paper explains the background of private carriage. Second, it examines the challenges that the industry faces when embracing the private carriage classification. Third, this White Paper urges the FCC to take specific, discrete actions to embrace private carriage more fully. Fourth, and finally, this White Paper concludes by analyzing the impact of the suggested solutions on various stakeholders in the industry. By following the steps outlined, the FCC can unleash the deregulatory potential of the private carriage classification.

PART ONE:

The Historical Purpose of Private Carriage and Reasons for its Advancement in the 21st Century Digital Economy

The law on private carriage, while well-settled, is neither well known by the telecommunications industry at large, nor was it well respected by the Commission or its universal service program administrators of the two prior administrations. Private carriers "make individualized decisions …whether and on what terms to deal."[4] Common carriers, on the other hand, "serve all potential customers indifferently."[5] Carriers may operate as private carriers with respect to some services and common carriers with respect to others.[6]

In determining a company's classification, courts have analyzed the following factors relating to the company's offerings to distinguish between services offered on a private and a common carriage basis:[7]

1. Contract Negotiations: Private carriers individually negotiate contract terms with customers. Common carriers, by contrast, offer services for set prices and terms.[8]
2. Length of Contracts: Private carriers are more likely to enter into contracts with a medium-to-long range term.[9]
3. Customers Involved: Private carriers enter into contracts with sophisticated business entities and stable clientele.[10] Customers of private carriers have unique communications requirements.

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[4] *Nat'l Asso. of Regulatory Util. Comm'rs v. Fed. Commc'ns Com.*, 525 F.2d 630, 641 (1976) ("*NARUC I*").

[5] *NARUC I*, 525 F.2d at 644 n.76.

[6] *See Nat'l Asso. of Regulatory Util. Comm'rs v. Fed. Commc'ns Com.*, 533 F.2d 601, 608 (1976) ("*NARUC II*"); *see also In re Audio Comm'cns, Inc.*, 8 FCC Rcd 8697, 8698-99 (1993) ("[A] single firm that is a common carrier in some roles need not be a common carrier in other roles.").

[7] *See, e.g., In the Matter of Philippine Long Distance Tel. Co.*, 12 FCC Rcd 15001 (1997); *Cellco P'ship v. F.C.C.*, 700 F.3d 534, 546-47 (D.C. Cir. 2012).

[8] *See In the Matter of Norlight*, Declaratory Ruling, 2 FCC Rcd 132, 133-34 (1987).

[9] *See id.*

[10] *See id.*

4. Tailoring: Private carriers tailor contracts and services to the special requirements of their customers.[11]

The private-common carriage distinction arose out of the Communications Act of 1934, which adopted requirements applicable to common carriers.[12] Congress preserved the distinction between common carriage and private carriage in the Telecommunications Act of 1996 ("the Act").[13] The Act aimed to promote competition dictated by market forces in place of heavy-handed government regulation,[14] and the private carriage classification was "consistent with and complementary to the deregulatory thrust of the" new Act.[15]

Specifically, private carriers are exposed to fewer regulations and less regulatory scrutiny than common carriers. Title II of the Act includes comprehensive regulatory requirements applicable exclusively to common carriers. With limited exceptions, these Title II common carrier regulations generally do not apply to private carriers. For example, private carriers contribute to the Universal Service

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[11] *See id.*

[12] *See* 47 U.S.C. § 153(h) (1988) (defining "common carrier").

[13] Specifically, the Act defined three service categories corresponding with differing regulatory treatment and classification. An "Information Service" is "the offering of a capability for generating, acquiring, storing, transforming, processing, retrieving, utilizing, or making available information via telecommunications . . ." 47 U.S.C. § 153 (24). Information services are largely unregulated. Classification as an information service generally exempts a service and a service provider from direct FCC regulation. "Telecommunications" is "the transmission, between or among points specified by the user, of information of the user's choosing, without change in the form or content of the information as sent and received." 47 U.S.C. § 153 (50). "Telecommunications" offerings are subject to some regulatory oversight. Providers that merely offer "telecommunications" (not "telecommunications services") are considered private carriers. "Telecommunications Service" is "the offering of telecommunications for a fee directly to the public, or to such classes of users as to be effectively available directly to the public, regardless of the facilities used." 47 U.S.C. § 153 (53). "Telecommunications service" offerings are subject to full Title II regulatory oversight. Providers of "telecommunications service" are considered common carriers. The Act also refers to "telecommunications carriers," defined as "any provider of telecommunications services." 47 U.S.C. § 153 (51). Telecommunications carriers are common carriers, but only to the extent that they are engaged in providing telecommunications services.

[14] *See generally* Peter Pitsch & Arthur Bresnahan, *Common Carrier Regulation of Telecommunications Contracts and the Private Carriage Alternative*, 48 Fed. Comm. L. J. 447, 450 (June 1996), available at http://www.repository.law.indiana.edu/cgi/viewcontent.cgi?article=1108&context=fclj ("The new law is the first broad and explicit legislative recognition that competition can provide a basis for rendering statutory requirements for telecommunications carriers obsolete."). One example of this deregulatory approach was the grant to the FCC of forbearance authority, allowing the agency to reduce regulation when competitive forces allowed and the public interest would be served. *See* 47 U.S.C. § 160; Pitsch, *supra,* at 450, 479-481. The FCC used forbearance to order detariffing in the early 2000s, and more recently, to reduce regulations imposed on broadband internet access service (BIAS) service providers. *See* Charles Helein, Jonathan Marashlian & Loubna Haddad, *Detariffing and the Death of the Filed Tariff Doctrine: Deregulating in the "Self" Interest*, 54 Fed. Comm. L. J. 281 (March 2002), available at http://www.repository.law.indiana.edu/cgi/viewcontent.cgi?article=1296&context=fclj; *In the Matter of Protecting and Promoting the Open Internet,* Report and Order on Remand, Declaratory Ruling, and Order, 30 FCC Rcd 5601, 5804 *et seq.* (2015).

[15] Pitsch, *supra* note 14, at 450.

EXAMPLES OF PRIVATE CARRIAGE:

#1: A carrier might enter into a wholesale agreement with another carrier to sell excess capacity on its network or to negotiate traffic exchange agreements.

#2: Provision of dedicated infrastructure for a specific business' mission critical applications, allowing for efficient management of infrastructure and network monitoring.

#3: A carrier operates a private wireless network for use by an electric, water, or natural gas utility, assisting the utility to meet specific operational needs and to support reliable delivery of services.

#4: Provision of other communications services on an individually negotiated basis where there is no change in the form or content of the information as sent or received.

Fund ("USF"), but are legally exempt from contributing to other universal service mechanisms established under Title II. Private carriers also enjoy less regulatory scrutiny at the state level by public utilities commissions.

Congress did not apply private carriage to all competitors in the communications marketplace. Instead, Congress endorsed a hybrid system where common carriage and private carriage would co-exist. A provider of telecommunications services is classified as a common carrier only to the extent that the company provides common carriage services.[16] Otherwise, to the extent that a company provides private carriage services, the company is able to take advantage of the private carrier classification. This hybrid system promotes two equally important aims:

- Public interest aims: The hybrid system maintains a public interest driven emphasis on essential services, interconnectivity, spread of basic infrastructure, and accessibility.

- Deregulatory aims: In the hybrid system, industry retains the freedom to design and implement tailored services. These services do not have the same nexus to the public interest and thus are not subject to as heavy a regulatory burden.

This dichotomy between private and common carriage honors the Act's emphasis on competition and market-based discipline as drivers of growth and innovation. In particular, the private carriage classification promotes the following competitive effects:

- Flexibility: Private carriage affords companies the flexibility and freedom to customize deals, including pricing, conditions of service, and choice of

[16] *See* 47 U.S.C. § 153 (51).

customers. In a free-market economy, flexibility to contract with other companies translates into mutually beneficial commercial arrangements.[17]

- Experimentation: Private carriage options empower market participants to develop and test compensation and service arrangements that may better accommodate individual market circumstances.[18]

- Modification: "Non-common carriage … enables parties to a contract to modify their arrangement over time as their respective needs and requirements change."[19]

- Leverage: Savvy customers can leverage competition among private carriers to obtain optimal quality and price for services purchased.[20]

- Risk Taking: Private carriers can work with customers to develop new products or applications despite risks involved, because the private carrier is not required to offer similar services or terms to other companies.[21]

- Competitive Pricing: Private carriage fosters competition, which generally leads to lower prices. Private carriers are also not required to list their service offerings or prices, because they instead negotiate contracts on a case-by-case basis. As a result, the private carriage marketplace is less likely to sustain price fixing that has been associated with knowledge of competitor prices.[22]

The next section addresses the challenges businesses face in taking advantage of private carriage classifications.

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[17] *See* Pitsch, *supra* note 14, at 473, 483-485; *see also Wireline Broadband Order*, 20 FCC Rcd 14853, 14899-14900 (Sept. 23, 2005), at ¶¶ 87-88.

[18] *See Wireline Broadband Order*, 20 FCC Rcd at 14899-14900.

[19] *Id.* at 14900.

[20] *See* Pitsch, *supra* note 14, at 473.

[21] *See id.*, at 484-485.

[22] Competitors in a common carriage market have access to each other's price details. *See* Pitsch, *supra* note 14, at 483; *In the Matter of Competition in the Interstate Interexchange Marketplace*, Notice of Proposed Rulemaking, 5 FCC Rcd 2627, 2644 (April 13, 1990), at ¶ 143 ("*IXC Competition NPRM*"). Detariffing did not change this dynamic in the telecommunications marketplace, because many previously tariffed common carriers must still maintain price and service offering details on their websites. *See* Helein, *supra* note 14, at 283. As Peter Pitsch explains, such knowledge facilitates collusive agreements, tacit collusion, detection of price cutting, and retaliation. *See* Pitsch, *supra* note 14, at 483.

PART TWO:

Barriers to Widespread Adoption of the Private Carriage Telecommunications Model

Specific barriers prevent full realization of the deregulatory benefits of private carriage. This section highlights a confluence of factors that have, in the experience of the authors, led many in the industry to avoid taking advantage of the private carriage classification.

#1: Uncertainty and Fear

The first barriers standing in the way of widespread adoption of the private carriage model are uncertainty and fear. While FCC law and decades-old judicial precedent provide a high-level framework for identifying common carriage services (whether the carrier "holds himself out to serve indifferently all potential users")[23], the result is somewhat of a patchwork that requires businesses to weigh and balance the facts which support adopting private carrier status against potentially serious financial and reputational risks of guessing wrong. The way the law on private carriage is presented to the industry simply does not provide the necessary degree of clarity and confidence needed to ensure the benefits of private carriage are realized to their full potential. For the risk-averse, the bottom line is that private carriage is not a feasible business model.

Currently, whether a provider has made a common carriage offering "must be determined on a case-by-case basis."[24] A variety of often unclear factors contribute to the regulatory classification analysis a business must conduct before reaching a decision whether to treat a particular offering as private or common carriage. Absent a bright-line test, the final arbiter of classification is too often an FCC enforcement official or an auditor working for the Universal Service Administrative Company ("USAC"), the administrator of the FCC's USF program. Meanwhile, the consequences of an incorrect decision are material in nature: exposure to years of unrecoverable contributions to Title II programs, enforcement

[23] *NARUC II,* 533 F.2d at 608; *see also U.S. Telecom Ass'n v. FCC*, 295 F.3d 1326, 1329 (D.C. Cir. 2002) ("[C]ommon carrier status turns on: (1) whether the carrier 'holds himself out to serve indifferently all potential users'; and (2) whether the carrier allows 'customers to transmit intelligence of their own design and choosing.'" (citation omitted)).

[24] *Bright House Networks, LLC, et al. v. Verizon California, Inc., et al.*, Memorandum Opinion and Order, 23 FCC Rcd 10704, 10717-19 (June 23, 2008), at ¶¶ 37-40.

actions, fines and penalties, and the reputational harm associated with becoming the target of a government investigation.

Without certainty in the form of definitive FCC guidance, companies will continue to view the private/common carrier classification as a somewhat futile exercise in risk management. It is no coincidence, then, that relatively few industry participants pursue broad private carrier business models. Some businesses taking advantage of private carriage options hedge their bets by simultaneously, and unnecessarily, subjecting themselves to Title II common carrier regulatory burdens – passing through the ultimate compliance costs to their sophisticated consumers – simply to mitigate risks. This current state of affairs hampers the effectiveness of the private carriage deregulatory solution. The Commission can act swiftly and definitively to offer certainty and clarity to businesses, while concurrently taking well-deserved recognition for reducing unnecessary and harmful regulatory burdens.

#2: Uneven Application

A second barrier arises from the uneven application of the private /common carriage precedent at the FCC, as applied to companies providing services with Voice over Internet Protocol ("VoIP") components. Broadly speaking, interconnected VoIP services are not eligible for the private carriage classification.[25] The result is that interconnected VoIP providers offering services with identifiable private carriage qualities are at a regulatory disadvantage as compared with traditional telecommunications competitors who enjoy private carrier status.

This uneven treatment actually originates from a generally favorable public policy for the VoIP industry.[26] Over a decade ago, the FCC chose not to apply full common carriage regulatory responsibilities to interconnected VoIP services, but to instead selectively extend specific regulations to interconnected VoIP.[27] As a result, interconnected VoIP services received relaxed regulatory treatment as compared with services provided on a common carriage basis. The drawback to

[25] Interconnected VoIP is defined as a service that: (1) Enables real-time, two-way voice communications; (2) Requires a broadband connection from the user's location; (3) Requires Internet protocol-compatible Customer Premises Equipment ("CPE"); and (4) Permits users generally to receive calls that originate on and to terminate calls to the PSTN. 47 C.F.R. § 9.3.

[26] Interconnected VoIP services were not, and have never been, classified as common carrier services or subjected to the full range of Title II requirements. *See, e.g., In the Matter of IP-Enabled Services; E911 Requirements for IP-Enabled Service Providers*, First Report and Order and Notice of Proposed Rulemaking, 20 FCC Rcd 10245, FCC 05-116 (May 19, 2005); *In the Matter of Universal Service Contribution Methodology*, Report and Order and Notice of Proposed Rulemaking, 21 FCC Rcd 7518, FCC 06-94 (June 21, 2006).

[27] *See, e.g., id.*

this approach has been that an interconnected VoIP service with private carriage qualities is treated no differently than any other interconnected VoIP service. Simply put, whereas private carrier telecommunications companies enjoy benefits of lesser regulation over their common carrier telecommunications services competitors, all interconnected VoIP is created equal.

This regulatory framework disadvantages systems integrators in particular.[28] Systems integrators package together component subsystems, ensure these subsystems function well together, and sell the entire package as a bundled solution, usually to enterprise customers. As an example, a systems integrator may package a communications service with a larger data, IT, or technical support solution and sell the package to a customer.

The FCC has recognized for two decades that regulatory barriers have no place in the systems integrator industry, but the rules are unevenly applied in the interconnected VoIP context. Currently, if a systems integrator bundles a traditional telecommunications service with non-telecommunications offerings, the entire bundle can be treated as a private carriage service, thus usually eliminating any Title II regulatory obligations. Additionally, another traditional systems integrator exemption frees many systems integrators from contributing to the USF.[29] But if the same systems integrator bundles a newer technological solution with an interconnected VoIP component with its systems integrator offerings, the entire bundle will be regulated as an interconnected VoIP service, and the exemptions may not apply.

#3: USAC Policies Prevent Common-Private Carriage Revenue Segregation

A third barrier to reliance on the private carriage model stems from the lack of enforcement of the private carriage exemption at USAC. Longstanding precedent exempts private carriers from contributing to non-USF Title II programs, which

[28] *See* Jonathan Marashlian & Seth Williams, *Principles of Neutrality Missing from FCC Systems Integrator Exemption Rules*, TECHZONE360 (March 24, 2015), http://www.techzone360.com/topics/techzone/articles/2015/03/24/400207-principles-neutrality-missing-from-fcc-systems-integrator-exemption.htm; *In the Matter of Petition of The Commpliance Group, Inc. for a Declaratory Ruling that the Systems Integrator Exemption Applies to the Resale of Provision of Interconnected VoIP by Systems Integrators*, Docket No. 06-122 (Mar. 17, 2015), available at https://prodnet.www.neca.org/publicationsdocs/wwpdf/31815compliance.pdf.

[29] In 1997, the FCC created an exemption for systems integrators by freeing "non-common carriers that obtain a *de minimis* amount of their revenues from the resale of telecommunications" from filing Form 499 and contributing directly to the Universal Service Fund. *In re Federal-State Joint Board on Universal Service; Access Charge Reform, Price Cap Performance Review for Local Exchange Carriers, Transport Rate Structure and Pricing, End User Common Line Charge,* Fourth Order on Reconsideration, 13 FCC Rcd 5318, 5471-75 (1997). For purposes of the exemption, "*de minimis*" is five percent of revenue. *Id.*

include the Telecommunications Relay Services ("TRS") Fund, Local Number Portability ("LNP") administration, and the North American Numbering Plan ("NANPA") program.[30] In contrast, common carriers are required to contribute to these support mechanisms.[31] But USAC has not provided a sure mechanism for separating common carriage and private carriage revenues earned by companies providing both types of services, to enable them to take advantage of the exemption with respect to private carriage revenues.

Specifically, carriers report revenue for purposes of contributing to the universal service programs on the Form 499. USAC collects the Forms 499 and administers the USF, whereas each of the other Title II funds (NANP, LNP and TRS) is administered by a separate non-governmental agency. USAC passes along FCC Form 499 revenue data to the administrators of the other Title II program funds to calculate and invoice provider contribution obligations based only on the provider's self-reported primary service category (from Line 105 on Form 499-A).[32] The primary service category in turn is reported based on the service that generates the most revenue for the company. Thus, the result is that a company with more common carriage service revenues than private carriage service revenues is treated as if *all* revenues are subject to the non-USF Title II fees and ineligible for the private carriage exemption. Common carriers with some private carriage revenues have been over-billed as a result. The same is true in the other direction: private carriers with some common carriage revenues could be under-billed.

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[30] *See* 47 C.F.R. 52.17, 52.32, 54.706, 64.604.

[31] *See* 47 C.F.R. § 64.604(c)(5)(iii)(A) (requiring providers of "interstate telecommunications services" to contribute to TRS); 47 C.F.R. § 52.32(a)(requiring LNP contributions "from all telecommunications carriers providing telecommunications service ..."); 47 C.F.R. § 52.17 ("All telecommunications carriers in the United States shall contribute on a competitively neutral basis to meet the costs of establishing numbering administration."). The Commission has ruled that the terms "common carrier" and "carrier" are synonymous with the term "telecommunications carrier" for the purposes of the Act and the FCC's rules. *In re AT&T Submarine Sys. Inc.,* File No. S-C-L.94-006, Mem. Opinion & Order, 13 FCC Rcd 21585, 21587-88 (1998), at ¶ 6 ("As the Commission has previously held, the term 'telecommunications carrier' means essentially the same as common carrier."); *see also Virgin Islands Telephone Corp. v. FCC,* 198 F.3d 921, 922, 926 (D.C. Cir. 1999) (affirming the FCC's conclusion that the terms "telecommunications carrier" and "common carrier" are synonymous for the purposes of the Act and the FCC's rules). The Commission has nonetheless required both common carriers and private service providers to contribute to USF. *See Federal-State Joint Board on Universal Service*, CC Docket No. 96-45, 12 FCC Rcd 8776, 9183-84 (1997), at ¶ 795; *In the Matter of Federal-State Joint Board on Universal Service*, *Report to Congress*, CC Docket No. 96-45, 13 FCC Rcd 11501, 11548-11549 (1998), at ¶ 98.

[32] *See In the Matter of Locus Telecommunications, LLC,* Petition for Declaratory Rulings Relative to the Treatment of Private Carriage Revenues, Docket No. 06-122 (Nov. 22, 2016) (petitioning the FCC to clarify how carriers with private carriage and common carriage revenues can separate their revenue reporting on FCC Form 499 to avoid payment of Title II fees on private carriage revenues), available at https://ecfsapi.fcc.gov/file/112276489876/ FINAL%20Petition%20for%20Declaratory%20Ruling%20Locus%20USAC%20Policy%20Revised.pdf.

This revenue reporting structure is inconsistent with the history of the private / common carriage distinction, which has always held that companies may operate as private carriers with respect to some services and as common carriers with respect to others.[33] To change this precedent would inevitably require companies to separate operations by classification to avoid payment of common carrier fees on private carriage revenues.

Conclusion: Barriers to Private Carriage Adoption Have Diminished Availability of Benefits Envisioned by Congress

To the extent that uncertainty and risk aversion have watered down the benefits to the industry of the private carriage classification, these realties have hampered true implementation of Congress's deregulatory aims defined in the 1996 Telecommunications Act. In the next section, this White Paper describes discrete actions the FCC can take to propel private carriers to compete and innovate through enforcement and clarification of private carriage laws already on the books.

[33] *NARUC II,* 533 F.2d at 608.

PART THREE:

Unleash Growth through Certainty for Private Carriers

At this time of new energy around deregulatory opportunities, the FCC has an opportunity to effect positive, lasting change. By clarifying and supporting private carriage, the Commission can promote new business opportunities while relieving itself and its Title II program administrators of regulatory oversight and administrative burdens associated with business-to-business transactions that are beyond the agency's public interest mission. The aim is not to roll back the important progress the FCC has made to expand universal access to communications technologies and to promote public interest aims in the provision of telecommunications service. Instead, the FCC should yield to boundaries already drawn by Congress, the courts and earlier Commissions, but which have become hazy by lack of enforcement under the past two administrations. The FCC can restore clarity to the classification distinction between a common carriage service and a private carriage service quickly and without risk of judicial delay by taking the actions detailed below. This section offers specific, tangible solutions immediately available to the Commission to tear down the barriers earlier described and unleash the full potential of the private carrier exemption from Title II regulations.

#1: Issue a Private Carriage Policy Statement

To combat uncertainty regarding the private carriage classification, the FCC should first and foremost set the record straight by issuing a policy statement that clarifies and lists the elements of private carriage. By endorsing these factors and listing them in one place, the FCC will send signals to the market that the agency is enforcing the laws on the books. This simple approach will have immediate consequences in the industry. Armed with a clear understanding of the rules, businesses will be better equipped to classify their own services and to reduce risk from unintended classification errors. In turn, a private carriage policy statement will lower costs and barriers to entry for service providers serving enterprise customers, resulting in more vibrant competition and a more level playing field.

#2: Resolve Outstanding Petitions in Favor of Clarity for Private Carriers

The FCC should take steps to resolve outstanding petitions for regulatory parity in matters relating to private carriage. By addressing petitions relating to the systems

integrator exemption[34] and USAC's handling of the private carrier Title II fee exemption,[35] the FCC will make significant progress towards eliminating doubt and confusion faced by private carriers.

The first pending petition asks the FCC to clarify that the systems integrator exemption applies to interconnected VoIP services, not just to legacy telecommunications services. The underlying rationale for this petition is regulatory parity. Systems integrators incorporating traditional telecommunications today are largely unregulated as a result of both the systems integrator exemption and the private carriage classification. Neither option is available to a systems integrator incorporating interconnected VoIP. From a regulatory standpoint, the optimal approach for systems integrators has been to avoid integrating new interconnected VoIP technologies to avoid heavy regulatory burdens that the FCC recognized two decades ago had no place in the systems integration arena. Clarity on this regulatory issue would give the industry an incentive to upgrade to VoIP technologies, inevitably driving growth in the industry.

More broadly, the systems integrator situation highlights the need for the FCC to consider affording interconnected VoIP companies the option to take advantage of the private carriage classification. Clearly, if interconnected VoIP companies are to lead the next generation of telecommunications innovation, these companies should have access to the same deregulatory opportunities as traditional telecommunications players. Ultimately, a final determination on this issue would require a rulemaking garnering input from stakeholders.

A second pending petition relates to confusion around USAC's handling of the private carrier Title II fee exemption. USAC has not offered service providers a method for separating private and common carriage revenues via the Form 499. In so doing, USAC has impermissibly charged non-USF, Title II fees based on private carriage revenues, effectively ignoring the private carrier Title II fee exemption. Companies with both common and private carriage revenues have therefore either over or under paid Title II fees as a result.

This financial hardship on companies is not the only effect of USAC's policy, however. More importantly, USAC's handling of the private carrier Title II fee exemption violates precedent dictating that a carrier can freely decide to offer either or both common carriage services and private carriage services. Companies should not have to choose one or the other – they should be free to offer services to

[34] *See supra* note 28.

[35] *See supra* note 32.

the public indifferently and to innovate and experiment by offering private services on their own terms. USAC's policy disrupts the entire premise of the private carriage classification: that the marketplace should govern private deals, and that companies must be free to contract on a private basis. Resolving this second petition will thus restore the original intention of the private carriage classification.

#3: Commit to Principles of Business Freedom in the Private Carriage Marketplace

The incoming FCC has an opportunity to re-dedicate the agency to the deregulatory principles of the 1996 Act. In this spirit, the FCC must not merely clarify and reinforce the existence of the private carriage classification, but commit to the market-based framework upon which private carriage is premised. Otherwise, private carriers face unending uncertainty. Should they negotiate business deals and draft contractual terms in anticipation of FCC or USAC scrutiny? Should they model their service distribution methods to avoid unanticipated regulatory exposure, including for their business partners? Will the FCC and USAC accept the terms of contracts or the outcome of litigation, or do regulators reserve the right to investigate on their own terms? Clearly, common carriers operating in the highly-scrutinized telecommunications industry know that they face exposure from the FCC for their business decisions at all times. In contrast, the answer to these questions is not readily available for private carriers. FCC law and precedent proclaim these private carriers as largely deregulated, but in reality, private carriers too often remain exposed to regulatory uncertainty and risk.

To tackle this uncertainty in the interests of protecting and promoting the private carriage classification, the FCC should publicly and categorically recognize the role of two key principles of business freedom in the private carriage marketplace.

First, the FCC must commit to full deregulation as envisioned in the private carriage precedent. Regulating a fully de-regulated industry is messy and complicated, and hampers the effect of underlying deregulatory policy aims. Regulated industries by definition require continuous monitoring by the regulatory agency. But deregulated industries cannot sustain irregular interventions where government effectively picks winners and losers. The FCC and even USAC must defer to the greatest extent possible to decisions made by private carriers with other sophisticated businesses. The FCC should instead expend its limited resources focusing on issues impacting the mass market of consumers, putting limited federal monetary resources where most needed to protect the most vulnerable.

Second, the FCC must set a clear policy of recognizing negotiation, contracts, and litigated remediation as the foundations of the private carriage ecosystem. Across the economy, sophisticated businesses use these three tools when implementing, structuring, maintaining, and enforcing business deals. Private carriage in the telecommunications industry should be no different. Accordingly, the FCC and USAC should at all times respect negotiated business decisions. In evaluating business arrangements, these agencies should look to the terms of binding contracts to understand business deals rather than engage in independent analyses or evaluate independent factors. Auditors should assess responsibility and agency in business arrangements based on the intent of governing contracts. As to disputes, these agencies should defer to courts or private dispute resolution rather than open enforcement or market disputes proceedings.

By committing to these principles of business freedom in the private carriage marketplace, the FCC will provide private carriers ever more incentive to rapidly develop new commercial arrangements with a growing list of business partners. Unhampered by regulatory uncertainty, private carriers will be better able to focus on investment in new partnerships and distribution channels, strengthening competition in the market and increasing the speed of deployment of services.

PART FOUR:

Conclusion

The FCC has the tools at its disposal to promote the deregulatory aims of the 1996 Act by clarifying the regulatory landscape encountered by private communications carriers. But should it? Clearly, as with any public policy decision, the FCC has a number of interests to weigh:

- ### Private Carriage Industry

For companies that knowingly or unknowingly provide their services on a private carriage basis, any action by the FCC to clarify their responsibilities and to remove regulatory doubt is a worthy investment of time and resources. Regulatory clarity promises to remove guesswork that hampers investment and discourages ambition. Companies should not fear economic reprisal for guessing wrong on how the private carriage system works. Quite to the contrary, private carriers must be able to take advantage of the deregulatory law and precedent on the books that favors their legal and economic interests.

- ### Public Interest Mission of the FCC

This deregulatory approach does not deter the public interest mission of the FCC. Right now, the FCC's law and precedent exempts private carriers from many regulations. Broadly, the FCC imposes a hybrid regulatory system, where common carriers providing services that impact the public interest are regulated whereas private carriers are largely unregulated. Maintaining and clarifying this system is consistent with the directives of Congress and does not disturb regulation on the common carrier side of the equation.

Critics may argue that reinforcing the common/private carrier dichotomy would decrease funding needed to support critical FCC programs. Admittedly, if the FCC goes down the road of allowing all interconnected VoIP carriers to take advantage of private carriage classification, the FCC will need to address the impact on funding in a rulemaking. Otherwise, any funding currently collected from private carriers incorrectly contributing to regulatory funds are undeserved and unfair. The FCC may choose to balance its books in a number of ways, but first should ensure that its current rules are closely enforced and clearly defined.

As an aside, if the FCC follows through with the recommendations in this White Paper, it will not be required to expend as many resources on the private carriage

industry. The FCC may consider analyzing whether potential savings from reduced regulatory oversight may offset any reductions in collected funding.

- **Business Customers of Private Carriage Services**

Buyers of private carriage services stand to gain from a more competitive marketplace for individualized telecommunications solutions. With fewer regulatory barriers, private carriers will be incentivized to expand business relationships, offer more competitive options, and take more risks. Sophisticated business customers would benefit from the availability of new, tailored options that open in the marketplace.

- **Regulatory Parity**

The proposals in this White Paper are targeted at improving regulatory parity, both with regard to the private carrier Title II fee exemption and the interconnected VoIP exception to private carriage exemplified by treatment of systems integrators. Regulatory parity promotes clarity and consistency in the industry, helping regulated entities better understand and carry out their regulatory obligations.

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By providing certainty to private carriers using the proposals in this White Paper, the FCC has an opportunity to improve the position of a number of market participants while furthering its public policy goals. These economic benefits are achievable by means of the deregulatory approach to competition already codified in law.

This is what deregulation should be about: promoting market discipline in areas where regulation is unnecessary and where competition already promotes innovation, investment, and job creation. Today, private carriage has not been given a chance with so much uncertainty surrounding its meaning and rules. The FCC has the tools at its disposal right now to correct course and free private carriers to grow within the confines of the free market. The only question that remains is whether the FCC will accept this unique invitation to reimagine the potential of the private carriage industry.