

Summary of the Supreme Court's Decision in *National Cable & Telecommunications Association v. Brand X Internet Services* and *FCC v. Brand X Internet Services*

June 27, 2005

Washington, DC—On June 27, 2005, the Supreme Court of the United States in a 6-3 decision, upheld a Declaratory Ruling of the Federal Communications Commission ("FCC" or "Commission") classifying broadband Internet access provided by cable companies (referred to as "cable modem service") as an "information service" that does not include a separate "telecommunications service" component. Justice Thomas authored the majority opinion, which was joined by Justices O'Connor, Rehnquist, Kennedy, Breyer, and Stevens. Justices Breyer and Stevens, while joining the majority opinion, filed separate concurring opinions, and Justice Scalia (joined in part by Justices Souter and Ginsburg) dissented.

Under the Court's decision, cable modem service will be exempt from the mandatory common carrier obligations that apply to all providers of "telecommunications services" under Title II of the Communications Act. Cable modem service will also be exempt from the wholesale access and network disclosure and architecture requirements of the FCC's *Computer Rules*. The Court's decision leaves open the question how broadband services provided by competitors to the cable companies, most significantly wireline telephone companies (referred to as digital subscriber line or "DSL" and, more recently, fiber-to-the-premises or "FTTP"), should be classified and regulated. Although the Court's opinion at least hints that parity of regulatory treatment is required, the Court expressly reserved the issue of the proper statutory classification and regulatory treatment of other broadband services and DSL in particular.

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Thus, the proper statutory classification of DSL and video services that are delivered over upgraded telecommunications networks will have to await further Commission proceedings. The good news is that the Court made quite clear that those issues will be decided by the FCC, based on traditional product and market analysis, and that the Commission enjoys broad discretion to place an integrated bundle of services including "pure transmission" in the deregulatory world of Title I.

Standard of Review

The *Brand X* case came to the Supreme Court from the United States Court of Appeals for the Ninth Circuit, which had previously held in a case where the FCC did not take a position on the issue that the Communications Act *required* the recognition of a "telecommunications service" within facilities-based broadband Internet access provided by cable operators. See *AT&T Corp. v. City of Portland*, 216 F.3d 871 (9th Cir. 2000). The *Portland* decision meant that all broadband services were presumptively subject to Title II common carrier regulation, including tariff, interconnection, and wholesale access requirements.

Following *City of Portland*, the FCC released a Notice of Inquiry seeking comment regarding how cable modem service should be classified and regulated. In the Declaratory Ruling that followed, the Commission determined that cable modem service should be classified as an "information service" and thus exempt from Title II common carrier requirements. Reviewing that decision in *Brand X*, the Ninth Circuit declined to apply the traditional *Chevron* analysis that ordinarily governs appellate review of administrative agency decisions, instead determined that it was bound by its previous decision in *City of Portland*, and thus reversed the FCC's Declaratory Ruling.

The Supreme Court found that the Ninth Circuit had erred by refusing to apply the *Chevron* analysis. The Court held that a prior court decision will only preclude application of *Chevron* principles to a subsequent administrative agency decision if that decision held the relevant statutory provision to be unambiguous within the meaning of *Chevron* step one.

Classification of Cable Modem Service

The Court proceeded to analyze under *Chevron* the FCC's determination in the Declaratory Ruling that cable modem service does not include a separate "telecommunications service" component. The Court found the Commission's decision to be a permissible construction of the statute, and thus reversed the Ninth Circuit's ruling to the contrary.

- **Cable Modem Service Does Not Include an "Offering" of Telecommunications to the Public and thus Does Not Contain a "Telecommunications Service" Component:** The Court first noted that "telecommunications service" is defined as "the offering of telecommunications for a fee directly to the public." In its Declaratory Ruling, the FCC had found that while cable companies use "telecommunications" to provide consumers with Internet service (as all Internet service providers do), whether cable modem service included a separate "offering" of telecommunications to the public depended on the nature of the functions delivered to the end-user. From the consumer's point of view, the Commission had concluded, cable modem service does not include an "offering" of

telecommunications because the consumer always uses the high-speed connection along with the other information-processing capabilities provided by Internet access, and because the transmission is a necessary component of Internet access service. The Court agreed with these determinations, finding that the FCC reasonably construed an "offering" as used in the statutory definition of "telecommunications service" to mean a "stand-alone" offering of telecommunications to the public. The Court also determined that the Commission reasonably found that because cable modem service providers do not offer telecommunications separate and apart from integrated Internet access service, they do not provide a "telecommunications service." This ruling suggests that the FCC will have broad discretion to find that integrated service offerings that could be viewed as containing separate identifiable services within them (e.g., a Title VI cable service packaged with information services and a broadband transmission function) can be treated as a single service and placed under the generally deregulatory rubric of Title I.

- **The FCC's Conclusion is Consistent with the Definitions of "Basic" and "Enhanced" Services that Pre-date the Addition of the "Telecommunications Service" and "Information Service" Definitions to the Communications Act:** The Court next found that the FCC's conclusion that cable modem service lacks a separate "telecommunications service" component is consistent with the distinction between "basic" and "enhanced" services that pre-dated the addition of the "telecommunications service" and "information service" definitions to the Communications Act.

First, the Court noted that the basic/enhanced service distinction was based on a functional analysis, focused upon how the consumer interacts with information, and that only a "pure" transmission service was deemed to be a basic service under that distinction. The Court found that the FCC's determination in its Declaratory Ruling that the term "telecommunications service" describes a "pure" or "transparent" communications path that is not separately present (from the end-user's perspective) in cable modem service, which is an integrated Internet service offering, was consistent with the basic/enhanced service dichotomy.

Second, the Court found that under the basic/enhanced service distinction, the mere provision of transmission service alone was not sufficient to subject a service provider to common carrier treatment. Thus, the Court rejected the arguments of certain parties that all information services that include a telecommunications component must be classified as "telecommunications services" because such a classification would subject entities that the Commission had never before regulated as common carriers to common carrier treatment. The Court was not willing to accept the proposition that, in adding the definition of "telecommunications service" to the Communications Act, Congress intended to radically alter FCC policy.

Third, the Court rejected arguments that the basic/enhanced service regime-under which the Commission regulates facilities-based providers of enhanced services more heavily than their non-

facilities-based counterparts (pursuant to the so-called *Computer Rules*)-compelled the FCC to regulate cable modem service providers more heavily because they own the facilities used to provide Internet access service. The Court agreed with the Commission's conclusion that Congress did not mean to freeze in time the pre-existing regulatory regime. Further, the Court found that the FCC had imposed the *Computer Rules* based on the unique competitive characteristics of the enhanced services market that existed in the 1970s and 1980s, and that the same characteristics do not exist in today's competitive broadband market.

- **The Commission's Determination Will Not Allow Evasion of Common Carrier Duties:** In its briefs to the Supreme Court, MCI had argued that the FCC's classification of broadband Internet access as an "information service" would allow a carrier to evade common carrier duties simply by bundling an information service with a telecommunications service. The Court found that the FCC did not say in its Declaratory Ruling that any telecommunications service that is priced or bundled with an information service is automatically exempt from common carrier regulation under Title II. Thus, the Court found it unnecessary to address whether the FCC *could* reasonably reach such a conclusion.
- **The FCC's Current Treatment of DSL as a Common Carrier Service Does Not Require Reversal:** MCI also had argued that the FCC's current treatment of DSL as containing a separate "telecommunications service" component subject to common carrier regulation was arbitrary and capricious and required reversal of the Commission's Declaratory Ruling. The Court concluded that the FCC had arrived at its current regulatory treatment of DSL "based on . . . history, rather than on an analysis of contemporaneous market conditions" and that the Commission reasonably found in the Declaratory Ruling that "changed market conditions"-namely the fact that "substitute forms of Internet transmission exist today"-warrant different treatment of facilities-based cable companies providing Internet access." The Court declined to address whether the FCC's rationale for exempting cable modem service providers from common carrier treatment applies with similar force to DSL providers. At the same time, the Court noted that "[t]he Commission's decision appears to be a first step in an effort to reshape the way the Commission regulates information-service providers" and pointed to the FCC's tentative conclusion in a pending proceeding that "DSL service provided by facilities-based telephone companies should also be classified solely as an information service."

Impact on Other Broadband Services

While, as noted above, the Supreme Court expressly did not reach the question of how broadband services other than cable modem services should be classified and regulated, the opinion strongly suggests that all such services should be classified in a similar fashion and should be minimally regulated. As was the case with respect to the FCC's Declaratory Ruling itself, each of the substantive bases provided for the Court's determination that the FCC properly classified cable modem service as an "information service" without a separate "telecommunications service" component applies with equal force to broadband services offered by

other providers. For example, most such services (including wireline, powerline, and satellite) consist of a "single, integrated offering" to end-users. In addition, the "changed market conditions" that the FCC found (and the Court agreed) "warrant different treatment of facilities-based cable companies providing Internet access," which include "substitute forms of Internet transmission" in the form of "multiple electronic platforms," apply equally to all participants in the competitive broadband market. Furthermore, the decision gives the FCC broad discretion to find that a package or bundle of services-which includes services that *could* be seen as separate services under Title II, III, or VI-can be treated as an integrated service that is properly classified under Title I. FCC Chairman Kevin Martin's statement on the release of the decision- which pledges to provide a uniform framework to "all providers" and to "move forward quickly" to accomplish this goal-indicates the Commission's understanding that the decision has implications beyond the cable modem service context.

Separate Opinions

Justice Stevens' Concurrence: Justice Stevens joined in the majority opinion but wrote a separate concurrence to express his view that, while a prior appellate level court decision does not conclusively foreclose an administrative agency from subsequently adopting a contrary conclusion unless the prior decision states that the statute at issue is unambiguous, the same might not be true with respect to a decision of the Supreme Court.

Justice Breyer's Concurrence: Justice Breyer also joined in the majority opinion but wrote separately to disagree with Justice Scalia's characterization of the Court's precedent regarding an administrative agency's ability to adopt a conclusion that is contrary to a prior court decision.

Justice Scalia's Dissent (Joined by Justices Souter and Ginsburg): Justice Scalia in his dissent concluded that the FCC exceeded the bounds of statutory authority and unreasonably found that cable modem service providers do not "offer[]" telecommunications service to the public because, in his view, end-users *do* perceive that they receive an independent offering of transmission service. Justice Scalia also stated that the majority provided too great a power to the Commission to interpret its governing statute. Finally, the dissent charged the majority with altering the relationship between courts and agencies by allowing judicial decisions-here, referring to *City of Portland*-to be reversed by executive officers.

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