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State Executive Orders Reimposing Net Neutrality Regulations Are Preempted by the *Restoring Internet Freedom Order*

by

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Introduction and Summary

The *Restoring Internet Freedom Order* (2017) repealed public utility regulation of broadband Internet services and reclassified those services as information services largely unregulated by the Federal Communications Commission. The FCC thereby established a free market-oriented national framework based on the deregulatory goals of the 1996 Telecommunications Act. Relying on Congressional policy, agency precedent, and Supreme Court jurisprudence, the Order expressly preempted any measure that effectively would reimpose the repealed rules at the state level.

Governors in Montana and New York have issued executive orders regarding state contracting as a roundabout way of reimposing repealed public utility-like regulation. Both attempts to establish statewide "net neutrality" regulatory regimes run afoul of the FCC's order and federal preemption principles. The New York and Montana executive orders are not narrowly confined to proprietary interests of their governments but instead are "tantamount to regulating" on a statewide basis broadband Internet service providers' (ISPs) conduct. Because both executive orders are inherently regulatory and seek to advance the repealed net neutrality restrictions as

general policy ends, they fail to qualify for immunity from preemption under the Supreme Court's market-participant doctrine. In short, federal law provides the FCC with ample authority to preempt both state executive orders.

Although ostensibly based on state procurement authority and proprietary roles, the Montana and New York executive orders expressly apply to broadband ISP conduct regarding all end user consumers within their states. Specifically, to be eligible to enter into public contracts with their state governments, ISPs in Montana and New York must agree to adhere to net neutrality restrictions identical to those that were repealed in the *Restoring Internet Freedom Order*. Those include no-blocking, no-throttling, and no paid prioritization rules. The Montana executive order adds the no-unreasonable discrimination rule as well as repealed transparency requirements, and it charges the Montana Department of Administration with interpreting and enforcing those rules. Unmistakably, the New York and Montana executive orders seek to reimpose net neutrality restrictions as statewide policy despite the FCC order's expressly stated intent to "preempt any state or local measure that would effectively impose rules or requirements that we have repealed or decided to refrain from imposing."

Further, both executive orders fail to satisfy the market-participant doctrine recognized by the Supreme Court in cases such as *Building & Construction Trades Council v. Associated Builders & Contractors of Massachusetts/Rhode Island, Inc.* (1993) and *Wisconsin Department of Industry v. Gould Inc*. (1986). The market-participant doctrine is rooted in a concern that state governments may attempt to conduct proprietary functions in ways unrelated to their proprietary interests and thereby alter the conduct of private actors in the market. Such conduct by state governments can result in *de facto* regulation and thwart congressional policies.

The market-participant doctrine immunizes from federal preemption state government actions in the marketplace that are narrow and consistent with the actions of ordinary private actors in the market. But broadband Internet access services are mass-market retail services. Broadband ISPs do not make their network management practices and engineering decisions subject to arms-length negotiation with end user consumers. The net neutrality requirements contained in the New York and Montana executive orders amount to a demand that broadband ISPs must alter or restrict the network and business-wide practices for their mass-marketed retail service.

Further, it is obvious that ordinary end user consumers in the broadband Internet access services market do not negotiate how their broadband ISP treats other end-user consumers. However, that is what the New York and Montana executive orders do by requiring that broadband ISPs seeking to enter into contracts with those states must agree to adhere to net neutrality restrictions regarding all of their end user subscribers in their states.

On their face, both the New York and Montana executive orders reveal their primary goal to be promoting net neutrality regulation as a general policy. Unmistakably, both executive orders are "tantamount to regulation," as they are clearly and specifically intended to impose net neutrality regulation. Allegedly proprietary actions by state governments that are regulatory in nature and aimed at promoting broad social policy goals do not receive immunity from preemption under the market-participant doctrine.

The *Restoring Internet Freedom Order* stressed that allowing state governments to adopt their own separate requirements could "impose far greater burdens than the federal regulatory regime," "significantly disrupt the balance" struck by the federal regime, and "impair the provision of such service by requiring each ISP to comply with a patchwork of separate and potentially conflicting requirements across all of the different jurisdictions in which it operates." The New York and Montana executive orders undoubtedly would impose greater regulatory burdens than the *Restoring Internet Freedom Order*'s balanced approach consisting of FCC transparency requirements and Federal Trade Commission enforcement against unfair and deceptive trade practices by broadband ISPs. Indeed, the New York and Montana executive orders would impose the same heavy regulatory burdens that the FCC's order sought to remove in favor of a deregulatory policy.

The restrictions on broadband ISPs contained in the New York and Montana executive orders conflict with the *Restoring Internet Freedom Order*'s reliance on the congressionally approved "preemptive federal policy of nonregulation for information services." The FCC's order concluded that "it is impossible or impracticable for ISPs to distinguish between intrastate and interstate communications over the Internet or to apply different rules in each circumstance" and that "any effort by states to regulate intrastate traffic would interfere with the Commission's treatment of interstate traffic." Both state executive orders also clash with those FCC policy pronouncements. Statewide reimposition of net neutrality restrictions on broadband ISPs would affect network engineering and other aspects of their services in a manner that would conflict with and unavoidably affect service in other states, all the while posing serious technological and other practical obstacles for broadband ISPs.

Given the solid preemptive authority behind the *Restoring Internet Freedom Order* and given the clash with federal deregulatory policy for interstate broadband Internet access services like the interstate broadband Internet access services that are the subject of the New York and Montana executive orders, the FCC should be in a position to preempt them.

Finally, it should be noted that, aside from the FCC's authority to preempt, there is a whole separate line of authority not discussed here under the Dormant Commerce Clause jurisprudence that, as a constitutional matter, likely would invalidate the state executive orders and similar state actions.

The *Restoring Internet Freedom Order* Has Preemptive Authority

In the *Restoring Internet Freedom Order* the FCC reclassified broadband information access services as largely nonregulated Title I information services. To that end, the Order expressly states the FCC's intent to "preempt any state or local measure that would effectively impose rules or requirements that we have repealed or decided to refrain from imposing." Among other things, this precludes states from requiring broadband Internet access service providers to adhere to the no-blocking, no-throttling, no-paid prioritization, and no-unreasonable discrimination rules that were repealed.

As paragraph 194 of the *Restoring Internet Freedom Order* correctly points out: "Federal courts uniformly have held that an affirmative federal policy of *de*regulation is entitled to the same

preemptive effect as a federal policy of regulation." The FCC's order cites, for instance, the Supreme Court's holding in *Arkansas Electric Cooperative Corp. v. Arkansas Public Service Commission* (1983): "[A] federal decision to forgo regulation in a given area may imply an authoritative federal determination that the area is best left *un*regulated, and in that event would have as much pre-emptive force as a decision *to* regulate." The order also cites *Minnesota Public Utilities Commission v. FCC* (8th Cir. 2007), which concluded that "deregulation" is a "valid federal interest[] the FCC may protect through preemption of state regulation."

The FCC based the preemptive authority of its order primarily on the "impossibility exception to state jurisdiction." The Supreme Court recognized that exception in *Louisiana Public Service Commission v. FCC* (1986), where it ruled: "FCC pre-emption of state regulation [has been] upheld where it was *not* possible to separate the interstate and intrastate components of the asserted FCC regulation." Lower courts have applied the impossibility exception in many relevant circumstances since then. Accordingly, the *Restoring Internet Freedom Order* concluded that "it is impossible or impracticable for ISPs to distinguish between intrastate and interstate communications over the Internet or to apply different rules in each circumstance" and that "any effort by states to regulate intrastate traffic would interfere with the Commission's treatment of interstate traffic."

Additionally, the FCC based its preemptive authority on the Congressionally approved "preemptive federal policy of nonregulation for information services." In bolstering that separate source of preemptive authority, the order cited provisions such as Section 230(b) of the Communications Act – adopted in 1996 – which established the policy of the United States "to preserve the vibrant and competitive free market that presently exists for the Internet . . . unfettered by Federal or State regulation." The FCC's order also cited Section 153(51)'s provision that service providers "shall be treated as a common carrier under [this Act] only to the extent that it is engaged in providing telecommunications services," as forbidding federal or state common carriage regulation of information services.

Given its strong basis in federal preemptive authority, the *Restoring Internet Freedom Order* clearly would preempt any state law that attempts to reimpose the repealed "net neutrality" or public utility-like regulation within that state's borders. In a strange twist, however, governors in New York and Montana have sought effectively to reimpose the FCC's repealed rules by restricting state contracting eligibility – as opposed to signing laws passed by their legislatures. Nonetheless, as will be discussed below, the governors' unusual approach is legally flawed and both the New York and Montana executive orders are subject to federal preemption.

The New York and Montana Executive Orders Are Preempted by the *Restoring Internet Freedom Order*'s Terms and Legal Authority

In late January New York Governor Cuomo and Montana Governor Bullock each issued executive orders ostensibly regarding private party eligibility for state contracting as means of reimposing the FCC's repealed rules on broadband ISPs within their states. Although ostensibly based on state procurement authority and proprietary roles, the Montana and New York executive orders expressly apply to ISP conduct regarding *all* end user consumers within their states. Specifically, in order to be eligible to enter into public contracts with their state

governments, broadband Internet service providers in Montana and New York would have to adhere to "net neutrality" or public utility-like rules identical to those repealed by the *Restoring Internet Freedom Order*.

By executive order, New York Governor Andrew Cuomo "order[ed] and direct[ed] New York State's government…not to enter into any contracts for internet service unless the ISPs agree to adhere to net neutrality principles." That is, beginning March 1, 2018, "all agencies and departments over which the Governor has Executive Authority" as well as many other state government entities, may only enter into or renew contracts with ISPs that agree they "will not block, throttle, or prioritize internet content or applications or require that end users pay different or higher rates to access specific types of content or applications."

Montana Governor Steve Bullock's executive order states: "After July 1, 2018, to receive a contract from the State of Montana for the provision of telecommunications services [which includes internet and data services], a service provider must not, with respect to any consumer in the State of Montana (including but not limited to the State itself)" engage in conduct that violates the no-blocking, no-throttling, no-paid prioritization, and no-unreasonable discrimination rules mirroring those contained in the repealed FCC *Title II Order* (2015). Additionally, to receive a contract from the State of Montana, broadband service providers "must publicly disclose to all of its customers in the State of Montana (including but not limited to the State itself)" network management information identical to disclosures required in the repealed *Title II Order*'s transparency rules.

In other words, the Montana executive order essentially copies the repealed *Title II Order* rules and requires broadband ISPs to adhere to them with respect to all end users within the state in order to be eligible to enter into procurement contracts with the state government and its agencies. The Montana executive order then sets up the Montana Department of Administration as the State's net neutrality police "to monitor its enforcement" and "resolve any dispute over the definition of terminology used in this Executive Order."

Given their mirroring of the repealed public utility-like regulation as well as their applicability to all end users within their states, both the New York and Montana executive orders are contrary to the *Restoring Internet Freedom Order*'s express preemption of "any state or local measure that would effectively impose rules or requirements that we have repealed or decided to refrain from imposing." Although executive orders regarding state contracting issued by governors are obviously different from generally applicable laws passed by state legislatures, both executive orders are "measures" applicable to all in-state broadband ISPs that become parties to public contracts with their states, and those measures "effectively impose" no-blocking, no-throttling, no-paid prioritization, no-unreasonable discrimination, and transparency rules that the FCC repealed.

The FCC's order stressed that allowing state governments to adopt their own separate requirements could "impose far greater burdens than the federal regulatory regime," "significantly disrupt the balance" struck by the federal deregulatory approach, and "impair the provision of such service by requiring each ISP to comply with a patchwork of separate and potentially conflicting requirements across all of the different jurisdictions in which it operates."

The New York and Montana executive order-based net neutrality restrictions undoubtedly would impose far greater regulatory burdens than the *Restoring Internet Freedom Order*'s balanced policy consisting of FCC transparency requirements and Federal Trade Commission enforcement against unfair and deceptive trade practices by broadband ISPs. Indeed, the purpose of the New York and Montana executive orders is to reimpose the exact same type of heavy regulatory burdens that the FCC's order sought to remove. The resulting restrictions on broadband ISPs would affect network engineering and other aspects of their services in a manner that would conflict with and unavoidably affect service in other states, all the while posing serious technological and other practical obstacles for broadband ISPs.

Both executive orders therefore are preempted under the "impossibility exception to state jurisdiction" because, as the FCC concluded in its order, it is impossible or impractical to regulate the intrastate aspects of broadband Internet access service without affecting interstate aspects of that service. Moreover, both state executive orders interfere with the federal government's nationwide deregulatory objective of not regulating information services in a public utility-like manner.

The New York and Montana Executive Orders Are Not Shielded from Preemption by Market-Participant Doctrine

In seeking to reimpose net neutrality requirements in their states, resort by Governors Cuomo and Bullock to executive orders concerning state contracting appears designed to achieve immunity from federal preemption under the market-participant doctrine. Despite the ostensibly proprietary purposes asserted in the New York or Montana executive orders, both such orders clearly attempt to impose statewide regulatory policy goals and fall outside the scope of that doctrine.

The Supreme Court's market-participant doctrine immunizes from federal preemption state governments actions in the marketplace that are narrow and consistent with other market participants. As the Supreme Court explained in *Building & Construction Trades Council v. Associated Builders & Contractors of Massachusetts/Rhode Island, Inc.* (1993), often referred to as the "*Boston Harbor*" case: "Our decisions in this area support the distinction between government as regulator and government as proprietor," and a state's proprietary acts are immune from preemption when those acts are "not tantamount to regulation or policymaking." Although state government proprietary acts serve important purposes and are not typically subject to preemption, in *Wisconsin Department of Industry v. Gould Inc*. (1986), the Supreme Court pointed out that "government occupies a unique position of power in our society, and its conduct, regardless of form, is rightly subject to special restraints." The market-participant doctrine is rooted in a concern that state governments may conduct proprietary functions in ways unrelated to their actual proprietary interests and thereby alter the conduct of private actors in the market or alter the markets itself. Such conduct by state governments can result in *de facto* regulation and unduly disturb or thwart congressional policies.

Under the market-participant doctrine, the Supreme Court and lower courts have immunized state proprietary acts from preemption when a state acts in the same manner that a private company might have acted in similar situations. In *Boston Harbor*, the Supreme Court upheld a

state agency's pre-hire agreement with a union workforce that included a no-strike guarantee because the agency was only "attempting to ensure an efficient project that would be completed as quickly and effectively as possible at the lowest cost." The state agency's action was narrowly limited to one particular contract job and was not a prohibition regarding all future contract bidders. Nor did it penalize bidders for practices on different projects for other clients. As the Fifth Circuit stated in *Cardinal Towing & Auto Repair v. City of Bedford* (5th Cir. 1999): "Courts have similarly shielded contract specifications from preemption when they applied to a single discreet contract and were designed to insure efficient performance rather than advance abstract policy goals."

In *Gould*, the Supreme Court struck down a statute that barred the state from contracting with employers who had repeatedly been sanctioned by the National Labor Relations Board (NLRB). The statute's prohibitions could be triggered by conduct unrelated to the state as a contracting party, and its prohibitions applied to all of the state's future contracting decisions. The Supreme Court observed: "[O]n its face the debarment statute serves plainly as a means of enforcing the NLRA." And because the statute "assumes for the State of Wisconsin a role Congress reserved exclusively for the Board," it was preempted. According to the Fifth Circuit in *Cardinal Towing*: "Following the logic of *Gould*, courts have found preemption when government entities seek to advance general societal goals rather than narrow proprietary interests through the use of their contracting power."

The market-participant doctrine is ably summed up in an oft-quoted paragraph from the Fifth Circuit's decision in *Cardinal Towing*:

> The Supreme Court has found that when a state or municipality acts as a participant in the market and does so in a narrow and focused manner consistent with the behavior of other market participants, such action does not constitute regulation subject to preemption… When, however, a state attempts to use its spending power in a manner "tantamount to regulation," such behavior is still subject to preemption.

Although issued under the guise of state procurement authority, the analysis that follows shows that both the New York and Montana executive orders are regulatory in nature, not proprietary, and therefore outside the scope of the market-participant doctrine.

A Market-Participant Doctrinal Analysis of the New York and Montana Executive Orders

As an initial matter, the net neutrality or public utility-like restrictions contained in both executive orders are not narrowly focused interactions with the market or characteristic of private party conduct in the market. Significantly, broadband ISPs do not make their network management practices subject to arms-length negotiation with end user consumers. According to FCC regulations and the *Restoring Internet Freedom Order*, "broadband Internet access services" is defined as "a mass-market retail service by wire or radio that provides the capability to transmit data to and receive data from all or substantially all Internet endpoints." As the FCC's order notes: "By mass market, we mean services marketed and sold on a standardized basis to residential customers, small businesses, and other end-user customers such as schools and

libraries." But that definition "does not include enterprise service offerings or special access services, which are typically offered to larger organizations through customized or individually negotiated arrangements." Although broadband ISPs routinely offer pricing discounts, service tier options, and bundling choices, such providers do not make network-wide engineering and related business-wide operational decisions for their mass-market retail offerings the basis of individualized contracts. Yet the net neutrality requirements contained in the New York and Montana executive orders amount to demands that broadband ISPs must alter or restrict the network management practices for their mass-marketed retail service.

Further, it is obvious that ordinary end user consumers in the broadband Internet access services market do not negotiate how their broadband ISP treats other end-user consumers. But as previously indicated, the New York and Montana executive orders do so. Both executive orders require that broadband ISP eligibility for state contracts must agree to adhere to net neutrality restrictions regarding all of their end user subscribers in their states. New York's executive order is titled "Ensuring Net Neutrality for New Yorkers," and its "whereas" clauses are directed to "all New Yorkers," "New York businesses," "New York Students," and "New Yorkers" generally. Similarly, the whereas clauses in the Montana executive order refer broadly to "Montanans," "Montana citizens," "Montana businesses," and "educational institutions in Montana."

On their face, both the New York and Montana executive orders are not at all narrowly confined to their states' proprietary interests. Instead, they expressly reflect the primary goal of promoting net neutrality regulation as a general policy. Unmistakably, both executive orders are "tantamount to regulation," as they are clearly and specifically intended to reimpose net neutrality regulation – albeit through unusual and nontraditional means.

The Supreme Court's decision in *Gould* is particularly instructive here. Just as the Wisconsin statute's prohibitions against the state contracting with employers subject to repeated NLRB sanctions could be triggered by conduct unrelated to the state as a contracting party, so too the prohibitions on contracting with broadband ISPs that do not agree to adhere to net neutrality rules can and almost surely would be unrelated to New York and Montana as contracting parties. Also, just as the statute's prohibitions in *Gould* applied to all of the state's future contracting decisions and not to one particular contract, the prohibitions on contracting with broadband ISPs that do not agree to adhere to net neutrality rules will apply to all of their states' future contracting decisions.

Moreover, similar to the Court's observations in *Gould* that "on its face the debarment statute serves plainly as a means of enforcing the NLRA," the New York and Montana executive orders plainly, on their faces, serve as a means of enforcing core regulatory requirements of the repealed *Title II Order*. Indeed, concerning the statute's aim of enforcing the National Labor Relations Act, the Court in *Gould* stated: "No other purpose could credibly be ascribed." Surely, no other purpose could be ascribed to the New York and Montana executive orders other than enforcing several of the FCC's repealed net neutrality rules. And whereas the Court in *Gould* concluded that the statute "assumes for the State of Wisconsin a role Congress reserved exclusively for the Board," both states' executive orders assume a role regarding information services that Congress reserved exclusively for the FCC and for the free market. As the Supreme

Court observed in *Metropolitan Life Insurance Company v. Massachusetts* (1985), "preemption… precludes state and municipal regulation concerning conduct that Congress intended to be unregulated."

Given the solid preemptive authority behind the *Restoring Internet Freedom Order* and given the clash with federal deregulatory policy for information services such as interstate broadband Internet access services created by the New York and Montana executive orders, the FCC should be in a position to preempt them.

Hypothetically Narrower Net Neutrality Requirements Would Also Be Preempted

Of course, even if a state's governor issued an executive order requiring only that broadband ISPs must agree to adhere to net neutrality restrictions in providing broadband Internet access services directly to state government agencies and their employees, such a restriction would still be highly questionable under the market-participant doctrine. Such a hypothetical state contracting requirement would not be narrowly focused and limited to one particular contract. Making adherence to the FCC's repealed net neutrality regulations a condition of state contracting and procurement of broadband Internet access services would remain decidedly inconsistent with ordinary end user actions in that retail mass market. (As previously stated, larger-size customers of broadband services that want customization and specific quality-of-service guarantees typically negotiate with providers that offer what are known as specialized services, enterprise broadband services, special access, or "business data services.")

Rather, such a requirement would embody a general regulatory policy and thus constitute a state measure that effectively reimposes net neutrality rules in contravention to the *Restoring Internet Freedom Order*'s express preemption proviso. Further, an ostensible proprietary requirement that broadband ISPs agree to adhere to net neutrality restrictions only in providing broadband Internet access services directly to state government agencies and their employees would conflict with the FCC's policy pronouncement that regulatory attempts to distinguish between interstate and intrastate Internet traffic are impossible or impractical and would result in harmfully inconsistent regimes among states and affect interstate broadband Internet access services.

Finally, it should be noted that, aside from the FCC's authority to preempt, there is a whole separate line of authority not discussed here under the Dormant Commerce Clause jurisprudence that, as a constitutional matter, likely would invalidate the state executive orders and similar state actions.

Conclusion

The *Restoring Internet Freedom Order*'s repeal of public utility regulation of broadband Internet services and reclassification of those services as largely unregulated information services established a free market-oriented national framework based on the deregulatory goals of the 1996 Telecommunications Act. The FCC's order, which is backed by congressional policy, agency precedent, and Supreme Court jurisprudence, expressly preempted any measure that effectively would reimpose the repealed rules at the state level. Given the solid preemptive authority behind the *Restoring Internet Freedom Order* and given the clash with federal

deregulatory policy for information services like the interstate broadband Internet access services that are the subject of the New York and Montana executive orders, the FCC should be in a position to preempt them.

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