Before the
FEDERAL COMMUNICATIONS COMMISSION
Washington, D.C. 20554

In the Matter of Petition of the Cellular Telephone & Internet Association for an Expedited Declaratory Ruling Confirming that: (1) Early Termination Fees in Wireless Contracts Are "Rates Charged" for Commercial Mobile Services Within the Meaning of Section 332(c)(3)(A) of the Communications Act and FCC Precedent; and (2) Any Application of State Law by a Court or Other Tribunal to Invalidate, Modify, or Condition the Use or Enforcement of ETFs Based, in Whole or in Part, Upon an Assessment of the Reasonableness, Fairness, or Cost-basis of the ETF, or to Prohibit the Use or Enforcement of ETFs as Unlawful "Liquidated Damages" or Penalties, Constitutes Prohibited Rate Regulation and Is Therefore Preempted by Section 332(c)(3)(A)	)	WT DOCKET NO. 05-194

To: The Commission:

COMMENTS OF VERIZON WIRELESS IN SUPPORT OF CTIA'S PETITION FOR DECLARATORY RULING

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SUMMARY

Wireless carriers operate in a highly competitive marketplace that offers customers a broad range of products and services. The development of the industry is not accidental. Wireless competition, and the consumer benefits that flow from competition, are the product of decisive Congressional action. Congress, in enacting the Communications Act of 1934 ("Communications Act"), recognized from the start the need for consistent federal treatment of radio-based communications. The Commission has faithfully implemented Congress's deregulatory model by preempting state and local regulation that frustrated the nationwide expansion of mobile telephony.

In 1993, Congress amended the Communications Act to bolster its deregulatory wireless model. Section 332, enacted as part of the 1993 amendments, places strict limitations on state and local wireless regulation and expressly prohibits states from regulating wireless "rates" and "entry." The Commission recently exercised its authority under Section 332 to preempt states from requiring or prohibiting line items on wireless carrier bills.

Early termination fees ("ETFs") are a critical aspect of the wireless rate plans that have fostered the availability of wireless service nationwide. Wireless carriers incur significant costs in acquiring and providing service to new customers. However, in exchange for a fixed term contract, the wireless carriers do not require customers to pay these costs at the inception of the subscription term. Rather, wireless carriers recoup these costs through the secure revenue stream fixed term contracts provide. ETFs therefore permit wireless carriers to offer attractive initial discounts and monthly pricing to customers willing to make a minimum service commitment. These popular fixed term rate plans are inextricably tied to and not economically viable without ETFs. ETFs, under Section 332 and FCC precedent, thus are both "rates charged" – in that they

are assessed for the provision of wireless services – and an integral and inseparable part of the wireless "rate structure."

Despite Section 332's mandate, states (including class action plaintiffs pursing actions in state courts) are attempting to regulate ETFs out of existence under a variety of legal theories. In lawsuits throughout the country, plaintiffs seek both a return of monies paid and a prospective ban of the use of ETFs. These lawsuits employ a variety of common law theories, including unconscionability, illegal penalty, and quasi-contract, as well as state consumer protection statutes. Each of these theories of recovery violates Section 332's ban on state rate regulation. As the Commission has found, Section 332(c)(3)(A) not only bans states from regulating the rate charged and the rate structure, but also forbids states – including state courts – from assessing the reasonableness of the rate. These state lawsuits uniformly breach this rule. As explained below, regardless of the label affixed to the cause of action, all of these common law and statutory claims turn on an assessment of the ETF's "reasonableness."

Any attempt to use Section 332's "other terms and conditions" language to regulate ETFs is thoroughly misplaced. Section 332 makes clear that ETFs are not "other terms and conditions." ETFs cannot be both a "rate" and an "other term and condition." These are mutually exclusive designations. Because these lawsuits specifically target wireless rates, preemption is warranted.

ETF litigation frustrates Congress's deregulatory framework. As the Commission explained in the Truth-in-Billing context, in addition to the express preemption of Section 332, the Commission is empowered to preempt any state or local regulation that conflicts with or frustrates the federal scheme or could lead to patchwork regulation. The state efforts to regulate wireless rates, and ultimately strike, down ETFs certainly will lead to patchwork regulations and impede the Commission's pro-competitive, deregulatory framework. In fact, this concern over patchwork regulation rightfully led the *SunCom* court to issue a primary jurisdiction referral to the Commission. Unfortunately, as explained below, several other state courts did not follow this sensible course and are instead interpreting Section 332 on their own. The Commission should promptly assert its authority and responsibility to oversee this national industry, and interpret the federal law applicable to it, by declaring that ETFs clearly are "rates" within Section 332.

Last, state regulation of ETFs violates the Commerce Clause in two ways. First, state regulation of ETFs imposes a "disproportionate burden" on interstate commerce. The Commerce Clause prevents a state from creating regimes that are in substantial conflict with the common regulatory schemes of other states. Piecemeal ETF regulation falls squarely within this category. Second, state superintendence over ETFs has an unconstitutional extraterritorial impact on conduct outside the state seeking to impose the regulations. Here, the risk of "inconsistent obligations" (given the regional and nationwide configuration of wireless plans) is grave. Accordingly, haphazard state regulation – whether through judicial action or otherwise – violates the Commerce Clause.

For these reasons, Verizon Wireless, respectfully submits these Comments in support of the Petition for Declaratory Ruling submitted by the Cellular Telecommunications & Internet Association ("CTIA"). Verizon Wireless requests a declaratory ruling that: (1) ETFs are "rates" charged; (2) ETFs are part of and inseparable from the wireless "rate structure"; (3) any common law or statutory legal theory that employs a "reasonableness" assessment to invalidate an ETF is preempted under Section 332(c)(3)(A); (4) state regulation of ETFs conflicts with and frustrates Congress's deregulatory model; and (5) state regulation of ETFs violates the Commerce Clause.

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I. BACKGROUND

Congress wisely chose to limit the regulation of the wireless industry, fostering the growth of a vibrant, efficient, and highly competitive industry that affords the customer a quality product at a competitive rate. In particular, Section 332's twin ban on state regulation of "rates" and market "entry" effectuates Congress's vision of a seamless national wireless market. Many states, however, continue to breach Section 332's unmistakable prohibition in their various efforts to regulate wireless "rates" and "rate structures." The FCC's recent *Truth-in-Billing* decision illustrates this point. The ongoing efforts in several states to regulate early termination fees ("ETFs") out of existence represent yet another example of impermissible rate regulation that threatens to upend the industry's competitive pricing model and replace it with a balkanized, heavy-handed regulatory regime.

The wireless industry, through CTIA, has asked the FCC to address the question whether federal law preempts state regulation of ETFs.[1] In its public notice, DA 05-1389, the FCC seeks comment on how the agency should respond to the aforementioned state regulatory efforts.[2] Verizon Wireless urges the FCC to take unequivocal action to clarify that ETFs are part of the "rates" and "rate structures" to be regulated, per Congress's policy choice, exclusively at the federal level and that Section 332(c)(3)(A)'s preemptive force bars state efforts to invalidate or modify these wireless rates.

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1 *See Petition of the Cellular Telecommunications & Internet Association for Expedited Ruling* ("*CTIA Petition*"), WT Docket No. 05-194, filed March 15, 2005.

2 The Public Notice was published in the Federal Register on July 6, 2005. *See* 70 Fed. Reg. 38,928 (July 6, 2005).

A. **Congress Envisioned A Nationally Competitive Wireless Market Unimpeded By Balkanized State Regulations.**

Since its inception, radio-based communications technology, by virtue of its diffuse nature, has transcended geographic or political borders.[3] Accordingly, Congress fashioned a comprehensive federal regulatory framework – beginning with the Communications Act of 1934 ("Communications Act") – "to make available, so far as possible, to all the people of the United States . . . a rapid, efficient, Nation-wide, and world-wide wire and radio communication service."[4] Pursuant to its expansive authority under the Communications Act, the FCC consistently has exercised "federal primacy over the areas of technological standards and competitive market structure for cellular service" because "state and local regulations might conflict with and thereby frustrate" the federal goal of nationwide compatibility for mobile telephony.[5]

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[3] *See Fed. Radio Comm'n v. Nelson Bros.*, 289 U.S. 266, 279 (1933). The FCC's own designations reveal the interstate nature of wireless communications. The FCC issues cellular and PCS licenses based upon various geographic market designations, including Census Bureau-defined Metropolitan Statistical Areas ("MSAs"), FCC-defined Rural Service Areas ("RSAs"), Rand McNally-defined Basic Trading Areas ("BTAs") and Major Trading Areas ("MTAs"), many of which cross state lines. *See* http://www.FCC.gov/oet/info/maps/areas/. For this reason, the FCC recently informed the United States Court of Appeals for the Eighth Circuit that "[t]o succeed in the marketplace, CMRS carriers typically operate without regard to state borders and, in contrast to wireline carriers, generally have come to structure their offerings on a national or regional basis." Brief Amicus Curiae of the Federal Communications Commission at 11, *Cellco Partnership v. Hatch*, (8th Cir. 2004) ("*FCC Amicus Brief*"); *see also Annual Report and Analysis of Competitive Market Conditions With Respect to Commercial Mobile Services* ("*2004 Competition Report*"), 19 FCC Rcd 20997, 20644 ("Today all of the nationwide operators offer some version of a national rate pricing plan in which customers can purchase a bucket of MOUs [minutes of use] to use on a nationwide or nearly nationwide network without incurring roaming or long distance charges.").

[4] 47 U.S.C. § 151 (2005); *see also NBC v. United States*, 319 U.S. 190, 214 (1943) (quoting *FCC v. Pottsville Broad. Co.*, 309 U.S. 134, 137 (1940)).

[5] *An Inquiry Into the Use of the Bands 825-845 MHz and 870-890 MHz for Cellular Communications Systems; and Amendment of Parts 2 and 22 of the FCC's Rules Relative to Cellular Communications Systems*, 86 FCC 2d 469, 503-05 (1981). Congress's 1993 amendments to Section 2(b) of the Communications Act confirm that the FCC has plenary authority to regulate CMRS. Section 2(b), as amended, specifically exempts from the States' general intrastate jurisdictional authority wireless services regulated by federal authorities under Section 332. *See* 47 U.S.C. § 152(b); *see also* H.R. Conf.

In 1993, Congress amended the Communications Act "to dramatically revise the regulation of the wireless telecommunications industry."[6] One of the most important provisions of the 1993 Act was Section 332(c)(3), entitled "State Preemption."[7] The FCC has made clear that this provision "express[es] an *unambiguous congressional intent to foreclose state regulation*."[8] By prohibiting state regulation, Congress sought to establish a uniform "national regulatory policy for CMRS" that replaced "a policy that [was] balkanized state-by-state."[9] Congress properly understood that preemption is necessary because "[s]tate regulation can be a barrier to the development of competition."[10] The FCC likewise understands that "overbroad state regulations in this area may frustrate our federal rules and the federal objective of minimizing regulatory burdens on the competitive CMRS industry. Moreover, we note that in

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Rep. No. 103-213, at 497 (1993) (Congress amended section 2(b) to "clarify that the FCC has the authority to regulate commercial mobile services.").

6 *See, e.g., Cellnet Commc'ns, Inc. v. FCC*, 149 F.3d 429, 433 (6th Cir. 1998); *Pet. of N.Y. State Pub. Serv. Comm'n to Extend Rate Regulation*, Report and Order, 10 FCC Rcd 8187, 8190 (1995) ("*New York Pet*."). In particular, the amendments created new regulatory wireless service categories – CMRS and private mobile radio service ("PMRS") – and altered the wireless regulatory framework in two important respects. First, Congress eliminated the historic dual federal and state regulatory framework by expressly preempting most state regulation of wireless services and expressly permitting the FCC to regulate intrastate CMRS services. Second, Congress implemented its "general preference in favor of reliance on market forces rather than regulation," *id.* at 8190, and thus allowed regulation only in situations in "which the FCC and the states [can] demonstrate a clear-cut need." *Pet. on Behalf of the State of Haw. Pub. Util. Comm'n, for Auth. to Extend Its Rate Regulation of Commercial Mobile Radio Servs. in the State of Haw.*, Report and Order, 10 FCC Rcd 7872, 7874 (1995) ("*Haw. Pet.*").

7 Section 332(c)(3)(A), in particular, expressly provides that "no State . . . shall have *any* authority to regulate the entry of or the rates charged by any commercial mobile service or any private mobile service." 47 U.S.C. § 332(c)(3)(A) (emphasis added).

8 *New York Pet.*, 10 FCC Rcd at 8190 (emphasis added).

9 *Pet. Of Conn. Dep't Pub. Util. Control to Retain Regulatory Control of the Rules of Wholesale Cellular Serv. Providers in the State of Conn.*, Report and Order, 10 FCC Rcd 7025, 7034 (1995) (citing H.R. Cong. Rep. No. 103-213, at 480-81 (1993)) ("*Conn. Pet.*").

10 *Id.* at 7034 n.44 (citing H.R. Cong. Rep. No. 103-213, at 480-481).

establishing the regulatory framework for CMRS, Congress expressly assigned certain tasks, including rate regulation, to the federal government."[11]

Section 332 strictly prohibits state authority over wireless rates and entry. The only state regulatory authority over wireless services that Section 332 does not eliminate is state authority to regulate "other terms and conditions" of wireless services – that is, terms and conditions of service other than rates.[12] The FCC and the federal courts consistently have struck down state attempts to exceed these limited regulatory confines of Section 332.[13] Furthermore, the FCC has faithfully implemented Congress's deregulatory purpose and guarded against state disruption of a uniform regulatory scheme.[14] In short, Congress and the FCC have left no doubt that inefficient and detrimental CMRS regulation – whether state or federal – must be eliminated in furtherance of a uniform national treatment of wireless services.[15]

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[11] *Truth-in-Billing and Billing Format*, Second Report and Order, Declaratory Ruling, and Second Further Notice of Proposed Rulemaking, 20 FCC Rcd 6448, 6460 (2004) ("*Truth-in-Billing*"). States may regulate wireless rates (but not entry) only after obtaining FCC authorization. *See* 47 U.S.C. § 332(c)(3)(A); *see also* 47 C.F.R. § 20.15.

[12] 47 U.S.C. § 332(c)(3)(A).

[13] *See*, *infra*, § II.A. In addition to eliminating traditional state regulation of CMRS, the 1993 amendments to Section 332 also limit regulations that the FCC may impose on CMRS and authorize the FCC to forbear from applying Title II rate and service regulation to CMRS carriers. *See* 47 U.S.C. § 332(c)(1).

[14] The development of this highly competitive and nationally integrated wireless industry is not accidental; it is the product of deliberate deregulatory choices, mandated and codified by Congress and faithfully implemented by the FCC. *See Presentation of Commissioner Kevin J. Martin*, 2004 LEXIS 5871, * 9 (recognizing that "[w]ireless could develop in this manner because of a consistent regulatory treatment throughout the country"); *see also Orloff v. Vodafone Airtouch Licenses LLC*, 17 FCC Rcd 8987, 8997 n.69 (2002), *pet. for review denied sub. Nom.*, *Orloff v. FCC*, 352 F.3d 415 (D.C. Cir. 2003), *cert. denied*, 124 S. Ct. 2907 (2004) (calling for reliance "on market forces, rather than regulation, except when there is market failure"); *Vonage Holdings Corp. Pet. for Declaratory Ruling Concerning An Order of the Minnesota Pub. Utils. Comm'n*, Memorandum Opinion and Order, 19 FCC Rcd 22404, 22416 (2004) (emphasis in original) (finding that regulation "*may actually harm consumers* by impeding the development of vigorous competition") ("*Vonage*").

[15] CMRS, because of technological innovation, organic growth, and industry consolidation, is fulfilling Congress's vision of a seamless, nationwide industry. *See* H.R. Rep. No. 103-111, at 260 (1993) (The 1993 Amendments were intended to "foster the growth and development of mobile services

B. **<u>ETFs Are A Crucial Aspect Of The Wireless Rate Plans That Are Integral To National Wireless Competition.</u>**

Wireless rate plans predominantly utilize term service agreements under which customers agree to pay for service on a monthly basis for a fixed length of time.[16] Although wireless providers' costs for acquiring and providing service to new customers are significant, the rate plans generally do not require customers to pay for these costs at the inception of the subscription term. Instead, carriers recover these "up front" costs through the customers' monthly payments over the contract term. The ETF is triggered when a wireless subscriber terminates service before the agreed-upon contract term expires,[17] and thus provides the carrier some revenue in case the customer does not fulfill the contract commitment.[18] Absent ETFs, many of the most popular wireless rate plans would be economically unsustainable and thus

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that, by their nature, operate without regard to state lines as an integral part of the national telecommunications infrastructure."). Moreover, the increased availability of competitive wireless service yields tangible benefits to consumers. As the FCC explained, "increased service availability, lower prices for consumers, innovation, and a wider variety of service offerings" flow from this robust competition. *In re Implementation of Section 6002(B) of The Omnibus Budget Reconciliation Act of 1993, Annual Report and Analysis of Competitive Market Conditions With Respect To Commercial Mobile Services,* Eighth Report, 18 FCC Rcd 14783, 14793 (2003) ("*2003 Competition Report*"). Today, the wireless industry is vigorously competitive. "During 2003, the CMRS industry continued to experience increased service availability, intense price competition, innovation, and a wider variety of service offerings." *2004 Competition Report*, 19 FCC Rcd at 20608 n.33.

16 Consumer wireless agreements typically run for 12 to 24 months. *See* CTIA Petition at 1.

17 ETFs, which typically range of $150 to $200 in the wireless context, are a standard rate element in many other sorts of contracts. *See, e.g. Baez v. Banc One Leasing Corp.*, 348 F.3d 972, 973 (11th Cir. 2003) (discussing early termination fees in automobile leases); http://www.freddiemac.com /singlefamily/ pdf/ppm.pdf> (describing operation of prepayment charges in certain mortgages).

18 *See Tele. No. Portability*, Memo. Op. and Order, 18 FCC Rcd 20971, 20975-76 (2003), *pet. for review denied*, 402 F.3d 205, 365 (D.C. Cir. 2005). (noting that ETFs allow wireless carriers to hedge against unmitigated customer migration and "recover[] their investment in their customers") ("*Tele. No. Portability*"); *see also In re Ryder Commc'ns, Inc. v. AT&T Corp.*, 18 FCC Rcd 13603, 13617 (2003) (wireline ETFs are "a valid quid pro quo for the rate reductions included in long term-plans").

unavailable to the consumer.[19] ETFs therefore are an indispensable part of the wireless rate and rate structure and provide access to wireless services, including access for lower-income consumers.

C. <u>States Throughout The Country Are Attempting To Regulate ETFs.</u>

As the *CTIA Petition* makes clear, ETFs are now the subject of state-court lawsuits in a number of states including California, Florida, South Carolina and Illinois. Although the claims vary according to state law, each suit is an attack on the rates and rate structures wireless carriers employ throughout the country. In these cases, Plaintiffs seek a return of the monies paid as ETFs and a ban on, or reduction of, the use this rate element in future wireless customer agreements.

First, several consolidated putative class actions that directly challenge the validity of ETFs are pending in the Superior Court of the State of California, County of Alameda.[20] These suits, filed against the major wireless service providers, including Verizon Wireless, allege that ETFs constitute unlawful penalties, unfair business practices, and unconscionable terms under California law.[21] The plaintiffs specifically request restitution, disgorgement, and compensatory and punitive damages,[22] as well as an injunction preventing service providers from disseminating contracts containing ETFs and "from enforcing the provision in existing contracts."[23]

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19 As the *CTIA Petition* explains, consumers are increasingly satisfied with the pricing and service options that wireless carriers offer pursuant to these plans. *See CTIA Petition* at 2 n.6 (citing *Quarterly Report on Informal Consumer Inquiries and Complaints Released*, 2005 WL 516803 (Mar. 4, 2005)).

20 *Cellphone Termination Fee Cases*, Superior Court of the State of California, County of Alameda, Case No. JCCP004332; *see* Third Consolidated Amended Complaint [Early Termination Fees] Against Verizon, June 24, 2005, ("*Ca. Verizon Compl*") (Complaint attached as Exhibit A).

21 *Id.* ¶¶ 9, 42-78.

22 *Id.* ¶¶ 10, 40, 45, 59, 68, 73 78.

23 *Id.* ¶ 40.

Early in the Alameda County litigation, the wireless defendants sought to dismiss the plaintiffs' ETF claims on the grounds that Section 332 of the Communications Act preempted the actions. The court rejected the motions, reasoning that the application of Section 332 to state-law claims challenging ETFs was "unsettled" and that it is "unclear what Congress intended" when it included the term "rates charged" in Section 332(c)(3)(A).[24] The court then granted the plaintiffs' motion for a jury trial on the facts underlying the preemption issue. Upon reconsideration of the plaintiffs' jury trial motion, the court subsequently issued an order reversing its early position. The new order set non-jury trial procedures for resolution of issues concerning preemption, and stated that the court, rather than the jury, would decide all factual issues related to preemption of the plaintiffs' claims; nonetheless, the court left open the door that the jury's fact-finding on the merits might be inconsistent with the court's fact-finding on preemption, thus leaving the issue of ultimate authority over the preemption issue somewhat unclear.[25]

After the FCC issued its Public Notice relating to this proceeding, the wireless carriers moved for a stay of the Alameda County actions, under the primary jurisdiction doctrine and in the exercise of the court's inherent supervisory powers, pending resolution of the preemption issue by the FCC. The court held that initiation of proceedings on the preemption issue by the FCC triggered the primary jurisdiction doctrine and ruled that the court would "wait for the FCC to decide whether ETFs are 'rates charged' or 'other terms and conditions' before addressing"

[24] *See Order* Overruling Demurrer to Early Termination Fee Claims Based on Preemption, at 5, January 20, 2004 (Order attached as Exhibit B).

[25] *See Order* (1) Granting and Denying Motion of Defendants re Conduct of Trial and (2) Resolving Issues Concerning Deposition of Expert Witnesses, at 4, February 14, 2005 (Order attached as Exhibit C).

the preemption issue, and granted defendants' stay motion to that extent.[26] The court declined to "stay [its] proceedings in their entirety until the FCC issues its decision," and held instead that the case could proceed on certain matters.[27] Regarding class certification, for example, the court held that the "class certification . . . issue appears ready for the Court to resolve" and that the "Plaintiffs can pursue class certification so that a class will be certified (or not) when the FCC issues its decision."[28] A writ petition seeking a stay of this case is pending.

A class action ETF suit also has been filed in Palm Beach County, Florida against Verizon Wireless. This case, brought under the Florida Deceptive and Unfair Trade Practices Statute,[29] asserts that the ETF is unconscionable and unenforceable.[30] The plaintiff seeks "equitable relief"[31] in the form of an order requiring Verizon Wireless to cease and desist enforcement of the ETF and disgorge ETF proceeds.[32] The same plaintiff subsequently filed a demand for nationwide class arbitration against Verizon Wireless with the American Arbitration Association.[33] The demand alleges that the ETF is an "unconscionable, void, and liquidated

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26 *See Order* re Motion to Stay Pending Resolution of FCC Proceedings Under the Primary Jurisdiction Doctrine, at 2, June 21, 2005 (Order attached as Exhibit D).

27 *Id.*

28 *Id.*

29 *Brown v. Verizon Wireless Services, LLC*, Circuit Court of the 15th Judicial Circuit, in and for Palm Beach County, Florida, Case. No. 04-80606-CIV ("*Fl. Verizon Compl*.") (Complaint attached as Exhibit E).

30 *Id.* ¶ 24.

31 *Id.* ¶ 10, Count II.

32 *Id.* ¶¶11-12.

33 *Brown and Cellco Partnership d/b/a Verizon Wireless*, No. 11-494-01274-05, American Arbitration Association ("Verizon Arb. Demand").

damages provision" and "constitutes an unjust, unreasonable, unlawful, unfair, and deceptive practice under all applicable statutes."[34] The demand seeks damages and injunctive relief.[35]

Finally, Verizon Wireless is being sued over ETFs in a putative class action in Madison County, Illinois,[36] in which the plaintiff asserts that the ETF is unlawful and unenforceable because it is an illegal penalty.[37] The Illinois plaintiff seeks damages and injunctive relief.[38] The Illinois action currently is stayed pending arbitration, which plaintiff is attempting to pursue on a statewide class basis.

The common thread of these actions is that Plaintiffs seek to invalidate, modify, and recover previously-paid ETFs and to prohibit the future use of this important rate mechanism.[39]

II. SECTION 332 PREEMPTS STATE ETF REGULATION

A. ETFs Are Part of Wireless Carrier Rates And Rate Structures.

Federal law preempts state regulation of "the *rates charged* by any commercial mobile service . . . ."[40] Under Section 332(c)(3)(A), state courts and commissions, and other bodies

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34 *Id.* ¶ 29.

35 *Id.* ¶ 57.

36 *Zobrist v. Verizon Wireless, Cellco Partnership, Verizon Communications, Inc.*, No. 02-L-1088 (Circuit Court, Third Judicial Circuit, Madison County, Illinois) ("*Ill. Compl*.") (Complaint attached as Exhibit F).

37 *Id.* ¶¶ 4-5.

38 *Id.* ¶ 61.

39 In addition, there is significant movement at the state-level, both through state-PUC regulations and direct legislative action, toward regulation of ETFs. *See, e.g.*, Public Utilities Commission of the State of California, Gen. Order No. 168, Telecommunications Consumer Protection Rule 3(f) (2004) (stayed pending reconsideration) ("Subscribers may cancel without termination fees or penalties any new tariffed service or any new contract for service within 30 days after the new service is initiated."); *see also* Assemb. 3935, 2004-2005 Leg., 211th Sess. (N.J. 2005); S. 4263, 2005-2006 Reg. Sess., 228th Annual Leg. Sess. (N.Y. 2005); S. 1790, 2005 Reg. Sess., 184th General Court (Mass. 2005); H.R. 2218, 73rd Leg. Assemb. (Or. 2005); S. 1261, 23rd State Leg. (Haw. 2005); H.R. 2468, 1st Reg. Sess., 47th Leg. (Ariz. 2005).

applying state law, do not have "any" authority to regulate the rates charged by wireless carriers.[41] The FCC has "interpreted the rate regulation provision of the statute to be broad in scope" and therefore has "made clear that that the proscription of state rate regulation extends to regulation of 'rate levels' and 'rate structures' for CMRS."[42] The FCC confirmed the breadth of the operative terms "rate" and "rate structure" in the recent *Truth-in-Billing* ruling.[43]

ETFs constitute "rates" under Section 332(c)(3)(A) for two independent reasons. First, ETFs are one of the charges that are assessed for the provision of wireless services. Second, ETFs are an integral part of wireless providers' "rate structures."

1. <u>**State Regulation of ETFs Is Preempted Because ETFs Are "Rates Charged" for Wireless Services.**</u>

Section 332(c)(3)(A) prohibits state regulation of the "rates charged" by wireless providers. The ETF is a "rate charged" because it is one of the charges that is assessed for the provision of wireless services.[44] Wireless providers offer service through a variety of rate plans made up of multiple components, including fees for activation, monthly access, special features,

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[40] 47 U.S.C. § 332(c)(3)(A) (emphasis added).

[41] *Id.*

[42] *Southwestern Bell Mobile Sys., Inc.*, Mem. Op. and Order, 14 FCC Rcd. at 19907-08 ("[W]e find that the term 'rates charged' in Section 332(c)(3)(A) may include both *rate levels* and *rate structures* for CMRS and that the states are precluded from regulating either of these. Accordingly, states not only may not prescribe how much may be charged for these services, but also may not prescribe the *rate elements* for CMRS or specify which among the CMRS services provided can be subject to charges by CMRS providers.") (*Southwestern Bell Mobile Sys., Inc.*") (emphasis added); *see also Wireless Consumers Alliance,* Mem. Op. and Order, 15 FCC Rcd. 17021, 17028 (2000) ("At the outset of our analysis on the preemptive scope of Section 332, we observe that Section(c)(3)(A) bars state regulation of, and thus lawsuits regulating . . . the rates or rate structures of CMRS providers.") ("*Wireless Consumer Alliance*").

[43] *See Truth-in-Billing*, 20 FCC Rcd at 4642 ("The Commission . . . consistently has interpreted the rate regulation provision of the statute to be broad in scope.").

[44] *See MCI Telecomms. Corp. v. FCC*, 822 F.2d 80, 86 (D.C. Cir. 1987) ("rates are a means by which the carrier recovers its cost of service from its customers"); *Ca. Energy Res. Conservation and Dev. Comm'n v. Bonneville Power Admin.*, 831 F.2d 1467, 1472 (9th Cir. 1987) ("[r]ates are simply the charges [a company] imposes on its customers for the provision of service")(citations omitted).

local and long distance airtime, certain roaming charges, and early termination. Together, the multiple rate components under any given plan are designed to compensate wireless providers for the services they provide – from acquisition costs to other ongoing business costs and risks, such as bad debt and collection expenses. These costs are recovered over the length of the customer relationship. These multiple rate plan components are also designed to compete with rate plans offered by other companies in the intensely competitive wireless industry.[45]

Wireless providers' costs for acquiring new customers are significant. They include the costs of subsidizing goods and accessories, including handset rebates and discounts,[46] and paying direct and indirect commissions and other amounts to dealers and retailers who sell handsets and wireless service to subscribers. Wireless providers also incur costs to provide other services to customers, such as: qualifying customers for the appropriate plan and equipment; running credit checks; programming phones; providing network service; setting up new accounts; counseling customers regarding the products and services providers offer; and creating and circulating

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[45] The FCC has recognized the highly competitive nature of the wireless industry for some time. *See 2004 Competition Report*, 19 FCC Rcd at 20621; *2003 Competition Report,* 18 FCC Rcd 14789; *Implementation of Section 6002(B) of The Omnibus Budget Reconciliation Act of 1993, Annual Report and Analysis of Competitive Market Conditions With Respect To Commercial Mobile Services*, Seventh Report, 17 FCC Rcd 24923, 24924 (2002) ("*2002 Competition Report*"); *In re Implementation of Section 6002(B) of The Omnibus Budget Reconciliation Act of 1993, Annual Report and Analysis of Competitive Market Conditions With Respect To Commercial Mobile Services,* Sixth Report, 16 FCC Rcd 13350, 13353, 13354 (2001) ("*2001 Competition Report*"); *In re Implementation of Section 6002(B) of The Omnibus Budget Reconciliation Act of 1993, Annual Report and Analysis of Competitive Market Conditions With Respect To Commercial Mobile Services*, Fifth Report, 15 FCC Rcd 17660, 17663, 17665, 17669, 17670, 17678 (2000) ("*2000 Competition Report*"); *In re Implementation of Section 6002(B) of The Omnibus Budget Reconciliation Act of 1993, Annual Report and Analysis of Competitive Market Conditions With Respect To Commercial Mobile Services*, Fourth Report, 14 FCC Rcd 10145, 10147-10152 (1999) ("*1999 Competition Report*").

[46] For example, Verizon Wireless currently offers the Motorola T300p handset for the deeply discounted price of $29.99. *See* http://www.verizonwireless.com/ b2c/store/ controller? item= phone First &action=viewPhoneOverview. The same handset is listed at a retail price of $149.99 on the Motorola Website. *See* http://motorola.digitalriver.com/servlet/ControllerServlet?Action=DisplayPage&Locale=en _US&id=ProductDetailsPage&SiteID=motostor&productID=36068500&Env=BASE. The Verizon Wireless Website also offers the LF VX 3300 handset for $29.99 and offers a "buy one, get one free" promotion on that phone.

service and equipment documentation. Most of the rate plans offered by wireless providers do not require customers to pay for these services up front, but permit the customer to pay for services gradually over the life of the contract.

Some or all of the costs of acquisition may be incurred by a provider when a customer renews a contract, depending upon such factors as the customer's reason for contract renewal, the nature of the contract renewal, and the components of the bargain reached with the customer. Wireless providers offer subsidized handsets and other discounts or promotions to many customers when they renew their contracts. The length of time required to recoup costs of customer acquisition varies with the price plan and with individual usage.

Like other rate components, ETFs are charged to compensate the carriers for the ongoing costs of providing wireless services, for the costs they incur in acquiring and retaining customers, and to earn a profit from these business activities. Akin to other fees wireless providers charge their customers, the ETF is a part of their "rates" within the meaning of Section 332(c)(3)(A).

Reasoned judicial analysis likewise supports this conclusion. In *Aubrey v. Ameritech Mobile Communications, Inc.*,[47] for example, the court held that a plaintiff's challenge to an ETF was preempted because the ETF itself was a "rate charged." The court found that by "alleging that the rates which [the carrier] charged for terminating a subscriber's service were exorbitant, it is clear that the Plaintiff is challenging the *rates charged* by [the carrier] for its wireless services."[48] The court also noted that a decision in the plaintiff's favor would "obligate [the carrier] to lower its rates for these services," so "claims, which relate to . . . the rates that are

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47 2002 U.S. Dist. LEXIS 15918 (E.D. Mich. June 14, 2002).

48 *Id.* at *12 (emphasis added).

attendant to *providing* [cellular] services" are preempted.[49] Courts have similarly held that fees charged to wireless subscribers, even with no overt connection to any particular service provided, are "rates charged" for preemption purposes.[50]

2. State Regulation of ETFs Is Preempted Because ETFs Are an Integral Part of Wireless Carriers' "Rate Structures."

The ETF is also a "rate" for preemption purposes because it is a fundamental part of wireless carriers' "rate structures." Section 332(c)(3)(A) prohibits state regulation of both "rate levels," as well as "rate elements" and "rate structures."[51]

The ETF plays a central role in the setting of prices for wireless services; accordingly, it is an integral part of wireless carriers' overall rate structures. The ability of wireless carriers to charge for early termination is a fundamental premise of and is inextricably linked with the price levels of other elements of wireless service offerings.[52] One of the important ways that wireless carriers sell their services is by offering goods and services at a low (or zero) initial price and with low monthly charges, in exchange for a subscriber's commitment to remain a customer for a minimum length of time (usually one or two years). A subscriber may elect to terminate service

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49 *Id.* (emphasis added).

50 *See, e.g,, Gilmore v. Southwestern Bell Mobile Sys.*, 156 F. Supp. 2d 916, 923-24 (N.D. Ill. 2001) (holding that challenge to a "Corporate Account Administrative Fee" was preempted because the fee was "rate charged," even though it was not tied to any recognizable service provided by carrier; challenge "explicitly raise[d] the issue of whether [the plaintiff] received sufficient services *in return* for the fee," which was a "rate issue") (emphasis added).

51 *Southwestern Bell Mobile Sys., Inc.*, 14 FCC Rcd at 19907.

52 *See Implementation of Section 6002(B) of The Omnibus Budget Reconciliation Act of 1993*, Annual Report and Analysis of Competitive Market Conditions With Respect To Commercial Mobile Services, First Report, 10 FCC Rcd 8844, 8868 at 70, (stating that "cellular prices" have "elements" including "contract length" and "fees" for "termination") ("*1995 Competition Report*"); *Petition of the People of the State of Ca. and the Pub. Util. Comm'n of the State of Ca. to Retain Regulatory Authority Over Interstate Cellular Serv. Rates*, 10 FCC Rcd 7486, 7536 (wireless pricing "is driven in part by . . . 'free' airtime offered with certain pricing plans, termination charges (if any) and contract length (monthly or for a period of months or years)") (emphasis added) ("*Ca. Pet.*").

before the end of the contract period if he or she pays the ETF. The ETF therefore permits wireless carriers to offer attractive initial discounts and monthly pricing to customers willing to make a minimum service commitment because it acts as an insurance policy, providing revenue when such customers do not fulfill their commitments.[53]

Indeed, the various rate plan options and prices offered by wireless carriers depend on the existence of ETFs. Customers who are presented with multiple plan options, some involving ETFs, some not, will most often choose the option that offers the lowest initial cost and monthly recurring charges.[54] For example, although wireless carriers offer wireless services on a prepaid basis with no ETF, the majority of customers do not choose prepaid plans. Under prepaid plans, wireless carriers offer lower subsidies to reduce the purchase price of handset equipment because the customers have not made a commitment to use wireless services for any minimum time. In addition, although prepaid subscribers, unlike post-paid subscribers, require no credit analysis, wireless carriers generally charge higher monthly service fees for prepaid service due to the absence of a minimum contractual commitment. When wireless carriers have offered postpaid contracts on a month-to-month basis with no ETF, rate structures for those contracts have also

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[53] *See, e.g., Ryder Commc'ns, Inc.*, Mem. Op. and Order, 18 FCC Rcd 13603, 13617 (2003) (recognizing that ETFs are "a valid *quid pro quo* for the rate reductions included in long-term plans," and acknowledging that "because carriers must make investments and other commitments associated with a customer's expected level of service for an expected period of time, carriers will incur costs if those expectations are not met, and carriers must be allowed a reasonable means to recover such costs") (*Ryder Commcn's, Inc.*"); *Tele. No. Portability*, 18 FCC Rcd at 20975-76 (noting that ETFs allow wireless carriers to hedge against unmitigated customer migration and "recover[] their investment in their customers").

[54] *See* Jerry A. Hausman, "Mobile Telephone," *Handbook of Telecommunications Economics*, M. Cave et al., eds. (2002), at 577 ("Empirical research has demonstrated repeatedly that consumers pay 'too much' attention to the initial cost compared to the operating cost of a durable good . . . . [C]ompetition hassled to large discounts and subsidies for mobile handsets, as demanded by consumers. This outcome has been observed in Australia, the U.S., Canada, and the U.K. Mobile companies' consumer research in the U.S. and Australia demonstrates that consumers are most price sensitive to the up front costs of the price of handsets and monthly rental, which is consistent with market outcomes and my previous academic research.").

included higher handset costs or service charges to compensate for the shorter expected contract duration.

By contrast to prepay plans, the one-year and two-year price plans currently offered by wireless carriers contain ETF provisions. The longer assured commitment under these price plans enables the providers to reduce handset prices at the inception of the term and to reduce monthly service charges, based on the expectation that initial and ongoing costs can be recouped gradually over the life of the contract. If the ETF were invalidated, term contracts would be more difficult to enforce, resulting in increases in the other elements of term-contract prices and the possibility that term contracts might no longer be viable.

Under one-year and two-year price plans, wireless carriers offer a substantial subsidy to offset the price the customer would otherwise pay for new handset equipment. The customer receives a larger subsidy for committing to a two-year contract than he or she would receive for committing to a one-year contract – and in either case, pays less than the handset would cost in the absence of a contractual commitment. These long-term rate plans depend, in part, on the existence of an ETF.

Thus, the ETF component of the rate structure provides the customer with a choice as to how to pay for the wireless provider's costs of providing service, including handset costs: terminate early and pay for a portion of these costs in a lump sum, or enjoy a longevity discount by paying for the costs over the full service term through regular monthly charges and other charges, enabling the provider to recover its costs of providing service to the customer over the length of the contract term. If wireless providers were not permitted to charge an ETF, they would have to increase their other charges and eliminate some rate plan options currently available to subscribers.

The adoption of a rate model based on longer-term commitments and use of ETFs is consistent with consumers' desire to obtain service and promotions without paying significant up-front costs. It is also consistent with the FCC's plan to encourage competitive pricing and rapid deployment of readily accessible wireless phone services.[55]

The recent *Truth-in-Billing* ruling further supports the argument that invalidation of wireless carrier ETFs under state law is impermissible regulation of wireless carrier rate structures. In the *Truth-in-Billing Order,* the FCC found that "[s]tate regulations that *prohibit* a CMRS carrier from recovering certain costs through a separate line item, thereby permitting cost recovery only through an undifferentiated charge for service," are preempted, because such rules "clearly and directly affect the manner in which the CMRS carrier structures its rates."[56] State laws that prohibits cost recovery through a line item (and thus requires that costs be recovered through a bundled service rate) are no different than state laws prohibiting cost recovery through the ETF (and thus requires that costs be recovered through bundled service rates or some other means). Both laws "clearly and directly" affect carrier rate structure.

Because the ETF is an integral part of wireless carriers' rate structures, the ETF is a "rate" within the meaning of Section 332(c)(3)(A).

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[55] For these reasons, the FCC and the courts have validated the economic rationale underlying the use of ETFs as part of the rate structure. *See e.g., Tele. No. Portability*, 18 FCC Rcd at 20976 (2003) ("Although we prevent carriers from imposing restrictions on porting beyond necessary customer validation procedures, this does not in any way invalidate provisions in carrier contracts pertaining to minimum contract terms, *early termination fees*, credit requirements, or other similar provisions.") (emphasis added); *MCI Telecomm. Corp.*, 822 F.2d at 86 (affirming Commission's determination that cancellation and discontinuance charges are part of "rates" for interstate private-line tariffs and reasoning that such rates allow carriers to recover "the cost incurred from last-minute cancellation of orders and early termination of service," which "result in customers' not paying rates sufficient to cover the cost of filling the orders"); *Equip. Distrib. Coal., Inc. v. FCC*, 824 F.2d 1197, 1201 (D.C. Cir. 1987) (affirming Commission's conclusion that there is nothing inherently anticompetitive about early termination charges for long-term wireline equipment leases, noting that "the use of termination charges is a routine commercial leasing practice available to any lessor").

[56] *Truth-in-Billing*, 20 FCC Rcd at 6463 (emphasis in original).

B. State-Law Challenges To ETFs Constitute State Regulation of ETFs.

It is well established that "judicial action can constitute state regulatory action for purposes of Section 332."[57] State-law claims that wireless carrier ETFs are unlawful, and that ETFs therefore must be prohibited, refunded, or modified to comply with state law, would subject ETFs to state supervision. Thus, actions based on such claims regulate ETFs and therefore regulate rates. These actions, currently being prosecuted around the country, also constitute rate regulation because the plaintiffs call on the court or arbitrator to determine the *reasonableness* of a prior rate" or to "set[] a prospective charge for services" under state law.[58]

This ban on assessing the "reasonableness" of rates under state law also extends to generally applicable contract or consumer laws. As the FCC explained, such laws may constitute preempted rate or entry regulation because "it is the substance, not merely the form" that determines whether a regulation is preempted under Section 332.[59] Thus, "whether a specific damage award is prohibited by Section 332 will depend on the specific details of the calculation methodology as applied in a particular case."[60] The FCC and the federal courts have

57 *Wireless Consumers Alliance*, 15 FCC Rcd. at 17027.

58 *Id*. at 17041 (emphasis added); *see id*. at 17035 (states may not make "determination[s] of whether a price charged for [wireless] service is unreasonable" or "set[ting] a prospective price for [wireless] service"); *Haw. Pet.*, 10 FCC Rcd at 7882 (state requirements that wireless carriers submit tariffs constitute impermissible rate regulation); *see also Fedor v. Cingular Wireless, Corp.*, 355 F.3d 1069, 1073 (7th Cir. 2004) (explaining that "state law claims are preempted where the court must determine whether the price charged for a service is unreasonable, or where the court must set a prospective price for a service."); *AT&T Corp. v. FCC*, 349 F.3d 692, 701 (D.C. Cir. 2003) (same); *Brown v. Baltimore/Washington Cellular, Inc.*, 109 F. Supp. 2d 421, 423 (D. Md. 2000) (Section 332 preempts all claims "that involve the reasonableness of the rates themselves.").

59 *Wireless Consumer Alliance*, 15 FCC Rcd at 17304, 17037.

60 *Id*. at 17026.

not hesitated to preempt state attempts to engage in any "reasonableness" analysis of wireless rates.[61]

Section 332(c)(3)(A) "not only prohibits states from prescribing how much may be charged for CMRS, but also prohibits states from prescribing the rate elements for CMRS or specify[ing] which among the CMRS services provided can be subject to charges by CMRS providers."[62] Suits that require courts to consider the "reasonableness" of a given contractual term violate this provision.[63] Here, the ETF lawsuits and arbitrations based on state law rest on a combination of statutory and common-law causes of action premised on the allegation that ETFs are "unreasonable," "unfair," or "inequitable." Accordingly, Section 332(c)(3)(A) expressly preempts these actions.

The suits at issue generally rely on three related common law equitable doctrines – unconscionability, illegal penalties, and quasi-contract – *each of which, as demonstrated below, requires a court to assess the "reasonableness" of ETFs*. As the *CTIA Petition* notes, the most common doctrine employed to overturn a contractual provision on equitable grounds is unconscionability. "In order to render a contract unenforceable under the doctrine of unconscionability, there must be both a procedural and substantive element[.]"[64] Importantly, a

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[61] *See Wireless Consumers Alliance*, 15 FCC Rcd at 17305; *Hawaii Pet.*, 10 FCC Rcd at 7882; *Fedor*, 355 F.3d at 1074; *AT&T Corp.*, 349 F.3d at 701.

[62] *Truth-in-Billing*, 20 FCC Rcd at 6462 (internal quotation marks omitted) (alteration in original).

[63] *See Fedor*, 355 F.3d at 1074.

[64] *Ferguson v. Countrywide Credit Indus., Inc.*, 298 F.3d 778, 783 (9th Cir. 2002); *see also Beaver v. Grand Prix Karting Ass'n, Inc.*, 246 F.3d 905, 910 (7th Cir. 2001); *Woodfield v. Providence Hosp.*, 779 A.2d 933, 937 (D.C. 2001); *Anderson v. Ashby*, 873 So. 2d 168, 194 (Ala. 2003), *cert. denied*, 124 S. Ct. 1506 (Mar. 1, 2004); *Little v. Auto Stiegler, Inc.*, 63 P.3d 979, 983 (Ca. 2003). Only a few states have invalidated contracts based on *either* procedural or substantive unconscionability. *See e.g., E. Ford, Inc. v. Taylor*, 826 So.2d 709, 714 (Miss. 2002); *Helstrom v. N. Slope Borough*, 797 P.2d 1192, 1200 (Alaska 1990). Thus, with few exceptions, a party must show *both* procedural and substantive unconscionability to invalidate an agreement. RICHARD A. LORD, WILLISTON ON CONTRACTS § 18:10 (4th ed. 2004); *see*,

"[d]etermination of whether a contract provision is substantively unconscionable rests on whether the provision is substantively *reasonable*."[65]

In some ETF cases,[66] plaintiffs have attempted to invalidate their contracts by alleging procedural unconscionability and by labeling the agreements as contracts of adhesion. However, "[t]he common law, recognizing that standardized form contracts account for a significant portion of all commercial agreements, . . . subjects terms in contracts of adhesion to scrutiny for *reasonableness*."[67] Accordingly, when a court is confronted with an alleged contract of adhesion, the terms will generally be enforceable unless they are so unfair as to be *unreasonable*.[68]

Plaintiffs also challenge ETF clauses by alleging that the fees impose an illegal penalty.[69] Although "[c]ontracting parties may agree to the payment of liquidated damages in the event of a breach, . . . [c]ourts will not enforce such a provision . . . if the stipulated amount constitutes a penalty."[70] A "penalty . . . is designed to coerce performance by punishing nonperformance . . . . '[T]he characteristic feature of a penalty is its lack of proportional relation to the damages which

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e.g., Alexander v. Anthony Int'l, L.P., 341 F.3d 256, 265 (3d Cir. 2003); *Ting v. AT&T Corp.*, 319 F.3d 1126, 1148 (9th Cir. 2003), *cert. denied*, 124 S. Ct. 53 (Oct. 6, 2003) (applying California law).

65 *Lozada v. Dale Baker Oldsmobile, Inc.*, 91 F. Supp. 2d 1087, 1102 (W.D. Mich. 2000) (citing *Andersons, Inc. v. Horton's Farm, Inc.*, 166 F.3d 308, 323 (6th Cir. 1998)) (other citations omitted) (emphasis added).

66 *See, e.g., California Verizon Compl.* ¶ 28; *Fl. Verizon Compl.* ¶ 17.

67 *Carnival Cruise Lines, Inc. v. Shute*, 499 U.S. 585, 600-01 (1991) (emphasis added) (finding forum selection clause in cruise line's passage contract ticket enforceable because it was *reasonable*).

68 "[W]hen a party of little bargaining power, and hence little real choice, signs a *commercially unreasonable* contract with little or no knowledge of its terms, it is hardly likely that his consent, or even an objective manifestation of his consent, was ever given to all of the terms." *Id.* (emphasis added) (quoting *Williams v. Walker-Thomas Furniture Co.*, 350 F.2d 445, 449-450 (1965)) (footnotes omitted).

69 *See, e.g., Ill.Compl.* ¶¶ 27-32.

70 *Vanderbilt Univ. v. DiNardo*, 174 F.3d 751, 755 (6th Cir. 1999) (citation omitted).

may actually flow from failure to perform under a contract.'"[71] In assessing "proportionality," the ultimate *reasonableness* of the ETF will shape a court's decision whether to treat the challenged contractual term as a valid damages clause or as an illegal penalty.[72] Section 332 prohibits the state-law "reasonableness" assessment that these illegal-penalty suits demand.

In still other cases, plaintiffs rely on quasi-contract doctrines to attack ETF clauses. Courts impose quasi-contractual obligations in the absence of an express contract in order to achieve a "just result" and do not consider the parties' intentions.[73] Although plaintiffs often describe the doctrine using differing labels – including implied-in-law, unjust enrichment, quantum meruit, and restitution – all quasi-contract claims require the plaintiff to satisfy the same basic criteria: "(1) [a] benefit conferred on the defendant by the plaintiff; (2) [a]n appreciation or knowledge by the defendant of the benefit; and (3) [t]he acceptance or retention by the defendant of the benefit under such circumstances as to make it *inequitable* for the defendant to retain the benefit without payment of its value."[74]

In considering such a quasi-contract theory, the court must disregard any contractual language and determine whether it should return the ETFs based solely on principles of equity.[75]

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71 *Demczyk v. Mut. Life Ins. Co.*, 126 F.3d 823, 828 (6th Cir. 1997) (quoting *Lake Ridge Acad. v. Carney*, 613 N.E.2d 183, 188 (Ohio 1993)); *see also DiNardo*, 174 F.3d at 755.

72 *See e.g.*, *Miller v. Nissan Motor Acceptance Corp.*, 362 F.3d 209, 226 (3d Cir. 2004) (interpreting Pennsylvania law); *Honey Dew Assocs. v. M & K Food Corp.*, 241 F.3d 23, 24 (1st Cir. 2001); *DJ Mfg. Corp. v. United States*, 86 F.3d 1130, 1133 (Fed. Cir. 1996); *Finkle v. Gulf & W. Mfg. Co.*, 744 F.2d 1015, 1021 (3d Cir. 1984).

73 *See, e.g.*, *Luden's Inc. v. Local Union No. 6*, 28 F.3d 347, 364 (3d Cir. 1994) (quoting WILLISTON ON CONTRACTS § 1:6).

74 *Cooper v. Salomon Bros.*, 1 F.3d 82, 86 n.1 (2d Cir. 1993) (quoting *CBS Surgical Group v. Holt*, 426 A.2d 819, 821 (Conn. Super. Ct. 1981)) (emphasis added); *see also* WILLISTON ON CONTRACTS § 68:5 (citation omitted).

75 *See R.B. Ventures, Ltd. v. Shane*, 112 F.3d 54, 60 (2d Cir. 1997) ("[C]laims for unjust enrichment or *quantum meruit* do not hinge on the existence of an agreement, oral or otherwise."); *Weichert Co. Realtors v. Ryan*, 608 A.2d 280, 285 (N.J. 1992) (citations and quotations omitted) ("[Q]uasi-contractual

As with equitable rulings generally, quasi-contract claims are grounded in broad notions of "fairness" and inherently turn on a "reasonableness" determination.[76] As the FCC presaged in another matter concerning CMRS rates, because "an award of quantum meruit would require the court to establish a value (i.e., set a rate) for the service provided, . . . there is substantial question whether a court may award quantum meruit or other equitable relief under state law without running afoul of section 332(c)(3)(A)."[77] The Commission found a "strong suggest[ion] that a claim based on quantum meruit [is] preempted."[78]

Finally, some state-court plaintiffs bring their claims through state unfair competition laws or similar legislative enactments.[79] State statutes prohibit a broad array of "unfair" practices.[80] Because these statutory claims, just like their common law progenitors, ultimately turn on *reasonableness*, these claims too are preempted by section 332(c)(3)(A).

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recovery . . . rests on the equitable principle that a person shall not be allowed to enrich himself unjustly at the expense of another.").

[76] *See Reisenfeld & Co. v. Network Group, Inc.*, 277 F.3d 856, 863 (6th Cir. 2002); *Heller v. Fortis Benefits Ins. Co.*, 142 F.3d 487, 495 (D.C. Cir. 1998); *Pioneer Operations Co. v. Brandeberry*, 789 P.2d 1182, 1189 (Kan. Ct. App. 1990).

[77] *Pets. of Sprint PCS and AT&T Corp.*, Declaratory Ruling, 17 FCC Rcd 13192, 13198 n.40 (2002).

[78] *AT&T*, 349 F.3d at 378. Furthermore, regardless of whether the cause of action itself involves a "reasonableness" inquiry, equitable and quasi-contract remedies uniformly require the court to engage in an assessment of "reasonable" damages. If a contract, in whole or in part, is deemed to be "unreasonable," the defendant is still entitled to recover from the plaintiff the amount of its "actual" damages. *See Lake River Corp. v. Carborundum Co*., 769 F.2d 1284, 1287 (7th Cir. 1985). The inquiry needed to discern the non-breaching party's "actual" damages involves the prohibited "reasonableness" assessment. *See Wallace Real Estate Inv. v. Groves*, 881 P.2d 1010, 1016 (Wash. 1994).

[79] The class action suits pending in California, for example, rely on a number of California statutes to challenge ETF as essentially unreasonable. *See Ca. Verizon Compl.* at ¶¶ 42-68.

[80] For instance, in California, the plaintiffs argue that the defendants violated the California Consumer Legal Remedies Act ("CLRA"), Ca. Civ. Code §§ 1750 *et seq*., by inserting "unconscionable, unenforceable and illegal provisions in their contracts." *See Ca. Verizon Compl*. at ¶ 49; *see also* Ca. Civ.

In sum, all state-law claims that demand a "reasonableness" inquiry – regardless of the label, or whether grounded in the common law or statute – are preempted under Section 332(c)(3)(A). All the claims in the pending ETF actions turn on a determination of the "reasonableness" of ETFs. As such, all are preempted under Section 332(c)(3)(A).[81]

C. <u>ETFs Are Not "Other Terms and Conditions" Outside the Scope of Express Preemption by Section 332.</u>

There is one exception to Section 332's express preemption of state law: it states that "this paragraph shall not prohibit a State from regulating the *other* terms and conditions of commercial mobile services."[82] Although some parties may attempt to rely on this language in arguing that their state-law claims are not preempted by Section 332, the "other terms and conditions" exception does not cover ETFs.[83] Congress did not contemplate that ETFs would be subject to multi-layered state regulation (legislative, judicial, or administrative) as "other terms and conditions."

Section 332(c)(3)(A) divides terms and conditions into two mutually exclusive categories. If ETFs are rates within the meaning of the first clause of the statute, they *cannot,* as a matter of statutory construction, be "*other*" terms and conditions. Should the Commission

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Code § 1770(a)(19) (making it a violation of the CLRA to insert "an unconscionable provision in the contract"). And, the plaintiffs argue under California's Unfair Competition Law ("UCL"), Ca. Bus. & Prof. Code §§ 17200 *et seq*., that the ETF is "a contract of adhesion" that offers "no meaningful choice" and contains terms that are "unreasonably favorable, . . . unduly harsh . . . [and] therefore is substantively unconscionable." *See Ca. Verizon Compl*. at ¶ 57.

81 Should there be any doubt that the state court suits at issue are prohibited rate regulation within the meaning of Section 332(c)(3)(A), the constitutional problems that the suits create under the Commerce Clause, *see infra* Part IV, compel that conclusion. *See Solid Waste Agency of N. Cook County v. United States Army Corps of Eng'rs*, 531 U.S. 159, 173 (2001) (quoting *Edward J. DeBartolo Corp. v. Fla. Gulf Coast Bldg. & Constr. Trades Council*, 485 U.S. 568, 575 (1988)) ("[W]here . . . an otherwise acceptable construction of a statute would raise serious constitutional problems, [courts] will construe the statute to avoid such problems unless such construction is plainly contrary to the intent of Congress.").

82 *See* 47 U.S.C. § 332(c)(3)(A) (emphasis added).

83 *Id*.

agree that ETFs are rates and part of rate structures, it need not engage in any further analysis of this language.

Suits that challenge ETFs do not resemble billing disputes or disclosure matters that might constitute "other terms and conditions." They do not challenge, for example, whether a customer was charged for the wrong plan or for usage on somebody else's phone number, but instead seek to invalidate as a matter of law an essential element of a carrier's rates by attacking the substance and operation of ETFs. The lawsuits are not based on allegations that the ETFs are not properly disclosed, and in any event no such allegation would be credible.[84]

State litigation over ETFs also is not the type of "neutral application of state contractual or consumer fraud laws"[85] that the FCC determined is not preempted by Section 332.[86] These suits are targeted at the wireless industry and, as explained above, clearly involve a determination of reasonableness under the various causes of action alleged, not to mention the adjudication of any damages.[87] These cases are not like *Wireless Consumers Alliance*, in which the Commission found that state damages awards are not necessarily rate regulation because such awards might have only an "uncertain" and "indirect" effect on CMRS prices.[88] Nor can the effort to invalidate ETFs be characterized as "incidental" to rates.[89] The reason the pending

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84 *See, e.g.,* Verizon Wireless Subscriber Agreement (Agreement attached as Exhibit G).

85 *Southwestern Bell Mobile Sys., Inc.*, 14 FCC Rcd. at 19903.

86 *See Wireless Consumers Alliance*, 15 FCC Rcd at 17025; *In the Matter of Petition of the State Indep. Alliance and the Indep. Telecomms. Group for a Declaratory Ruling that the Basic Universal Serv. Offering Provided by W. Wireless in Kan. Is Subject to Regulation as Local Exch. Serv.*, 17 FCC Rcd 14802, 19819 n.119 (2002).

87 *See supra* Part II.B.

88 *Wireless Consumers Alliance*, 15 FCC Rcd. at 17034.

89 *See id.* at 17041.

actions challenge rates is not that invalidating the ETF would indirectly affect rates by increasing carriers' costs. Rather, the actions challenge rates because they would prohibit carriers from using a particular rate, the ETF, to recover their costs. For all these reasons, the state-court actions cannot be fairly characterized as within the scope of properly enforceable consumer fraud or contract laws of general application. These lawsuits seek to invalidate a central component of wireless carriers' rate structures and therefore fall squarely within the ban on state rate regulation found in Section 332(c)(3)(A) and outside the "other terms and conditions" language.

D. Section 332 Does Not Leave Consumers Without Remedy for ETF Claims

Section 332 does not work a radical reduction of substantive rights or leave consumers without recourse. Wireless carriers' rates and rate structures remain subject to federal review under the "unjust or unreasonable" standard set forth in 47 U.S.C. § 201(b), and the nondiscrimination requirements contained in 47 U.S.C. § 202(a).[90] Hence, Section 332 does not foreclose challenges to wireless carrier rates – it simply requires plaintiffs to pursue those claims in the forum dictated by Congress.

III. STATE ACTIONS CHALLENGING OR REGULATING ETFs FRUSTRATE AND IMPEDE CONGRESS'S DEREGULATORY MODEL

The FCC has plenary authority and the responsibility to consider any proposed regulation of the wireless industry.[91] The Supreme Court has flatly stated that "[t]he statutorily authorized

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[90] The FCC has found however that wireless rates are presumptively reasonable and nondiscriminatory because wireless carriers lack market power in this highly competitive industry. *See Implementation of Sections 3(n) and Section 332 of the Commc'ns Act Regulatory Treatment of Mobile Serv.*, Second Order and Report, 9 FCC Rcd 1411, 1478 (1992).

[91] *See Cavalier Tel., LLC v. Verizon Va., Inc.*, 330 F.3d 176, 186 (4th Cir. 2003), *cert. denied*, 124 S. Ct. 1144 (Jan. 20, 2004) ("[T]he FCC has the responsibility of coordinating the national telecommunications market."); *Revision of the FCC's Rules to Ensure Compatibility With Enhanced 911 Emergency Calling Systems*, 17 FCC Rcd 25576, 25610 (2002) (The FCC "has jurisdiction over interstate telecommunications and the providers of such services . . . [and] . . . [s]uch authority extends to commercial mobile services by operation of section 332 of the Act.").

regulations of an agency will pre-empt any state or local law that conflicts with such regulations *or frustrates the purposes thereof*."[92] Thus, even apart from the express preemption of these state law challenges to ETFs by Section 332, the FCC possesses authority to find the challenges preempted based on the fact that they pose an obstacle to the accomplishment of federal policy as embodied by the Commission's regulations.

In the *Truth-In-Billing Order,* the FCC again declared that any "regulation of interstate services that conflicts with federal *rules and objectives* may be subject to future preemption."[93] In preempting state regulations regarding wireless line item requirements, the FCC held that the state regulations conflicted with "the federal policy of a uniform, national and deregulatory framework for CMRS."[94] Even before the passage of the Telecommunications Act, the FCC had long acted to prevent "state and local regulations [from] conflict[ing] with and thereby frustrat[ing]" the federal goal of nationwide compatibility for mobile telephony.[95] As a general rule, the national framework has "rel[ied] on the competitive marketplace to ensure that CMRS carriers do not charge rates that are unjust or unreasonable, or engage in unjust or unreasonable discrimination."[96]

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92 *New York v. FCC*, 486 U.S. 57, 64 (1988) (emphasis added).

93 *Truth-in-Billing*, 20 FCC Rcd at 6465-66 (emphasis added).

94 *Id*. at 6466-67.

95 *An Inquiry Into the Use of the Bands 825-845 MHz and 870-890 MHz for Cellular Comm'ns Sys.; and Amendment of Parts 2 and 22 of the FCC's Rules Relative to Cellular Comm'ns Sys.*, Report and Order, 86 FCC 2d 469, 503-05 (1981). Even before the passage of Section 332, the FCC has long reiterated the strong federal nature of many elements of the wireless industry. *See generally Amendment of Parts 2 and 22 of the FCC's Rules to Permit Liberalization of Technology and Auxiliary Service Offerings in the Domestic Public Cellular Radio Telecommunications* Service, 3 FCC Rcd 7033 (1988).

96 *Wireless Consumers Alliance*, 15 FCC Rcd at 17033 n.71; *see also Petitions of Sprint PCS and AT&T Corp. for Declaratory Ruling Regarding CMRS Access Charges*, 17 FCC Rcd 13192, 13197 n.33 (2002) (citation omitted).

The FCC also exercises its preemption authority based on "the significant possibility that state regulation would lead to a patchwork of inconsistent rules[.]"[97] Specifically, the FCC has stated that a "CMRS carrier forced to adhere to a varying patchwork of state . . . requirements . . . would be forced to adjust its rate structure from jurisdiction to jurisdiction."[98] Such a patchwork arrangement would substantially undercut the existing "uniform, national and deregulatory framework" and "would undermine the benefits derived from allowing CMRS carriers the flexibility to design national or regional rate plans."[99]

Because of the FCC's fidelity to the "pro-competitive, deregulatory framework for CMRS prescribed by Congress . . . wireless competition [has] flourish[ed], with substantial benefits to consumers."[100] Importantly, as noted above, the wireless market has become vigorously competitive on a nationwide level.[101] For example, the FCC noted in its most recent report on the state of competition in the wireless industry that "competitive pressures continue to compel carriers to introduce innovative pricing plans and service offerings, and to match the

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97 *Truth-in-Billing*, 20 FCC Rcd at 6466-67.

98 *Id*. at 6463-64.

99 *Id*. at 6466-67. This concern understandably led to the primary jurisdiction referral in the *SunCom* litigation, and more importantly, should have led the other state courts to issue stays pending the outcome of this FCC proceeding. Courts are supposed to utilize primary jurisdiction referrals in two circumstances: (1) "to obtain the benefit of an agency's expertise and experience"; and (2) "to promote uniformity and consistency within the particular field of regulation." *See Access Telecommunications v. Southwestern Bell Telephone Co.*, 137 F.3d 605, 608 (8th Cir. 1998) (citations omitted). Here, the FCC expertise in examining the contours of Section 332 and the obvious need for uniformity should have led to stays in the pending state-court ETF suits. Again, only the South Carolina court has so far followed this sensible course. As noted, the Alameda County court in California has declined to enter a complete stay of the actions before it.

100 *Truth-in-Billing*, 20 FCC Rcd at 6466

101 *See 2004 Competition Report*, 19 FCC Rcd at 20608 n.33.

pricing and service innovations introduced by rival carriers."[102] Additionally, wireless providers have expanded their networks and their reach.[103] The expanded networks provide carriers with "certain economies of scale and increased efficiencies compared to operators with smaller footprints."[104] As a result of these efficiencies and improved service areas, carriers have offered a "continued rollout of differentiated pricing plans," a strong indication of "a competitive marketplace."[105] As Chairman Martin recently stated, "wireless has become a more national service [and] is a robustly competitive field[.]"[106]

State regulation of ETFs through the lawsuits documented above threatens to substantially impair the "uniform, national, and deregulatory" wireless framework established by the FCC. Moreover, the disparate state regimes produced by this litigation will result in a patchwork of haphazard oversight that requires wireless carriers "to adjust [their] rate structure[s] from jurisdiction to jurisdiction."[107] Such state regulation of ETFs thus conflicts with the national, pro-competitive "rules and objectives" that the FCC is charged with enforcing, and are subject to preemption on this basis as well.[108]

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102 *2004 Competition Report*,, 19 FCC Rcd at 20600 (2004) (stating that "competition continues to afford many significant benefits to consumers").

103 *Id*. at 20623 ("More recently, national operators have sought to fill in gaps in their coverage areas, as well as to increase the capacity of their existing networks.").

104 *Id*.

105 *Id*. at 20644 ("In the mobile telephone sector, we observe independent pricing behavior, in the form of continued experimentation with varying pricing levels and structures, for varying service packages, with various available handsets and policies on handset pricing.").

106 *Presentation of Commissioner Kevin J. Martin*, 2004 FCC LEXIS 5871, at * 10 (2004).

107 *Truth-in-Billing*, 20 FCC Rcd at 6464.

108 *Id*. at 6465-66.

The importance of national regulation of uniquely interstate services "compelled" the FCC recently to preempt the Minnesota Public Utilities regulation of Voice over Internet Protocol (VoIP) because such regulation "could severely inhibit the development" of such services.[109] Just as in the VoIP context, the FCC should determine that it "cannot, and will not, risk eliminating or hampering" new CMRS services because such innovation "facilitates additional consumer choice, [and] spurs technological development,"[110] and accordingly preempt the actual and impending state efforts that will thwart the uniform, deregulatory scheme for wireless service.

IV. STATE REGULATION OF ETFs RUNS AFOUL OF THE COMMERCE CLAUSE.

State superintendence over ETFs not only violates federal preemption law, but also contravenes the federal commerce power. As in *Vonage*, the Commission can and should rely on this ground to buttress the decision to declare ETFs either expressly preempted by Sections 332(c)(3)(A) or impliedly preempted in light of the inconsistencies between state regulation of those charges and the federal goals of uniformity and light regulation for wireless services.[111] The Commerce Clause forbids state regulation of ETFs for two reasons.

First, state regulation of ETFs "impose[s] a disproportionate burden on interstate commerce."[112] State ETF oversight, whether through legislative act or judicial intervention,

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[109] *Vonage*, 19 FCC Rcd at 22418 (VoIP is "far more similar to CMRS, which provides mobility, is often offered as an all-distance service, and needs uniform national treatment on many issues.").

[110] *Id.* at 22417 .

[111] *Id.* at 22412 (noting that "multiple state regulatory regimes would likely violate the Commerce Clause"); *id.* at 22427 (observing that "our decision [to preempt state regulation of VOIP] today is fully consistent with the Commerce Clause").

[112] *Nat'l Elec. Mfrs. Ass'n v. Sorrell*, 272 F.3d 104, 112 (2d Cir. 2001); *see also Cloverland-Green Spring Dairies, Inc. v. Pa. Milk Mktg. Bd.*, 298 F.3d 201, 211 (3d Cir. 2002) ("[I]t is clear that state laws

would result in a balkanized regime, whereby wireless carriers would need to adjust their rates and rates structures from state to state. Each state regime would be "in substantial conflict with a common regulatory scheme in place in other states"[113] and would impose prohibitive compliance costs that far exceed any local benefit. The Supreme Court repeatedly invalidates state regulations that "prescribe standards for interstate [companies] that . . . conflict with the standards of another State" and require the company to change an important element of the company's behavior "once another state line was reached."[114] The varying ETF regulations will force CMRS providers to adjust their rates and their contracts in a similar manner.

Second, state regulation of ETFs has an unconstitutional extraterritorial impact on conduct outside of the state.[115] As one court observed, "the serious risk of inconsistent obligations wrought by the extraterritorial effect of [a state law] demonstrates why it constitutes a per se violation of the Commerce Clause."[116] The possibility of inconsistent state regulation is

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that are facially neutral but have the effect of eliminating a competitive advantage possessed by out-of-state firms trigger heightened scrutiny.").

113 *Nat'l Elec. Mfrs. Ass'n*, 272 F.3d at 112; *see also Pike v. Bruce Church, Inc.*, 397 U.S. 137, 145 (1970) (noting that "the Court has viewed with particular suspicion state statutes requiring business operations to be performed in the home State that could more efficiently be performed elsewhere").

114 *Bibb v. Navajo Freight Lines, Inc.*, 359 U.S. 520, 526 (1959) (invalidating an Indiana regulation regarding mudguards when that regulation conflicted with other states' mudguard rules); *see also Brown-Forman Distillers Corp. v. New York State Liquor Auth.*, 476 U.S. 573, 583 (1986) (invalidating statute that required a distiller to "seek the approval of the New York State Liquor Authority before it may lower its price for the same item in other States."); *S. Pac. Co. v. Ariz. ex rel. Sullivan*, 325 U.S. 761 (1945) (invalidating statute that posed similar problems regarding train lengths).

115 *See Healy v. Beer Inst., Inc.*, 491 U.S. 324, 332 (1989).

116 *NCAA v. Miller*, 10 F.3d 633, 639-40 (9th Cir. 1993); *see also S.D. Myers, Inc. v. City and County of San Francisco*, 253 F.3d 461, 470 (9th Cir. 2001) ("However, it is clear in context that the likelihood of conflicting legislation in *NCAA* [*v. Miller*] was far from speculative. Such legislation had in fact been adopted by three states and introduced in five states. In addition, we emphasized that the risk of inconsistent regulation was serious.") (internal citation omitted).

not only a "serious" risk but is a virtual certainty, evidenced by the actual or pending litigation in state courts around the country, as well as the other state regulatory initiatives also underway.

The foregoing authorities address the constitutional imperative to ensure that national markets operate free of state interference. "The courts have long recognized that certain types of commerce demand consistent treatment and are therefore susceptible to regulation only on a national level."[117] Here, the impact of state wireless regulation on interstate commerce is even more troubling given the uniquely interstate nature of CMRS and because of Congress's clearly expressed desire for a consistent federal policy of minimal regulation at the national level in the area of wireless service.[118] Hence, as the FCC explained, "courts have held that 'state regulation of those aspects of commerce that by their unique nature demand cohesive national treatment is offensive to the Commerce Clause.'"[119] State regulation of ETFs violates this rule. Patchwork state regulation over this uniquely national service runs afoul of the Commerce Clause.

V. CONCLUSION

For the foregoing reasons, the Commission should declare that: (1) ETFs are rates and rate structures within the meaning of Section 332(c)(3)(A); (2) the state law claims, whether common law or statutory, currently being raised against ETFs seek to regulate rates under the

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117 *Am. Library Ass'n v. Pataki*, 969 F. Supp. 160, 181 (S.D.N.Y. 1997) ("The courts have long recognized that certain types of commerce demand consistent treatment and are therefore susceptible to regulation only on a national level."); *ACLU v. Johnson*, 194 F.3d 1149, 1162 (10th Cir. 1999) (applying *Pataki* analysis). For example, "because of 'the Internet's boundary-less nature,' regulations of Internet communications may not be 'wholly outside' a state's borders, but nonetheless may impose extraterritorial regulation in violation of the Commerce Clause." *Vonage*, 19 FCC Rcd at 22428 and n.135 (quoting *Am. Booksellers Found. v. Dean*, 342 F.3d 96, 103 (2d Cir. 2003)).

118 *See, e.g., Sprint Spectrum L.P.*, 244 F. Supp. 2d at 112 (quoting *Cellular Tel. Co. v. Town of Oyster Bay*, 166 F.3d 490, 492-93 (2d Cir. 1999)) ("Congress enacted the TCA 'to provide a pro-competitive, de-regulatory national policy framework designed to accelerate rapidly private sector deployment of advanced telecommunications and information technologies and services . . . by opening all telecommunications markets to competition[.]'").

119 *Vonage*, 19 FCC Rcd at 22428 and n.134 (quoting *Pataki*, 969 F. Supp. at 169 (citing *Wabash, St. Louis & Pac. Ry. Co. v. Ill.*, 118 U.S. 557 (1886))).

statute; and (3) the state law claims are therefore expressly preempted by Section 332(c)(3)(A). In the alternative, the Commission should declare that the state law claims at issue are preempted because they will thwart the long-standing federal goals of uniform, deregulatory treatment of wireless services that have thus far promoted the development of a vibrantly competitive national market for wireless services.

Respectfully submitted,

/s/

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