

Wither Net Neutrality Regulation? Net Neutrality Special Issue Blog #3

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Net neutrality rules are not the way to maintain a free and open Internet, according to Michael Katz, Sarin Professor Emeritus in Strategy and Leadership at the UC Berkeley Haas School of Business and Professor Emeritus at the Berkeley Department of Economics.

This post is the third in a series highlighting the contents of a recent special issue of the *Review of Industrial Organization*, organized by the Technology Policy Institute and the University of Pennsylvania's Center for Technology, Innovation, and Competition. Katz's contribution, "[Wither, Net Neutrality?](#)," analyzes the relationship between current net neutrality regulations and the outcomes they were adopted to achieve.

The 2015 rules passed by the Federal Communications Commission (FCC) under Chairman Tom Wheeler were intended to preserve a "free and open Internet," and by extension, to foster creativity and innovation, protect free speech, and prevent exclusionary behavior in vertically integrated broadband Internet access service (BIAS) providers. Katz concludes that at best, the net neutrality rules are unlikely to yield those benefits, and are more likely to harm consumers.

Key to net neutrality, according to proponents, are the rules forbidding BIAS providers from charging edge providers to access their networks or implementing paid prioritization of traffic.

Supposedly, these bans would foster competition by "leveling the playing field" for edge providers and encouraging entry, and prevent exclusionary behavior by vertically integrated BIAS firms. Katz contends that these outcomes do not necessarily follow.

Regulation never "levels" a playing field because that assumes we know the optimal balance between firms. We don't, and if an optimal balance exists today it might be different tomorrow. In this case, proponents believe tilting the field more towards edge providers is important for innovation. One problem with that belief, Katz argues, is that the Internet has never been neutral. For example, the Internet was designed in a way that "works relatively poorly for applications that are highly sensitive to packet loss and require very low latency (e.g., telepresence) and works relatively well for applications that require little bandwidth and are not time sensitive (e.g., email)."

Another problem with the level playing field argument is that it should apply to many industries and services, not just the Internet. Yet, we know that paid prioritization has become crucial in other areas, like package delivery (think FedEx, UPS, or expedited shipping in e-commerce).

Finally, the argument tends to focus on particular firms that might not do well with paid prioritization at the expense of consumer welfare. However, consumer welfare may be improved by new services that cannot currently exist, or must exist via workarounds that are not technically "paid prioritization." The point is not that one of these necessarily outweighs the other, only that it is incorrect to automatically conclude that the net effect of paid prioritization is negative.

Katz also argues that a ban on access charges is not necessary to prevent vertically integrated BIAS firms from engaging in anticompetitive exclusionary behavior, although he acknowledges that this "is perhaps the most coherent concern expressed by proponents of net neutrality regulation." The problem here is that the Commission offered no evidence that this was a widespread problem or that these rules offered any incremental protection beyond those already offered by state and federal antitrust policies.

Proponents of the net neutrality regulations also argue that they will bring about increased innovation, since, freed from the obligation of paying BIAS providers, edge companies would have more resources to invest in creative endeavors. Perhaps. But this ignores the effects on end users.

One key economic point that proponents miss is that in two-sided markets, such as BIAS, it is not the case that it is always better for only one side—end users, in this case — to be charged.

In addition, a ban on access charges poses a risk to the supply of end users. If BIAS providers could charge edge providers and end users, end users may end up paying less. It follows, then, that a ban on access charges amounts to end users subsidizing edge providers. While this encourages free speech and innovation in edge providers, it could have the opposite effect in end users. Instead of encouraging end users to consume content a ban on access charges could potentially price some end users out of the market and depress broadband adoption.

Katz argues that economic theory strongly concludes that bans on access fees for edge providers and paid prioritization are unlikely to protect free speech, encourage creativity or innovation, protect against discriminatory behavior by vertically integrated firms, or level the playing field. Worse, they are likely to harm, rather than benefit, consumers. Yet, he acknowledges, the argument has become so polarized that “...there is no reason to believe that the political battles over net neutrality will end anytime soon (Katz, 2016, p.40).”

Note: Our intent is to summarize Katz’s paper, but mistakes are ours alone, not his.