Before the
FEDERAL COMMUNICATIONS COMMISSION
Washington, DC 20554

Further Inquiry into Two Under-	)	GN Docket No. 09-191
Developed Issues in the Open	)	WC Docket No. 07-52 and
Internet Proceeding	)	

Comments of The American Consumer Institute

The American Consumer Institute Center for Citizen Research (ACI) is a nonprofit (501c3) educational and research institute with the mission to identify, analyze and protect the interests of consumers in selected policy and rulemaking proceedings in information technology, health care, retail, insurance, energy and other matters.

In this proceeding, the Commission seeks comments on two under-developed issues – open Internet rules for special services and for wireless Internet access services. The Commission has indicated its intent to focus on facts and reasoned analyses to determine whether imposing new Internet regulations would produce more benefits for society than costs. We continue to find no factual or analytical support that identifies specific market failures that warrant *ex ante* regulations, and we have seen no evidence that any of the proposed remedies would produce a net increase in consumer welfare, the criterion set out by Congress in seeking the development of a nationwide broadband plan.[1]

We urge the Commission to conduct a welfare analysis before imposing any market remedies in the form of new Internet regulations. We also encourage the Commission to monitor industry conduct and performance, and to postpone the imposition of *ex ante*-based Internet regulations.

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[1] Recovery Act § 6001(k)(2)(D).

No Evidence of Failure in the Broadband Market

If improving economic welfare is a goal of the Commission, a discussion and collection of comments on regulatory remedies should come after an identification of market failures. To date, we find no empirical evidence entered into the public record that demonstrates the presence of market failure. However, substantial evidence has been provided that demonstrates that proposed Internet regulations would impede network investment, increase consumer prices and reduce consumer welfare.[2] The Commission should insist on empirical evidence of market failures before suggesting remedies to address problems that may not exist.

Even if hypothetical problems can be identified, competition in the broadband market has heightened in recent years and market forces are providing naturally occurring protections. Today, there is simply no urgency for addressing these potential problems, particularly given the body of economic research that demonstrates that the proposed solutions would substantially reduce consumer welfare.[3]

The fact is that the broadband market is competitive and becoming more so. Industry investment is strong and consumers have increased choice. As the broadband market continues to expand in terms of output and penetration,[4] prices are declining.[5] For

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[2] For example see comments "In the Matter of Preserving the Open Internet Broadband Industry Practices," the American Consumer Institute Center for Citizen Research, GN Docket No. 09-191 and WC Docket NO. 07-52, comments filed January 14, 2010; and essays in *The Consequences of Net Neutrality Regulations on Broadband Investment and Consumer Welfare: A Collection of Essays*, The American Consumer Institute Center for Citizen Research, November 19, 2009. See http://www.theamericanconsumer.org/2009/11/19/aci-releases-a-book-holds-a-capitol-hill-event-the-evidence-on-net-neutrality/.

[3] *The Consequences of Net Neutrality Regulations on Broadband Investment and Consumer Welfare: A Collection of Essays*, The American Consumer Institute Center for Citizen Research, November 19, 2009. See http://www.theamericanconsumer.org/2009/11/19/aci-releases-a-book-holds-a-capitol-hill-event-the-evidence-on-net-neutrality/.

[4] "High-Speed Services for Internet Access: Status as of June 30, 2006," FCC Wireline Competition Bureau, Industry Analysis and Technology Division, January 2007. http://hraunfoss.fcc.gov/edocs_public/attachmatch/DOC-270128A1.pdf.

[5] A number of sources report significant price decreases, such as prices falling from $80 to $15 per month. See Jerry Ellig, "Public Interest Comment on Broadband Connectivity Competition Policy," Mercatus Center, Project No. V070000, George Mason University, February 28, 2007; "Wireline Broadband Pricing 2001-2007," United States Telecom Association, Washington, DC, June 2008, available online at http://www.ustelecom.org/uploadedFiles/Learn/Broadband.Pricing.Document.pdf; and J. Gregory Sidak, "A

instance, the latest Bureau of Labor Statistics' Consumer Price Index for Internet Services and Electronic Information Providers shows that prices fell 23% from August 2003 to August 2010.[6] Over the same period, the overall Consumer Price Index increased by 18%, suggesting that inflation-adjusted Internet prices have declined by over 40%.[7] Meanwhile, broadband speeds have increased.

Based on SEC filings covering the latest three years of operations, the top 10 network service companies have invested over $170 billion. In addition, a study by Darby, Fuhr and Pociask found that network communications companies reinvested 64% of cash flow from operations, while edge companies reinvested 28%.[8] The study also found that network companies create twice as many jobs compared to edge companies; and that network companies earn 14% of cash flow as profits, while edge companies earn 49%.[9] In other words, the broadening and deepening capital formation underway is occurring without extraordinary profits. In fact, the profits by Internet Service Providers are generally below the average experienced by the S&P 500.[10] The much higher rates of profit among edge companies does not support the claim that network companies are stifling innovation or the success of edge companies, nor does it provide evidence of market power among network providers.

Wireless Competition

Competition in the wireless market is particularly intense. Compared to other countries, the U.S. wireless market is the least concentrated as measured by the Herfindahl-Hirschman Index. Also, U.S. subscribers pay the second lowest average rates per minute

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Consumer Welfare Approach to Network Neutrality Regulations of the Internet," forthcoming in the *Journal of Competition Law & Economics*, Oxford Press, Vol. 2:3, 2006, p. 400.

[6] BLS CPI-U indexes available at www.bls.gov and downloaded on October 10, 2010.

[7] Ibid.

[8] Larry F. Darby, Joseph P. Fuhr and Stephen B. Pociask, "The Internet Ecosystem: Employment Impacts of National Broadband Policy," The American Consumer Institute Center for Citizen Research, Washington, DC, January 28, 2010, p. 24, Chart 4.

[9] Ibid.

[10] Ibid, p. 9, Table 1. Also see "Facts about Market Power and Profits in the Internet Space," ConsumerGram, The American Consumer Institute, October 8, 2009.

in the world, and the average U.S. subscriber uses more wireless minutes than the average subscriber in other countries.[11]

The U.S. is a leader in wireless investment. According to the GSM Association and Deutsche Bank, 80% of North American investment will be put towards wireless broadband networks, compared to 50% for Europe and Asia/Pacific.[12] The nationwide investments in 4G technologies (LTE and Wi-MAX) by AT&T, T-Mobile, Verizon, Sprint Nextel and Clearwire will heighten broadband competition in the U.S., and spur additional broadband penetration. The U.S. is the leader in wireless broadband subscribers, the number of wireless handsets offered and smart phone sales.[13] Imposing regulations on a competitive market, and one with significant capacity restrictions, would reduce investment, raise industry costs and lead to consumer welfare losses.

Based on the rate of broadband market growth, especially for wireless broadband, and in light of falling consumer prices, increased investment, faster subscriber speeds, decreasing market concentration and modest profits, we conclude there no evidence of market power that would justify net neutrality regulations for the broadband market, particularly for wireless providers.[14] Since the broadband market exhibits the characteristics of a competitive market, we would expect that if any carrier inappropriately blocks websites, that carrier would risk losing subscribers to other providers.

Under-Developed Issues

In terms of specialized services, we see no consumer benefit in setting limits on the extent to which services can be similar or dissimilar from one another. Also, we see no

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[11] FCC's Mobile Wireless Competition Report in 2010 and Bank of America Merrill Lynch Research in 2010 are among several sources for this data.

[12] The ITU cites TelecomPaper as the source, which sites the GSM association and Deutsch (Feb. 2010), see http://www.itu.int/ITU-D/ict/newslog/CategoryView,category,World.aspx).

[13] Ovum, Mobile Technology Forecast, December 2009; and Strategy Analytics, Global Smartphone Sales Forecast by Country, August and October 2009.

[14] For a more complete analysis see Larry F. Darby, "To Regulate; or Not to Regulate: Where's the Market Failure?" and other essays available in *The Consequences of Net Neutrality Regulations on Broadband Investment and Consumer Welfare: A Collection of Essays*, The American Consumer Institute Center for Citizen Research, November 19, 2009. See http://www.theamericanconsumer.org/2009/11/19/aci-releases-a-book-holds-a-capitol-hill-event-the-evidence-on-net-neutrality/.

consumer benefit from prohibiting specialized services from being integrated into service bundles. If consumers see value in differentiated and bundled services, then these service offerings will maximize consumer welfare and benefits. For example, consider a specialized health monitoring service for home-bound patients. Why shouldn't consumers have an option to reduce their costs by buying this type of service as part of a bundle? How do such limitations protect consumers? The fact is that product differentiation and economic price discrimination are well-accepted ways for increasing consumer welfare. Further, possible limitations on quality of service agreements might discourage the development of such monitoring services because providers might not be able to guarantee a necessary level of performance. Rules that bar prioritization could frustrate the timely performance required to ensure the effectiveness of Internet-based medical services.

We also oppose setting regulations on the capacity and performance of services during peak and off-peak periods, since this would interfere with the ability of network investors to manage their networks, which would raise network costs and discourage investments, particularly for wireless services that are uniquely constrained by capacity limitations.

On the other hand, we do support the Commission's monitoring of market conduct and performance. If anti-competitive conduct is suspected, we hope the Commission will use case-by-case adjudication to deal with any specific threats as they occur (an *ex post* approach). Such an approach has worked successfully to protect consumer interests in a variety of venues.

Asymmetric Information

On the topic of truth-in-advertising and disclosure, consumers are disadvantaged by imperfect or asymmetric information, when sellers have more and better information than buyers.[15] Unlike consumers in the textbook models of perfect competition,[16] consumers

[15] The implications of imperfect information on consumer choices have been intensively studied. An extensive review and summary is beyond our scope here, but we can recommend a handful of studies and the references they cite. See, Joan K. Lewis, Teresa Mauldin, "Returns to Investments in Information: Can

generally have an incomplete or inaccurate understanding of facts material to a particular choice. At the time of purchase, consumers may not be totally informed about the full costs of using a good or service, particularly the costs of complementary products. The costs of acquiring pertinent information -- search costs -- are often substantial, leading to poor decisions by consumers.[17] In the absence of better information, consumers can make poor decisions that will not maximize their welfare and may lessen market rivalry. Therefore, well-conceived disclosure rules that provide consumers with better information in plain language can improve consumer decision-making and yield benefits at a relatively low cost.

Conclusion

Given Congresses' goal of developing a national broadband plan, instituting network regulations that could reduce consumer welfare and discourage investment to support further expansion of broadband services would be premature and could jeopardize other national goals. Given the lack of market failure, the potential risks of such regulation far outweigh any conceivable benefit. We believe the wiser course is close monitoring of industry conduct and performance so that the Commission can respond if actual problems arise, while postponing for now the imposition of new network regulations.

Investments Reduce Bad Purchase Experiences of Consumers?" *Journal of Consumer Studies and Home Economics*, 20 (2), 183–199, 1996. The authors examine the impact of consumer information, information sources, information acquisition costs, and consumer demographics on "bad purchase" experience. The results suggest that age, education, extent of social contacts with relevant information and others were relevant. See also, George B. Sproles, Loren V. Geistfeld, and Suzanne B. Badenhop, "Types and Amounts of Information Used by Efficient Consumers," *Journal of Consumer Affairs*, Vol. 14, Issue 1, p. 37, June 1980. The paper examines the efficiency of consumer decision-making as indicated by the types and amounts of informational resources utilized. They classify consumers in three groups ranked by their relative efficiency in making optimal choices in the context of their wants/needs/preferences and the information available about alternatives. Taken together these papers indicate that inadequate consumer information leads to loss of consumer welfare; that information acquisition by consumers is often costly; and that investing in better information can lead to increased consumer welfare.

[16] For example, the model of perfect competition assumes that buyers and sellers have perfect information to make their choices.

[17] See A. Postlewaite, *Asymmetric Information, Allocation, Information, and Markets*, (John Eatwell, Murray Milgate, Peter Newman, eds.), The New Palgrave, WW Norton, NY and London, 1989, pp. 35-38.