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Perspectives from FSF Scholars
July 23, 2018
Vol. 13, No. 30

California Privacy Law Will Increase the Cost of Accessing Online Content

by

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Introduction

On June 28, 2018, California Governor Jerry Brown [signed](#) the California Consumer Privacy Act of 2018, which some are [calling](#) the “toughest data privacy laws in the United States.” The law will impose regulations broadly preventing Internet companies from collecting and selling consumer data without the consumer’s permission.

Specifically, the law states that consumers must have the ability to opt out of data collection and Internet companies cannot change the price or level of service for consumers who choose to “opt out.” These overly restrictive rules could upend the business models of many companies in the Internet ecosystem and ultimately could lead to edge providers, like Google and Facebook, employing subscription-based services to replace much of their current “free” access to Internet content. Moreover, imposing state-level privacy regulations creates a patchwork regulatory problem for Internet companies. The additional regulatory restrictions and the costs they impose could cause broadband providers to reduce infrastructure investment throughout California and other parts of the country.

How the California Consumer Privacy Act Changes Internet Business Practices

Internet service providers (ISPs) and edge providers use business models based on advertising revenues as a means of offering, without charge, innovative services to consumers. Instead of charging consumers an annual or monthly subscription, for example, edge providers often collect consumer information and deliver targeted advertisements to cover the costs of offering content. ISPs sometimes use this business model as well, like offering public WiFi to non-subscribers. For more detail on how these business models are used by Internet companies, see my [August 2016 Perspectives from FSF Scholars](#) titled “FCC Privacy Rules Would Harm Consumers by Creating Barriers for ISP Advertising.”

The California Consumer Privacy Act of 2018 establishes restrictions for how Internet companies (both ISPs and edge providers) can collect and use consumer data and discourages them from selling targeted advertisements. The California Consumer Privacy Act has the [following](#) mandates:

- Businesses must disclose what information they collect, the business purpose for collection, and any third parties with whom they share that data.
- Businesses are required to comply with official consumer requests to delete data.
- Consumers can opt out of their data being sold, and businesses can’t retaliate by changing the price or level of service for consumers who choose to opt out.
- Businesses can, however, offer “financial incentives” for being allowed to collect data.
- California authorities are empowered to fine companies for violations.

These restrictive rules likely will distort the way Internet companies deliver services in the future. Because this new law prevents Internet companies from altering the price or quality of service for consumers who choose to “opt out” of data collection, consumers will have little incentive to share their data. This could encourage large companies, like Google and Facebook, to start charging subscriptions for their services, making it even more likely that fewer and fewer California consumers will share their data. Because the law will require such companies to impose subscription fees on *all* consumers, those who do not mind sharing their data (of which many are low-income consumers) will be negatively impacted, as will consumers who shop online and benefit from the information they receive from targeted advertising.

Many consumers also use Facebook, Google, and other online services as a source of news, to search for jobs and housing and other important information, and to engage politically. If a significant share of these consumers opt out and are unwilling to pay for these services, it is likely that the quality of services will decline as the traffic and revenues needed to support these various services decrease.

Notably, the California Consumer Privacy Act avoids one problem that was created by the FCC’s 2015 *Title II Order* in that it applies to both ISPs, like cable and mobile broadband companies, and also to edge providers, like Google and Facebook. In contrast, the *Title II Order* applied only to ISPs, so that edge providers would have had an advantage in areas where they compete with ISPs, like online advertising, because the proposed FCC *Broadband Privacy Order* would have applied to ISPs but not to Google and Facebook.

As of December 2017, Google and Facebook [accounted for 73%](#) of the U.S. online advertising market, so while subscription-based services likely will decrease their overall advertising revenue in the short term, the two companies probably hold enough market power to retain their dominance of the online advertising market. Smaller content and social media companies, on the other hand, often do not have the popularity or market reach to employ a subscription-based model. But they will have to comply with the same burdensome privacy rules in California and it will cost them substantial advertising revenue.

Therefore, while Facebook and Google say they [oppose](#) the new law, their position in the market could allow them to capture an even greater share of advertising revenue from small competitors who cannot afford to comply with the costly new regulatory requirements.

The California Bills and “Net Neutrality”

Despite not being able to alter the price or level of service for consumers who choose to opt out of data collection, the California Consumer Privacy Act does allow companies to offer financial incentives for consumer data collection. But this could lead to edge providers favoring their own content, which is exactly what net neutrality supporters have warned against. For example, Amazon could offer customers who opt in to data collection a “free” month of Prime membership. And Google may offer the same consumers a “free” month of YouTube Red.

California Senator Scott Wiener recently introduced a net neutrality bill, [SB 822](#), which would hamper the ability of broadband providers to offer “free data,” or zero-rated services. Free data services are mobile broadband offerings which allow consumers to access certain online content with an exemption from monthly data caps. Typically, that means consumers can access unlimited curated online content at no additional cost, which is why these services are particularly popular among [low-income](#) consumers. So, while SB 822 would discourage ISPs from favoring their own content in the form of free data services, the new privacy law may encourage edge providers to favor their own content in other ways.

California Consumer Privacy Act Creates a Patchwork of Regulatory Requirements

When the FCC adopted the *Restoring Internet Freedom Order*, the FTC, the nation’s leading [expert agency](#) with respect to consumer protection on the Internet, regained its authority to protect consumers’ online privacy. Although the California law applies to both ISPs and edge providers, ISPs [only have](#) access to 30% of consumer data due to encryption and WiFi offloading, whereas edge providers like Facebook, Google, and Amazon can access significantly more information. Because privacy violations can occur across a wide variety of platforms, Daniel Lyons, a member of FSF’s Board of Academic Advisors, explained in a [March 2017 Perspectives from FSF Scholars](#) that the right way to protect privacy throughout the Internet ecosystem is through case-by-case adjudication at the FTC. Therefore, imposing privacy regulations at the state-level is redundant and it creates a patchwork regulatory problem for ISPs when delivering interstate communications services.

As the FCC's *Restoring Internet Freedom Order* explains:

It is impossible or impracticable for ISPs to distinguish between intrastate and interstate communications over the Internet or to apply different rules in each circumstance. Accordingly, an ISP generally could not comply with state or local rules for intrastate communications without applying the same rules to interstate communications.

In March 2018, I testified before the Maryland House of Delegates, where I raised this issue pertaining to a similar privacy bill in Maryland. In written [testimony](#), Randolph May and I stated:

As the FCC said in its December 2017 order: "[O]nly the FTC operates on a national level across industries, which is especially important when regulating providers that operate across state lines." The burdens and costs imposed on ISPs having to comply with a patchwork of differing state privacy regulatory regimes – like the burdens and costs imposed by a patchwork of differing state net neutrality regimes – may well deter investment in broadband facilities in [California] and the provision of innovative services to [California] consumers.

Additionally, many practical questions arise about enforcement of these new California regulations. If a person has a fixed connection in California but accesses the Internet in a neighboring state, do the rules apply to that individual? If a California resident travels across state lines and uses his or her mobile device, do the rules no longer apply? And if other states adopt their own unique privacy laws that conflict with California's, how will ISPs and edge providers know which law applies? Most likely such questions can only be resolved through costly and time-consuming litigation, and the ensuing uncertainty likely will delay investment and innovation by the affected companies in the states under question.

Conclusion

Despite strong demand and competition for broadband services in California, the state-by-state patchwork regulatory problems created by the new privacy law, along with the regulatory costs and uncertainty pertaining to enforcement, likely will slow investment by broadband providers. This will increase the cost of accessing online content. Moreover, because the privacy law will restrict the ability of broadband providers and edge providers to collect consumer data, it likely will lead to more subscription-based services and content favoritism by edge providers, harming those who rely most heavily on free access to valuable content.

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