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Deregulation as Scapegoat

by

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The financial services bailout threatens to give all deregulatory efforts a bad name. And it threatens to give those who reflexively favor more regulation, regardless of the marketplace circumstances, a new regulatory cudgel. If this reflexive approach is applied to today's communications marketplace, this would be most unfortunate.

Consumers have benefited from the deregulation that has occurred, however haltingly at times, in the communications marketplace since passage of the Telecommunications Act of 1996. There is now competition among providers of broadband service in most parts of the country, and these providers offer an array of innovative Internet, video, and voice services over constantly evolving wireline, cable, wireless and satellite technologies.

Even confronted with the reality of competitive communications markets, there remain many who want to reverse the regulatory relaxation that already has occurred, or even to impose entirely new regulations. In considering such calls, a brief look back is instructive. In August 1999, under the leadership of then-Chairman William Kennard, the Federal Communications Commission released a "Strategic Plan: A New FCC for the 21st Century."

In its first sentence, the strategic plan forecasts: "In five years, we expect U.S. communications markets to be characterized predominately by vigorous competition that will greatly reduce the need for direct regulation."

So the FCC proposed transitioning itself "from an industry regulator to a market facilitator." The notion that a market characterized predominately by vigorous competition needs market facilitation is questionable. But at least the plan's focus on creating and sustaining additional competition, rather than resorting to traditional regulation, was sensible.

Now, almost a decade later, it is useful to recall the agency's 1999 strategic vision, if only for the purpose of assessing knee-jerk calls for more regulation. The commission's prediction turned out to be correct. Communications markets, including broadband, are now generally competitive, driven largely by the ongoing technological advancements that characterize the digital revolution. Changing the agency's regulatory mindset, in the face of institutional bureaucratic imperatives, has proven more difficult.

The FCC has reported that, as of June 2007, the most recent period for which its data are available, 96 percent of the nation's zip codes had two or more broadband providers. The rapid expansion in the availability of broadband service has not come cheap. Cable operators have spent well more than \$100 billion upgrading their systems to handle digital broadband since passage of the 1996 Telecom Act. Determined to remain competitive, AT&T and Verizon reportedly have spent more than \$70 billion in the last two years to expand capacity with fiber optic technology and other capacity-enhancing equipment.

As a result, in many communities across the nation cable operators and telephone companies are locked in fierce battles to attract and retain broadband Internet subscribers. These competitive battles often involve price reductions for stand-alone broadband service and discounts for the popular "triple play" bundled package of Internet, voice and video.

In truth, the FCC thus far has failed to do enough to change its role from "industry regulator" to "market facilitator." This failure harms consumers because continuation of legacy command-and-control regulation stifles investment and innovation.

The FCC's recent forays into net neutrality regulation are examples of inappropriate clinging to a legacy regulatory role. By its terms, net neutrality regulation, like traditional public utility regulation in monopolistic markets, requires the service provider to operate in a strictly nondiscriminatory manner. In 2007, when the FCC auctioned prime wireless frequencies, it required the auction winner to operate under net neutrality regulation, even though the wireless market is competitive.

The commission ignored the point that, in a competitive market, service providers will be driven to satisfy consumer demand in the most economically efficient manner. Otherwise, they will be punished by consumers.

Rather than allowing the market to perform its function, in that instance the agency adopted an "industry regulator" role. And, acting as industry regulator, the FCC recently sanctioned Comcast for conduct the company had reason to believe constituted reasonable network management practices.

The FCC should be facilitating creation of even more facilities-based competition. A case in point is the pending proposal by Sprint Nextel and Clearwire to build a new broadband network using WiMAX, a new wireless technology. Even though the proposed service may not be substitutable in all respects for services provided by existing broadband providers, the added competition from the new WiMAX network should lead to lower prices and improved broadband service.

In 2000, not long after the release of the FCC's strategic plan, then-FCC Commissioner Michael Powell declared: "Our bureaucratic process is too slow to respond to the challenges of Internet time." Internet-time has become faster since, but FCC bureaucratic processes haven't. If the agency is to be a "market facilitator," it will need to render decisions in a more timely manner. Acting on the Sprint-Clearwire applications without delay is a good place to start.

Admittedly the FCC is not always confronted with an either-or choice - industry regulator versus market facilitator. There are instances in which regulation is warranted. But the key point is this: By focusing much more on a market facilitation role, the commission can foster additional marketplace competition that lessens the need for continuing a direct regulatory role. Once the Sprint-Clearwire applications for a new network are granted, for instance, calls for continuing to impose legacy regulation in the form of net neutrality mandates will be weaker still.

When the FCC is further along in the transition from industry regulator to market facilitator, it will be closer to embodying the "model agency for the digital age" envisioned by the 1999 strategic plan. The commission should not be deterred by those who seek to tar all deregulatory efforts by whatever regulatory intervention may be justified in the financial markets.

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