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INCOMPAS Mischaracterizes FSF's Cost-Benefit Analysis Comments

by

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I. Introduction

In its May 18, 2017, *Restoring Internet Freedom* Notice of Proposed Rulemaking (NPRM), the Federal Communications Commission proposed conducting a cost-benefit analysis of the current Title II regulation of Internet service providers (ISPs).[1] Free State Foundation scholars supported this proposal in both their initial comments[2] and reply comments.[3] INCOMPAS, however, filed reply comments[4] that mischaracterized the Free State Foundation's comments and which appear to demonstrate a lack of understanding of the FCC's NPRM and cost-benefit analysis generally.

The INCOMPAS reply makes two erroneous claims about the Free State Foundation comments. First, INCOMPAS claims that the Free State Foundation brief considers only the impact of the *Open Internet Order* on broadband capital investment and ignores other impacts of the *Order*. The FSF submission does not ignore other impacts of the *Open Internet Order*. Indeed, it

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[1] Federal Communications Commission, "Protecting and Promoting the Open Internet Notice of Proposed Rulemaking," WC Docket No. 17-108; FCC 17-60 at ¶¶ 105-14, adopted May 18, 2017, available at https://www.fcc.gov/document/restoring-internet-freedom-notice-proposed-rulemaking.

[2] Comments of Free State Foundation, WC Docket No. 17-108 (July 17, 2017), at 61-62, available at http://www.freestatefoundation.org/images/FSF_Initial_Comments_-_Restoring_Internet_Freedom_-_071717.pdf.

[3] Reply Comments of Free State Foundation, WC Docket No. 17-108 (August 30, 2017), at 47-50, available at http://www.freestatefoundation.org/images/FSF_Restoring_Internet_Freedom_Reply_Comments_-_Final_-_083017.pdf.

[4] Reply Comments of INCOMPAS, WC Docket No. 17-108 (August 30, 2017), at 16-17, available at https://ecfsapi.fcc.gov/file/10830895219123/INCOMPAS%20RIF%20Reply%20Comments-30Aug%20FINAL.pdf.

contains two long sections listing many impacts of the *Order* that the FCC should consider that are not specific to broadband capital investment.

Second, INCOMPAS claims that there is a contradiction between a focus on lost capital investment and the guidance in Section E of the OMB Circular A-4. There is no contradiction. INCOMPAS ignores the discussion of the capital investment multiplier in both the FCC's NPRM and the FSF comments that specifically addresses the relationship between lost capital investment and the total economic impact of the *Open Internet Order*.

The Commission should rely on the Free State Foundation's comments to support its proposed use of cost-benefit analysis and to show the extent to which the costs of maintaining the current regulatory regime in place imposes costs that outweigh the benefits.

II. The INCOMPAS Reply Comments

INCOMPAS is a trade association that advocates keeping the current utility-style Title II regulation of broadband providers. The INCOMPAS reply comments cite two brief snippets from FSF's comments as somehow leading it to conclude that FSF "follows [a] misguided path" and "trips over its own reasoning."[5] However, INCOMPAS only demonstrates its misunderstanding of the points made by FSF in its comments as it ignores other passages in FSF's filing that discuss what INCOMPAS claims we ignore. The relevant passage from the INCOMPAS comments states:

> Any CBA [cost-benefit analysis] must account for the entire Internet ecosystem, not just a subset of those that provide access to the Internet. That means quantifying as much as possible all of the costs and benefits, including, but not limited to, infrastructure investment, losses from innovation on the edge, decreased consumer surplus, and increased uncertainty from venture capitalists. To limit the CBA to infrastructure investment would render it invalid, also because it would ignore important non-economic interests, including diversity of speech.
>
> Free State's CBA submission follows the same misguided path, but also manages to trip over its own reasoning. Drawn to the beacon of allegedly depressed investment by broadband providers, Free State argues that the Commission "is correct to focus much of its cost analysis on how broadband capital investment is being adversely affected." But it also advocates following Section E of the OMB Circular A-4, which would lead to the opposite conclusion—that it should not focus much of its cost analysis on that. Instead, as the Circular dictates, the "analysis should focus on benefits and costs that accrue to citizens and residents of the United States." Free State appears to have omitted this part of the Circular in its analysis and focused solely on infrastructure investment. That narrow scope would fail the Circular's test (citations omitted).[6]

[5] Id.
[6] Reply Comments of INCOMPAS, at 16-17.

III. FSF's Analysis Does Account for the Entire Internet Ecosystem, Not Just a Subset of Those That Provide Internet Access

The claim by INCOMPAS that "Free State appears to have omitted this part of the [OMB] Circular in its analysis and focused solely on infrastructure investment" is demonstrably incorrect. My *Perspectives* paper, which was attached to the Free State Foundation filing and specifically cited by INCOMPAS, contains two sections on other factors the FCC should consider. For example, this paper pointed out that "foregone networks will lead to many lost societal benefits, in terms of lost employment, lost opportunities for governments to offer improved services, and increased risk for local governments."[7]

This *Perspectives* also points out that "Federal, state, and local governmental units in the future may want Amber alerts, severe weather alerts, and Homeland Security warnings given priority over other Internet traffic. . . . The FCC should include some costs in its analysis reflecting how enhancement in these types of government functions may be delayed by the restrictions in the *Open Internet Order*."[8] Another impact on governments I noted was the impact of delays in capital investment on state and local governments that are considering municipal broadband projects in response to slow capital investment in their areas by broadband providers.[9]

My *Perspectives* further describes how some specialized services for dedicated users require a high level of end-to-end reliability, which may not be available now or in the future under the current ban on paid prioritization:

> New entrants in existing markets may be willing to pay more to ensure that delays are avoided in order to enhance their chances of gaining a foothold and establishing a customer base. And it may be that allowing some form of prioritization provides incentives for differentiating services, especially those offered by a new entrant trying to establish a market presence. This is another way that eliminating an absolute ban on paid prioritization is likely to be pro-competitive.
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> Autonomous vehicles, interactive e-learning, and telemedicine are examples of applications in their early stages of development that may require access to fast and stable Internet connections. Investors may be unwilling to take the risk of investing in these applications if they cannot be assured of reliable prioritized broadband connections.[10]

My *Perspectives* concludes: "These types of costs can be difficult to quantify but they are nevertheless foreseeable consequences of the *Open Internet Order*. Therefore, they are important to include in the cost-benefit analysis."[11]

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[7] Theodore R. Bolema, "An Assessment of the FCC's Proposal to Conduct a Cost-Benefit Analysis," Free State Foundation (July 14, 2017), at 13, available at http:// www.freestatefoundation.org/images/An_Assessment_of_the_FCC_s_Proposal_to_ Conduct_a_Cost-Benefit_Analysis_071417.pdf.

[8] Id. at 13.

[9] Id. at 13-14.

[10] Id. at 16-17.

[11] Id. at 14.

Thus, while INCOMPAS erroneously asserts that the Free State Foundation failed to consider these other impacts of the Open Internet Order, it does so by quoting selectively from earlier in my *Perspectives* and then ignoring the later analysis that contains the material INCOMPAS claims FSF failed to consider. This is wrong.

IV. There Is No Contradiction Between Advocating That the FCC Consider the Impact on Capital Investment and Advocating That the FCC Follow OMB Circular A-4

The FCC states in paragraph 106 of the NPRM that it is proposing to follow the same guidance in Section E of OMB Circular A-4[12] that has been used by executive branch agencies since 2003. I describe in my *Perspectives* how the guidance used by executive branch agencies is entirely appropriate for the FCC to adopt.[13]

Advocating that the FCC follow the guidance in OMB Circular A-4 is entirely consistent with the FCC being "correct to focus much of its cost analysis on how broadband capital investment is being adversely affected."[14] The amount of capital investment in broadband has important implications for the "benefits and costs that accrue to citizens and residents of the United States."[15]

INCOMPAS is arguing against a straw man. Free State Foundation scholars, as well as other comments cited by INCOMPAS that focus on the impact of the *Open Internet Order* on capital investment,[16] are not arguing that the FCC should only consider the effect of the *Order* on capital investment while ignoring all other impacts. Rather, the capital investment impact is only the starting point, and it must be connected to the total economic impact. Paragraph 111 of the NPRM proposes to connect the lost investment effects from the *Open Internet Order* to the total economic cost of the regulation using the capital investment multiplier. My *Perspectives* describes out how the FCC's proposed investment multiplier approach serves this purpose:

> The investment multiplier approach is used to quantify the impact public or private investment spending has on the general economy. It provides an estimate of the additional effects of a policy that are not immediately measurable. A larger multiplier means that the investment was more efficient at creating wealth in the economy.[17]

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[12] Office of Management and Budget, "OMB Circular No. A-4: Regulatory Analysis" (September 3, 2003), available at https://obamawhitehouse.archives.gov/omb/memoranda_m03-21/.
[13] Theodore R. Bolema, "An Assessment of the FCC's Proposal to Conduct a Cost-Benefit Analysis," at 8.
[14] Reply Comments of INCOMPAS, at 16, citing Theodore R. Bolema, "An Assessment of the FCC's Proposal to Conduct a Cost-Benefit Analysis," at 11.
[15] Reply Comments of INCOMPAS, at 16, citing Theodore R. Bolema, "An Assessment of the FCC's Proposal to Conduct a Cost-Benefit Analysis," at 8.
[16] See Reply Comments of INCOMPAS, WC Docket No. 17-108 (August 30, 2017), at 15, citing Comments of American Cable Association, WC Docket No. 17-108, at 58-59; and Comments of CTIA, WC Docket No. 17-108, Exhibit B, Hahn Decl. ¶ 39 (July 17, 2017).
[17] Id. at 17.

This paper also notes that much of the lost broadband investment found by Free State Foundation and other scholars might not be entirely lost to the economy because some of it might have been redirected to other sectors of the economy.

> The lost investment impact of the *Open Internet Order* discussed above is substantial. However, the FCC correctly suggests in paragraph 111 that the total economic impact is not necessarily the same. It could be lower if much of the investment spending is redirected elsewhere and would still contribute to the economy even under the baseline scenario. Or the investment multiplier could be higher if the additional investment spending leads to a large increase in other spending.[18]

My *Perspectives* further documents how the capital investment multiplier approach is used by economists to evaluate the economic impacts of both government and private infrastructure investment. The investment multiplier relationship has been carefully studied in the economics literature by scholars such as former Congressional Budget Office Director Douglas Holtz-Eakin.[19]

Thus, the multiplier approach is widely recognized in the economics literature as a methodology for connecting capital investment impacts to total economic impacts. Notably, the INCOMPAS Reply says nothing at all about the FCC's proposed use of the multiplier approach. Nor does the INCOMPAS reply address my application of this approach to use such a multiplier approach to convert a previous Free State Foundation estimate of lost investment of $5.6 billion in 2015 and 2016[20] to an estimate of the total net benefits that accrue to citizens and residents of the United States in the range of negative $7.0 to negative $9.8 billion attributable to the *Open Internet Order*.

V. Conclusion

Requiring regulators to conduct cost-benefit analyses has a long history of bipartisan support and should not be controversial.[21] Every President since Jimmy Carter has required executive branch regulatory agencies to conduct cost-benefit analyses of economically significant regulations. Moreover, President Obama's Executive Order 13579 explicitly encourages independent agencies to conduct retrospective review of their existing regulations, which is exactly what the FCC's NPRM proposes to do.[22]

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[18] Id. at 14.
[19] Id. At 15-16, citing Douglas Holtz-Eakin and Michael Mandel, "Dynamic Scoring and Infrastructure Spending," McGraw Hill Financial Global Institute (July 6, 2015), at 10, available at http://media.mhfi.com/documents/201511-MHFIGI-Dynamic-Scoring.pdf.
[20] See Michael J. Horney, "Broadband Investment Slows by $5.6 Billion Since Open Internet Order," Free State Foundation Blog (May 5, 2017), available at http://freestatefoundation.blogspot.com/2017/05/broadband-investment-slowed-by-56.html.
[21] See Michael J. Horney, "Opposing Cost-Benefit Analysis Raises a Red Flag, Free State Foundation Blog (September 12, 2017), available at http://freestatefoundation.blogspot.com/2017/09/opposing-cost-benefit-analysis-raises.html.
[22] Executive Order No. 13,579, Federal Register 76, No. 14 (January 21, 2011).

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Second, INCOMPAS claims that there is a contradiction between a focus on lost capital investment and the guidance in Section E of the OMB Circular A-4. There is no contradiction. INCOMPAS ignores the discussion of the capital investment multiplier in both the FCC's NPRM and the Free State Foundation filing that specifically addresses the connection between lost capital investment and the total economic impact of the *Open Internet Order*.

Thus, the INCOMPAS reply comments mischaracterize the comments of the Free State Foundation and appear to demonstrate INCOMPAS's lack of understanding of the FCC's NPRM and cost-benefit analysis generally.

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