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Wireless Report Data Undermine the FCC's Rationale for Regulation

by

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Introduction and Summary

Amidst the 2015 holiday season, the Federal Communications Commission released its [*Eighteenth Wireless Competition Report*](#). Considering the FCC's less-than-stellar track record in timely producing some of its statutorily-required reports, perhaps the Commission simply hoped to release the report before year's end. Then again, the December 23 release of *Eighteenth Report* all but guaranteed reduced public attention.

What the Commission might prefer the public overlook is this: The *Eighteenth Report* contains evidence that undermines the Commission's rationale for imposing public utility-style regulation on mobile broadband services as it did in its recent *Open Internet Order* (2015). One obvious line of evidence is supplied by the large scale of competing wireless broadband provider coverage. Another line of evidence consists of market trends toward no-contract wireless services and elimination of early Termination Fees (ETFs), thereby reducing consumer switching costs.

A highly dubious premise of the *Open Internet Order* was that "broadband providers have both the incentive and the ability to act as gatekeepers standing between edge providers and consumers." The *Order* claimed that broadband providers – including mobile broadband

providers – can “block access altogether,” “target competitors, including competitors to their own video services,” and “extract unfair tolls.” Of course, effective market competition provides a strong check against any such incentives or the ability to engage in such anti-consumer behavior. Service providers in competitive markets risk losing subscribers to rival providers.

The Commission’s dubious mobile broadband gatekeeper premise is refuted by data cited in the *Eighteenth Report* concerning competing wireless provider coverage. As of the middle of last year – around the time the FCC issued its *Open Internet Order* – 91.5% of the U.S. population lived in census blocks with 4G LTE network coverage provided by three or more wireless providers. At that same time, 82.2% lived in census blocks with four or more LTE providers. The existence of the scale of such competing mobile coverage was widely recognized when the *Open Internet Order* was released. But the Commission ignored it. Even so, updated numbers in the *Eighteenth Report* mark a significant advancement in LTE capabilities. This fresh data points up the reality of wireless consumer choices and the emptiness of the *Order*’s gatekeeper label for mobile broadband.

Another shaky premise of the *Open Internet Order* was that “[s]witching costs are a significant factor in enabling the ability of mobile broadband providers to act as gatekeepers.” Wireless provider-imposed ETFs were singled out as one such barrier. Yet the *Eighteenth Report*’s observations of pro-consumer marketplace trends in wireless service and pricing options also challenge this underpinning of the *Order*. Those trends indicate that wireless consumers enjoy competitive choices among a variety of service plans, along with easier ability and incentives to switch providers. The *Eighteenth Report* identifies “a rapid shift from traditional postpaid contract plans to no-contract plans.” Bring your own device (“BYOD”) and handset leasing options are now widely available to consumers. Also, “marketing tactics have increasingly focused on Early Termination Fee (“ETF”) buyouts to encourage customers to switch from rivals.”

Needless to say, the *Eighteenth Report* contains further data – highlighted below – that shows the competitive state of the wireless market. But were the Commission to expressly conclude that there is effective competition in the market, it would be tantamount to admitting its rationale for imposing public utility regulation on mobile broadband is faulty. Making such a concession would put the Commission’s public utility regulatory policy for mobile broadband into further legal jeopardy. Unfortunately, the Commission appears locked into its public utility agenda, regardless of the reality of the wireless market data.

The Commission continues to kick up obstructionist dust over the answer to whether or not there is effective competition in the wireless market. But a clear-sighted view of the data contained in the *Eighteenth Report* supports the conclusion that – yes – there is effective wireless competition. A clear sighted view of 4G LTE provider coverage and pro-consumer trends toward reduced switching costs also supports the conclusion that the Commission’s rationale for imposing public utility regulation on mobile broadband was wrongheaded.

The Data Demonstrate the Existence of Effective Competition

Section 332(c) of the Communications Act requires the FCC to annually prepare a report that includes an analysis of “whether or not there is effective competition” in the wireless market. The [*Eighteenth Wireless Competition Report*](#) is chock full of evidence to support a positive finding of effective competition in the wireless market:

- Over the past five years, wireless providers’ capital investments totaled \$146 billion. Carriers spent between \$31 and \$32 billion in capital investment in 2014 alone;
- Total mobile wireless connections grew from between 336-340 million in December 2013 to between 355-357 million in December 2014 – an annual growth rate of 5%-6%;
- 97.2% percent of the U.S. population lived in census blocks with coverage by at least three wireless providers as of July 2015, and 91.7% lived in census blocks with four or more providers;
- 91.5% of population lived in census blocks with 4G LTE network coverage provided by three or more wireless providers as of July 2015, and 82.2% lived in census blocks with four or more providers offering LTE coverage;
- Three major wireless providers – Verizon Wireless, AT&T, and T-Mobile – have already begun deploying voice-over-LTE (VoLTE) service across their networks, while Sprint and U.S. Cellular are planning or testing future VoLTE deployments;
- “[T]he price (in constant dollars) of wireless service has continued to decline.” From December 2013 to December 2014, the annual Wireless Telephone Services consumer price index (CPI) decreased 2.1% while the overall CPI increased 1.6%;
- “Smartphone use has continued to increase over the last three years...although smartphone use flattened out in 2015.” About 77% of mobile subscribers had a smartphone in the third quarter of 2015, compared to 51% in the third quarter of 2012. And the smartphone penetration rate among new phone purchases was 88% in the third quarter of 2015, up from 67% just three years earlier;
- In 2014, the Apple App Store generated about \$10 billion in revenue to developers, while the Google Play marketplace paid out \$7 billion to app developers. App revenue from both app stores is expected to double by 2018;
- “[T]he number of American homes with only wireless telephones continues to grow.” As of June 2015, 46.7% of adults live in a household that is wireless-only and 55.3% of children live in a wireless-only household;

Regrettably – but not unexpectedly – the *Eighteenth Wireless Competition Report* excuses itself from making any finding or conclusion about “whether or not there is effective competition” in the wireless market. That makes the fifth consecutive report in which the Commission has dodged the question underlying its mandated analysis. (On [prior occasions](#) I have explained that Section 332(c) is best understood as requiring a “yes” or “no” finding. And earlier reports made such a finding.) Instead, the *Eighteenth Report* repeats some now-familiar but misguided boilerplate. That is, the *Report* claims that any conclusion about “whether or not there is effective competition” somehow would be misleading and that no accepted definition of “effective competition” exists among antitrust authorities.

A Competing Provider Analysis Brings Effective Wireless Competition Into Focus

In truth, the FCC already has a standard for measuring effective competition, which it uses in the local cable services context. As I have previously written, the “[FCC Should Be Clear and Consistent on Effective Competition in the Wireless Market](#).” The Commission’s wireless report analysis of the wireless market should include a “competing provider test” analysis similar to the one it applies pursuant to Section 623 concerning whether effective competition exists in local video markets.

An analogous application of the Section 623 competing provider test to wireless would presume that there is effective competition in a metropolitan statistical area if: (1) it is served by at least two competing wireless providers, each of which offers wireless voice and broadband services to at least 50% of all area households; and (2) the number of subscribers other than the area’s largest provider exceeds 15 percent of area households.

The Commission should also consider nationwide population coverage by multiple wireless providers in light of competing provider test thresholds. Effective competition in the wireless market is clearly evident according to this type of metric. As indicated above, estimates cited by the *Eighteenth Report* reveal that 97.2% percent of the U.S. population lived in census blocks with coverage by at least three wireless providers as of July 2015, and 91.7% lived in census blocks with four or more providers. As of that same date, 91.5% of population lived in census blocks with 4G LTE network coverage provided by three or more wireless providers, and 82.2% lived in census blocks with four or more LTE providers.

There is also agency precedent for applying an analysis similar to the competing provider test for purposes of determining whether or not effective competition exists in the wireless market. As my [above-cited Perspectives from FSF Scholars paper](#) pointed out:

The *Ninth*, *Tenth*, and *Eleventh Wireless Competition Reports* pointed to the percentage of the total U.S. population living in counties with access to multiple providers as one indicator of “effective competition” in the wireless market. Additionally, the *Tenth* and *Eleventh Reports* pointed to the absence of any one provider having a dominant share of the market.

The Commission's *Effective Competition Order* (2015) offers yet another precedent, this one very recent, for the Commission to build on. Based on its competing provider analysis, the *Order* established a rebuttable presumption that local cable markets are subject to effective competition. Positive findings of effective competition for wireless services should similarly lead the Commission to adopt a rebuttable presumption that there is effective competition in national and local wireless markets. Such an approach would bring into sharper focus the strong competition that characterizes today's wireless market. And it should prompt the Commission to demand actual evidence of consumer harm before it intervenes in the market with new regulation.

Wireless Provider Coverage Data Undermine the Rationale for Public Utility Regulation

Unfortunately, the Commission is now beset by a conflict-of-interest concerning the status of wireless competition. That conflict-of-interest centers on the Commission's policy agenda for subjecting mobile broadband Internet access to Title II public utility-style regulation. Any path to admitting there is effective competition in the wireless market would call into question the validity of the Commission's application of public utility regulation to wireless services. The [*Open Internet Order*](#) was premised on wireless broadband providers possessing a monopoly-like gatekeeper power over wireless broadband network traffic.

The validity of the Commission's wireless gatekeeper premise is significantly undermined by data cited in the *Eighteenth Report* concerning competing provider coverage. Availability of other alternative broadband providers and platforms calls that premise into further question.

Pro-Consumer Trends Undermine the Rationale for Public Utility Regulation

The *Eighteenth Report* also contains another line of evidence that casts serious doubt on the viability of the Commission's premise for subjecting wireless to public utility regulation – the observations of pro-consumer marketplace trends in wireless service and pricing options. Those trends indicate that wireless consumers enjoy competitive choices among a variety of service plans, along with easier ability and incentives to switch providers. Pro-consumer trends in the wireless market also undermine a significant aspect of the Commission's rationale for imposing public utility regulation on wireless services.

Until 2013 most wireless subscribers to postpaid plans signed two-year service contracts in exchange for discounted or subsidized handsets that consumers paid for through higher monthly fees. Consumers who wanted out of their two-year contracts were typically subject to early-termination fees. But as the *Eighteenth Report* points out, since 2013 there has been “a rapid shift from traditional postpaid contract plans to no-contract plans.” Bring your own device (“BYOD”) and handset leasing options are now commonplace in wireless service offerings. Further, “marketing tactics have increasingly focused on Early Termination Fee (“ETF”) buyouts to encourage customers to switch from rivals. ETF buyouts typically include a cash payment or credit to reimburse ETFs for customers on traditional contract plans, or alternatively, to pay off the remaining balance of an EIP, plus a separate device credit for trading in a customer's current handset.”

This rapid market trend toward no-contract options and away from ETFs drastically undercuts concerns about wireless consumer lock-in or barriers to switching providers. In critical respects, the *Eighteenth Report*'s observations about wireless switching costs and incentives undermines one of the Commission's pretenses for subjecting mobile broadband Internet access to Title II public utility regulation. As the Commission stated in its *Open Internet Order*: "[W]e agree with those commenters that argue that mobile broadband providers have the incentives and ability to engage in practices that would threaten the open nature of the Internet, in part due to consumer switching costs. Switching costs are a significant factor in enabling the ability of mobile broadband providers to act as gatekeepers." The *Order* continued: "[C]ustomers may face a variety of hassle-related and financial switching costs. Disconnecting an existing service and activating a new one may involve early termination fees (ETFs), coordinating with multiple members of a family plan, billing set-up, transferring personal files, and porting phone numbers, each of which may create delays or difficulties for customers."

Switching nearly any service will typically impose some minimal costs on a consumer, whether in time or money. Those holds true even for free services, such as email, where a user might have to migrate old e-mail address books or messages to a new service account. It is a serious fact-specific question as to when switching costs for a given service might become so onerous as to produce consumer harm and require regulation to alleviate. In the *Open Internet Order*, ETFs were cited by the Commission as factors that ostensibly made wireless providers into "gatekeepers" and made wireless services uniquely subject to switching costs. Even assuming the Commission was correct, with the rise of no-contract postpaid wireless options and ETF buyouts its concerns appear grossly exaggerated. And they can scarcely constitute a sound basis for subjecting mobile broadband to public utility regulation.

The timing of the wireless market's trending toward no-contract services and away from ETFs makes even more pronounced the wrongheadedness of the *Open Internet Order*'s imposition of public utility regulations on mobile broadband on account of switching costs. The *Order*'s depiction of the market was at odds with market reality on the day it was released. The *Eighteenth Report* covers the second half of 2014 and the first half of 2015 – the very same timeframe in which the Commission prepared and issued its *Order*.

Worse still is the fact that the Commission relied on a static picture of the mobile broadband market's service and pricing in imposing public utility regulation on mobile broadband. In just a handful of years, the wireless market has transformed from interconnected analog voice services to a myriad of digital high-speed data communications services. The wireless market is a dynamic one, not a static one. The Commission should know better. The *Eighteenth Report* suggests it does know better, as it recognizes that "there is wide variety of pricing plans offered by the different mobile wireless service providers that vary along several dimensions, and that may frequently change."

Conclusion

A clear-sighted view of the data contained in the *Eighteenth Wireless Competition Report* demonstrates that there is effective competition in the wireless market. A clear-sighted view of 4G LTE provider coverage and pro-consumer trends toward reduced switching costs also

supports the conclusion that the Commission’s rationale for imposing public utility regulation on mobile broadband was wrongheaded. The Commission may continue to duck or downplay these developments in the wireless market, out of concern for defending its own regulatory preferences. But consumers more closely connected to marketplace reality are enjoying the variety of choices and sources of value offered by mobile broadband services in a wireless market that is effectively competitive.

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Further Readings

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