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Hearing on "Ensuring Competition on the Internet: Network Neutrality and Antitrust"

before the

Subcommittee on Intellectual Property, Competition, and the Internet

Committee on the Judiciary

U.S. House of Representatives

February 15, 2011

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Mr. Chairman and Members of the Committee, thank you very much for inviting me to submit this written statement for inclusion in the Committee's record of the February 15, 2011, hearing on "Ensuring Competition on the Internet: Net Neutrality and Antitrust." I am President of The Free State Foundation ("FSF"), a non-profit, nonpartisan research and educational foundation located in Rockville, Maryland. The Free State Foundation is a free market-oriented think tank that, among other things, does research in the communications and Internet law and policy areas.

Despite ongoing efforts by Congress to consider the creation of a new legislative framework for addressing broadband Internet service issues, the FCC imposed a network neutrality regulatory regime in December 2010. But the new regulatory framework for broadband Internet services is plagued by several serious legal problems and policy defects.

In significant measure the problems with the FCC's net neutrality regulation spring from the Commission's inability or unwillingness to identify any current market failure problems in the broadband Internet marketplace. The FCC instead adopts its regulatory framework as a prophylactic response to the Commission's own supposed concerns over hypothetical future conduct in the evolving broadband Internet marketplace. The FCC flatly rejected employing a market power or consumer harm evidentiary standard as the basis for regulatory intervention. Instead, it opted to grant

itself wide-ranging authority to decide what kinds of future conduct it wants to prohibit and how deeply into the market it wants to insert government restrictions and mandates.

In opting for this new nearly unconstrained regulatory regime, the FCC has likely exceeded its statutory authority. A federal appeals court ruling less than a year ago rejected the Commission's claims for authority to regulate broadband Internet services, and the Commission's new attempt to regulate such services will likely suffer the same fate in court. Congress has not expressly granted authority to the FCC to regulate broadband Internet services. And one of the statutory provisions on which the Commission principally relies to claim it has "ancillary" regulatory authority is actually a Congressional policy statement favoring *de*regulation to promote the deployment of broadband networks, not new regulation.

Moreover, the regulatory framework adopted by the Commission raises serious constitutional issues under the First Amendment. Prior court cases have recognized that First Amendment protections accorded to the editorial judgments of newspaper, radio and broadcasting media are accorded to broadband ISPs' editorial discretion regarding the traffic they choose to carry on their networks and what kind of content they choose not to carry. But the FCC's regulations now restrict such editorial discretion on the part of broadband ISPs. And lacking any existing market power or consumer harm evidentiary findings, the FCC cannot likely show its regulations further any substantial governmental interest. Parties challenging the constitutionality of the FCC's rules will likely be able to show that the regulatory burdens placed on broadband ISP editorial judgments sweep more broadly than necessary to advance any government interest. To the extent that any government interest is shown to exist, a variety of less onerous

alternatives for addressing Internet provider practices are available to the Commission and to other federal agencies through antitrust enforcement.

The FCC's net neutrality regulations constitute unsound public policy, especially because they threaten future innovation and investment in broadband infrastructure and services. For example, investment and innovation likely will be chilled because the FCC's new rules prohibiting "unreasonable discrimination" by Internet providers necessarily will have a deterrent effect on ISPs wishing to differentiate their services from their competitors in response to rapidly evolving consumer demands. Innovation, and investment to support such innovation, depends on the prospects for realization of real returns, rather the prospects for realizing recurring litigation. While the Commission acknowledges that some "discrimination" by Internet providers is beneficial to consumers, based on the FCC's history of administrative overreaching, it is likely the sorting out process will not be conducive to fostering entrepreneurial experimentation.

Moreover, the FCC's regulatory framework establishes a set of anticipatory *ex ante* rules built upon dubious, non-exclusive, and unstable definitional distinctions. For example, the regulations distinguish between "edge providers" and other "end users" in a way that gives the former special privileges over the latter regarding pricing arrangements with broadband ISPs. This constitutes a "competitor welfare" approach to the broadband Internet market, rather than a "consumer welfare" approach. And it invites special interest lobbying for future Commission rulings regarding who should receive "edge provider" favoritism. By rejecting market power and consumer harm evidentiary showings as a predicate for regulatory enforcement under its framework, the Commission necessarily arrogates to itself nearly unbridled discretion in determining

what kinds of services and practices in the Internet marketplace should be permitted and how it should regulate them.

I. The FCC's Net Neutrality Regulations Are Not Authorized by Congress

The FCC's net neutrality regulations most likely lack proper congressional authority. The Commission's previous attempt to regulate broadband network management practices was struck down by the U.S. Court of Appeals for the District of Columbia Circuit last April.[1] In that ruling, the D.C. Circuit concluded that the FCC did *not* have statutory authority to regulate the Internet network management practices at issue in that case.

The FCC's new broadband Internet services regulatory framework will more likely than not be struck down for the same reason. (Lawsuits challenging the FCC's regulation have already been filed.) A federal court, be it the D.C. Circuit or some other court, will likely reiterate that Congress never granted the FCC the power to regulate broadband Internet services.

The FCC's claimed legal basis for imposing regulation is highly problematic. The weakness of the FCC's claimed statutory authority is revealed by the Commission's resort to an "everything-but-the-kitchen-sink" approach to asserting its authority over broadband Internet services. The Commission invokes numerous provisions that deal with separate, specific subjects — such as common carrier telephony, broadcasting and licensed mobile radio service or wireless, and multivideo programming services such as cable television.[2] But nowhere do Titles II, III and VI of the Communications Act ever give the Commission authority to regulate broadband Internet services. Rolling all of

[1] *See Comcast Corp. v. FCC*, 600 F.3d 642 (D.C. Cir. 2010).
[2] *See* FCC, Report & Order ("Order"), *In the Matter of Preserving the Open Internet*, GN Docket No. 09-191, WC Docket No. 07-52 (December 23, 2010), at 68-77.

those provisions together does not somehow create any new delegation of agency authority to regulate broadband Internet services. And neither do any Title II, III or VI provisions, singly or jointly, provide grounds for the Commission to anchor its exercise of ancillary authority under Title I.

The Commission's arguments that Section 706 gives it authority over broadband Internet services are also highly dubious. Section 706 is best read as a statement of Congressional policy, not a separate delegation of authority to the FCC. In particular, both Section 706(a) and –(b) state Congressional policy in favor of *de*regulation and "removing barriers to infrastructure deployment," not new regulation and raising additional barriers.[3] For these reasons, the Commission's order establishing its regulatory framework also has to overcome and explain away the Commission's prior interpretation of Section 706 as a statement of policy that provides no independent basis of authority.[4] But even if Section 706 provided an independent source of agency authority, that authority would best be understood as authority for eliminating regulation, not establishing regulation. It strains credulity to think that an expansive, open-ended broadband Internet services regulatory framework can be created by invoking a deregulation-minded statutory provision.

The FCC's attempts to claim that adopting its broadband Internet services regulatory framework is reasonably ancillary to satisfying the purposes behind the several statutory provisions it listed will likely prove futile. Taken on its own terms, the FCC's rationale for its claimed statutory authority under Title I ancillary jurisdiction

[3] *See* 47 U.S.C. §§ 1302 (a), (b).
[4] *See* Order, at 64-65, para. 118 (discussing the Commission's *Advanced Services Order*). *See also Comcast v. FCC*, note 1, *infra*, at 655, observing with respect to Section 706 that the FCC "[a]cknowledged that it has no express statutory authority over [an Internet service provider's network management] practices".

admits no limiting principle. Federal courts have rejected limitless agency ancillary powers.[5] The D.C. Circuit rejected precisely that kind of limitless exercise of Title I ancillary authority last April in *Comcast v. FCC*.[6] A future court will likely do the same when the FCC's broadband Internet services regulatory framework is subjected to judicial review.

II. The FCC's Regulation Is Likely Unconstitutional Under the First Amendment

Constitutional problems also plague the FCC's net neutrality regulation. Fifth Amendment regulatory takings issues are implicated by the FCC's broadband Internet services regulatory framework. But this written statement will focus on First Amendment issues raised by such regulation.

By characterizing broadband ISPs as "conduits of speech,"[7] the Commission attempts to push broadband Internet access services outside the scope of First Amendment protection. The FCC also tries to downplay the editorial decisionmaking of broadband ISPs, reducing it to a level of constitutional insignificance. But a federal court will *not* readily allow an administrative agency to shrink the scope of constitutionally protected activity in order to regulate it. The FCC's attempt to escape constitutional scrutiny by relabeling speech and editorial activities that it seeks to restrict as mere transmission is misguided. A federal court will look past the Commission's relabeling attempt and look instead at the regulation's burden on speech and editorial activity.

Private actors, including persons acting in association through media corporations, possess freedom of speech rights in making editorial judgments about

[5] *See, e.g.*, *FCC v. Midwest Video Corp*, 440 U.S. 689 (1979).
[6] *See* note 1, *infra*.
[7] Order, at 78, para. 141.

whether and what sorts of contents are delivered through their respective speech communication mediums. Courts have recognized that First Amendment protections for editorial judgments about content apply with respect to newspapers.[8] They also apply to those engaged in editorial and other speech activities using modern mass media technologies such as cable TV companies.[9] Rulings by two federal district courts have treated broadband ISPs as deserving of free speech protection from government restrictions.[10] It follows that regulation that limits or infringes on broadband ISPs' editorial judgments to the extent that such regulation dictates whether or to what extent broadband Internet service providers can or cannot block, filter, or otherwise decide what sort of content can travel through their networks is constitutionally suspect.

The FCC's broadband Internet services regulatory framework includes significant restrictions on editorial judgments by broadband ISPs. It includes a rule that generally prohibits the blocking or degrading of content.[11] And another rule prohibits broadband ISPs from giving discriminatory, preferential treatment to certain types of content over others, depending on its source and the content message.[12] These rules are subject to exceptions, including where the FCC concludes it is reasonable to block or degrade certain types content that consumers would not likely want, including spam or viruses.[13] As FCC Commissioner McDowell pointed out in his statement dissenting from the

[8] *See, e.g., Miami Herald Publishing Company v. Tornillo*, 418 U.S. 241 (1974).
[9] *See, e.g.*, *Turner Broadcast Systems, Inc v. FCC*, 512 U.S. 622, 636 (1994); *Nat'l Cable Television Ass'n v. FCC*, 33 F.3d 66 (D.C. Cir. 1994).
[10] See *Illinois Bell Telephone Co. v. Village of Itasca*, 503 F. Supp. 2d 928 (N.D. Ill. 2007); *Comcast Cablevision of Broward County, Inc. v. Broward County*, 124 F. Supp. 2d 685 (S.D. Fla. 2000).
[11] Order, at 37-38, para. 62; *id*. at 39, para. 66.
[12] Order, at 40, para. 68.
[13] *See* Order at 47-52 (adopting and discussing "reasonable network management" rule).

FCC's order imposing net neutrality regulation: "[W]hat are acts such as providing quality of service (QoS) management and content filters if not editorial functions?"[14]

Once First Amendment scrutiny is applied, the FCC's regulatory restrictions on how broadband ISPs manage their networks will most likely be found unconstitutionally burdensome. Absent any evidence of market failure or consumer harm problems, the FCC will have difficulty establishing any "substantial" government interest being furthered by its regulation. Importantly, the First Amendment is a limit on government's power over private conduct — and not a grant of power for government to regulate speech activity. This means the FCC's claims that it can impose net neutrality regulation in the name of promoting speech values will be rejected by a federal court because such claims simply turn the First Amendment on its head.[15]

Lacking any substantial government interest to support its regulation, the FCC will have serious difficulty showing that its regulatory approach does not "burden substantially more speech than is necessary." It is easy to name a number of ways by which the FCC could have limited the reach of its net neutrality regulation. For instance, the FCC could have required a showing of anticompetitive conduct before engaging in regulatory intervention. But as discussed below, the FCC instead adopted an open-ended approach that gives the Commission expansive powers over the Internet marketplace. The Commission could also have clearly placed the burden of proof on complainants alleging rule violations. Instead, however, the Commission requires broadband ISPs to justify their actions by rebutting the claims of complainants who simply make a *prima facie* showing of alleged violations of the FCC's regulation.

[14] Dissenting Statement of Commissioner Robert M. McDowell (December 23, 2010), at 26.
[15] *See Order*, at 80, para. 146.

III. The FCC's Regulations Address No Existing Problems and Constitute Unsound Public Policy

The FCC's net neutrality regulation is unwise as a matter of public policy. As a foundational matter, its order establishing net neutrality regulation is devoid of any empirical basis for imposing such regulation. The Commission imposed its regulatory framework in the absence of any market power finding. In fact, the Commission made no market power or consumer harm analysis at all. It expressly rejected suggested proposals that any regulation adopted or enforced be based on standards involving anticompetitive conduct.[16] Lacking any solid market analysis to support its new regulation, the Commission merely pointed to a couple well-known anecdotal instances – such as Comcast/BitTorrent – that are well known to all and which were essentially resolved through private efforts.[17] Revealingly, the FCC expressly declined to say whether the broadband network management practices alleged to have occurred in instances like Comcast/BitTorrent would even constitution violations of its new regulatory framework.[18]

Rather than even trying to establish evidence of any kind of existing market failure or consumer harm problem, the FCC justified its new framework as "prophylactic" regulation.[19] In other words, absent evidence of any existing market failure or consumer harm in the broadband Internet services market, the FCC decided to regulate based on its own predictions about what could happen sometime in the future. In particular, the Commission based its regulation on predictions about what might happen in the future

[16] Order, at 45-46, para. 78.
[17] *See* Order at 21-23. *See also* note 1, *infra*.
[18] Order, at 22, para. 36.
[19] *See, e.g.*, Order, at 24, para. 39.

to make the Internet market different than what the Commission would like it to be. And so the FCC – for the very first time – imposed an expansive and open-ended set of government regulation on broadband Internet services.

The Commission's adoption of a set of *ex ante*, anticipatory rules will likely have the effect of reducing investment and stifling innovation. Aggressive investment in broadband infrastructure by competing broadband ISPs is crucial to continuing technological advances and to increasing availability and adoption. A study commissioned by the FCC and released fifteen months ago puts past investments and projected future investments at approximately $30 billion a year by industry.[20] That study projected total broadband investment between 2010 and 2016 of $182 billion.[21] That kind of investing must be further encouraged to meet increasing demands. In fact, the FCC task force that put together the National Broadband Plan estimated that a nationwide network providing 100Mbps speeds would require investment of up to $350 billion over the next several years.[22]

But under the guise of prohibiting discrimination, the FCC's regulations likely will inhibit the ability of broadband ISPs to actively engage in innovative new traffic management practices to meet growing and changing demands. Heaping regulatory restrictions on an industry or industry segment is an unlikely method for encouraging that industry or segment to sustain or increase its investments. But that is precisely what the FCC has done by adopting its net neutrality regulation. The FCC thereby fails

[20] Robert C. Atkinson & Ivy E. Schultz, *Broadband in America: Where It Is and Where It Is Going (According to Broadband Service Providers)*, Preliminary Report Prepared for the Staff of the FCC's Omnibus Broadband Initiative (November 11, 2009), at 11.
[21] *Id.* at 68. *See also id*. at 66, Table 15.
[22] FCC Broadband Task Force, Commission Open Meeting Presentation on the Status of the Commission's Processes for Development of a National Broadband Plan (September 29, 2009), at 45.

to take seriously the propensity of regulatory restrictions on broadband network management practices to stifle broadband infrastructure investment.

Investment and innovation will be chilled because of regulatory uncertainty and intrusiveness regarding "discrimination" that the FCC determines to be harmful as opposed to discrimination that it acknowledges is beneficial and therefore reasonable. Entrepreneurial experimentation requires freedom to attempt new technological, pricing and service offerings. This is no less the case when it comes to the Internet. Under the FCC's broadband Internet services regulatory framework, however, federal regulators are the arbiters of what broadband network management practices will be permissible.

In many instances the FCC's broadband Internet services regulatory framework establishes standards in general terms rather than specific requirements. This makes it uncertain whether existing or future network management practices will be permissible or not. In order to flesh out the scope of those general terms, the FCC will in many instances make judgments based on a balancing of competing interests.

FCC enforcement of its net neutrality regulation will be as open-ended as whatever purposes the FCC believes will likely create the kind of Internet market that the FCC wants. Because the FCC rejected proposals that anticompetitive conduct and consumer harm findings be required as the basis for adjudicating claims under its broadband Internet services regulatory framework, its reliance on its vaguely articulated "broad purposes" could well result in arbitrary and protectionist regulation for selected segments of the Internet marketplace.[23]

[23] *See* Order, at 45, para. 78.

In particular, the FCC adopted a set of non-exclusive categories for Internet "edge providers" and "end users."[24] It treats Internet "edge providers" differently, and more favorably, than all other "end users" for purposes of judging the lawfulness of pricing and other Internet market transactions with "broadband providers." Under the FCC's regulatory framework, for instance, broadband ISPs apparently have pricing freedom to offer usage-based or metered pricing to end users.[25] But edge providers receive special protections from any broadband ISP practices that would give priority on broadband ISP networks to certain content over others. Broadband ISPs are prohibited from offering priority service to certain edge provider content for a fee.[26]

The durability of the Commission's definitional categories is itself highly questionable. For instance, many consumers reasonably regarded as "end users" under the Commission's framework also produce and make content available on the Internet. Separating privileged "edge providers" from all other "end users," therefore, is no clear-cut task. Future technical determinations by the Commission of what actors are "edge providers" as opposed to mere "end users" could become the occasion for extensive lobbying efforts. The Commission may be opening itself up as a new venue for considering claims of competing parties who hope to gain advantage over broadband ISPs or other marketplace competitors via regulatory adjudications.

Extensive regulatory intrusion is all but invited by the FCC's complaint process. Under the procedural rules contained in its regulatory framework, the FCC gives "any person" the ability to file a formal complaint before the Commission to challenge

[24] Order, at 3, para. 4, fn. 2. *See also id.* at 11, para. 20 (describing "three types of Internet activities").
[25] Order, at 41, para. 72.
[26] Order, at 43, para. 76.

broadband ISP practices.[27] Rather than firmly placing the burden of proof on complainants, the FCC requires broadband ISPs to rebut *prima facie* showings of rule violations.[28] These procedural rules therefore make it relatively easy for the Commission to justify its own regulatory intrusion into the broadband market. And by rejecting any market power or consumer harm evidentiary standard, the Commission assumes for itself a roving mandate for adjudicating such complaints, deciding what kinds of transactions it should permit or restrict based on the Commission's own preferences for what the broadband Internet market should look like.

As a general matter, the FCC has adopted a policy approach making competitor welfare — "edge provider" interests — the underpinning of its regulation. An approach emphasizing consumer welfare — "end user" interests — would make market power and consumer harm the touchstones of its framework. The FCC's policy approach is also unreasonable in light of less onerous alternative approaches to addressing any actual problems in the broadband Internet market.

In contrast to the FCC's approach, antitrust law is premised on consumer welfare. Antitrust enforcement provides a more disciplined set of safeguards in cases of behavior that forecloses market competition. The Federal Trade Commission and the Department of Justice already have authority to investigate and pursue legal action in instances where broadband ISPs engage in anticompetitive conduct. The existing protections for consumers that are supplied by antitrust law need to be taken seriously before any rash move toward regulating the Internet takes place. A significant upshot to antitrust enforcement is its disciplined, case-by-case approach, which requires factual

[27] Order, at 83, para. 156; *id*. at 90 (Appendix B: Procedural Rules: Formal Complaints).
[28] Order, at 84, para. 157.

evidence of actual market power problems or consumer harms and clearly puts the burden of proof on complainants.

Mindful of existing FTC and DOJ authority to pursue antitrust violations by broadband ISPs, the better policy approach would be for the FCC to respect the rapidly advancing dynamic nature of the Internet marketplace by refraining from imposing regulation. It could instead observe market trends, monitor and investigate alleged violations of its *Open Internet Principles*, and bring public attention to areas of concern. At the very least, the FCC could work more closely with Congress to obtain proper authority to address matters involving broadband network management practices.

Thank you for giving me the opportunity to submit this statement for the record.

February 23, 2011