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Questioning the Premises of DOJ's Usage-Based Pricing Investigation

by

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Online video services are a new and fledgling force in the video marketplace. In the space of a few short years, consumers have come to enjoy a voluminous variety of video content using high-speed broadband Internet services. But according to recent news reports, the U.S. Department of Justice has opened a wide-ranging investigation of cable companies. DOJ reportedly is looking into whether so-called data caps on the volume of consumers' monthly broadband Internet usage are harming the ability of online video distributors (OVDs) to compete in the market.

It's by no means obvious that cable companies are engaged in any anticompetitive conduct with respect to OVDs. Indeed, there are reasons to be skeptical of DOJ's investigation, beginning with common sense observations relating to the [rapid changes and competitiveness](#) of the video market.

Unlike the early 1990s when cable companies maintained a market share of more than 90% of subscribing households, entry by two nationwide direct broadcast satellite (DBS) providers as well as traditional telephone companies into the video market have reduced that market share to approximately 60%. In many instances, consumers can choose from three or even four multichannel programming video distributors (MVPDs). Now that broadband Internet networks offer consumers increasing speed and capacity

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capabilities, online video services now constitute *both* complementary additions to cable and other MVPD services and competing alternatives. Consumers who prefer not to maintain MVPD subscriptions, for instance, can use their broadband services for delivery of cheaper OVD services such as Netflix to their Xbox 360 consoles. They can also combine broadband Internet-delivered OVD service with rabbit ear antennas for over-the-air high-definition TV broadcasting.

That OVDs such as Netflix, Hulu Plus, Microsoft Zune, and Amazon Prime could emerge so rapidly and achieve such popularity suggests the counter-intuitiveness of DOJ's investigation. Rather, the sudden emergence of OVD services attests to the underlying innovative and competitive forces at work in the video market. DOJ will be hard pressed to identify concrete instances of conduct demonstrating monopolistic or other anticompetitive harm when such conditions are present in the market.

That OVD services are a recent, emerging phenomena – with significant expansion and experimentation by existing and entering players underway – also counsels against DOJ investigation and intervention. Why investigate and possibly seek to impose legal restrictions in a video market that is in such a competitive flux and that offers consumers multiple choices? One plausible explanation is that DOJ remains beholden to the static market mindset that has characterized its other enforcement actions. [DOJ's legal complaint](#) challenging AT&T's thwarted merger with T-Mobile, for example, focused myopically on current market concentration and market share estimates while all but ignoring innovation and investment incentives for next-generation wireless networks. So perhaps DOJ is viewing the market for MVPD and broadband Internet services through the same static lens.

Treating cable companies offering broadband Internet services as if they still maintained the last-mile "bottlenecks" upon which early 1990s cable regulations were premised won't do justice to today's video market. Snapshot estimates of current market concentration or market share may be necessary factors to consider. But by themselves they are inadequate for analyzing markets characterized by continuous technological change.

Static market indicators fail to capture the [dynamism](#) that is so critical to the continuing advance of the video market. Forward-looking considerations include the growing complexity and convergence of the video market. There is also the necessity for cable companies and other broadband Internet service providers to find ways to monetize their services and finance network deployment and upgrades. This is a matter of basic business survival. MVPDs also offering broadband Internet services must find ways to pay for their massive capital investments in infrastructure, to maintain operations, and find new ways to meet changing consumer demands.

One way for MVPDs offering broadband Internet services to meet those challenges is to charge consumers based on how much data they upload and download each month. Comcast, Time Warner Cable, and others are now experimenting with different price packages or service tiers based on the amounts of bandwidth consumers use every

month. Variations of this approach include so-called "caps" or seldom enforced "soft caps" on monthly bandwidth use, tied to a consumer's chosen tier or usage amount. In Northern Virginia, for example, Cox Communications' soft cap range starts at 30GB for its \$25 per month plan and runs upward to a 400GB limit for its \$110 per month plan. Customers who reach or exceed their monthly allotments typically are warned, or eventually moved into a higher tier. Hard caps appear to have seldom been part of consumer experience, with Comcast's recent announcement that it's [moving away from caps](#) perhaps marking a broader market trend.

Although DOJ now appears to be investigating these kinds of broadband Internet pricing arrangements, one of its recent major enforcement actions took no exception to usage-based pricing or to data caps, in particular. DOJ's consent decree approving the Comcast/NBCU merger prohibited differential treatment of Internet traffic, depending on whether it was affiliated or unaffiliated with Comcast. But those restrictions were part of a proviso expressly recognizing that Comcast may offer broadband Internet services "under a package that includes caps, tiers, metering, or other usage-based pricing."

OVD services consume much larger amounts of bandwidth than e-mail or browsing of web pages with text and simple graphics. And Netflix has voiced opposition to usage-based pricing because, under a usage-based plan, its service uses up more of a subscriber's bandwidth allotment than other services or applications. In particular, [Netflix and others have complained](#) about Comcast's arrangement with Microsoft to stream video content to its subscribers through Xbox 360 consoles riding on Comcast's private video network instead of the public Internet. Video content streamed to the Xbox doesn't count toward a Comcast subscriber's broadband Internet services usage but Netflix content streamed to the same subscriber via the Internet does. Netflix regards this as discriminatory and anticompetitive. So, as reported in the *Wall Street Journal* on June 15, OVDs such as Netflix are supportive of DOJ's investigation of cable companies.

From a consumer standpoint, it's hard to see any long-term harm resulting from tiered pricing systems that use caps. Remember that legacy cable regulation was premised on the idea of a bottleneck and the idea that consumers would otherwise be denied access to diverse content. But no MVPD blocks lawful content available on the public Internet. Current FCC net neutrality regulations forbid blocking of lawful content, including video content provided by OVDs via the Internet. And prior to adoption of the FCC's net neutrality rules, no major reported incidents of OVD service blockage occurred either.

And "[Paying For Use Is Fair](#)." Usage-based pricing for commodities is common throughout the economy – and for good reason. It generally aligns rates with those imposing costs on the networks, so that heavy users pay more than light users. Consider how consumers stand to benefit from further experimentation with tiered or usage-based pricing for broadband Internet services. On the one hand, consumers will have access to additional video functionalities when cable companies and other MVPDs seek to retain subscribers by enhancing their services through their own video networks, even cannibalizing their own traditional MVPD services in the process.

Meanwhile, non-subscribers to MVPD services can select from their choice of disruptive OVD services and enjoy cost savings.

Supreme Court precedent regarding regulated industries also imposes a possible impediment to DOJ's investigation of cable companies. Absent price fixing, agreements to restrict output, or other traditional types of conduct considered *per se* illegal under antitrust law, DOJ would face difficulty in restricting or altering MVPD business practices so as to conform to DOJ's own ideas for better promoting competition.

Ultimately, any antitrust analysis of the video market must treat the overall welfare of consumers as its touchstone. By contrast, the law does not look favorably upon protecting competitor interests alone. An assertion that government intervention will bolster the competitiveness of OVDs vis-à-vis MVPDs might be used to try to sway some in the court of public opinion. But it will not be enough to carry the day in a court of law.

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