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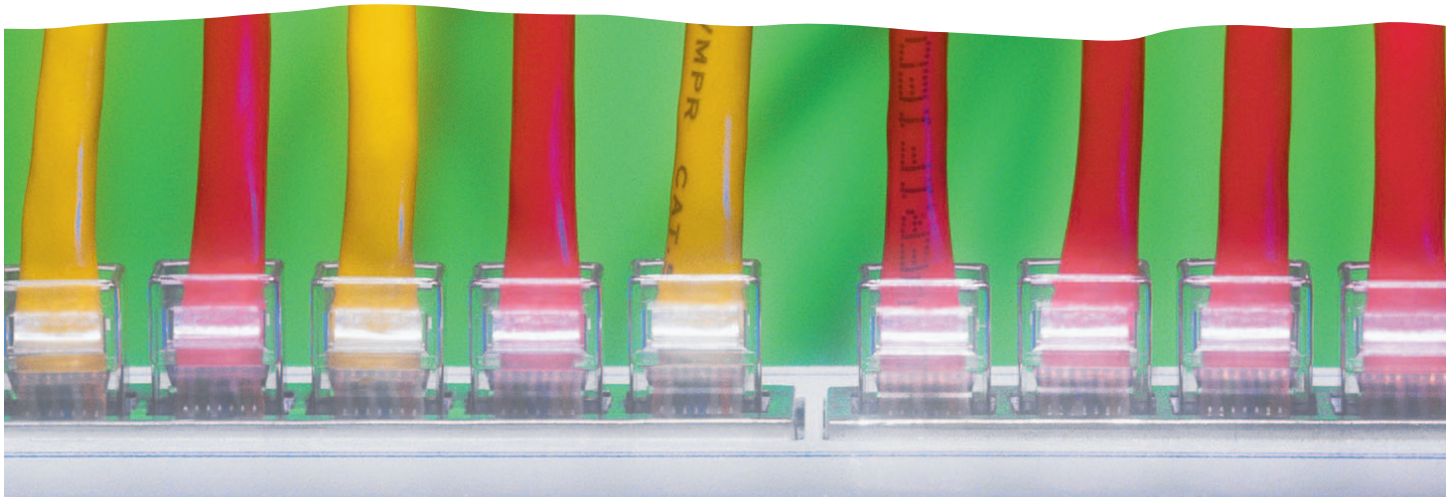
Blocked Net



One of the most important debates in telecommunications today is over "net neutrality." Advocates of a strong net-neutrality policy argue that broadband Internet providers may block or limit users' access to various Internet content and services either by favoring their affiliated businesses or by charging content providers for better service. And they want a new law that would bar such conduct.

They frame this issue as one of discrimination. But that's too limited a view. Advocates would do better to describe the issue as a matter of monopoly: Because content providers have no choice but to go through the subscriber's broadband provider to reach the user, the broadband provider can exploit this monopoly, much as some telephone companies have done in the past when setting interconnection charges.

Ironically, the Bell phone companies are proposing to change the Internet's interconnection rules to resemble the traditional telephone model at the same time that the Federal Communications Commission considers reforming telephone interconnection to look more like the Internet.

CONGRESS AND THE FCC

So what, exactly, is net neutrality all about? In the current debate "net neutrality" is a catchy but somewhat vague term used

to describe a regulatory effort to enshrine a nondiscrimination principle in the nation's laws governing Internet broadband access. The idea is to prevent broadband providers from "discriminating" against particular applications or particular content by blocking subscribers' access completely or by transporting certain bits more slowly unless payment is made for greater or guaranteed bandwidth.

The FCC has approached net-neutrality issues gingerly. In perhaps the FCC's first net-neutrality case, Madison River Communications, a small incumbent local phone company, blocked a competitor's Voice over Internet Protocol (VoIP) services. In March 2005 the FCC reached a consent decree with the company, putting an end to this egregious practice while carefully avoiding a written decision that might have precedential value in a more nuanced scenario.

In September 2005, when the FCC generally deregulated wireline Internet broadband access, it also issued a nonbinding policy statement setting out certain net-neutrality principles designed to protect consumers' access to the lawful Internet content of their choice and consumers' ability to attach devices of their choice to the Internet (e.g., VoIP equipment).

Such proposals are most likely to affect content providers, such as streaming video and VoIP companies, that need good bandwidth for their services to work. Although such content providers have always had to pay for their own Internet access, they have not previously had to pay anything to their customers' broadband providers.

Significantly, the FCC's policy statement, even where binding, would not necessarily prevent such premium charges. Moreover, while the rejected amendment would have explicitly prohibited these premium charges, the COPE Act would codify the FCC's policy statement.

Upset about this potentially dramatic change to the Internet's economic model, net-neutrality advocates argue this is just another form of discrimination that must be stamped out. Besides, they say, it would be unfair—and ultimately more expensive for consumers—if broadband providers could double dip by charging both their own customers and the content providers for transporting content.

But the Bells' proposal does not easily fit into the discrimination framework that so far has driven net-neutrality advocacy. Even if nondiscrimination obligations like those that apply to

Advocates of net neutrality need to focus on broadband's moment of monopoly.

BY ALFRED M. MAMLET AND DANIEL C.H. MAH

Since then, the issue has continued to gather steam. At the end of 2005 the FCC required compliance with its policy statement before it would approve the Verizon-MCI and SBC-AT&T mergers.

Now Congress is stepping into the act. Last week, the House Energy and Commerce Committee adopted the Communications, Opportunity, Promotion and Enhancement Act of 2006. Although the COPE Act would codify the FCC's nonbinding policy statement, an amendment with much stronger language was defeated.

The full House may consider the COPE Act on a fast-track basis as early as this month. But the legislation faces an uncertain future in the Senate in this election-shortened congressional session, and the debate over net neutrality is likely to top the telecom agenda for several years to come.

So far, net-neutrality advocates—primarily consumer groups and online content companies—have been concerned that cable and phone companies supplying broadband access will use their control over the user's connection to the Internet to discriminate against other companies' content, applications, or services in favor of their own content, applications, or services. Net-neutrality advocates say such discriminatory conduct is anti-competitive and should be prohibited.

In January 2006, while professing no intention to block competitors' services, the Bell companies proposed to charge all online content providers for "premium" access (that is, enhanced or guaranteed bandwidth) to their broadband subscribers, essentially creating a "fast lane" for content providers willing to pay.

common carriers were applied to now largely deregulated broadband access services, only "unreasonable" discrimination would be prohibited. Charging all content providers a premium price for premium service is not obviously unreasonable. Phone and cable companies can contend there is a rational basis for premium charges for greater or guaranteed bandwidth and that such charges are industry norms for other telecom services.

The issue is closer when a cable company charges competitors a premium to stream video while providing the same premium bandwidth to its affiliated content provider for only the "cost" of an interaffiliate transfer payment.

The Bells, by contrast, have very little affiliated content, and they would gladly charge *all* content providers for the ability to get premium access to their broadband subscribers. They argue that it is reasonable for broadband providers to recover the costs of providing higher or guaranteed data speeds from both end users and the online companies wanting to reach them. They contend that providers of services that need greater bandwidth, such as streaming video, should pay for it.

NEW WINE, SAME BOTTLENECK

Net-neutrality advocates would have a stronger argument against these premium charges if the Bells' proposed fees were analyzed as interconnection charges, rather than as a species of discrimination.

Interconnection charges—the payments that carriers make to each other to connect a call between end users on different net-

works—are well known in the world of traditional circuit-switched phone service. They have been the subject of extensive analysis and difficult reform efforts. Viewed through this lens, the Bells' proposal starts to look familiar.

In the telephone world the calling party's carrier generally pays the called party's carrier a charge to connect (or "terminate") a call. But as the FCC itself has noted, this system essentially gives the called party's carrier a "termination monopoly" over its customers. According to one 2000 FCC study, "This market power arises from the fact that the calling party's carrier . . . has no alternative carrier that can terminate a call to a particular called party. Thus, the calling party's carrier must pay the terminating network whatever price it demands in order to reach the called party."

As the same study noted, even new-entrant local phone companies could exploit this monopoly by charging fees to long-distance carriers that were far in excess of what the incumbent Bells were charging. Similarly, until the FCC intervened, some local phone companies were exploiting this monopoly by signing up as customers dial-up Internet service providers, which typically only receive calls, and charging fees to other carriers to complete the calls.

With the Internet, the system of interconnection payments is different and not based on the direction of the traffic flow. A handful of nationwide Internet "backbones" share customer traffic with one another for free under arrangements known as "peering." Smaller Internet service providers may also peer with one another but generally must pay for transit connections with at least one of the major backbones (or with providers connected to backbones) to ensure full connectivity. Thus, in many instances, there is no direct relationship (and no payments) between the networks serving different Internet end users. As a result, there has not been a comparable opportunity to exploit a termination monopoly such as exists with telephone interconnection.

By proposing to charge a premium to content providers that want greater or guaranteed bandwidth, the Bells would be importing the termination monopoly from the telephone world. At any given time, a broadband subscriber typically accesses content through only a single broadband provider's network. This leaves the content provider with no alternative but to connect through the subscriber's broadband provider.

Although the content provider would still have a choice between paying for fast-lane access or falling back to the slow lane, this choice may be more theoretical than real. The broadband provider may leave too little bandwidth in the slow lane for the content provider's application to work. Moreover, the content provider may have no competitive alternative but to purchase fast-lane access to keep up with other content providers.

Past examples of how the termination monopoly has been exploited with telephones underscore the need for government intervention. And this is true despite the fact that broadband providers compete for customers—because at any given time, a subscriber will have only one broadband provider.

SOLUTIONS?

The existing telephone interconnection regime nets the Bells and other incumbent phone companies billions of dollars a year. Not surprisingly, reform of this complex and outdated system has been slow in coming.

Still, the need for change is widely recognized, particularly given the inefficiencies created by termination monopolies. Although debate continues, the general direction of the reform efforts has been to phase out interconnection payments and to move toward "bill-and-keep"—a system in which the connecting carriers do not pay each other but instead recover interconnection costs from their own customers only.

Indeed, a principal argument for bill-and-keep is to eliminate the possibility of exploiting termination monopolies and to require that payments come only from end users because they have competitive alternatives.

If broadband providers begin charging content providers for fast-lane access to their subscribers, they will effectively be re-creating the termination monopoly on the Internet—a move at odds with reform efforts in the telephone world.

Unless the FCC wants to be in the business of regulating Internet interconnection payments long after it hopes to have reformed telephone interconnection payments, it should prevent the imposition of such charges. Instead of exploiting termination monopolies, broadband providers should recover infrastructure costs from their subscribers, with prices constrained by competitive forces.

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