

The New Network Compact: Consumers Are in Charge

For the Internet Innovation Alliance

July 30, 2014

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Consensus: Fulfill core values

Traditional, embodied in *Communications Act of 1934*:

- **Public safety**
- **Universal connectivity**
- **Consumer protection**

New, added in *Telecommunications Act of 1996*:

- **Competition**

Regulators' dilemma:

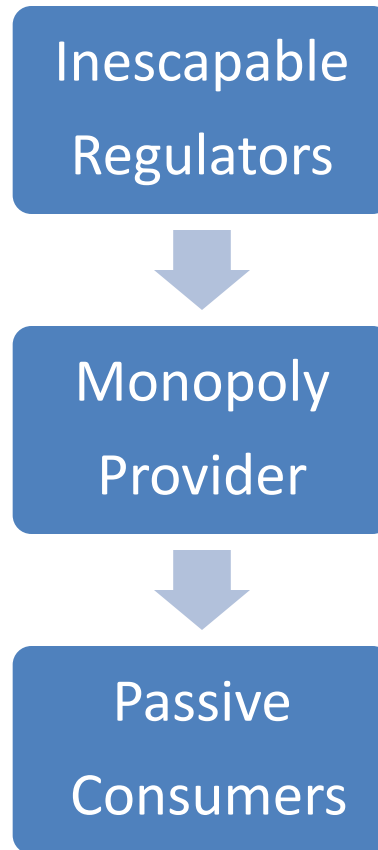
How to sustain traditional core values
premised in monopoly
once competition
has given consumers choices,
including the choice to evade core values?

Old regulatory model

- A single provider, controlled by regulator, has a monopoly
- Consumers have to purchase what regulators design and monopolist provides
- Consumers can be treated as homogeneous because they have no choices
- Regulators can apply 'one size fits all' solutions
- Consumers can't evade traditional core values

The Old Network Compact

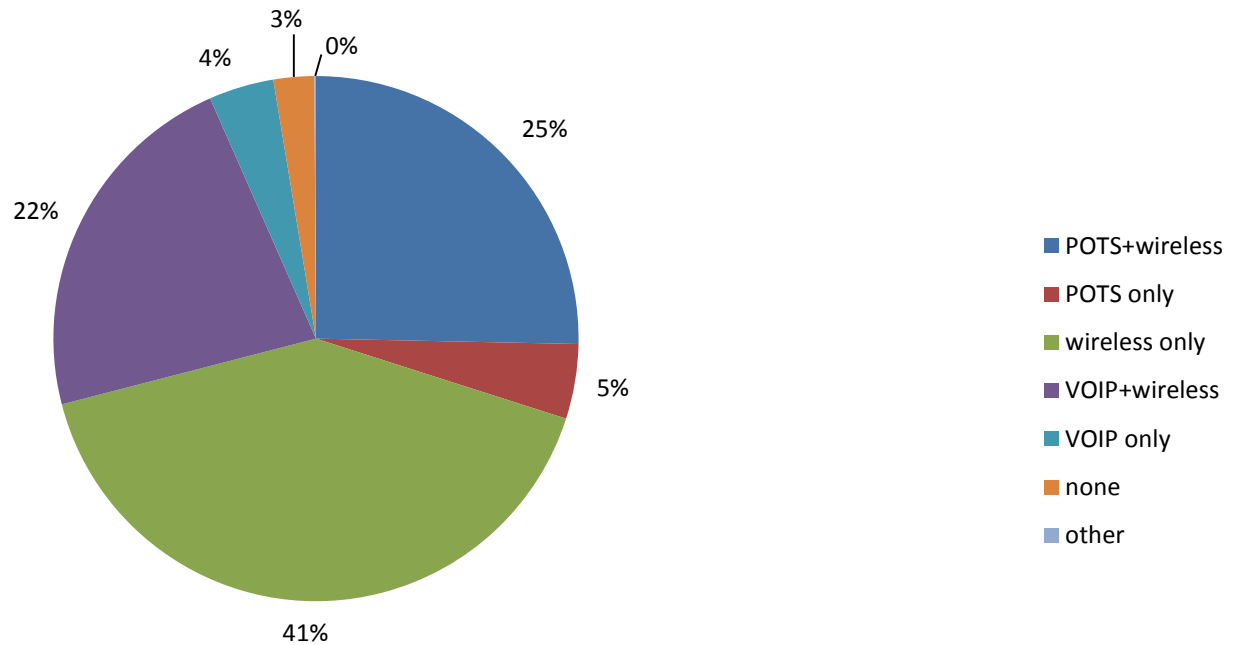
Regulators in charge



**The world has changed:
Consumers have choices**

Consumer voice market 2013

(% of households)

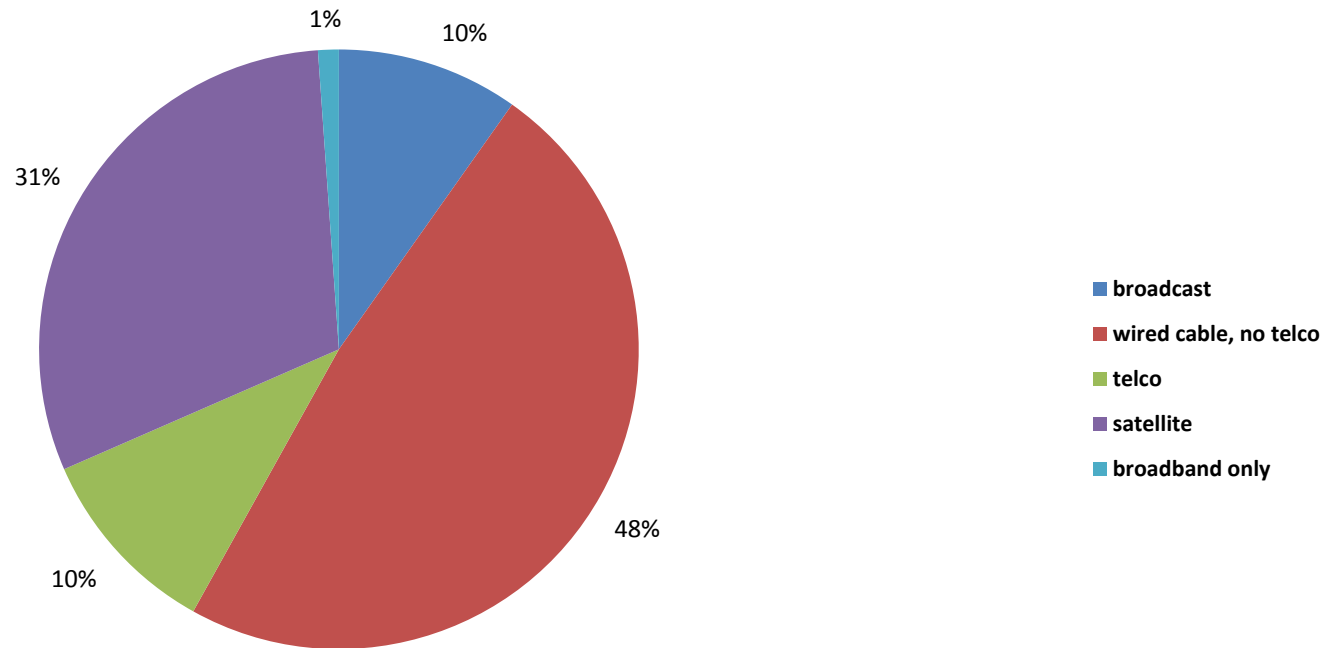


Sources: CDC, FCC

Video market

year-end 2013

(% households)

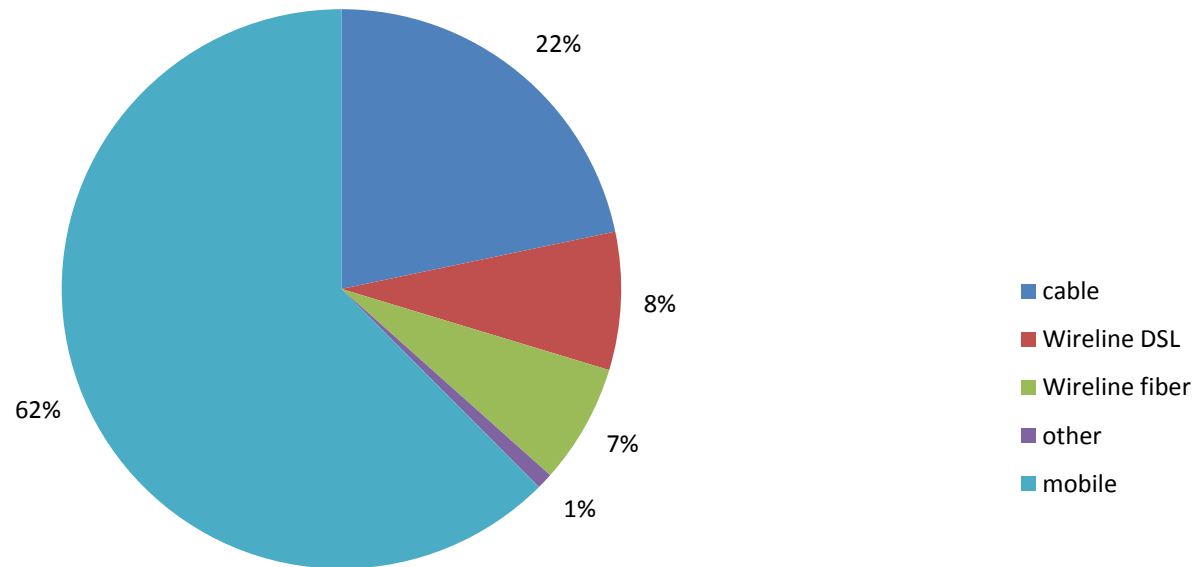


Source: Nielsen

Consumer Internet-access market

mid-2013

(% of residential connections)



Sources: FCC, UBS

Consumers make cross-platform choices based on the message, audience, context

- Voice communication – Wireline? Wireless? VOIP?
- Text
- E-mail (with attached video clip?)
- Skype
- Social networking—Facebook, Twitter
- Other

Consumers' choices vary with demographics

- Income
- Education
- Racial or ethnic background
- Age
- Health
- Disability
- Housing configuration
- Geography: rural/suburban/urban
- Other

Consumers' purchase decisions cut across regulatory silos

- Choice of voice plan may depend on favorite shows offered in the video package that is part of a bundle
- Choice of voice plan may depend on broadband package offered as part of a bundle
- Wireless voice may or may not be accompanied by fixed broadband
- Wireless broadband may or may not be accompanied by fixed broadband

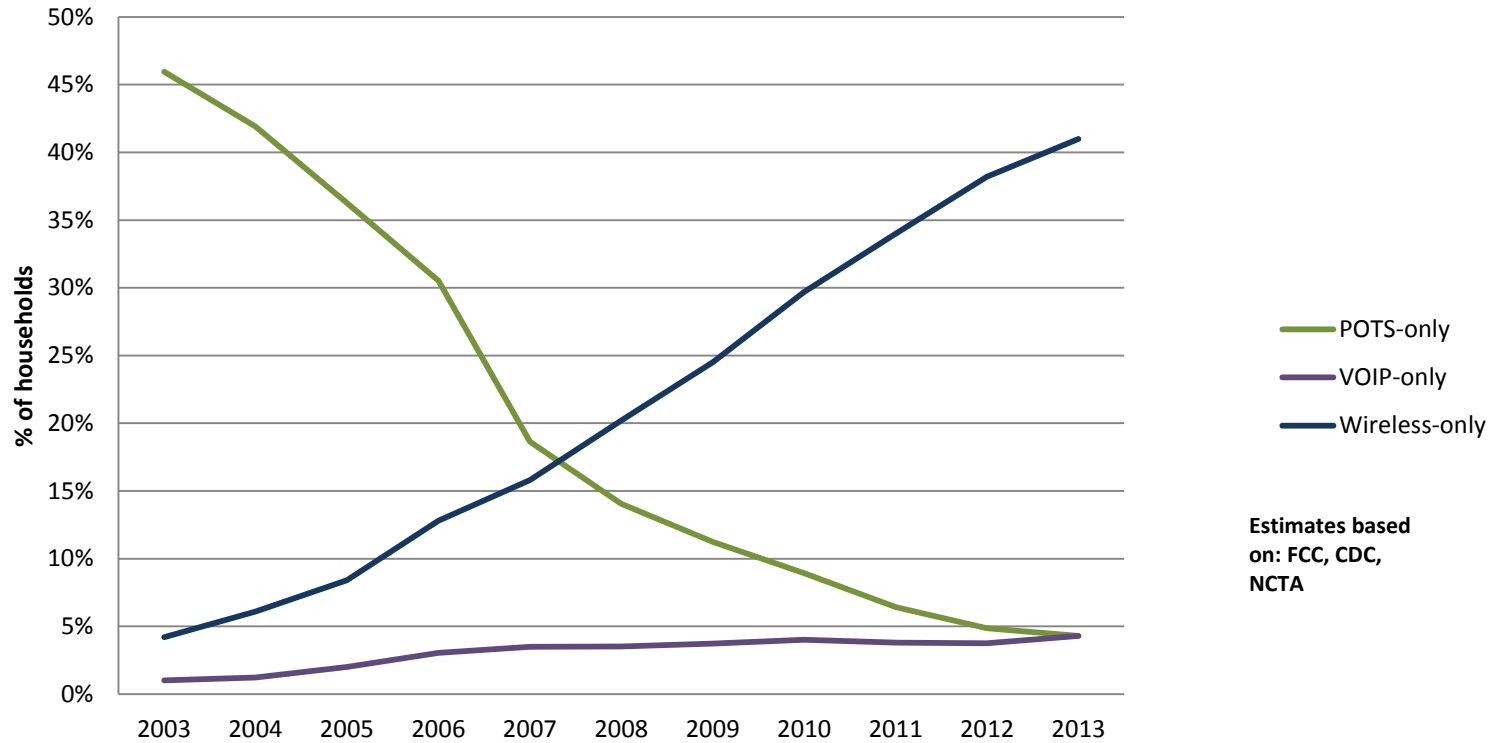
New reality: Consumers are in control

- Consumers have plethora of choices
- Consumers' choices are too complex for regulators and providers to satisfy with 'one size fits all' solutions
- Consumers can evade providers who have to provide core values

Consumers can evade core values

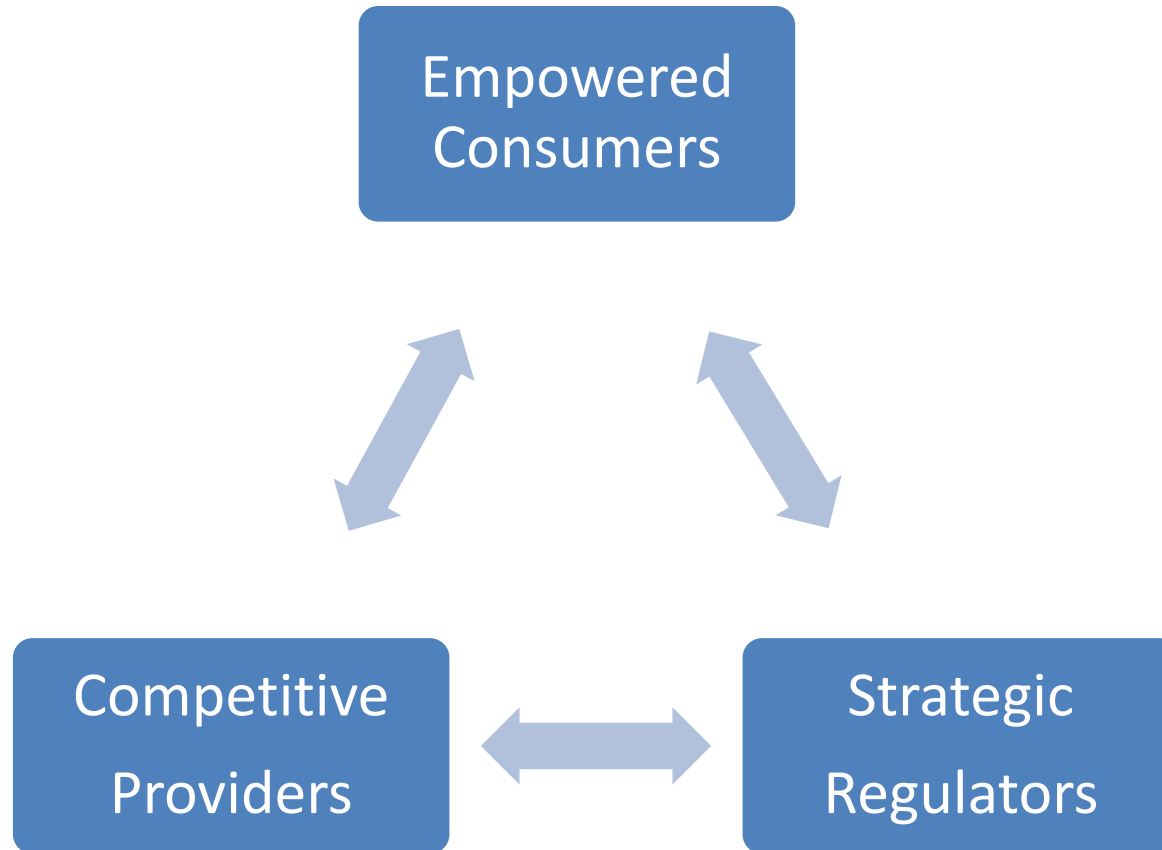
- Many Kansas City consumers are choosing Google Fiber, which does not provide interconnected voice and automatic 911
- Consumers replace multiple voice calls with a tweet or a post on a social network, which do not support Universal Service
- Only 5% of consumers rely on POTS exclusively

Consumers abandon the most regulated choice when selecting a single voice provider (2003-2013)



The new network compact

Consumers in charge



Investment implications of consumer choice

- Old model—no choices:
 - Cross-subsidies work because they can't be avoided
 - Regulators can guarantee floor as well as ceiling on provider's earnings
- New Model—plethora of choices:
 - Providers face extensive and varied competition
 - Consumers buy what they want: across providers, platforms, regulatory silos
 - Revenues and earnings go with consumers
 - Cross-subsidies don't work—consumers can flee the subsidizing services
 - Regulators can limit providers' earnings on the upside but can't protect the downside
 - Providers can only survive if they give consumers what consumers want

How can regulators respond?

Strategically targeted regulation

- Recognize that consumers have varied needs and desires
- Respect consumers' own choices
- Focus on vulnerable consumers
- Focus only on specific needs not addressed by the market
- Address the need, not the specific technology

Strategic regulation

