

Reed Hundt
NOVEMBER 11, 2003
“The Revolution Revolves Again”

We are here today to discuss a new stage in the metamorphosis of the Net, the addition of another of the five senses that may be incorporated in this new medium, which as McLuhan predicted two generations ago may subsume and extend all previous media.

We are here to talk about talking on the Internet. We are here to talk about voice on the Net.

The Internet’s messaging is still a matter of fingertips. How much more effective will it be – how much quicker can the people share knowledge– when we are talking and listening to each other on the Net even more easily than we can do in this very room.

A fully developed Internet is a Net that will unite voice, ears, eyes, and link not just a person to a page, but people to people.

So this is what Voice over the Internet is really about: a step to a different form of society and a different kind of politics.

If VOIP develops as its science suggests, then carriers will have much greater incentive to build fiber to homes. They will charge for such connectivity, and abandon the soon to be defunct pricing per minute of voice calls. Imagine a household today paying \$30 a month for DSL and \$20 a month for local voice. Suppose that a household could instead pay the aggregate of \$50 a month but buy for that not copper access but fiber to the premises providing broadband at 100 megabits per second, with voice as an application that is carried essentially for free in the huge bit stream surging up and down this very high speed connection. Being able to count on \$50 a month from 80 million households with PCs, and perhaps some government subsidy for the 20 million low income and rural households left out of this deal, the telcos then would be looking at revenue streams that could make them much more eager to build out fiber to every home. They could become Connection Companies as well as service providers

The main risk to a walk on this sunny side of the street is the possibility of regulatory storm clouds brewing over Washington.

In Washington many think that entrepreneurs are barbarians at the gate, and change is by definition a threat to the livelihood of everyone who has a stake in the status quo.

It is true that entrepreneurs carry the disruptive idea that we are each endowed by our creator with the inalienable right to try to change the world. This is the central idea of democracy and of technology.

VOIP is disruptive by definition because it changes the business model for the biggest market in communications: fixed line voice. But as indicated by Qwest's recent announcement of its VOIP plans, telcos see that this new service at last brings the promise of retail price deregulation for voice service.

Nearly 10 years ago your FCC declared wireless voice to be totally deregulated at the retail price level. This was called the section 332 order. So states like California that wanted to set prices for this new service were told they could not do so. As a result of this decision, coupled with fairly easy entry by numerous companies into the market, cellular became the biggest and most competitive new communications market in the last decade.

In the last 10 years cellular prices are down 74% and subscribers are up 780%; jobs are up 383%; capital investment is up 800%; minutes of use are up 200%. Not bad! VOIP could travel the same road, if a true deregulatory way is followed.

For many years, the bane of all policy in wireline telephone markets has been state regulation of retail prices. This policy has protected some consumers at the expense of many who would have had lower prices and better offers under more efficient schemes.

VOIP can disrupt this state regulation. It can force states to adopt only such universal service policies as are applicable to all technologies, funded from general revenue instead of arbitrageable levies on specific services, and used to address real needs such as fiber to poor and remote locations instead of merely helping certain middle or upper income classes at the expense of most consumers. These changes will force business model changes as well as regulatory changes, but all can benefit in the end.

Let's be specific to illustrate the point: if a consumer in, say, Bethesda, Maryland, can choose from three broadband suppliers; Vonage, Skype, and a few other VOIP services; a half-dozen cellular service providers; and three UNEP sellers, then why does that consumer need retail price regulation of basic voice service? That actually does describe much of Bethesda today. And that's

not all that different from neighborhoods containing millions of consumers across the country. Zip code by zip code, state by state, region by region, the FCC should be preparing Operation Deregulation. If not now, when?

But what will the FCC do with VOIP? There's no promise that it will follow this deregulatory prescription. I haven't heard that the FCC wants to deregulate voice pricing. I wonder if the FCC's DNA instead will cause it to generate another era of regulation, just when innovation gives us a chance to break into the clear, sunny upland of free market competition in voice.

Should we fear the encroachment of the FCC into new areas of regulation? Look at the record of the last couple of years. This agency ordered that every American must pay for a digital tuner in every TV set, even though almost 90 percent of households already do not tune in to over the air reception. This is a \$20 billion annual tax on the American consumers, with the money going principally to foreign manufacturers.

Should we worry that we might have a hard time figuring out what this agency intends to do? Let's be post-modernists and study the texts. On November 5, 2003, the FCC chair told Senator Ron Wyden that he will hold a hearing on Voice over Internet Protocol on December 1. He said he will invite "industry and government." Who is the industry that has been invited? What government is attending? Who will represent the people?

In the same letter, the chair said "shortly after the forum, the FCC will initiate a Notice of Public Rule Making on VOIP services." Not to be picky but there is no such procedure under the law. Does the FCC mean a NOI, or Notice of Inquiry? If that is the intended notice, we can breathe a little easier, because a NOI often means there is no pre-existing decision to regulate. But what if the FCC really meant a Notice of Proposed Rulemaking? Then we should worry, because such a notice typically portends an intent to put on the books new regulation. A rulemaking is the name of the process that produces new regulations. And how can we believe the December 1 hearing is part of a neutral, non-biased inquiry if the FCC already intends to propose new regulations "shortly" afterwards?

Moreover, in this letter the FCC says it will issue a report and order within a year. A report and order typically is the name of the document that contains regulations. If the FCC doesn't intend to

regulate VOIP then it wouldn't need to issue any Report and Order. This isn't just fog that shrouds the FCC, but thunderheads brewing trouble for VOIP.

Normally on the eve of a Presidential election even the FCC knows it should abide the will of the people and wait for their judgment on who will set policy. But there's no sign in this letter that the FCC intends to wait on the 2004 elections; perhaps the agency, as it should be, highly confident that the President will be re-elected. Yet for those in either party or no party at all who do not favor regulating VOIP, the urge to move before the election should not be taken as a positive signal. Positive would be a statement by the FCC that it doesn't intend to do anything about VOIP for at least a year or two, or certainly until the service become more well-established in the marketplace. My thesis: If the regulatory system ain't broke, don't fix it; and by the way when and if it is broke, consider just throwing it out.

When the Internet was in its salad days, your FCC decided that ISP's should be able to use the telephone network without paying extra charges. The result was 5,000 ISPs promoting narrowband Internet, and selling it at prices that were one tenth of what was charged in Europe and one hundredth of what was charged in Asia. That's a primary reason why the Internet flourished principally in the United States, a main reason why the Net became an American medium. To follow this reasoning with respect to VOIP, the FCC need only say that VOIP is just like e-mail and needs no regulation. That, like the treatment of internet access, would be a decision not to pour new wine into old bottles. That approach worked out well for narrowband. Why not copy it for VOIP, even if its authors are now old and gray (or Democrats). But in its letter to Senator Wyden, the FCC mentioned a desire to place uppermost in its proposal "E911, universal service, and securing our homeland."

When the FCC talks about the shibboleth of security, the people should be on guard. To address homeland security, the FCC should create a single national swath of spectrum for all public safety to use. It should encourage municipalities and federal agencies to coordinate their communications, to adopt the most advanced security measures. It should take virtually wasted spectrum held by broadcasters and find ways to use its economic value and its propagation characteristics to give us the world's leading homeland defense. These are homeland security imperatives, not regulating VOIP.

As to E911, FCC delayed for years the imposition of that requirement on wireless carriers. That was a critical issue. E911 for VOIP doesn't come close to the importance of that issue. After all, consumers are certainly likely to be able to use either or both wireless or wire service providers for 911 for years to come, even if VOIP is unregulated from its inception in the marketplace.

Then there's the universal service bugaboo. There could be nothing more potentially universal than the new cost reductions that VOIP can offer not just for one-to-one voice calls but for a range of services such as conference calls, distance learning, and health care delivery. Why isn't the right goal the delivery of VOIP universally, instead of the universal regulation of VOIP?

And indeed why isn't the highest universal service goal the universal build out of fiber and wireless broadband? Universal broadband would probably add a million jobs to the economy. And since the network would be here in our homeland, the jobs to build and maintain it couldn't be exported to foreign lands. There's nothing wrong with homeland job security.

Some believe the FCC should burden or tax VOIP with charges that are then given to circuit-switched voice providers. This is what is euphemistically called a transition. But should we add a charge on airline tickets in order to raise revenue for railroads? Add a charge to e-mail in order to raise money for the United States Postal Service? Add a charge to PCs in order to subsidize mainframes? Why should VOIP require a transition that starts with regulation? At some point, new goods and services should not subsidize old; new networks should not be taxed to support old; new market competition can eradicate the case for price regulation of old, static, non-competitive markets. The goal in all events is a competition policy that obliges competitors to seek advantage by obtaining and generating productivity gains.

The only right national economic policy is to create a high and rising standard of living for the nation's citizens. I copy this from "Competitive Advantage of Nations" by Michael Porter of the Harvard Business School. To do that a country must seek full employment and productivity gains in all sectors. Communications is both a sector and an input to other sectors. Therefore, countries are doubly advised to focus on policies to generate highly productive communications sectors.

Following this rule, countries like Korea and Japan know they need the most efficient communications networks. They are

structuring their markets, and their government pump-priming subsidies, to get this result. They seek “a high-speed, congestion-free, always reliable, friction-free, packet switched, big bandwidth, data friendly network that is universally available, competitively priced, and capable of driving our economy to new heights.”

They know that what they need – and I quote again – “a data network that can easily carry voice, instead of what we have today, a voice network struggling to carry data.”

These are quotes from the FCC of 1997, long ago and far away in time, yet now heard echoing in Asia. But every FCC has the same job in a sense: the job of helping the new drive out the old, helping new efficiencies overcome bottlenecks and first mover advantages in order to get to the market. The help should be in the nature of assuring competitive market structure and rational universal service schemes if any such are necessary. It should not be help in the form of technology bias or preference for individual firms. It should be help in the sense of a desire to see efficiencies translated through a competitive process to marketplace rivalry. This philosophy, if it animated the FCC today, would not lead to regulating VOIP but to opening the door to entrepreneurs at both new companies and old who would create new business models that emphasized connectivity and creativity and consumer benefits and productivity gains. These are all worthy ways for the United States to continue to fight the competitive battle of nations.

Of course we in the United States are fighting not only for economic success, but also for democracy around the world. This is also not a new goal for the United States. To this end we must renew democracy here at home. At the FCC, democracy means showing a willingness to take decisions that are considered in the plain view of the people, done for the people, and ultimately taken by the people, and not by a privileged elite.

Will the FCC’s treatment of the new and exciting technology of voice over the Internet meet this test? Will the FCC listen to the people and do what serves the best interest of the people? There’s a chance for this to happen. But that will require VOP – the Voice of the People – to be heard. Now the choice is yours.

--30--