

Net Neutrality – How relevant is to Australia and New Zealand?

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Research objectives

- Why has the issue of net neutrality received so little attention from regulators and policy makers in Australia and New Zealand?
- Does Australia and New Zealand need specific net neutrality regulation?

Outline

1. The net neutrality debate so far
2. What is net neutrality?
3. The economics of net neutrality
4. How relevant is net neutrality to Australia and New Zealand?
5. Conclusions

1. The net neutrality debate so far

- The net neutrality debate has its origin in the United States where it has received significant attention from the FCC and policy makers.
 - In September 2009 the chairman of the FCC announced that the it would begin to formalise net neutrality rules (the so-called Four Freedoms internet policy principles plus two more principles)
 - President Obama campaigned on being ‘a big believer in net neutrality’
- In Australia the net neutrality debate is widely considered to be a uniquely American problem.
- In New Zealand regulators and policy makers have, to date, given little attention to the issue of net neutrality.

2. What is net neutrality?

- The concept of net neutrality is best understood as a series of propositions:
 1. ISPs should be prevented from charging more for priority delivery of content;
 2. ISPs should not be allowed to deny access to specific websites or Internet applications; and
 3. ISPs should not be allowed to integrate backwards into the production of content or applications.
- The common theme underlying all of these propositions is the ability of ISPs to discriminate among content or applications.
- Importantly, the concerns net neutrality advocates concern both price and non-price discrimination.

3. The economics of net neutrality

- Economics tells us that price and non-price discrimination is rational and can be welfare enhancing:
 - Third degree price discrimination by a monopolist can expand output thereby increasing both consumer and producer surplus.
 - In markets that exhibit economies of scale, discrimination and differential pricing is usually the result of competition.
 - Hence, price and non-price discrimination is common place in the provision of telecommunication services and in many other network industries (i.e. road pricing)
- It easy to think how discriminatory behaviour by firms with market may give rise to concerns of anti-competitive effect and/or purpose.

3. The economics of net neutrality cont...

- Concerns about market power and discrimination does not necessarily require a blanket prohibition.
- Instead, any justified policy response should satisfy the following two pre-conditions:
 1. The existence of substantial (or significant) market power in the provision of an access service; and
 2. Any practice of discrimination should have adverse consequences for competition and consumer welfare.

4. How relevant is net neutrality to Australia and New Zealand?

4.1 The competitive landscape

4.2 Business models and pricing structures

4.3 Access regulation

4.4 Conduct regulation

4.1 The competitive landscape

- Competition in the retail provision of Internet access coupled with low barriers to entry and expansion dampens the incentives for network operators and ISPs to block access to content.
- In terms of competition:
 - Australia has 638 ISPs in operation. Almost all geographic areas are served by at least two competing ISPs.
 - New Zealand has over 50 ISPs in operation. Most consumers have a choice of at least 2 competing ISPs regardless of their geographic location
- New entrants in both countries have available a range of entry and expansion options:
 - To resell the incumbent's or another provider's wholesale service (i.e. Layer 2 bitstream services and VMO arrangements)
 - Partial facilities based competition (i.e. ULL and LSS)
 - Full facilities based competition by investing in alternative fixed or wireless communication networks

4.2 Business models and pricing structures

- In both Australia and New Zealand the use of volumetric pricing by ISPs is widespread.
- Volumetric pricing dampens the incentives that ISPs and network operators face to discriminate against or block traffic based on its source or type.
- Volumetric pricing has the following advantages:
 - Allows ISPs to more effectively set user prices to marginal costs
 - Provides strong incentives to invest in additional network capacity and capabilities – as demand for Internet traffic grows ISP's revenues also grow
 - Provides strong incentives for ISPs to maximise the transmission of all network traffic because this will allow ISPs to earn additional revenues and maximise profits
 - It is a transparent network management practice whereby the ISP is agnostic about what traffic is shaped . Instead network congestion is managed on the basis of willingness to pay.

4.3 Access regulation

- In both Australia and New Zealand the regulators have available to them industry specific access regimes which negate the need for specific net neutrality regulation.
- In each country, if the regulator was to form the view that discriminatory treatment of network traffic was undesirable (i.e. not in the interest of users) they could effectively mandate access to an Internet access service which would oblige the ISP or network operator to provide access on non-discriminatory price and non-price terms and conditions. Specifically
 - In Australia, the regulator (i.e. ACCC) could declare an Internet access service under Part XIC of the *Trade Practices Act 1974*
 - In New Zealand, the Commerce Commission could designate, or specify, the an Internet access service under Part 2 of the *Telecommunications Act*.

4.4 Conduct regulation

- In Australia, the ACCC has two anti-competitive conduct provisions of the TPA – section 46 and Part XIB – that it could rely on to prevent or remedy undesirable discriminatory treatment of Internet traffic.
- In New Zealand, the Commerce Commission could rely on section 36 of the Commerce Act if it formed the view that the discriminatory treatment of Internet traffic, by an ISP or network operator amounted to a taking advantage of a substantial degree of power for an anti-competitive purpose.
 - Importantly purpose may be inferred by effect.

5. Conclusions

- There is little justification for specific net neutrality regulation in either Australia or New Zealand. This is due to:
 - Strong competition coupled with low barriers to entry dampens incentives for network operators and ISPs to block access to types of internet traffic
 - Volumetric pricing provides strong incentives for ISPs to maximise the transmission of all network traffic regardless of source or type
 - The existing regulatory frameworks that apply to the Australian and New Zealand telecommunications sectors are well placed to deal with any competition concerns that may arise from discriminatory network practices on behalf of ISPs or network operators.