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**TESTIMONY OF
SCOTT WALLSTEN, PH.D.**

**BEFORE THE
COMMITTEE ON SMALL BUSINESS AND ENTREPRENEURSHIP
U.S. SENATE**

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Communications, Broadband and Competitiveness

Before the
Committee on Small Business and Entrepreneurship
U.S. Senate

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Mr. Chairman and members of the Committee, thank you for inviting me here and giving me the opportunity to testify. I will make three points.

First, there is little evidence of a U.S. broadband problem. Telephone, cable, and wireless companies are investing billions in new high-speed infrastructure, and consumers and businesses are adopting broadband at remarkable rates.

Second, those who believe there is a problem advance proposals that sound appealing, but they fail to provide solid analysis showing that their proposals would actually benefit consumers or small businesses.

Third, despite significant infrastructure investment, we can do better. In particular, we need to collect better data that would allow us to rigorously analyze proposed policies and to remove arbitrary barriers to entry that continue to prevent the market from reaching its full competitive potential. Government can help achieve both goals.

I'll elaborate on those points.

First, the sky isn't falling. There is scant evidence of a U.S. broadband problem. Nearly half of all American households subscribe to high-speed Internet connections, more than twice as many as just a few years ago.¹ About 60 percent of businesses with fewer than 100 employees have broadband connections.² Earlier this month the National Federation of Independent Businesses reported the results of a survey that asked members to state their most important problem.³ Broadband did not make the list.

Internet service providers are investing in broadband infrastructure at unprecedented rates. Cable companies are expected to spend about \$15 billion this year upgrading their networks.⁴ Verizon alone is planning to spend \$23 billion on its fiber-optic network by 2010.⁵ By the second quarter of 2007 its fiber services were available to nearly 8 million homes, and are expected to reach 9 million by the end of the year.⁶ Cellular mobile companies continue to upgrade and build high-speed networks, while other firms are building out new wireless networks that offer coverage ranging from very local to national.⁷

Supply is not the only factor that affects the state of broadband. Demand is also crucial in determining broadband penetration and speeds. I understand that some advocates believe faster is always better. Like them, I live online and place a high value on a very fast connection. But not everyone has the same preferences that we do. Few small businesses, for example, download multiple

¹ http://www.pewinternet.org/pdfs/Broadband_Commentary.pdf

² IDC market analysis, March 2007. "U.S. Small Business Internet 2007-2011 Forecast."

³ http://www.nfib.com/object/IO_34726.html

⁴ <http://www.infonetics.com/resources/purple.shtml?msna07.cpx.2h06.nr.shtml>

⁵ <http://policyblog.verizon.com/policyblog/blogs/policyblog/czblogger1/290/fios-fact-sheet.aspx>

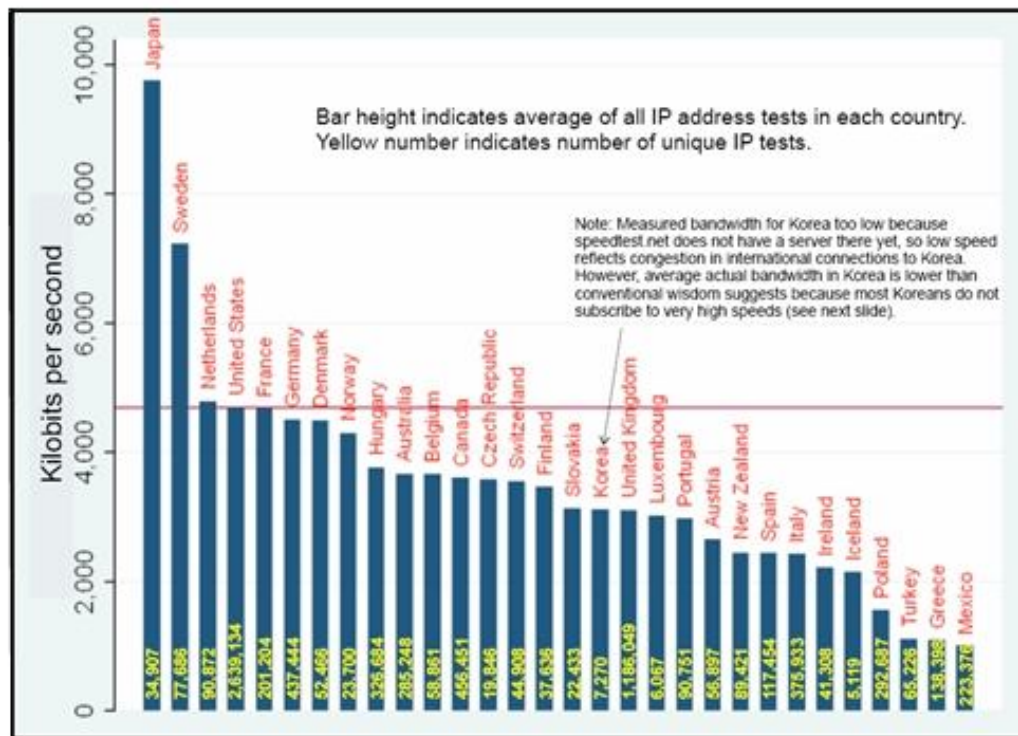
⁶ <http://investor.verizon.com/financial/quarterly/vz/2Q2007/2Q07Bulletin.pdf>

⁷ See, for example, <http://www.pcmag.com/article2/0,1895,2186108,00.asp> or <http://www.believwireless.com/>.

movies every day or engage in bandwidth-intensive online gaming. Many people and small businesses are simply unwilling to pay more for higher speeds. That's why not everybody signs up for the fastest speed they can get.

Those who believe the U.S. has a broadband problem claim that broadband speeds in the U.S. are much slower than elsewhere. These claims are simply wrong. They are based on comparisons of advertised, not actual, speeds. According to speedtest.net, which has data from nearly 200 million unique speed tests of actual broadband connections around the world, the average U.S. speed ranks about third or fourth globally (Figure 1).

Figure 1
Average Actual Broadband Connection Speeds Across Countries



Source: Speedtest.net. Average of tests from August 2006 - June 2007.

In short, the evidence contradicts the argument that there is too little investment in broadband infrastructure or that most consumers or small businesses are desperate for more.

The important question is whether market failures or other obstacles hinder broadband investment, competition, and adoption by consumers and businesses. Because investment dollars are scarce and because policies have costs as well as benefits, we should analyze policies carefully and rigorously to ensure that their expected benefits exceed their expected costs. Unfortunately, few proposals are accompanied by serious analysis. For example, many who believe the U.S. has a broadband problem argue that France and Japan are doing well because they require their biggest telecom companies to open their infrastructure to competing broadband providers. This regulation is known as unbundling, which is sort of like making Starbucks lease space and equipment to any freelance barista.

The truth is more subtle.

France does not apply unbundling regulations to fiber optic lines. And in Japan, the regulated price for a firm to use the fiber is so high that essentially no company takes advantage of the regulation. Instead, the incumbent telephone company and the electric power utilities are building and operating fiber networks themselves. In other words, unbundling proponents point to Japan and France as models to emulate, but those countries have, for all practical purposes, not applied unbundling to the very type of infrastructure those proponents want to see here.

As another example, some might argue that expanding the Universal Service Fund to include broadband services might benefit small businesses. But expanding the fund is more likely to harm small businesses since they, like all other consumers, pay for universal service expenditures through taxes on their own telecommunications services. That's why the National Federation of Independent Businesses argues strongly against increasing the fund.⁸

I do not, however, intend to imply that the market is perfect. We know that the overall positive picture of broadband in the U.S. can mask underserved geographic areas and socioeconomic groups. Data collection efforts should be targeted at identifying potential problems and at gathering the information necessary to evaluate whether proposed policies are likely to address them effectively. That's why models like ConnectKY appear to be successful—they carefully identify areas where there might be a problem and help tailor specific solutions.

In addition, certain regulations continue to make it more expensive than necessary for new companies to enter the market. For example, there's no economic justification for requiring a special license to offer cable television services over broadband lines.

And despite strong investment in wireless networks, hundreds of megahertz of spectrum remain unused or are used inefficiently by the private sector and by the government. Every day that spectrum remains unavailable for high-value uses represents a tremendous opportunity cost—a significant loss to our economy.

⁸ <http://www.nfib.com/page/technology.html>

To conclude, let me reiterate that the key to good broadband policy is careful analysis that attempts to identify market failures or artificial barriers suppressing broadband investment and adoption, followed by rigorous evaluation of whether proposed interventions are likely to yield net benefits.

And precisely because the Internet is so important, Congress should be cautious and consider carefully interventions in this fast-changing industry to ensure that they do not unintentionally reduce incentives to invest in the very infrastructure we all believe is so important.

Thank you.