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# I THINK WE SHOULD SEE OTHER PEOPLE: THE BENEFITS OF ELIMINATING HANDSET EXCLUSIVITY AND INSTITUTING TIERED PRICING IN THE MOBILE BROADBAND MARKET

## INTRODUCTION

In 1973, the first portable handset cell phone was introduced at a press conference in New York City.<sup>1</sup> Since that time, cell phones have evolved almost unimaginably. First, there was the flip phone, then slim phones, and then features such as email and mobile broadband access were introduced.<sup>2</sup> Between 2005 and 2008, the number of mobile wireless data plan subscribers exploded from zero to over 14.5 million.<sup>3</sup> The continued evolution of cell phones has led to handset exclusivity.<sup>4</sup> Handset exclusivity results when a contract between a handset manufacturer and a wireless carrier explicitly requires that a new handset is exclusively compatible with a specific carrier.<sup>5</sup> This type of agreement is most famously illustrated by the iPhone, which, until February 2011,<sup>6</sup> had been compatible only with AT&T's wireless network.<sup>7</sup>

The two main governing bodies overseeing the mobile broadband market are the Federal Communications Commission (FCC) and the Federal Trade Commission (FTC). The FCC regulates mobile broadband relating to handset exclusivity and net neutrality through two key regulatory decisions made by the FCC. The first is the *Cellular CPE Bundling Order*, issued in 1992, in which the FCC repealed an earlier decision requiring wireless carriers, like traditional landline carriers, to sell their services unbundled from the hardware used to connect to the network.<sup>8</sup> As a result, wireless carriers who were originally prevented from selling handsets

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1. Robert Hahn & Hal J. Singer, *Why the iPhone Won't Last Forever and What the Government Should Do to Promote its Successor*, 8 J. TELECOMM. & HIGH TECH. L. 313, 317 (2010).

2. *Id.* at 317–23.

3. Christopher S. Yoo, *Free Speech and the Myth of the Internet as an Unintermediated Experience*, 78 GEO. WASH. L. REV. 697, 748 (2010).

4. See Hahn & Singer, *supra* note 1, at 317.

5. Handset Exclusivity, PUB. KNOWLEDGE, <http://www.publicknowledge.org/issues/handset-exclusivity> (last visited Jan. 15, 2012).

6. Press Release, Apple Inc., Verizon Wireless & Apple Team Up to Deliver iPhone 4 on Verizon (Jan. 11, 2011), <http://www.apple.com/pr/library/2011/01/11Verizon-Wireless-Apple-Team-Up-to-Deliver-iPhone-4-on-Verizon.html>.

7. See Hahn & Singer, *supra* note 1, at 324.

8. See Use of the Carterfone Device in Message Toll Telephone Service, 13 F.C.C. 2d 420, 423 (1968) [hereinafter Use of the Carterfone Device]; Bundling of Cellular Customer Premises Equip. & Cellular Serv., 7 FCC Rcd. 4028 (1992) (report & order) [hereinafter CPE Bundling Order].

exclusively tied to their networks were given the freedom to do so.<sup>9</sup> The second is the decision by the FCC to classify mobile broadband as an information service.<sup>10</sup> This decision, in light of recent events, has limited the FCC's ability to regulate mobile broadband.<sup>11</sup> Yet, when one door closes, another opens. Due to the FCC's decision to classify mobile broadband as an information service, the FTC, which does not have regulatory power over common carriers, but possesses the power to regulate information services, gained the ability to exert regulatory control over mobile broadband.<sup>12</sup>

Agreements between wireless providers and handset manufacturers resulting in handset exclusivity have a significant impact on net neutrality. Simply defined, net neutrality is the concept that internet users should have unrestricted access to legal content, and Internet Service Providers (ISPs) should not be able to impede the dissemination of such information.<sup>13</sup> The idea of maintaining an open and unrestricted internet is based on the philosophy that the information traveling through a network should remain completely independent from the provider of the network and not influence the flow of information on an ISP's network.<sup>14</sup>

Proponents of net neutrality fear that if left unrestricted, ISPs would be free to block or slow the delivery of content for reasons such as corporate partnerships or direct competition with the provider itself.<sup>15</sup> This fear is not unfounded. In the past, the FCC has had to take action in cases where broadband providers were blocking content from passing through their networks.<sup>16</sup> In 2005, Madison River Communications paid \$15,000 and agreed to abstain from blocking subscribers' use of the internet telephone service Vonage.<sup>17</sup> Professor Edward Felton explains that the internet has been successful because of "its openness to new services. Google and

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9. See generally CPE Bundling Order, *supra* note 8 ("Despite our concerns about the status of competition in the cellular service market, the records supports [sic] the conclusion that clarifying the current bundling policy to allow facilities-based carriers to bundle cellular CPE and service would not have an adverse impact on the cellular CPE market.").

10. See Appropriate Regulatory Treatment for Broadband Access to the Internet over Wireless Networks, 22 FCC Rcd. 5901 (2007) (declaratory ruling) [hereinafter Appropriate Regulatory Treatment].

11. See *Comcast Corp. v. FCC*, 600 F.3d 642 (D.C. Cir. 2010).

12. See FTC, STAFF REPORT, BROADBAND CONNECTIVITY COMPETITION POLICY 38 (June 2007) [hereinafter BROADBAND CONNECTIVITY COMPETITION POLICY].

13. Claire Cain Miller & Brian Stelter, *Web Plan is Dividing Companies*, N.Y. TIMES, Aug. 12, 2010, at B.1.

14. *Internet Freedom and Innovation at Risk: Why Congress Must Restore Strong Net Neutrality Protection*, ACLU (Sept. 22, 2006), <http://www.aclu.org/free-speech/internet-freedom-and-innovation-risk-why-congress-must-restore-strong-net-neutrality-pro> [hereinafter *Internet Freedom and Innovation at Risk*].

15. See *id.*

16. See *Comcast*, 600 F.3d at 644; *Madison River Commc'ns, LLC*, 20 FCC Rcd. 4295, 4297 (2005) (consent decree).

17. *Madison River Commc'ns, LLC*, 20 FCC Rcd. at 4297.

Facebook were started by students; eBay was started by a guy in his apartment. These innovators didn't need to beg or buy permission from anyone. . . . [T]heir traffic got the same treatment as everyone else's."<sup>18</sup> If the "open" internet was to be transformed into one governed, not by users, but by service providers, net neutrality proponents argue that the incentive to innovate that existed at the infancy of some of the most popular and influential websites today would be extinguished.<sup>19</sup> Without the guarantee that their inventions would be compatible with all internet connections, the creators of Facebook, Google, and eBay may have seen the time commitment and financial risk involved in developing their new technology stacked too heavily against them.<sup>20</sup> Albert Wenger, a partner at Union Square Ventures, points out that "it is easy to lose sight of the most basic principle that net neutrality is trying to achieve: the ability for innovative start-ups to deliver their content and services on a level playing field with incumbents."<sup>21</sup> In addition to concern about how content flows through broadband networks, net neutrality proponents are equally concerned with how a customer is able to access the content. The ability for a consumer to attach any device to any network is a basic tenet of net neutrality.<sup>22</sup>

New policies, such as tiered pricing for wireless broadband access, although viewed negatively by some net neutrality proponents, provide incentives for wireless broadband providers to expand network capabilities.<sup>23</sup> Additionally, these pricing schemes would alleviate overstressed networks<sup>24</sup> and offer greater customer clarity regarding the services received, coupled with valuable pricing options. Handset exclusivity, however, greatly reduces customer freedom since customers are locked in to a specific provider. This lockup causes concern over content discrimination due to vertical and horizontal integration and the financial impracticability of switching carriers and purchasing a compatible handset.

This note will discuss both handset exclusivity and tiered pricing as they apply to net neutrality. The elimination of handset exclusivity, coupled with the implementation of tiered pricing for mobile broadband data, strikes

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18. Edward W. Felton, *'Neutrality' Is Hard to Define*, N.Y. TIMES, Aug. 10, 2010, <http://www.nytimes.com/roomfordebate/2010/8/9/who-gets-priority-on-the-web/net-neutrality-is-hard-to-define>.

19. *Neutrality Encourages Innovation*, OPPOSING VIEWS, <http://www.opposingviews.com/arguments/neutrality-encourages-innovation> (last visited Mar. 14, 2012).

20. *Id.*

21. Nick Bilton, *More on the Net Neutrality Debate*, BITS N.Y. TIMES (Aug. 12, 2010, 1:19 PM), <http://bits.blogs.nytimes.com/2010/08/12/inside-the-net-neutrality-debate/> (quoting Albert Wenger) (omission in original).

22. *Internet Freedom and Innovation at Risk*, *supra* note 14.

23. Editorial, *The Internet's Future*, WASH. POST, June 12, 2006, <http://www.washingtonpost.com/wp-dyn/content/article/2006/06/11/AR2006061100707.html>.

24. Morgan Stanley, *The Mobile Internet Report Key Themes* 405 (Dec. 15, 2009), available at [http://www.morganstanley.com/institutional/techresearch/mobile\\_internet\\_report122009.html](http://www.morganstanley.com/institutional/techresearch/mobile_internet_report122009.html) [hereinafter *Key Themes*].

a fair balance between net neutrality concerns and the need for effective network management tools, leading to a realistic idea of net neutrality as the market stands today. Part I of this note will outline a definition of net neutrality and provide an introduction to the arguments both for and against net neutrality. Part II provides an in-depth look at both past and present federal regulation of broadband services. Part III discusses handset exclusivity and the effects of the FCC's decision to allow carriers to bundle services with hardware, along with the effects that vertical and horizontal integration have on net neutrality. Part IV provides insight into tiered pricing, the FTC's ability to regulate deceptive practices, and tiered pricing's ability to properly manage stressed mobile broadband networks. Finally, Part V examines why the elimination of handset exclusivity and the implementation of tiered pricing strikes the best balance between net neutrality and carriers' needs for the customer.

## I. NET NEUTRALITY

In 2005, the FCC released a statement on net neutrality, which set forth four principles to maintain an open internet.<sup>25</sup> In its report, the FCC stated:

[T]o ensure that broadband networks are widely deployed, open, affordable, and accessible to all consumers, the Commission adopts the following principles:

- . . . consumers are entitled to access the lawful Internet content of their choice.
- . . . consumers are entitled to run applications and use services of their choice, subject to the needs of law enforcement.
- . . . consumers are entitled to connect their choice of legal devices that do not harm the network.
- . . . consumers are entitled to competition among network providers, application and service providers, and content providers.<sup>26</sup>

Consequently, this line of thinking is in direct opposition with that of handset exclusivity.

Opponents of net neutrality argue that tiered pricing would increase broadband infrastructure.<sup>27</sup> An experiment conducted in England

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25. See FCC, 05-151 POLICY STATEMENT ON NET NEUTRALITY 3 (2005), available at [http://hraunfoss.fcc.gov/edocs\\_public/attachmatch/FCC-05-151A1.pdf](http://hraunfoss.fcc.gov/edocs_public/attachmatch/FCC-05-151A1.pdf) [hereinafter POLICY STATEMENT ON NET NEUTRALITY].

26. *Id.* at 3 (footnotes omitted).

27. SARA PHILPOTT, IBM, EVOLVING MOBILE BROADBAND BUSINESS MODELS 7 (Mar. 2011), available at <http://ibmtelconewsletter.files.wordpress.com/2011/03/broadband-paper-march-2011.pdf>.

highlighted the need for more robust broadband networks.<sup>28</sup> Three hundred gigabytes of data were divided and loaded onto USB drives that were then attached to a group of carrier pigeons.<sup>29</sup> The pigeons were then directed to a site 120 miles away.<sup>30</sup> At the same time, the 300-gigabyte video file carried by the birds was sent to the same location via the internet.<sup>31</sup> The results were noteworthy. “One hour and fifteen minutes later, all ten carrier pigeons had successfully delivered their USB drives. Only 25% of the video had . . . been successfully downloaded.”<sup>32</sup> This experiment illustrates the need for the expansion of broadband network infrastructure. Consequently, net neutrality opponents contend that allowing service providers to alter their pricing structures would incentivize the construction of more robust networks.<sup>33</sup> Additionally, opponents of net neutrality argue that the broadband market is competitive enough, making governmental regulation unnecessary.<sup>34</sup> As Professor David Gelernter explains, “Maybe a company should be allowed to do what it likes on its own . . . . If Verizon users don’t like Verizon’s service, they’ll switch to a different I.S.P. [That] is called ‘competition.’”<sup>35</sup> Although both proponents and opponents of net neutrality have drawn clear battle lines, both sides can agree that the issue surrounding mobile broadband will ultimately be decided by the federal government, either through administrative or congressional action.

## II. FEDERAL REGULATION OF BROADBAND SERVICE

Under Title II of the Communications Act of 1934, common carriers are subject to strict regulations by the FCC.<sup>36</sup> In 2002, however, the FCC issued a declaratory ruling finding that “cable modem service is a single, integrated service that enables the subscriber to utilize Internet access service through a cable provider’s facilities.”<sup>37</sup> Therefore, “[c]able modem service is not itself and does not include an offering of telecommunications

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28. Renee Oricchio, *Where Carrier Pigeons Are Faster Than the Internet*, INC. (Sept. 23, 2010), available at [http://www.inc.com/tech-blog/where-carrier-pigeons-are-faster-than-the-internet.html?utm\\_source=feedburner&utm\\_medium=feed&utm\\_campaign=Feed%3A+inc%2Ftheadlines+%28Inc.com+Headlines%29](http://www.inc.com/tech-blog/where-carrier-pigeons-are-faster-than-the-internet.html?utm_source=feedburner&utm_medium=feed&utm_campaign=Feed%3A+inc%2Ftheadlines+%28Inc.com+Headlines%29).

29. *Id.*

30. *Id.*

31. *Id.*

32. *Id.*

33. See *The Internet’s Future*, supra note 23.

34. Robert A. Penchuk, *Unleashing the Open Mobile Internet*, 10 J. HIGH TECH L. 74, 83 (2009).

35. David Gelernter, *Call It ‘Net Irrationality’*, N.Y. TIMES, Aug. 10, 2010, <http://www.nytimes.com/roomfordebate/2010/08/09/who-gets-priority-on-the-web/call-it-net-irrationality-2>.

36. See Communications Act of 1934, 47 U.S.C. §§ 201–212 (2006) (affording the FCC power to regulate a common carrier’s service, charges, pricing policies, and corresponding violation penalties).

37. Inquiry Concerning High-Speed Access to the Internet over Cable and Other Facilities, 17 FCC Rcd. 4798, 4823 (Mar. 14, 2002) (declaratory ruling and notice of proposed rulemaking).

service to subscribers.”<sup>38</sup> Consequently, broadband cable modem service is “properly classified as an interstate information service” and not as a common carrier.<sup>39</sup> The Supreme Court upheld this decision.<sup>40</sup> As a result, broadband cable modem service was no longer governed by Title II and, consequently, was no longer subject to the same restrictions as common carriers.<sup>41</sup> Subsequently, in 2007, the FCC extended the moniker of “information service” to cover mobile broadband service.<sup>42</sup>

Removal of Title II restrictions leaves broadband providers subject only to the FCC’s Title I ancillary jurisdiction.<sup>43</sup> The FCC has the power to regulate ancillary jurisdiction under Title I under the following conditions: “(1) the Commission’s general jurisdictional grant under Title I [of the Communications Act] covers the regulated subject and (2) the regulations are reasonably ancillary to the Commission’s effective performance of its statutorily mandated responsibilities.”<sup>44</sup> Ancillary regulatory power under Title I is significantly weaker than the FCC’s direct regulatory power under Title II because no precise definition of “reasonably ancillary” is provided. A pro-net neutrality organization, Public Knowledge, explains, “The problem is that every time the FCC trie[s] to act in the broadband space, it would essentially be rolling the dice. Whenever the FCC trie[s] to protect consumers it would have to wait to see if a court agreed with its claim of authority before taking meaningful action.”<sup>45</sup> This concern was illustrated in *Comcast Corp. v. FCC*. In *Comcast*, subscribers of Comcast’s broadband service discovered that Comcast had been blocking some file-sharing websites.<sup>46</sup> Comcast argued that the interference of service was simply network management due to a limited amount of broadband capacity. The FCC, acting pursuant to what it believed was its Title I ancillary jurisdiction, ordered Comcast to disclose the details of its network management policy and stated that it would issue an injunction against Comcast should it not disclose its policy or continue to discriminate against the file-sharing sites.<sup>47</sup> Comcast appealed the order, and the Court of Appeals for the District of Columbia found that the FCC’s Title I ancillary jurisdiction did not apply to a broadband service provider’s network management because “the Commission . . . failed to tie its assertion of

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38. *Id.*

39. *Id.* at 4802.

40. See *Nat’l Cable & Telecomms. Ass’n v. Brand X Internet Servs.*, 545 U.S. 967, 974 (2005) (holding that cable broadband providers are exempt from mandatory common carrier regulation).

41. *Id.* at 1000.

42. Appropriate Regulatory Treatment, *supra* note 10, at 5901.

43. *Brand X*, 545 U.S. at 976.

44. *Comcast Corp. v. FCC*, 600 F.3d 642, 646 (D.C. Cir. 2010) (alteration in original) (quoting *Am. Library Ass’n v. FCC*, 406 F.3d 689, 691 (D.C. Cir. 2005)).

45. *Public Knowledge Explains: The Comcast-Bittorrent Decision*, PUBLIC KNOWLEDGE (Apr. 6, 2010, 3:48 PM) (on file with author).

46. *Comcast*, 600 F.3d at 644.

47. *Id.*

ancillary authority over Comcast's Internet service to any 'statutorily mandated responsibility.'"<sup>48</sup> Because the FCC classified wireless broadband as an information service, this decision severely inhibited the FCC's ability to regulate wireless broadband and opened the door to allow wireless broadband providers to regulate their networks as they see fit, without regulatory oversight. Thus, in response to the *Comcast* decision, the FCC has hinted that it may seek to reclassify broadband service as a telecommunication service. Doing so would bring broadband service back within the fold of Title II regulation.<sup>49</sup>

In the meantime, however, the FTC has shown renewed interest in net neutrality.<sup>50</sup> Pursuant to the Federal Trade Commission Act (the FTC Act), the FTC has the authority "to prevent persons, partnerships, or corporations . . . from using unfair methods of competition in or affecting commerce and unfair or deceptive acts or practices in or affecting commerce."<sup>51</sup> Under the FTC Act, the FTC does not have the power to regulate common carriers; however, since broadband services are not classified as common carriers, they are subject to FTC regulation.<sup>52</sup> Consequently, the FTC has investigated broadband providers regarding internet access,<sup>53</sup> access to and pricing of content, and deceptive marketing and billing practices.<sup>54</sup> The FTC describes its jurisdiction over broadband as follows:

[First,] the FTC has both authority and experience in the enforcement of competition and consumer protection law provisions pertinent to broadband Internet access. Second, the FTC Act provisions regarding "[u]nfair methods of competition in or affecting commerce, and unfair or deceptive acts or practices in or affecting commerce," are general and flexible in nature, as demonstrated by judicial and administrative decisions across diverse markets. Third, the FTC's investigative and enforcement actions have been party- and market-specific; that is, neither the general body of antitrust and consumer protection law nor the FTC's enforcement and policy record determines any particular broadband connectivity policy or commits the Commission to favoring any particular model of broadband deployment.<sup>55</sup>

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48. *Id.* at 661 (citation omitted).

49. Austin Schlick, General Counsel, FCC, Statement Outlining the FCC's New Approach to Internet Oversight (May 6, 2010), available at [http://news.cnet.com/8301-1023\\_3-20004324-93.html?tag=mncol;txt](http://news.cnet.com/8301-1023_3-20004324-93.html?tag=mncol;txt).

50. Aruna Viswanatha, *Could the FTC Regulate Net Neutrality?*, MAIN JUSTICE (Apr. 12, 2010, 5:45 PM), <http://www.mainjustice.com/2010/04/12/could-the-ftc-regulate-net-neutrality/>.

51. 15 U.S.C. § 45(a)(2) (2006).

52. BROADBAND CONNECTIVITY COMPETITION POLICY, *supra* note 12, at 38.

53. See Complaint, *In re Am. Online, Inc. & Time Warner Inc.*, No. C-3989 (FTC. Dec. 14, 2000), available at <http://www.ftc.gov/os/2000/12/aolcomplaint.pdf>.

54. BROADBAND CONNECTIVITY COMPETITION POLICY, *supra* note 12, at 39.

55. *Id.* at 41 (alteration in original) (footnote omitted).



As a result, “the FTC could require a broadband provider to disclose how it manages its network and what speeds it offers.”<sup>56</sup> Nonetheless, some are skeptical of the FTC’s ability to actually prosecute such a case. “[T]he kinds of practices that often come up under the guise of net neutrality would rarely be a violation of the antitrust laws. . . . [I]n order to achieve the broad objectives of people advocating net neutrality, you have to have congressional action or reclassification.”<sup>57</sup>

On December 21, 2010, the FCC passed new net neutrality regulations.<sup>58</sup> The new rules “create two classes of Internet access, one for fixed-line providers and the other for the wireless Net.”<sup>59</sup> As a result, landline providers are prevented from blocking or unreasonably discriminating against content; however, due to heavy lobbying by Google and Verizon, wireless internet providers are not completely restricted from doing so.<sup>60</sup> Therefore, in light of the *Comcast* decision and the questions surrounding the FTC’s ability to effectively regulate broadband, absent congressional intervention, it is unclear how the federal government could properly address wireless net neutrality concerns. Therefore, the issues of handset exclusivity and tiered pricing remain a significant concern in the discussion of mobile broadband neutrality.

### III. HANDSET EXCLUSIVITY

The FCC has stated that “consumers are entitled to connect their choice of legal devices that do not harm the network.”<sup>61</sup> When cell phones first entered the market, exclusivity deals between handset manufactures and wireless carriers were unheard of. Since 2004, however, almost every popular phone to enter the market has been subject to exclusivity.<sup>62</sup> Initially, the Razer V3, Sidekick, iPhone, Blackberry Pearl, and Blackberry Curve were only compatible with a single wireless carrier.<sup>63</sup>

There are essentially two ways in which carriers in the United States achieve handset exclusivity.<sup>64</sup> First, Code Division Multiple Access

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56. Viswanatha, *supra* note 50.

57. *Id.* (quoting Donald Russell).

58. *Net Neutrality*, NYTIMES.COM (Dec. 22, 2010), [http://topics.nytimes.com/topics/reference/timestopics/subjects/n/net\\_neutrality/index.html](http://topics.nytimes.com/topics/reference/timestopics/subjects/n/net_neutrality/index.html).

59. *Id.*

60. *Id.*

61. POLICY STATEMENT ON NET NEUTRALITY, *supra* note 25, at 3 (footnote omitted).

62. Hahn & Singer, *supra* note 1, at 318.

63. *Id.* at 319; Parul Sharma, *Motorola DRIOD X in July and Motorola DROID 2 in August...Get Ready to Grab*, ABH NEWS (June 13, 2010), <http://abh-news.com/motorola-driod-x-in-july-and-motorola-droid-2-in-august-get-ready-to-grab-3245.html>.

64. Tim Wu, *Wireless Net Neutrality: Cellular Carterfone and Consumer Choice in Mobile Broadband 8* (New Am. Found., Working Paper No. 17, 2007), available at [http://www.newamerica.net/publications/policy/wireless\\_net\\_neutrality](http://www.newamerica.net/publications/policy/wireless_net_neutrality).

(CDMA) carriers,<sup>65</sup> like Verizon,<sup>66</sup> designate phones with an ID number, which allows the phone to access the network.<sup>67</sup> “Without an approved ID number, telephones not sold by Verizon will not be recognized and cannot be used on the network. This effectively makes Verizon Wireless the gatekeeper of market entry for telephones on their network . . . .”<sup>68</sup> Second, Global System for Mobile Communications (GSM) carriers,<sup>69</sup> like AT&T,<sup>70</sup> make use of phones with SIM cards.<sup>71</sup> The SIM card was designed to make switching from one network to another as simple as removing the phone’s original SIM card and replacing it with a new one.<sup>72</sup> Yet, “[t]he mobile device itself . . . can be designed to recognize and reject certain types of SIM cards based on information carried on the SIM, creating a ‘lock.’”<sup>73</sup> Thus, a customer who purchases a handset subject to exclusivity cannot access any other network aside from his or her carrier’s network. Accordingly, if an AT&T customer—who owns a phone subject to exclusivity with AT&T—wants to switch to Verizon, that customer is forced to purchase a new handset compatible with the Verizon network.<sup>74</sup>

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65. “CDMA stands for Code Division Multiple Access. It is a technique used for digital communication, and wireless technology in particular, that involves multiplexing. Whereas conventional communication systems use constant frequencies, CDMA uses multiple access, or multiplexing.” S. Roberts, *What is CDMA?*, WISEGEEK, <http://www.wisegeek.com/what-is-cdma.htm> (last visited Apr. 4, 2012).

66. R. Kayne, *What is the Difference Between GSM and CDMA?*, WISEGEEK, <http://www.wisegeek.com/what-is-the-difference-between-gsm-and-cdma.htm> (last modified Feb. 23, 2012).

67. Wu, *supra* note 64, at 8.

68. *Id.*

69. Ken Black, *What is GSM?*, WISEGEEK, <http://www.wisegeek.com/what-is-gsm.htm> (last visited Mar. 14, 2012).

GSM, or Global System for Mobile Communications, is a cellular phone protocol that is popular in many parts of the world . . . .

. . . .

One of the distinctive features of the GSM system is the use of SIM cards. This card will store all personal data and contacts on it. Once a phone is traded for a new one, transferring the data and activating the phone becomes simply a matter of changing the card.

*Id.*

70. *Our Mobile Broadband and GSM Technology*, AT&T, <http://www.wireless.att.com/learn/why/technology/mobile-broadband-and-GSM.jsp> (last visited Dec. 22, 2010).

71. Black, *supra* note 69.

72. Wu, *supra* note 64, at 9.

73. *Id.*

74. Interestingly, beginning April 8, 2012, AT&T

will offer qualifying customers the ability to unlock their AT&T iPhones. The only requirements are that a customer’s account must be in good standing, their device cannot be associated with a current and active term commitment on an AT&T customer account, and they need to have fulfilled their contract term, upgraded under one of our upgrade policies or paid an early termination fee.

This concept is directly at odds with the idea that consumers should be free to access content using equipment of their choosing.<sup>75</sup>

In response to handset exclusivity and concerns about the relationship between handset manufacturers and carriers, Skype, an internet company, formally requested that the FCC apply the principles set forth in the Commission's *Carterfone* decision to the wireless industry.<sup>76</sup> Skype's concern was that "[i]n an effort to prefer their own affiliated services and exclude rivals, carriers have disabled or crippled consumer-friendly features of mobile devices."<sup>77</sup> Skype argued that applying *Carterfone* "[would] ensure both that consumers retain a right to run the applications of their choosing and [the] right to attach all non-harmful devices to the wireless network."<sup>78</sup>

In *Carterfone*, AT&T penalized customers for attaching a device, known as the Carterfone, to their network.<sup>79</sup> The penalty was based on an FCC rule which stated that "no equipment, apparatus, circuit or device not furnished by the telephone company shall be attached to or connected with the facilities furnished by the telephone company, whether physically, by induction or otherwise."<sup>80</sup> The FCC found that the Carterfone had no adverse effect on the network and that AT&T's continued prohibition on third-party equipment "would be unreasonable and unduly discriminatory."<sup>81</sup> As a result, "the provisions prohibiting the use of customer-provided interconnecting devices should accordingly be stricken."<sup>82</sup> Initially, like wireline telecommunication services, the FCC required mobile equipment to be available for purchase unbundled from wireless service.<sup>83</sup> In 1992, the FCC repealed that decision in the *Cellular CPE Bundling Order*.<sup>84</sup> As a result, Skype requested that the FCC apply the standard in *Carterfone* to wireless carriers. Central to its decision to allow

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Andrew Munchbach, *AT&T to Begin Unlocking Off-Contract iPhones This Sunday, April 8th*, ENDGAGET (Apr. 6, 2012, 1:23 PM), <http://www.engadget.com/2012/04/06/atandt-to-begin-unlocking-iphone-sunday-april-8/>. iPhones still under contract will continue to be subject to exclusivity. *Id.*

75. *Internet Freedom and Innovation at Risk*, *supra* note 14.

76. Petition to Confirm a Consumer's Right to Use Internet Commc'ns Software & Attach Devices to Wireless Networks, 22 FCC Rcd. 5042 (2007) (order).

77. Petition to Confirm a Consumer's Right to Use Internet Commc'ns Software and Attach Devices to Wireless Networks 2, *In re* Skype Commc'ns S.A.R.L. (RM-11361), (FCC Feb. 20, 2007), available at [http://files.ctia.org/pdf/Skype\\_Wireless\\_Device\\_Petition\\_2-20-07.pdf](http://files.ctia.org/pdf/Skype_Wireless_Device_Petition_2-20-07.pdf).

78. *Id.* at 2.

79. Use of the Carterfone Device, *supra* note 8, at 421.

80. *Id.*

81. *Id.* at 424.

82. *Id.*

83. Everett M. Ehrlich, Jeffrey A. Eisenach & Wayne A. Leighton, *The Impact of Regulation on Innovation and Choice in Wireless Communication*, 9, 1 REVIEW OF NETWORK ECONOMICS, 23 (2009), available at <http://www.degruyter.com/view/j/rne.2010.9.1/rne.2010.9.1.1194/rne.2010.9.1.1194.xml>.

84. *Id.* at 25.

handset and service bundling was the existence of sufficient competition within the wireless service market and the finding that “carriers did not possess market power in the upstream market for handsets.”<sup>85</sup> The FCC stated that “modifying the bundling policy is in the public interest because the public interest benefits of bundling in the cellular market outweigh the potential for competitive harm.”<sup>86</sup> In coming to this decision, the FCC highlighted that “the records supports [sic] the conclusion that clarifying the current bundling policy to allow facilities-based carriers to bundle cellular CPE and service would not have an adverse impact on the cellular CPE market.”<sup>87</sup> Proponents of applying the *Carterfone* standard to wireless carriers argue that “[y]ou just can’t sell in [the wireless] market like you do in others. The carriers have ultimate control over what products reach the market. If they don’t like what you’re doing, that’s too bad.”<sup>88</sup>

Since the FCC’s decision to allow bundling was so closely tied to competition within the market, some believe that in order for the FCC’s position to change regarding handset exclusivity, the FCC would need to be presented with evidence of consumer harm due to a lack of competition.<sup>89</sup> This theory is evidenced by an FCC decision involving the Public Utilities Commission of Hawaii.<sup>90</sup> In the petition, Hawaii asked the FCC for permission “to retain state regulatory authority over the rates for intrastate commercial mobile radio services.”<sup>91</sup> In response, the FCC stated “that a petition must be based on demonstrable evidence of anticompetitive activity, or unjust and unreasonable, or unreasonably discriminatory, rates.”<sup>92</sup> According to the FCC, “specific allegations of fact” are required to establish “anticompetitive or discriminatory practices or behavior by commercial mobile radio service providers.”<sup>93</sup> Implementation of the *Carterfone* principles on the wireless broadband market would clearly be a decision made by the FCC and not by an individual state, but the FCC’s position in *Petition on Behalf of the State of Hawaii* shows a strong aversion to creating new regulation in the mobile communications market without clear evidence of anticompetitive behavior.

In terms of handset exclusivity, the anticompetitive behavior the FCC covets in order to impose regulation may be found in two places. The first is

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85. *Id.* at 24.

86. CPE Bundling Order, *supra* note 8, at 2 (citation omitted).

87. *Id.* at 9.

88. Wu, *supra* note 64, at 7 (quoting anonymous source).

89. Saul Hansell, *F.C.C. Weighs Need for New Cellphone Handset Rules*, N.Y. TIMES, Aug. 10, 2009, at B.2.

90. See *Petition on Behalf of the State of Hawaii, Public Utility Commission, for Authority to Extend Its Rate Regulation of Commercial Mobile Radio Services in the State of Hawaii*, 10 FCC Rcd. 7872 (1995) (report and order).

91. *Id.* at 7872.

92. *Id.* at 7876.

93. *Id.*

in the context of rural wireless carriers,<sup>94</sup> and the second is in relation to vertical and horizontal integration. Phones subject to exclusivity cannot access networks other than the network their contract provides. As a result, rural, small, and even midsize carriers are unable to provide the same phones to their customers as those provided by major carriers. As the Rural Cellular Association points out, “If the nation’s small and mid-size wireless carriers are unable to get access to handsets that consumers have an interest in purchasing, the ability of these carriers to effectively compete with the nation’s largest carriers is significantly harmed.”<sup>95</sup> Additionally, “customers served by smaller carriers and new entrants are prevented from accessing the most popular handsets and benefiting from the advances in wireless handset technology until years after their urban counterparts.”<sup>96</sup> In conjunction with the Rural Cellular Association, the Public Interest Spectrum Coalition states, “Without handset exclusivity arrangements, the consumer could choose service provider and device independently. Instead, rural and small wireless carriers face substantial obstacles to gaining new customers by being unable to offer their customers desirable smartphones . . .”<sup>97</sup>

Although the FCC did not see any harm to consumers by allowing bundling, it is hard to imagine that the FCC could have envisioned harm to consumers, in the form of net neutrality concerns in regards to mobile communication, when the *CPE* decision was made in 1992. Professor Robert Frieden, an opponent of handset exclusivity, explains that “[w]e take for granted the right to own and attach telephones to the wired network. That freedom should extend to wireless networks . . . .”<sup>98</sup> Proponents, however, contend that exclusivity fosters innovation in part because both the handset provider and carrier shoulder the risk of launching the new product.<sup>99</sup> This is done partly by the wireless carrier subsidizing the cost of

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94. See Petition for Rulemaking Regarding Exclusivity Arrangements Between Commercial Wireless Carriers and Handset Manufacturers (2009) (RM No. 11497) (comments of RTG, OPASTCO, and NTCA), available at [http://www.ntca.org/index.php?option=com\\_content&view=article&id=2599:020209-joint-comments-re-exclusivity-arrangements-rm-11497&catid=379:2009-federal-filings-&Itemid=1161](http://www.ntca.org/index.php?option=com_content&view=article&id=2599:020209-joint-comments-re-exclusivity-arrangements-rm-11497&catid=379:2009-federal-filings-&Itemid=1161).

95. Petition for Rulemaking Regarding Exclusivity Arrangements Between Commercial Wireless Carriers and Handset Manufacturers at 19, *In re Rural Cellular Ass’n* (FCC Feb. 2, 2009) (RM No. 11497) (summary of reply comments), available at <http://www.rca-usa.org/associations/6491/files/exclusive-handset-reply-comment-summary.pdf>.

96. *Id.*

97. Petition for Rulemaking Regarding Exclusivity Arrangements Between Commercial Wireless Carriers and Handset Manufacturers 3, *In re Rural Cellular Ass’n* (FCC Feb. 2, 2009) (RM-11497) (comments of the *Ad Hoc* Public Interest Spectrum Coalition), available at <http://www.publicknowledge.org/node/1973#ftr14>.

98. Nancy Gohring, *Senators Challenge AT&T’s Exclusive iPhone Deal*, MACWORLD (June 18, 2009, 3:27 PM), [http://www.macworld.com/article/141238/2009/06/iphone\\_congress.html](http://www.macworld.com/article/141238/2009/06/iphone_congress.html) (quoting Robert Frieden).

99. See Hahn & Singer, *supra* note 1, at 340.

the new phone, thereby making the retail price accessible to customers.<sup>100</sup> Although handset exclusivity may promote innovation, this overlooks the net neutrality concerns of content discrimination and the financial impracticability of switching from one carrier to another created by these exclusive deals. This, in turn, harms the consumer.

In the context of the net neutrality debate, handset exclusivity, as it relates to vertical and horizontal integration, is of great concern. Vertical integration is defined as “the merging together of two businesses that are at different stages of production.”<sup>101</sup> A clear example of vertical integration can be seen in the merger between NBC Universal and Comcast.<sup>102</sup> Comcast is a distributor of content through its cable and internet services.<sup>103</sup> Through the merger, Comcast gained control of NBC Universal, a producer of content through its ownership of local NBC stations, MSNBC, and Bravo.<sup>104</sup> Therefore, Comcast is now not only a distributor of content, but also a major producer of content. As a result, the concern is that Comcast will discriminate against other content producers, limiting what is available to the consumer.<sup>105</sup> In a 2007 staff report on broadband competition, the FTC found that “[i]n particular, proponents [of net neutrality] are concerned that providers may block or discriminate against unaffiliated content and applications, to the benefit of affiliated offerings.”<sup>106</sup> This scenario could manifest itself when a broadband provider with significant market power in a given market has an interest in content or applications, creating an incentive to block or degrade competing content or applications.<sup>107</sup> In 2005, the internet phone company Vonage filed a complaint with the FCC, stating that Madison River Communications, a phone and internet provider, was intentionally blocking internet users from accessing Vonage over the Madison River network.<sup>108</sup> “For Madison River Communications, the interest in protecting current voice-based revenues made the case for

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100. *Id.*

101. *Vertical Integration*, THE ECONOMIST, Mar. 30, 2009, <http://www.economist.com/node/13396061>.

102. Brian Stelter & Tim Arango, *Comcast Receives Approval for NBC Universal Merger*, N.Y. TIMES, Jan. 19, 2011, at B.9, available at <http://www.nytimes.com/2011/01/19/business/media/19comcast.html>.

103. Cecilia Kang, *Franken Presses Holder On Comcast-NBC Merger*, POST TECH WASH. POST (Apr. 15, 2010, 10:14 AM), [http://voices.washingtonpost.com/posttech/2010/04/senator\\_franken\\_presses\\_us\\_ag.html](http://voices.washingtonpost.com/posttech/2010/04/senator_franken_presses_us_ag.html).

104. Cecilia Kang, *Planned Comcast-NBC Merger Ignites TV Access Battle*, POST BUS. WASH. POST (Dec. 4, 2009), <http://www.washingtonpost.com/wp-dyn/content/article/2009/12/03/AR2009120300947.html>.

105. Brian Stelter, *Democrats Question Comcast on NBC Deal*, N.Y. TIMES, Feb. 4, 2010, at B.2, available at <http://www.nytimes.com/2010/02/05/business/media/05comcast.html>.

106. BROADBAND CONNECTIVITY COMPETITION POLICY, *supra* note 12, at 70.

107. *Id.*

108. See Declan McCullagh, *Telco Agrees to Stop Blocking VoIP Calls*, CNET (Mar. 3, 2005, 1:08 PM), [http://news.cnet.com/Telco-agrees-to-stop-blocking-VoIP-calls/2100-7352\\_3-5598633.html?part=rss&tag=5598371&subj=news](http://news.cnet.com/Telco-agrees-to-stop-blocking-VoIP-calls/2100-7352_3-5598633.html?part=rss&tag=5598371&subj=news).

blocking [voice-over-internet protocol] services quite compelling.”<sup>109</sup> Ultimately, Madison River settled the matter by agreeing to remove the blockade and pay \$15,000 pursuant to a consent decree.<sup>110</sup>

The Madison River scenario is a significant concern in the wireless market. As of March 23, 2011, four wireless carriers showed a commanding grip on the wireless market in the United States.<sup>111</sup> Verizon possessed a 31.3 percent market share, AT&T a 26.6 percent share, Sprint a 16.1 percent share, and T-Mobile rounded out the big four with a 12.2 percent share.<sup>112</sup> With such a high level of market penetration, there is a significant incentive for any one of these carriers to show preferential treatment to affiliated content and discriminate against nonaffiliated or competitive content and services. This point was illustrated when it was reported that “Apple has declined to approve the Google Voice application for the iPhone and has removed related (and previously approved) third-party applications from the Apple App Store.”<sup>113</sup> AT&T implied it was not involved, and Apple declined to comment.<sup>114</sup> It is easy, however, to see the correlation between the Madison River case and the Google Voice matter. Like Vonage, Google Voice offers services via the internet that AT&T offers via its wireless network, including text messaging and voice services.<sup>115</sup> In a similar case, Skype, another application that allows users to make phone calls via the internet, was initially approved only for use on the iPhone while the phone was connected to the internet through a Wi-Fi connection.<sup>116</sup> This restriction prevented Skype users from using their phone as a substitute for AT&T’s wireless phone service. There is no question that restrictions like these in the mobile broadband market reduce the open internet and are contrary to the principle that “consumers are

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109. Philip J. Weiser, *The Next Frontier for Network Neutrality*, 60 ADMIN. L. REV. 273, 285 (2008).

110. Madison River Commc’ns, LLC, 20 FCC Rcd. 4295, 4297 (2005).

111. See David Goldman, *Time for Verizon to Buy Sprint?*, CNNMONEY (Mar. 23, 2011, 6:21 AM), [http://money.cnn.com/2011/03/23/technology/sprint\\_verizon/index.htm](http://money.cnn.com/2011/03/23/technology/sprint_verizon/index.htm).

112. *Id.*

113. Letter from James D. Schlichting, Acting Chief, Wireless Telecomms. Bureau, FCC, to Catherine A. Novelli, Vice President, Worldwide Gov’t Affairs, Apple, Inc. (July 31, 2009), available at <http://online.wsj.com/public/resources/documents/wsj-2009-0731-FCCApple.pdf> (footnote omitted).

114. Jason Kincaid, *FCC Takes On Apple and AT&T over Google Voice Rejection*, TECHCRUNCH (July 31, 2009), <http://techcrunch.com/2009/07/31/fcc-takes-on-apple-and-att-over-google-voice-rejection/>.

115. See Kevin Purdy, *Google Voice Is Cool, But Do You Need It?*, LIFEHACKER (July 1, 2009, 5:00 PM), <http://lifehacker.com/5304800/google-voice-is-cool-but-do-you-need-it>. Since this issue arose, Google Voice has become available in the Apple App store. ITUNES.APPLE.COM, <http://itunes.apple.com/us/app/google-voice/id318698524?mt=8> (last visited Mar. 12, 2012).

116. *Skype Launches iPhone App*, CONSUMERREPORTS.ORG (Mar. 31, 2009, 5:04 PM), <http://blogs.consumerreports.org/electronics/2009/03/skype-launches-iphone-app.html>.

entitled to run applications and use services of their choice, subject to the needs of law enforcement.”<sup>117</sup>

In contrast to vertical integration, horizontal integration is defined as the “acquisition of additional business activities that are at the same level of the value chain in similar . . . industries.”<sup>118</sup> Once again, the Comcast/NBC Universal merger provides a clear example. As Dr. Mark Cooper explained in testimony before the Senate Commerce Committee,

NBC content is available online in a variety of forms and on different websites and services. Most prominently, of course, NBC is a stakeholder in Hulu – an online video distribution portal that draws millions of viewers. Comcast has put resources into developing its own online video site – “Fancast” – where consumers can find content owned by the cable operator. The merger eliminates this nascent, head-to-head competition.<sup>119</sup>

The fear is that horizontal integration destroys competitive practices.<sup>120</sup> Professor John Blevins points out that “[s]ince 2000, the [wireless] industry has rapidly consolidated in a wave of mergers of all sizes.”<sup>121</sup> He goes on to highlight the fact that “[t]hese mergers have created a much different world than existed at the beginning of the decade . . . . [T]he top four carriers now command roughly 87% of subscribers (compared to less than half a decade earlier).”<sup>122</sup> The fear expressed concerning the destruction of competitive practices regarding the Comcast/NBC Universal merger is the same regarding the rapid consolidation of the wireless industry.<sup>123</sup> In letters to the FCC and the Department of Justice in 2009, Senator Herb Kohl stated, “I am concerned that the concentrated nature of the cell phone marketplace could lead to future price increases for this and other cell phone services relied upon by millions of Americans.”<sup>124</sup> This fear became even more prevalent when the now defunct AT&T/T-Mobile merger was proposed last

117. POLICY STATEMENT ON NET NEUTRALITY, *supra* note 25, at 3.

118. *Horizontal Integration*, INVESTOPEDIA, <http://www.investopedia.com/terms/h/horizontalintegration.asp#axzz1rNg9Ri4L> (last visited Apr. 7, 2012).

119. Mark Cooper, Dir. of Research, Consumer Fed’n of Am., Testimony before the Commerce Comm., U.S. Senate: Consumers, Competition and Consolidation in the Video Broadband Market 5 (Mar. 11, 2010), available at [http://commerce.senate.gov/public/?a=Files.Serve&File\\_id=e6645c9b-71a8-4b9a-9552-dd0dafd0ba46](http://commerce.senate.gov/public/?a=Files.Serve&File_id=e6645c9b-71a8-4b9a-9552-dd0dafd0ba46).

120. *See id.*

121. John Blevins, *Death of the Revolution: The Legal War on Competitive Broadband Technologies*, 12 YALE J.L. & TECH. 85, 92 (2009). “These mergers include: NextWave/Cingular (2004); Cingular/AT&T Wireless Services, Inc. (AT&T) (2004); Alltel/Western Wireless Corp. (2005); Nextel/Sprint (2005); AT&T/BellSouth Corp. (2007); AT&T/Dobson (2007); T-Mobile/SunCom Wireless (2008); AT&T/Aloha Partners (2008); Verizon Wireless/Rural Cellular (2008); Verizon/Alltel (2008); AT&T/Centennial (2009) (announced).” *Id.*

122. *Id.* (footnote omitted).

123. *See* Cecilia Kang, *Key Senator Backs Telecom Probe*, WASH. POST, July 7, 2009, at A.12, available at <http://www.washingtonpost.com/wp-dyn/content/article/2009/07/06/AR2009070603526.html>.

124. *Id.* (quoting Senator Herb Kohl).



year.<sup>125</sup> Horizontal integration has a direct effect on wireless broadband neutrality because as the wireless market becomes more consolidated, there is less consumer choice regarding service and a reduced incentive on the part of the carriers to offer data plans at competitive prices. If competition is eliminated, prices can be set at whatever level the carrier chooses. This issue is further compounded by handset exclusivity because fewer choices within the wireless market are available due to a customer's inability to connect their device to any of the other remaining networks. Therefore, if competition is reduced due to horizontal integration within the wireless market and a carrier decides to set data plans at monopoly prices, a customer subject to handset exclusivity would be trapped into either paying the higher price for a data plan or spending additional money to purchase a new handset with a different carrier.

During the AOL/Time Warner merger, the FTC acted on this concern of anticompetitive pricing in the wireline broadband market.<sup>126</sup> Fearing that the merger would reduce AOL's incentive to offer broadband internet at a competitive price to cable, the FTC issued an order requiring "the company, in areas where it provided cable broadband service, to offer AOL's DSL service in the same manner and at the same retail pricing as in areas where it did not provide cable broadband service."<sup>127</sup> Clearly, there is regulatory concern over horizontal mergers similar to those seen in the wireless industry in the past decade and "[t]he FTC maintains any term that is 'likely to affect [consumers'] choice of, or conduct regarding a product' is material and enforceable."<sup>128</sup> As we have seen, there is at least some evidence that horizontal integration, coupled with handset exclusivity, significantly affects a consumer's choice of product—an affect which is at odds with the FCC's statement that "consumers are entitled to competition among network providers . . . ."<sup>129</sup>

For critics of net neutrality, it is easy to argue that if wireless customers do not approve of the actions of their current carrier, they can simply switch to a different one. Yet, for a customer who has purchased an internet-capable smartphone subject to a contract of exclusivity (making his or her phone inoperable on a different wireless network), simply switching to a different carrier is financially impracticable since it would require purchasing a new smartphone that is compatible with the new network. This

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125. Michael J. De La Merced, *AT&T Ends \$39 Billion Bid for T-Mobile*, DEALBOOK N.Y. TIMES (Dec. 19, 2011, 4:44 PM), <http://dealbook.nytimes.com/2011/12/19/att-withdraws-39-bid-for-t-mobile/>.

126. Cody Vitello, *Network Neutrality Generates a Contentious Debate Among Experts: Should Consumers Be Worried?*, 22 LOY. CONSUMER L. REV. 513, 535 (2010).

127. BROADBAND CONNECTIVITY COMPETITION POLICY, *supra* note 12, at 39 (footnote omitted).

128. Vitello, *supra* note 126, at 536 (quoting Federal Trade Comm'n, Staff Report, Broadband Connectivity Competition Policy, 135 (2007)) (alteration in original) (footnote omitted).

129. POLICY STATEMENT ON NET NEUTRALITY, *supra* note 25, at 3.

sentiment was echoed in a report issued by the Government Accountability Office (GAO), which stated that “consumer groups . . . perceive . . . exclusive handset arrangements as creating . . . anticompetitive switching costs.”<sup>130</sup> Because of this, if a wireless carrier decides to exhibit preferential treatment to certain content carried via its data network, the customers could feel as though their only choices are to either remain with their current carrier, subject to the content discrimination, or be forced to purchase a new handset with a different carrier. Similarly, with regards to switching to AT&T for the iPhone, one commentator stated that with the extra cost of buying the iPhone itself, “it may make more financial sense to stay put with your existing carrier and buy a comparable device instead.”<sup>131</sup> This scenario is at odds with the notion of maintaining an open internet.

Wireline broadband providers argue that prioritizing content is essential to network management due to the high demand for limited bandwidth.<sup>132</sup> The issue of network congestion, however, is not limited to standard wireline broadband. Network congestion exists in the wireless world as well.<sup>133</sup> According to a 2009 study, when wireless networks reach 75 percent utilization, the networks encounter problems with just a slight increase in data traffic during high-usage periods.<sup>134</sup> The study goes on to point out that, at the time the data was collected, network utilization in major markets was between 80–90 percent, well over the 75 percent warning level.<sup>135</sup> Additionally, it has been estimated that “[g]lobal mobile IP traffic [is] likely to grow [sixty-six times] by 2013,”<sup>136</sup> and rising “smartphone penetration [and] emerging usage models (such as video/audio streaming) will stress carrier wireless networks.”<sup>137</sup> In line with these predictions, Verizon has stated that it predicts 70–80 percent of its customers will eventually utilize smartphones for their wireless needs.<sup>138</sup>

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130. UNITED STATES GOV'T ACCOUNTABILITY OFFICE, GAO-10-779, ENHANCED DATA COLLECTION COULD HELP FCC BETTER MONITOR COMPETITION IN THE WIRELESS INDUSTRY, 26 (2010), available at [http://www.gao.gov/docsearch/locate?searched=1&o=0&order\\_by=date&search\\_type=publications&keyword=wireless&Submit=Search](http://www.gao.gov/docsearch/locate?searched=1&o=0&order_by=date&search_type=publications&keyword=wireless&Submit=Search) [hereinafter ENHANCED DATA COLLECTION].

131. Lisa Scherzer, *Switching Carriers to Get the iPhone Can Cost You*, SMARTMONEY (July 3, 2008), <http://www.smartmoney.com/spending/deals/switching-carriers-to-get-the-iphone-can-cost-you-23405/#ixzz13sg64F38>.

132. See Formal Complaint of Free Press & Public Knowledge Against Comcast Corp. for Secretly Degrading Peer-to-Peer Applications, 23 FCC Rcd. 13028, 13055 (2008) (memorandum opinion and order).

133. See MORGAN STANLEY, THE MOBILE INTERNET REPORT SETUP 62 (Dec. 15, 2009), available at [http://www.morganstanley.com/institutional/techresearch/mobile\\_internet\\_report\\_122009.html](http://www.morganstanley.com/institutional/techresearch/mobile_internet_report_122009.html) [hereinafter MOBILE INTERNET REPORT SETUP].

134. *Id.*

135. *Id.*

136. *Key Themes*, *supra* note 24, at 400.

137. *Id.*

138. Lance Whitney, *Verizon Wireless Eyeing Tiered Data Service*, CNET (June 18, 2010, 7:10 AM), [http://news.cnet.com/8301-1035\\_3-20008138-94.html](http://news.cnet.com/8301-1035_3-20008138-94.html).

This congestion has led wireless providers to begin implementing tiered-pricing models for data plans.<sup>139</sup> Although consumers fear the change to tiered-pricing plans,<sup>140</sup> this structure is in the best interest of both mobile broadband neutrality and the consumer.

#### IV. TIERED PRICING

Due to considerable network congestion throughout wireless networks, a transition from the standard “unlimited” data plans to a tiered-pricing structure will help manage already stressed networks<sup>141</sup> and provide financial incentives for carriers to make networks more robust.<sup>142</sup>

During the infancy of the mobile communications market, individual states had the power to regulate mobile pricing.<sup>143</sup> The federal government, however, wrestled away police power over mobile communications pricing in 1993 by amending the Communications Act of 1934 to read, “[N]o State or local government shall have any authority to regulate the entry of or the rates charged by any commercial mobile service or any private mobile service . . . .”<sup>144</sup> As a result, the power to regulate any new pricing plans lies within the federal government’s purview.

The FCC has acknowledged that tiered pricing is a “permissible network management technique.”<sup>145</sup> Professor Babette Boliek points out, “[T]he move to two-tiered pricing for broadband consumption by the mobile industry would appear a natural development. The industry, by extensive trial and evolution, established a multi-tiered pricing structure, based primarily on usage for its core voice transmission business.”<sup>146</sup> This change may not only be a natural transition, it might be a necessary one. The chairman of the FCC has predicted an ominous future, indicating “a looming spectrum crisis” if more broadband space cannot be allocated for mobile internet use.<sup>147</sup>

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139. See Amy Thomson, *Verizon Sees Wireless Moving to Tiered Pricing with 4G Network*, BLOOMBERG (June 17, 2010, 5:08 PM), <http://www.bloomberg.com/news/2010-06-17/verizon-sees-wireless-moving-to-tiered-pricing-with-4g-network.html>.

140. See Sean Fallon, *Outrage Prompts Time Warner to Drop Tiered Pricing Until We Can Be Educated*, GIZMODO (Apr. 16, 2009, 4:34 PM), <http://gizmodo.com/5215266/outrage-prompts-time-warner-to-drop-tiered-pricing-until-we-can-be-educated>.

141. *Key Themes*, *supra* note 24, at 405.

142. Penchuk, *supra* note 34, at 76.

143. Babette E.L. Boliek, *Wireless Net Neutrality Regulation and the Problem with Pricing: An Empirical, Cautionary Tale*, 16 MICH. TELECOMM. & TECH. L. REV. 1, 22 (2009).

144. Communications Act of 1934, 47 U.S.C. § 332(c)(3)(A) (2006) amended by Pub. L. No 103-66, 107 Stat. 312 (1993).

145. Christopher Fedeli, *Carpool Lanes on the Internet: Effective Network Management*, 26 COMM. LAW. 1, 29 (July 2009).

146. Boliek, *supra* note 143, at 20.

147. *FCC Warns of Mobile’s Looming Spectrum Crisis*, MSNBC (Oct. 7, 2009, 7:49 PM), [http://www.msnbc.msn.com/id/33216878/ns/technology\\_and\\_science-wireless/](http://www.msnbc.msn.com/id/33216878/ns/technology_and_science-wireless/) (quoting the FCC Chairman Julius Genachowsk).

AT&T and Verizon have already implemented a consumption-based tiered-pricing scheme for its data plans.<sup>148</sup> Sprint is currently the only major carrier still offering an unlimited data plan.<sup>149</sup> A shift in pricing structure is beneficial for three reasons: First, a tiered-pricing structure allows customers to choose a tier based on their actual usage without subsidizing high volume users.<sup>150</sup> Professor Boliek explains, “Under differential pricing, the grandmother who sends occasional e-mails will pay less for Internet access than the individual who downloads 1,500 HD movies in one month. Price is the most common means by which scarce resources may be most efficiently allocated.”<sup>151</sup> Second, allowing providers to offer a consumer-based tiered-pricing system is content neutral.<sup>152</sup> Unlike tiered-pricing structures in which content producers pay broadband providers for prioritized delivery of their content, consumer-based tiered pricing does not favor any type of content over another.<sup>153</sup> Third, tiered pricing creates greater transparency between the provider and consumer. Under the common “unlimited” data plans, the term “unlimited” never really held true to the definition of the word.<sup>154</sup>

Professor Catherine Sandoval writes that in light of the FTC’s standard for deceptive practices, advertisements for “unlimited” data plans with restrictions buried in the seemingly never-ending fine print “would not meet the FTC Act’s standard.”<sup>155</sup> The FTC Act prohibits “unfair or deceptive acts or practices in or affecting commerce.”<sup>156</sup> “To prove a deceptive act or practice under § 5(a)(1), the FTC must show three elements: (1) a representation, omission, or practice, that (2) is likely to mislead consumers acting reasonably under the circumstances, and (3) [that] the representation, omission, or practice is material.”<sup>157</sup> “The law is violated if the first contact . . . is secured by deception . . . even though the true facts are made known to the buyer before he enters into the contract of purchase.”<sup>158</sup> Tiered

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148. Jenna Worthan, *As Networks Speed Up, Data Hits a Wall*, N.Y. TIMES, Aug. 14, 2011, at B.1, available at <http://www.nytimes.com/2011/08/15/technology/as-mobile-networks-speed-up-data-gets-capped.html?pagewanted=all>.

149. *Id.*

150. Boliek, *supra* note 143, at 19.

151. *Id.* (footnote omitted).

152. Boliek, *supra* note 143, at 19–20 n.85.

153. Larry Greenemeier, *FCC Ends Net Neutrality Debate (for Now) by Passing Its Open Internet Order*, SCIENTIFIC AMERICAN (Dec. 21, 2010), <http://www.scientificamerican.com/article.cfm?id=fcc-ends-net-neutrality-debate>.

154. Catherine J. K. Sandoval, *Disclosure, Deception, and Deep-Packet Inspection: The Role of the Federal Trade Commission Act’s Deceptive Conduct Prohibitions in the Net Neutrality Debate*, 78 FORDHAM L. REV. 641, 669 (2009).

155. *Id.*

156. Federal Trade Commission Act, 15 U.S.C. § 45(a)(1) (2006).

157. *FTC v. Med. Billers Network, Inc.*, 543 F. Supp. 2d 283, 303 (S.D.N.Y. 2008) (quoting *FTC v. Verity Int’l, Ltd.*, 443 F.3d 48, 63 (2d Cir. 2006)).

158. *Id.* at 304 (quoting *Exposition Press, Inc. v. FTC*, 295 F.2d 869, 873 (2d Cir. 1961)) (alteration in original).

pricing would not eliminate all claims of this nature; however, the proposed Broadband Internet Fairness Act sets forth viable safeguards against unfair tiered-pricing plans.<sup>159</sup> Professor Boliek points out, “[T]here is no carve out for mobile operators and . . . this would likely cover a great many participants in the mobile industry who offer even limited Internet access.”<sup>160</sup> The Broadband Internet Fairness Act states, “It shall be unlawful for major broadband Internet service providers to offer volume usage service plans imposing rates, terms, and conditions that are unjust, unreasonable, or unreasonably discriminatory.”<sup>161</sup> Under the Act, if a broadband provider intends to implement tiered pricing, the provider is required to file a plan analysis with the FTC that does the following:

- (1) identifies the different service tiers of broadband Internet service to be offered on the basis of different data transmission volumes;
- (2) specifies the different rates, terms, and conditions to be imposed for such tiers;
- (3) provides an analysis of the economic reasonableness and necessity for imposing such tiers.<sup>162</sup>

Under the Act, enforcement of tiered-pricing plans would be under the FTC’s jurisdiction,<sup>163</sup> and any violation would “be treated as a violation of a rule defining an unfair or deceptive act or practice prescribed under section 18(a)(1)(B) of the Federal Trade Commission Act.”<sup>164</sup> Safeguards such as those proposed by the Broadband Internet Fairness Act would ensure that, unlike the vague “unlimited” data plans, consumers would know, pursuant to the act, exactly what the individual tiers offer and that they have been deemed fair and reasonable. This would allow for a more informed and transparent decision when choosing a data plan.

Unfortunately, tiered pricing coupled with handset exclusivity limits the consumer’s options in the same way that handset exclusivity limits the consumer’s options in the context of content discrimination and vertical and horizontal integration discussed above. Because the customer is tied to the carrier through handset exclusivity, the customer would be unable to shop for the tiered-pricing plan for their specific needs without incurring the additional cost of purchasing a compatible handset, assuming the consumer chose to change carriers. One of the criticisms of tiered pricing is that the possible overage charges associated with exceeding the allocated bandwidth

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159. See generally Broadband Internet Fairness Act, H.R. 2902, 111th Cong. (2009), available at <http://www.govtrack.us/congress/billtext.xpd?bill=h111-2902>.

160. Boliek, *supra* note 143, at 21 (footnote omitted).

161. Broadband Internet Fairness Act, H.R. 2902, 111th Cong. § 3(a) (2009), available at <http://www.govtrack.us/congress/billtext.xpd?bill=h111-2902>.

162. *Id.* § 3(b)(3).

163. *Id.* § 4(a).

164. *Id.* (citation omitted).

per month may discourage some users from accessing the internet, reducing the overall “openness” of the internet that net advocates of neutrality are fighting to maintain.<sup>165</sup> Handset exclusivity exacerbates these concerns. Typically coupled with a handset, subject to exclusivity, is a contract with the carrier that binds the consumer to a sizeable early termination fee.<sup>166</sup> Verizon charges an early termination fee of up to \$350,<sup>167</sup> AT&T \$325,<sup>168</sup> and T-Mobile up to \$200.<sup>169</sup> In January 2010, AT&T settled a class action lawsuit claiming that the early termination fees included in customer contracts were unfairly high.<sup>170</sup> Customers filed the suit claiming “the fees were illegal because they bore no relation to the carrier’s actual costs, and discouraged customers from switching carriers.”<sup>171</sup> AT&T did not acknowledge any wrongdoing, but agreed to pay \$18 million to customers to avoid litigation.<sup>172</sup> Previously, Sprint settled similar claims to the tune of \$17.5 million.<sup>173</sup> Due to the settlement, the court did not rule on the legality of these early terminations.<sup>174</sup> Still, customers acknowledged that the fees discourage switching carriers, contributing to the problems associated with handset exclusivity. Proponents fear that tiered pricing could restrict use of the mobile internet. The cost of many new model smartphones, provided that the consumer signs another contract subject to a similar termination fee, can be as much as \$399.<sup>175</sup> As a result, a consumer who is locked into a carrier through handset exclusivity, who does not find a pricing level that is suitable to his or her needs, may have to pay \$550 simply to change carriers

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165. See Cecilia Kang, *AT&T Tiered Data Plan and Questions About Regulatory Oversight*, POST TECH WASH. POST (June 4, 2010, 9:30 AM), [http://voices.washingtonpost.com/posttech/2010/06/thanks\\_reader\\_bitter\\_bill\\_for.html](http://voices.washingtonpost.com/posttech/2010/06/thanks_reader_bitter_bill_for.html).

166. See ENHANCED DATA COLLECTION, *supra* note 130, at 2.

167. *Return Policy*, VERIZON WIRELESS, <http://www.verizonwireless.com/ReturnPolicy.shtml> (last visited Mar. 1, 2012).

168. *1.2 What Happens If My Service is Cancelled or Terminated Before the End of My Agreement? Is There a Cancellation/Early Termination Fee?*, AT&T, [http://www.wireless.att.com/cellphoneservice/legal/index.jsp?q\\_termsKey=wirelessCustomerAgreement&q\\_termsName=Wireless+Customer+Agreement&subSection=whatHappensIfMyServIsCancelled](http://www.wireless.att.com/cellphoneservice/legal/index.jsp?q_termsKey=wirelessCustomerAgreement&q_termsName=Wireless+Customer+Agreement&subSection=whatHappensIfMyServIsCancelled) (last visited Nov. 21, 2010).

169. *T-Mobile Terms & Conditions*, TMOBILE, [http://www.tmobile.com/Templates/Popup.aspx?PAsset=Ftr\\_Ftr\\_TermsAndConditions&print=true](http://www.tmobile.com/Templates/Popup.aspx?PAsset=Ftr_Ftr_TermsAndConditions&print=true) (last visited Nov. 21, 2010).

170. Brian Barrett, *AT&T Reaches \$18 Million Settlement in New Jersey ETF Class Action Case*, GIZMODO (Jan. 26, 2010, 12:41 PM), <http://gizmodo.com/5457345/att-reaches-18-million-settlement-in-new-jersey-etf-class-action-case>.

171. Peter Svensson, *AT&T Settles Class Action over Termination Fees*, MSNBC (Jan. 27, 2010, 12:31 PM), [http://www.msnbc.msn.com/id/35101538/ns/technology\\_and\\_science-wireless/t/att-settles-class-action-over-termination-fees/#.TyRS5YEXLV0](http://www.msnbc.msn.com/id/35101538/ns/technology_and_science-wireless/t/att-settles-class-action-over-termination-fees/#.TyRS5YEXLV0).

172. *Id.*

173. *Id.*

174. *Id.*

175. See, e.g., *Apple iPhone 4s 64GB*, VERIZON WIRELESS, <http://www.verizonwireless.com/b2c/store/controller?item=phoneFirst&action=viewPhoneDetail&selectedPhoneId=5777> (enter zip code: 11201) (last visited Mar. 15, 2012) (stating that a \$350 early termination fee applies to two-year contracts); *PDAs & Smartphones*, AT&T, <http://www.wireless.att.com/cell-phone-service/cell-phones/pda-phones-smartphones.jsp> (last visited Jan. 28, 2012).

and find a favorable pricing structure. This scenario could force customers to restrict internet usage as a result of having to settle for a plan that does not adequately address their usage needs. Not only does this exasperate the concerns of those who fear tiered pricing may restrict use of the mobile internet, but it also adds to the limitations already discussed concerning consumer choice. Eliminating the cost of purchasing a new handset from a new carrier and permitting customers to use their existing handsets on their new network creates greater freedom of mobility and allows customers searching for suitable pricing plans to test the market instead of being forced into a tier on their existing network.

Additionally, although consumers may initially have a negative reaction to the implementation of tiered pricing,<sup>176</sup> consumer-based tiered pricing is in line with consumer interests. As one commenter noted, “Consumers are used to paying about \$30 or so for ‘unlimited’ data with a smartphone . . . .”<sup>177</sup> Yet, “[m]ost people don’t even come close to using enough mobile data to justify spending \$30 a month.”<sup>178</sup> According to AT&T, almost half of their network capacity is being used by a staggeringly low 3 percent of its customers.<sup>179</sup> As a result, as noted above, “the majority of users are essentially subsidizing the costs of these heavy data users and that doesn’t seem fair.”<sup>180</sup> The system, as it stands now, is analogous to going out to dinner with a group of people and ordering a salad while everyone else orders the lobster dinner, and then at the end of the meal, splitting the cost evenly with everyone else. No consumer wants to pay for someone else’s service when there is no need to do so. Therefore, the tiered-pricing model is advantageous to consumers.

## V. STRIKING A BALANCE

Today, as more people access the internet via their mobile handsets,<sup>181</sup> the network has become severely congested.<sup>182</sup> Heavy network traffic results in broadband providers expressing the need to prioritize content as a form of network management in order to maintain service to their customers. One way to combat network congestion, in a neutral manner, is to institute tiered-pricing structures for data plans. Tiered pricing addresses both the need to allocate bandwidth efficiently and discourage content discrimination. In the context of the mobile broadband market, the concern of content discrimination and an open internet can also be addressed with

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176. See Fallon, *supra* note 140.

177. Marin Perez, *Tiered Data Pricing Might Not Be That Bad*, KNOW YOUR CELL (May 28, 2010), [http://www.knowyourcell.com/features/494834/tiered\\_data\\_pricing\\_might\\_not\\_be\\_that\\_bad.html](http://www.knowyourcell.com/features/494834/tiered_data_pricing_might_not_be_that_bad.html).

178. *Id.*

179. *Id.*

180. *Id.*

181. See Mobile Internet Report Setup, *supra* note 133, at 12.

182. See *id.* at 62.

the abolition of handset exclusivity. Allowing customers to attach a device of their choosing to any mobile broadband network is essential to combating the discrimination problems associated with vertical integration and maintaining a neutral internet. Perhaps most importantly, instituting tiered pricing and eliminating handset exclusivity adheres to the FCC's four principles of net neutrality.<sup>183</sup> The elimination of handset exclusivity would allow consumers to connect devices of their choice to any network, in effect fostering competition,<sup>184</sup> and disincentivizing content discrimination.<sup>185</sup> The application of tiered-pricing structures would allow necessary, content-neutral network management,<sup>186</sup> greater customer choice regarding service,<sup>187</sup> and greater transparency between carrier and customer.<sup>188</sup>

## CONCLUSION

In today's world, instituting tiered pricing for mobile data plans, while at the same time abolishing handset exclusivity, addresses both the concerns of net neutrality advocates as well as the pressing needs of broadband providers. Therefore, tiered pricing strikes the proper balance between maintaining a neutral internet and providing effective services.

*Ethan Zweig\**

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183. See discussion *supra* Part I.

184. See discussion *supra* Part III.

185. See *id.*

186. See discussion *supra* Part IV.

187. See *id.*

188. See *id.*

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