

Commissioner Jon Leibowitz
Competition in the Information Society
Uncorked and Unplugged
Remarks before the 2005 Global Forum
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Good morning. It is a true pleasure to be here with you today in this spectacular palace, and I thank Dr. Sylviane Toporkoff and Professor Miriam Sapiro for inviting me to participate in the Global Forum. I am honored to be before you: government officials and industry experts who are lighting the path toward a fairer, safer, more efficient information society.

Before I begin my remarks, I need to offer the Federal Trade Commission's standard disclaimer that the views expressed here today are my own, and do not necessarily reflect those of the Commission or of any other individual Commissioner.

For those of you who are unfamiliar with the Federal Trade Commission, I'll begin by explaining a bit about who we are. Next, I'd like to spend some time discussing an issue that should be of interest to you and has a significant impact on competitiveness in our global Information society: state barriers to competition, and to e-commerce in particular, in the United States.

The FTC is an independent agency with a broad consumer protection and antitrust enforcement mandate. When I say independent, I mean that we are a creation of Congress; not

the executive branch. We don't work for the President.

The Commission consists of five members, nominated by the President and confirmed by the Senate. Commissioners serve staggered terms, which offers the benefit of both continuity of expertise and incremental policymaking. Additionally, by statute, no more than three Commissioners may be from any one political party. This ensures diversity of opinion. Our agency is a small one, comprised of just over 1000 attorneys, economists, and other staff.

With respect to our consumer protection mandate, our priorities remain anchored in fighting "traditional" consumer fraud, but they have been changing in the past decade as the nature of commerce -- especially e-commerce -- has changed. Recently, we have centered our efforts on areas such as cyber-fraud, focusing on spam, spyware, phishing, spoofing, and other abuses of cyberspace that threaten to undermine the promise of the Internet. In fact, I spent the latter part of last week in London participating in a conference on global spam enforcement. We have also focused recently on computer fraud and identify theft; recognizing that privacy and data security have become increasingly important, especially in light of recent high profile security breaches like Choicepoint, and Citibank.

With respect to our competition mission, investigating and challenging mergers and anticompetitive conduct, such as price-fixing and agreements among competitors that restrict competition, make up the vast bulk of the antitrust caseload. We are an agency with general jurisdiction, so you'll see us in a variety of markets; however, we have frequent business in

certain economic sectors, such as:

- oil and gas,
- industrial chemicals,
- food and retail,
- pharmaceuticals,
- physician and hospital markets,
- computer hardware and software, and
- the Internet.

Additionally, unlike our counterparts at the Antitrust Division of the Department of Justice, our charter grants us a policymaking function in addition to our enforcement mandate. In support of that mission, we have a specialized shop which assists the FTC in developing recommendations on a wide array of policy issues.

Part of this program includes advocacy efforts directed at state impediments to competition, an issue with which the EC has dealt for some time, recently in the form of sectoral inquiries into energy and gas, and financial services. I would like to spend some time today talking about the FTC's efforts to address state regulations that impede competition.

Specifically, I'd like to talk about an old world issue – wine – and a new world issue – municipal provision of broadband internet service, or “muni broadband,” as we call it. You

might wonder what these two things have in common. The short answer is, they both have faced, or are currently facing, regulatory barriers to competition within the United States, and these barriers would restrict the use or expansion of Internet technology.

Just as important, you might wonder why you should care. Here's why: the Internet is crucial to consumers. Barriers to e-commerce – whether erected by the state or around the state; west of the Atlantic, or on the Continent, locally, or across borders – have the potential to undermine the promise of the Internet that we as a global society have worked so hard to nurture, and that many of you here today have made a part of your work.

Let's begin with wine.

concerns by local “bricks and mortar” retailers, who often feel “squeezed” by Internet-based competition.

Most wine in the United States is distributed through a complicated distribution network, which was developed after the repeal of Prohibition (a 13 year nationwide ban on consumption of alcohol in the U.S.) in 1933. Under this system, a wine producer must first obtain a permit from the federal government. The wine then must be sold to a licensed wholesaler, who delivers the wine to a retailer. The retailer may then sell the wine directly to a consumer. Most states prohibit vertical integration among these three tiers.¹

This is, according to some, the most expensive distribution system of any U.S. packaged goods industry by far.²

Several years ago, the FTC undertook a comprehensive study that addressed potential barriers to e-commerce in the wine industry.³ Particularly troubling to the Commission were certain state regulations that either limited⁴ or outright forbade direct shipments of wine and

¹ *Possible Anticompetitive Barriers to E-Commerce: Wine*, A Report from the Staff of the Federal Trade Commission, July 2003. (“Wine Report”) at 5 (citations omitted).

² *Id.* at 22. (citations omitted).

³ *Possible Anticompetitive Barriers to E-Commerce: Wine*, A Report from the Staff of the Federal Trade Commission, July 2003.

⁴ Some of these limitations include very low ceilings on annual purchases, bans on advertising from out-of-state su

The FTC took a close look at this issue and concluded in its Wine Report that bans on direct shipping of wine prevented consumers from saving as much as 21 percent.⁹ Additionally, these regulations precluded convenient access to a multitude of popular wines – many of which were European imports -- and from literally thousands of smaller wineries. The Report thus concluded that states could significantly enhance consumer welfare by allowing the direct shipment of wine to consumers.

Many of those supporting the restrictions claimed that they are necessary to prevent underage drinkers (in the U.S., those under 21 years of age) from receiving direct shipments of wine.¹⁰ However, these concerns could be addressed by simply requiring a signature from a qualified adult upon delivery. In fact, the Commission's study found that of the states that allowed direct shipping, most reported few or no problems with shipments to minors.

There is a happy turn to this story, or at least one we can raise our glasses to. Earlier this year, in an opinion that cited heavily to the Commission's Wine Report, the United States Supreme Court issued a ruling outlawing regulations in two states – New York and Michigan – that banned direct shipments of wine by out-of-state suppliers, but allowed in-state wine

⁹ According to private estimates cited in the Report, a wholesaler typically marks up a bottle of wine by 18-25%. Wine Report at 22 (citations omitted)

¹⁰ Due to a magnitude of alcohol-related problems, the various United States prohibit consumption of alcohol by individuals under a certain age, which is in most instances, twenty-one. One study, cited in the Wine Report, estimated that in 1996, the total costs of underage drinking – including traffic crashes, violent crime, burns, drowning, suicide attempts, fetal alcohol syndrome, alcohol poisoning, and treatment – was \$52.8 billion. Wine Report at 11 (citations omitted).

suppliers to ship directly to customers.¹¹ (Interestingly, C. Boyden Gray, nominated to be the next U.S. ambassador to the EU, joined the fight on the side of the wine wholesalers, who sought to ban direct sales. Let's hope that his views will ripen with age....)

Though the Supreme Court's ruling was widely heralded as "the best day for [American] wine lovers since the invention of the corkscrew,"¹² there are clear limits to the high court's ruling. While the ruling struck down laws that favored in-state wine suppliers over out-of-state competitors, it does not outlaw the practice of banning direct shipping to consumers completely. Indeed, in the months since the Supreme Court's ruling, many states have proposed legislation that would prohibit direct shipping entirely. Additionally, the court's ruling leaves open the issue of how states may regulate direct shipments from European suppliers. Which way the wine flows from here remains to be seen.

Now that we've been uncorked, let's get unplugged.

It is almost universally acknowledged that Internet access is essential to economic growth and education. High speed access, particularly wireless access, benefits students, parents, small businesses, emergency workers and anyone else who values enhanced portability, flexibility and speed. In its most fundamental form, broadband is about consumer empowerment – giving users

¹¹ Granholm v. Heald, 125 S. Ct. 1885 (May 16, 2005)

¹² Clint Bolick, strategic litigation counsel for the Institute for Justice, as cited in Michael Lear-Olimpi and Tony Mauro, *Supreme Court Clears the Way for Wine to Flow in and Out of States*; E Commerce Law and Strategy, June 2005.

access to and control of information.

This is true in the U.S., in Europe, and around the globe.

In fact, in this day and age, access to broadband in the U.S. could be considered even more vital than some traditional government services because the Internet is both a repository of information, like a library, and a shared common space, like a park, to which the public should have access. To that end, local governments are beginning to step up in communities across the United States to meet the information and technology needs of their residents by offering high-speed wireless Internet access or broadband, as a public service. In other words, a growing number of U.S. municipalities are establishing broadband networks that potentially compete with commercial operators.

Take Philadelphia, for example. Beginning last year, the city undertook plans to offer wireless Internet access. The city's rationale was straightforward: many of its residents did not have access to broadband, and Wi-Fi service would spur economic development, improve education,¹³ attract tourists, and benefit city agencies at lower cost than the current telecom

¹³ Philadelphia's chief information officer also stressed the importance of providing broadband for education – noting that while schools have heavily invested in their computer systems, only 58 percent of Philadelphia's students have Internet access at home. David Haskin, *Philly CIO: Public Wi-Fi Needed to Close Digital Divide*, MOBILEPIPELINE, January 25, 2005, available at www.mobilepipeline.com/57703505.

infrastructure.¹⁴

These plans, however, were almost terminated at their inception by the efforts of commercial operators pressing for state legislation prohibiting municipal wi-fi. But fortunately, after a public outcry, reason won out and today the city is moving forward with its plans.¹⁵ Many additional U.S. cities – perhaps 300 in all – are considering or implementing broadband networks.

Municipal development of broadband may be the best option in some cities where many residents cannot afford the high prices of private Internet providers, or where Internet providers simply did not see enough economic incentive to provide universal coverage. It may be the only option in rural areas where phone and cable companies have not extended any service – often contending that it would be prohibitively expensive. Indeed, even the mere threat of local government entering the broadband market may entice phone and cable companies to compete in these low-income and low-density areas.

Although in Philadelphia, the city prevailed, many similar municipal initiatives are being challenged by the efforts of commercial incumbents who simply don't want the competition. To

¹⁴ Peter Loftus, *Philadelphia Waits for Wi-Fi*, THE WALL STREET JOURNAL, March 3, 2005.

¹⁵ With respect to the construction of its network, it is interesting to note that Philadelphia is turning to two highly capable private-sector companies to potentially provide this service – undermining the position of some that cities cannot provide broadband competently and the position of others that this issue breaks down as a fight between the private sector and local government.

put this in context, imagine if Borders and Barnes & Noble – or Waterstone's, Thalia, or FNAC – claiming it was hurting their book sales, asked lawmakers to ban cities from building libraries. At the very least, this would be considered somewhat of a stretch. Yet so far, phone and cable companies have successfully pressured about a half dozen states to place some sort of restrictions on their books, and similar measures are being considered in many others.

To be certain, opponents of municipal broadband make several arguments that, at first blush, might seem persuasive. They assert that supplying access to the Internet simply is not a proper function for local government. They argue that municipal participation in the establishment of wi-fi networks would amount to “unfair competition” because municipalities have certain advantages over private providers, such as lower fixed costs and no need to pay for rights of way, an argument that seems to raise concerns similar to those embodied in the EC's proscription on state aid. And they claim that their vBuld be cinompetithsat sepe

Thank you. I've enjoyed being here.