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The Problems with Municipal Broadband

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Background: President Joe Biden's American Jobs Plan calls for "future proof" broadband infrastructure, with priority for broadband networks "owned, operated by, or affiliated with local governments, non-profits, and co-operatives—providers with less pressure to turn profits and with a commitment to serving entire communities."

But... Municipal broadband and other options that decouple Internet service from profits and losses do not serve consumers in a cost-effective way. Municipal providers rely heavily on subsidies (including cross-subsidies from electric co-ops) to continue operations, creating an uneven playing field. The presence of a municipal provider also means less incentive for private companies to enter or expand in the market. On the other hand, benefits from municipal broadband are minimal and it represents a risky investment for taxpayers that should only be considered a last resort.

KEY TAKEAWAYS

NO PROFIT-AND-LOSS TEST

The fundamental problem with municipal broadband is that it is not subject to the profit-and-loss test of the marketplace. While some see this as an advantage, because it allows municipal providers to pursue the public interest, this misunderstands the market process and its importance in promoting the best use of scarce resources.

The pursuit of profit is not inherently harmful to the public interest; it offers incentives to create value for society in a cost-effective way. Profits also act as a signal to other firms to enter the market. Profits and losses communicate how resources can be better allocated in society. Even nonprofits must bring in more revenue than they spend or they will eventually no longer exist.

Unlike private ISPs, municipal broadband providers do not rely solely on revenue from subscribers to remain a going concern. Municipal providers have access to subsidies from local treasuries financed by taxation and government-issued bonds, as well as cross-subsidies from government-run utilities. Evidence suggests there are no municipal broadband providers whose operations are completely independent of these government funds.

As a result, municipal broadband often can offer symmetrical super-fast fiber services, at prices even lower than private providers. But the costs of these services are hidden. What's more, these silent subsidies essentially serve as a regressive wealth transfer from those who do not rely on high-bandwidth Internet to high-demand users like streamers and gamers.

HIGH RISK OF FAILURE

Municipal provision of broadband has proven a very risky investment for the public. Studies show that municipal providers are unlikely to recover project costs within the 30-40 year life expectancy of a municipal fiber build.

Several high-profile failures have led municipal systems to be sold for less than the public invested in the infrastructure. For example, Thames Valley Communications of Groton, Connecticut—completed in 2006—failed to bring in more revenue than expenses, even with heavy subsidies from the city. It was sold in 2013 for $550,000, leaving taxpayers responsible for $27.5 million in debt for the costs of construction and accumulated losses.

Due to this high risk of failure, public investment in municipal broadband should be limited, for reasons similar to the need to limit public subsidies for sports stadiums.

DISCOURAGING PRIVATE INVESTMENT

Municipal broadband crowds out private investment, which can mean less entry in markets with municipal broadband; reduced profits for incumbent ISPs; greater chance private providers will exit the market; and less investment in maintaining and improving private systems.

The FCC has acknowledged the potential crowding-out effect, stating in the National Broadband Plan: "Municipally financed service may discourage investment by private companies. Before embarking on any type of broadband buildout, whether wired or wireless, towns and cities should try to attract private sector broadband investment."

MUNICIPAL BROADBAND'S LIMITED BENEFITS

Increased economic growth is often touted as a benefit of municipal broadband, but the evidence suggests such claims are overstated.

One recent research paper found the presence of a municipal network does not appear to generate statistically significant improvement in economic conditions, as measured by changes in the unemployment rate or labor participation rate. Another paper similarly found that "there is no observable correlation between high-speed, muni-owned networks and private-sector employment growth."

There is also evidence that whatever limited benefits do arise from communities that adopt municipal broadband comes at the expense of neighboring communities. Thus, from a federal perspective, stimulating municipal broadband merely serves to transfer wealth between communities without actually providing net benefits to society.

For more on this issue, see Ben Sperry's *Truth on the Market* blog post, "Islands of Chaos: The Economic Calculation Problem Inherent in Municipal Broadband"; George Ford, et al.'s "The Law & Economics of Municipal Broadband"; and "A Dynamic Analysis of Broadband Competition" by Geoffrey Manne, Kristian Stout, & Ben Sperry.

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