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The *Federal Communications Law Journal* is co-published by the Federal Communications Bar Association and the Indiana University School of Law–Bloomington. The *Journal* publishes three issues per year, including articles, student notes, commentaries, and book reviews examining a wide range of domestic and international communications and information issues, including telecommunications, the First Amendment, broadcasting, telephony, computers, mass media, intellectual property, communications and information policy making, and related fields.

As the official journal of the Federal Communications Bar Association, the *Journal* is distributed to the Association's more than 2,500 members and more than 550 additional legal practitioners, industry experts, government officials, and academics. The *Journal* is also distributed by Westlaw and Lexis and is available on the Internet at <http://www.law.indiana.edu/fclj>.

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# FEDERAL COMMUNICATIONS LAW JOURNAL

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## Articles

### ***Brand X and the Wireline Broadband Report and Order: The Beginning of the End of the Distinction Between Title I and Title II Services***

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*Triennial Review* and the media ownership proceedings are symptomatic of a broad agency inefficiency that should be remedied by drastically cutting the size of the FCC and placing it under the exclusive control of the executive branch to ensure electoral accountability. Taylor argues that while these suggestions may have value, such a rush to action should not be premised on anecdotal evidence, but instead must rest on a more empirical, objective undertaking that would study the FCC's track record. Furthermore, Taylor points out that there are numerous other avenues for reforming the communications regulatory regime: Congress, states, and international organizations. Taylor concludes by analogizing the United Kingdom's OFCOM to the FCC proposed by May. He argues that though OFCOM's centralized structure and greater accountability have advantages, it also results in a more partisan regulatory process with less transparency. Further, the delays and inefficiencies that May criticizes in the FCC may be inherent in any agency decisionmaking that solicits and invites public comment, regardless of the agency's structure.

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In 1990, Congress passed the Children’s Television Act (“CTA”), which directed the FCC to establish standards for broadcasters regarding the amount of children’s programming aired and to enforce limits on the amount of commercial time aired during children’s programming. The limits are meant to protect children from various harms caused by advertising aimed at children. This Note examines the constitutionality and the effectiveness of these commercial limits. The Note concludes that while the CTA’s commercial limits are probably constitutional under the Court’s test for regulations of commercial speech, the limits do not provide children with adequate protection from the harms of advertising. The Note suggests several changes that should be made in the regulation of advertising aimed at children. Most importantly, the Note argues that the focus of the regulation should shift from limiting the amount of commercial material viewed by children to reducing the misleading nature of advertising aimed at children. The Note argues that the suggested content-based regulation would be constitutional under the Court’s test for regulation of commercial speech and would more effectively protect children from the harms of advertising than the current regulation.

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# ***Brand X and the Wireline Broadband Report and Order: The Beginning of the End of the Distinction Between Title I and Title II Services***

**J. Steven Rich\***

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## I. INTRODUCTION

At the time of writing this Article in early fall 2005, the ink is barely dry on the Supreme Court's decision in *Brand X*, in which the Court upheld a 2002 ruling by the Federal Communications Commission ("FCC" or "Commission") that cable modem service is properly classified as an information service and does not involve a separate offering of telecommunications service.<sup>1</sup> However, both houses of Congress and the FCC have already reacted in the form of proposed legislation<sup>2</sup> and a *Report and Order*,<sup>3</sup> respectively, in an effort to expand the deregulatory approach taken by the Commission in its *Declaratory Ruling* on cable modem service,<sup>4</sup> which the Supreme Court upheld.<sup>5</sup>

This Article will examine the development of the FCC's distinction between common carrier services regulated pursuant to Title II of the Communications Act of 1934, as amended ("Act"), and those regulated—if at all—pursuant to the Commission's ancillary jurisdiction under Title I of the Act.<sup>6</sup> This Article will trace the evolution of this distinction from the *Computer Inquiry*<sup>7</sup> line of decisions through the *Stevens Report*,<sup>8</sup> the Telecommunications Act of 1996,<sup>9</sup> *Brand X*,<sup>10</sup> and the recent *Wireline Broadband Report and Order*.<sup>11</sup> This Article will conclude that the

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1. Nat'l Cable & Telecomm. Ass'n v. Brand X Internet Serv., 125 S. Ct. 2688, 2706–08 (2005).

2. See *Ensign Bill*, *infra* Part IV.C.

3. See *Wireline Broadband Report and Order*, *infra* Part IV.B.

4. Inquiry Concerning High-Speed Access to the Internet Over Cable and Other Facilities, *Declaratory Ruling and Notice of Proposed Rulemaking*, 17 F.C.C.R. 4798 (2002) [hereinafter *Declaratory Ruling*].

5. *Brand X*, 125 S. Ct. 2688, 2702.

6. Communications Act of 1934, ch. 652, 48 Stat. 1064 (codified as amended at scattered sections of 47 U.S.C.).

7. Regulatory and Policy Problems Presented by the Interdependence of Computer and Communication Services and Facilities, *Tentative Decision*, 28 F.C.C.2d 291, para. 20 (1970) [hereinafter *Computer I Tentative Decision*], modified by *Final Decision and Order*, 28 F.C.C.2d 267 (1971).

8. Federal-State Joint Board on Universal Service, *Report to Congress*, 13 F.C.C.R. 11501 (1998) [hereinafter *Stevens Report*].

9. Telecommunications Act of 1996, Pub. L. No. 104-104, 110 Stat. 56 (codified at scattered sections of 47 U.S.C.).

10. *Brand X*, 125 S. Ct. 2688.

11. Appropriate Framework for Broadband Access to the Internet over Wireline

*Wireline Broadband Report and Order* may be vulnerable to reversal on appeal and will suggest some of the policy considerations that the Commission may wish to consider if this order is remanded.

## II. EVOLUTION OF THE BOUNDARIES BETWEEN REGULATED AND UNREGULATED SERVICES

### A. *Basic Versus Enhanced Services: The Computer Inquiry Line of Decisions*

Nearly forty years ago, the FCC first faced the issue of whether and how to regulate the provision of data processing services by common carriers. The Commission recognized, even at that time, that applying traditional economic regulation to data processing services might stifle the growth of the then-nascent computer industry.<sup>12</sup> In fact, as early as 1970, the FCC found in the *Computer I* proceeding that “the offering of data processing services is essentially competitive and that, except to the limited extent hereinafter set forth, there is no public interest requirement for regulation . . . of such activities.”<sup>13</sup> At the same time, the Commission also recognized that, given the growing interdependence of telecommunications and data processing, control by regulated common carriers over bottleneck facilities could give such entities an opportunity to cross-subsidize their services, thereby gaining an unfair advantage in the data processing industry.<sup>14</sup>

As a result of its concerns regarding cross-subsidy and unfair competition, the FCC undertook in *Computer I* what would today— notwithstanding the Commission’s statement in the above paragraph— hardly be considered “limited” regulation of data-processing activities by common carriers. Under the rules adopted in *Computer I*, the FCC elected to forbear from regulating data-processing services and to allow common carriers<sup>15</sup> to provide such services through affiliates.<sup>16</sup> However, such affiliates were subject to rigid structural separation requirements and were

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Facilities; Universal Services Obligations of Broadband Providers, *Report and Order and Notice of Proposed Rulemaking*, FCC 05-150, <http://ftp.fcc.gov/FCC-05-150A1.pdf> [hereinafter *Wireline Broadband Report and Order*].

12. E.g., *Computer I Tentative Decision*, *supra* note 7, para. 23.

13. *Id.* para. 20.

14. *Id.* para. 25.

15. This true except for AT&T and its affiliates, which the FCC concluded were prohibited by a consent judgment from entering into the data processing industry. *Id.* para. 24 (citing *United States v. Western Electric Co.*, consent judgment, 13 RR 2143, 1956 Trade Cas. 71, 134 (D.N.J. 1956)).

16. *Id.* paras. 36–37.

strictly prohibited from providing services to affiliated common carriers, even on an arm's-length basis.

The Commission distinguished regulated communications services from unregulated data processing services by defining data processing as "[t]he use of a computer for the processing of information as distinguished from circuit or message-switching."<sup>17</sup> "Processing involves the use of the computer for operations which include, *inter alia*, the functions of storing, retrieving, sorting, merging and calculating data, according to programmed instruction."<sup>18</sup> Anticipating that both common carriers and providers of data processing services would provide hybrid services containing elements of communications and data processing, the Commission adopted a test for hybrid services that focused on the dominant characteristic of the overall package offering. Where a package consisting primarily of data-processing features contained communications elements that were "an integral part of and as an incidental feature" of the data processing, then the Commission determined that forbearance was appropriate with respect to the entire service.<sup>19</sup> Conversely, the FCC found that hybrid services that were "essentially communications" should be subject to Title II regulation.<sup>20</sup>

By the late 1970s, technological advances in the computer industry had significantly blurred the boundaries drawn in *Computer I*. In particular, computing applications no longer resided exclusively on large mainframe computers, but also ran on mini- and microcomputers that allowed the decentralization of data processing operations.<sup>21</sup> In light of such developments, the FCC undertook the *Computer II* proceeding to reevaluate its regulatory framework governing the provision of computer processing services via common carrier telecommunications facilities.<sup>22</sup>

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17. *Id.* para. 15(a).

18. *Computer I Tentative Decision*, *supra* note 7, para. 15(a).

19. Regulatory and Policy Problems Presented by the Interdependence of Computer and Communication Services and Facilities, *Final Decision and Order*, 28 F.C.C.2d 267, para. 31 (1971).

20. *Id.* para. 32.

21. See, e.g., Amendment of Section 64.702 of the Commission's Rules and Regulations (Second Computer Inquiry), *Final Decision*, 77 F.C.C.2d 384, para. 1 (1980) [hereinafter *Computer II Final Decision*] (observing that "dramatic advances" in technology had "permitted fabrication of mini-computers, microcomputers, and other special purpose devices" that were capable of duplicating many capabilities previously available only on large, centralized computer systems), *modified on recon.*, *Memorandum Opinion and Order*, 84 F.C.C.2d 50 (1980) [hereinafter *Computer II Reconsideration Order*], *further modified*, *Memorandum Opinion and Order on Further Reconsideration*, 88 F.C.C.2d 512 (1981), *aff'd sub nom.*, *Computer and Communications Indus. Ass'n v. FCC*, 693 F.2d 198 (D.C. Cir. 1982).

22. *Computer II Final Decision*, *supra* note 21, para 1.

In *Computer II*, while the Commission retained the notion of distinguishing between regulated, traditional common carrier services and unregulated computer processing services, it developed what was, at the time, a more workable distinction between the two. It defined “basic service” as “the common carrier offering of transmission capacity for the movement of information.”<sup>23</sup> On the other hand, “enhanced service combine[d] basic service with computer processing applications that act on the format, content, code, protocol or similar aspects of the subscriber’s transmitted information, or provide the subscriber additional, different, or restructured information, or involve subscriber interaction with stored information.”<sup>24</sup> Put differently, the provision of the “pipe” by a common carrier would be subject to Title II regulation while applications carried over such pipe would not.

In *Computer II*, the FCC abolished the requirement that common carriers form separate subsidiaries for the provision of enhanced services except with respect to AT&T, which the Commission found to pose a substantial threat to competition.<sup>25</sup> The Commission also found that AT&T’s offering of enhanced services and customer premises equipment through a structurally separate subsidiary would not violate the 1956 *Western Electric* consent decree.<sup>26</sup> In the Third Computer Inquiry, the FCC replaced its structural separation requirements with nonstructural safeguards, such as comparably efficient interconnection, open network architecture, and nondiscrimination requirements.<sup>27</sup>

#### B. *The Telecommunications Act of 1996*

Section 8(b) of the Telecommunications Act of 1996 (“1996 Act”) added several key definitions to Section 3 of the Communications Act of 1934. While the fundamental distinctions between enhanced services and basic services remained, these terms were replaced with information services and telecommunications services, respectively. These terms derive from, and closely track, the definitions contained in the *Modification of*

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23. *Id.* para. 5.

24. *Id.*

25. *Id.* para. 12. Note that in the *Computer II Final Decision*, the FCC applied the structural separation requirements to both GTE and AT&T. However, the Commission decided upon reconsideration that the costs of these requirements outweighed their benefits with respect to GTE and retained structural separation requirements only for AT&T. *Computer II Reconsideration Order*, *supra* note 21, para. 66.

26. *Computer II Final Decision*, *supra* note 21, para. 13.

27. Amendment of Sections 64.702 of the Commission’s Rules and Regulations (Third Computer Inquiry), *Report and Order*, 104 F.C.C.2d 958, paras. 3–6 (1986), *vacated and remanded*, 905 F.2d 1217 (9th Cir. 1990), *remanded to* 118 P.U.R.4th 419 (1990).

*Final Judgment* that governed the Bell Operating Companies in the aftermath of the breakup of the former AT&T monopoly.<sup>28</sup>

First, the 1996 Act defined “information service” as the “offering of a capability for generating, acquiring, storing, transforming, processing, retrieving, utilizing, or making available information via telecommunications, and includes electronic publishing, but does not include any use of any such capability for the management, control, or operation of a telecommunications system or the management of a telecommunications service.”<sup>29</sup> The 1996 Act’s legislative history shows that Congress did not contemplate a radical change in the way in which the Commission distinguishes between services that are subject to Title II regulation and those that are not. To the contrary, the Conference Committee stated that new subsection (pp) of the 1996 Act “defines ‘information service’ similar to the . . . Commission definition of ‘enhanced services.’ The Senate intends that the Commission would have the continued flexibility to modify its definition and rules pertaining to enhanced services as technology changes.”<sup>30</sup>

The 1996 Act defined “telecommunications service” as “the offering of telecommunications for a fee directly to the public, or to such classes of users as to be effectively available directly to the public, regardless of the facilities used.”<sup>31</sup> The 1996 Act in turn defined the term “telecommunications” as “the transmission, between or among points specified by the user, of information of the user’s choosing, without change in the form or content of the information as sent and received.”<sup>32</sup> The

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28. *United States v. AT&T*, 552 F. Supp. 131, 335–38 (D.D.C. 1982) [hereinafter *Modification of Final Judgment*], *aff’d sub nom.*, 460 U.S. 1001 (1983).

29. *Compare* 47 U.S.C. § 153(20) (2000), *with Modification of Final Judgment*, which defines “information service” as:

the offering of a capability for generating, acquiring, storing, transforming, processing, retrieving, utilizing, or making available information which may be conveyed via telecommunications, except that such service does not include any use of any such capability for the management, control, or operation of a telecommunications system or the management of a telecommunications service.

*Modification of Final Judgment*, *supra* note 28, at 335.

30. JOINT EXPLANATORY STATEMENT OF THE COMMITTEE OF CONFERENCE, H.R. REP. NO. 104-458 (1996) (Conf. Rep.), [www.vortex.com/privacy/tel-96.rpt](http://www.vortex.com/privacy/tel-96.rpt) [hereinafter JOINT EXPLANATORY STATEMENT].

31. *Compare* 47 U.S.C. § 153(46) (2000), *with Modification of Final Judgment*, at 337 (defining “telecommunications service” as “the offering for hire of telecommunications facilities, or of telecommunications by means of such facilities.”).

32. *Compare* 47 U.S.C. § 153(43) (2000), *with Modification of Final Judgment*, which defines “telecommunications” as:

the transmission, between or among points specified by the user, of information of the user’s choosing, without change in the form or content of the information as sent and received, by means of electromagnetic transmission . . . including all

Conference Committee intended the definition of “telecommunications service” to include “commercial mobile service (‘CMS’), competitive access services, and alternative local telecommunications services to the extent that they are offered to the public or to such classes of users as to be effectively available to the public.”<sup>33</sup> Notably, the examples cited by the Conference Committee are all services that either provide, or substitute for, access to the public switched telephone network (“PSTN”).

The Conference Committee also indicated that Congress intended the definition of “telecommunications service” to include only “those services and facilities offered on a ‘common carrier’ basis . . . .”<sup>34</sup> This statement, together with the above list of examples of telecommunications services, shows the following: (1) Congress intended telecommunications services to be the equivalent of basic services under *Computer II*; and (2) Congress envisioned that this term would describe only services provided by entities already subject to Title II regulation or those that choose to act as a common carrier.

### III. INITIAL DIVERGENT TREATMENT OF BROADBAND INTERNET ACCESS SERVICES

#### A. *The Stevens Report*

Over the years, communications services in the United States have evolved from a luxury good to an essential service. During the course of this evolution, the Commission developed policies and regulations designed to assure that even the poorest citizens had access to telecommunications services. The 1996 Act sought to replace the myriad, implicit forms of universal service support that existed at the time with a mechanism that would be explicit, competitively neutral, and able to withstand the local competition that was envisioned in the 1996 Act. As universal service contributions under the 1996 Act were to be payable only with respect to telecommunications, in 1997 Congress required that the FCC issue a report to Congress describing the effect of certain new definitions contained in the 1996 Act on universal service support.<sup>35</sup>

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instrumentalities, facilities, apparatus, and services (including the collection, storage, forwarding, switching, and delivery of such information) essential to such transmission.

*Modification of Final Judgment*, *supra* note 28, at 336–37.

33. JOINT EXPLANATORY STATEMENT, *supra* note 30.

34. *Id.*

35. Departments of Commerce, Justice, and State, the Judiciary, and Related Agencies Appropriations Act, 1998, Pub. L. No. 105-119, § 623, 111 Stat. 2440, 2521–22 (1998).

The FCC responded to its congressional mandate in 1998 with what is popularly known as the *Stevens Report*.<sup>36</sup> In addressing the definitional issues, the Commission first found that Congress intended information services and telecommunications services to be mutually exclusive terms. The Commission disagreed with the position advanced by Senators Stevens and Burns that the term “telecommunications carrier” includes “anyone engaged in the transmission of ‘information of the user’s choosing.’”<sup>37</sup>

The text of the 1996 Act provided part of the basis for the Commission’s determination that information service and telecommunications service are mutually exclusive categories. If a service provider offers telecommunications (i.e., “transmission, between or among points specified by the user, of information of the user’s choosing, without change in the form or content of the information as sent and received . . . .”<sup>38</sup>), the Commission reasoned that such a service must necessarily exclude the provision of an information service, since an information service by definition includes some “capability for generating, acquiring, storing, transforming, processing, retrieving, utilizing, or making available information via telecommunications, and [such term] includes electronic publishing . . . .”<sup>39</sup> Further, the definition of information service states that such a service is provided via telecommunications, suggesting that telecommunications services are distinguishable from information services.

The Commission also examined the legislative history and concluded that the drafters of the House and Senate bills had viewed telecommunications and information services as mutually exclusive.<sup>40</sup> Notably, earlier versions of the House bill and the Senate Report had explicitly stated that the term telecommunications service excludes information services.<sup>41</sup> While Senators Stevens and Burns attached a great deal of weight to the fact that this language had been deleted in later versions of the respective documents, the Commission found that the Senate Report omitted this language because of a manager’s amendment that was “intended to clarify that carriers of broadcast or cable services are not intended to be classed as common carriers under the Communications Act to the extent they provide broadcast services or cable services.”<sup>42</sup> Numerous other senators supported the Commission’s view that Congress

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36. *Stevens Report*, *supra* note 8.

37. *Id.* para. 35. (citation omitted).

38. *Id.*

39. *Id.* para. 30.

40. *Stevens Report*, *supra* note 8, para. 44.

41. *Id.*

42. *Id.* (citations omitted).



had intended telecommunications services and information services to be mutually exclusive.<sup>43</sup> Finally, the Commission observed, in what was perhaps the strongest justification for its interpretation, that the *Computer II* framework had been in place for sixteen years at the time the 1996 Act was adopted and that the interpretation advanced by Senators Stevens and Burns would result in a greatly increased level of regulation on services theretofore unregulated.<sup>44</sup> In light of the procompetitive, deregulatory goals espoused by the 1996 Act, such a reading of Congress's intent would be at best a strained interpretation, and at worst, completely at odds with the 1996 Act's purpose.

*B. The Advanced Services Memorandum Opinion and Order*

In 1998, the Commission issued the *Advanced Services Memorandum Opinion and Order* in response to six petitions proposing actions the Commission could take to speed the deployment by wireline carriers of advanced services such as digital subscriber line ("DSL")-based Internet access.<sup>45</sup> The Commission noted the goals of Congress with respect to the 1996 Act, such as encouraging innovation and investment and opening markets to competition. It indicated that it was adopting the *Advanced Services Memorandum Opinion and Order* in furtherance of these goals.<sup>46</sup>

Before the Commission could address the issue of what statutory obligations would apply to the provision of "advanced services," which the Commission defined as "wireline, broadband telecommunications services, such as services that rely on digital subscriber line technology . . . and packet-switched technology," the Commission first had to address the proper regulatory classification of advanced services.<sup>47</sup> The Commission observed that its application of the 1996 Act's definitions would determine the statutory obligations to which advanced services would be subject.<sup>48</sup>

The Commission concluded that "advanced services are telecommunications services," noting that it had repeatedly found specific packet-based services to be basic services (i.e., pure transmission

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43. *Id.* paras. 37–38.

44. *Id.* paras. 45–46.

45. Deployment of Wireline Services Offering Advanced Telecommunications Capability, *Memorandum Opinion and Order*, and *Notice of Proposed Rulemaking*, 13 F.C.C.R. 24011 (1998) [hereinafter *Advanced Services Memorandum Opinion and Order*]. The following entities filed the petitions that led to the adoption of the *Advanced Services Memorandum Opinion and Order*: Bell Atlantic Corp.; U S WEST Comm., Inc.; Ameritech Corp.; Alliance for Public Tech.; Ass'n for Local Telecomm. Serv. ("ALTS"); and, Southwestern Bell Tel. Co., Pacific Bell, and Nevada Bell (filing jointly). *Id.*

46. *Id.* paras. 1–2.

47. *Id.* para. 3 (citations omitted).

48. *Id.* para. 35.

services).<sup>49</sup> In support of its conclusion, the Commission observed that DSL and packet switching are “simply transmission technologies” and briefly summarized its treatment of transmission services as basic services under the *Computer Inquiry* line of decisions.<sup>50</sup> The Commission further explained that it had previously found the 1996 Act’s definitions of telecommunications services and information services to be equivalent to the *Computer II* definitions of basic services and enhanced services, respectively.<sup>51</sup>

The Commission found that “[a]n end-user may utilize a telecommunications service together with an information service, as in the case of Internet access.”<sup>52</sup> However, the Commission also determined that it would treat these services separately (i.e., the DSL-enabled transmission path would be regulated as a telecommunications service, and the Internet access would be an information service).<sup>53</sup> The Commission explicitly acknowledged its determination in the *Stevens Report* that the terms telecommunications service and information service are mutually exclusive,<sup>54</sup> strongly suggesting that the Commission saw no conflict between this finding and the notion that a service package including both transmission and Internet access could be viewed as containing two separate and distinct services.

The Commission’s decision in the *Advanced Services Memorandum Opinion and Order* to classify DSL as a telecommunications service closely followed the reasoning of its *Computer Inquiry* decisions and did not generate substantial controversy at the time. For example, neither the petitioners nor any of the commenters challenged the Commission’s finding that DSL service was properly classified as a telecommunications service.<sup>55</sup> Moreover, none of the Commissioners who took part in the decision questioned this finding.<sup>56</sup>

In its four subsequent orders in the *Advanced Services* proceeding, the Commission did not question its decision to classify DSL service as a

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49. *Id.*

50. *Advanced Services Memorandum Opinion and Order*, *supra* note 45, para. 35.

51. *Id.* para. 35 n.56.

52. *Id.* para. 36.

53. *Id.* (citations omitted).

54. *Id.* para. 34 n.50.

55. *Id.* para. 36 (citation omitted).

56. *See id.* at 24117–22 (concurring statements of Comm’rs Ness, Tristani, and Powell); *see also* Deployment of Wireline Services Offering Advanced Telecommunications Capability, *Order on Remand*, 15 F.C.C.R. 385 (1999) (Comm’r Harold Furchtgott-Roth, approving in part & dissenting in part) (disagreeing with classification of advanced service as “telephone exchange service,” but not questioning the decision to classify such service as a “telecommunications service”) [hereinafter *Advanced Services Remand Order*].

telecommunications service.<sup>57</sup> To the contrary, in the *Advanced Services Remand Order*, the Commission expressly affirmed its prior conclusion that DSL services constitute telecommunications services.<sup>58</sup>

### C. The Declaratory Ruling on Cable Modem Service

Section 706 of the 1996 Act directed the Commission to initiate a notice of inquiry within 30 months of the enactment of the 1996 Act, and regularly thereafter, concerning the deployment of advanced telecommunications capabilities in the United States.<sup>59</sup> In response to its statutory mandate, the Commission released its *First Section 706 Inquiry* in 1998 and raised the issue of what regulatory treatment should apply to cable modem service.<sup>60</sup> While the issue arose several times from 1999 to 2000, the Commission did not adopt a regulatory classification for cable modem service that would apply on an industry-wide basis.<sup>61</sup> In 2000, following its *Second Section 706 Inquiry*,<sup>62</sup> the Commission decided that it must address the appropriate classification of cable modem service and released a *Notice of Inquiry* the same year that sought information concerning this service.<sup>63</sup> Two years after issuing the *Notice of Inquiry* regarding cable modem service, the Commission released its *Declaratory Ruling* for the purpose of resolving the status of this service under the Act and determining how to regulate cable modem service, if at all.<sup>64</sup> The Commission stated that three principles guided it in reaching its conclusions: (1) “encourag[ing] the ubiquitous availability of broadband to

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57. See Deployment of Wireline Services Offering Advanced Telecommunications Capability, *First Report and Order and Further Notice of Proposed Rulemaking*, 14 F.C.C.R. 4761 (1999); Deployment of Wireline Services Offering Advanced Telecommunications Capability, *Second Report and Order*, 14 F.C.C.R. 19237 (1999); Deployment of Wireline Services Offering Advanced Telecommunications Capability, *Third Report and Order*, 14 F.C.C.R. 20912 (1999); *Advanced Services Remand Order*, *supra* note 56.

58. *Advanced Services Remand Order*, *supra* note 56, at 388.

59. Telecommunications Act of 1996, Pub. L. No. 104-104, § 706(b), 110 Stat. 56, 153 (1996).

60. See Inquiry Concerning the Deployment of Adv. Telecomm. Capability to All Americans in a Reasonable & Timely Fashion, & Possible Steps to Accelerate Such Deployment Pursuant to Section 706 of the Telecommunications Act of 1996, *Notice of Inquiry*, 13 F.C.C.R. 15280, paras. 4–8 (1998).

61. See *Declaratory Ruling*, *supra* note 4, para. 2.

62. See Inquiry Concerning the Deployment of Advanced Telecommunications Capability to All Americans in a Reasonable and Timely Fashion, and Possible Steps to Accelerate Such Deployment Pursuant to Section 706 of the Telecommunications Act of 1996, *Second Report*, 15 F.C.C.R. 20913 (2000).

63. Inquiry Concerning High-Speed Access to the Internet Over Cable & Other Facilities, *Notice of Inquiry*, 15 F.C.C.R. 19287, para. 1 (2000).

64. See *Declaratory Ruling*, *supra* note 4, para. 1.

all Americans”; (2) allowing “broadband services [to] exist in a minimal regulatory environment that promotes investment and innovation in a competitive market”; and (3) “seek[ing] to create a rational framework for the regulation of competing services that are provided via different technologies and network architectures.”<sup>65</sup>

The Commission devoted a great deal of attention in the *Declaratory Ruling* to the commercial arrangements between and among cable system operators and Internet Service Providers (“ISPs”), noting that some cable operators have historically chosen to make capacity available to unaffiliated ISPs while others have not.<sup>66</sup> The Commission also described the various functions that cable operators often include in their service offerings, such as “protocol conversion, IP address number assignment, domain name resolution through a domain name system (“DNS”), network security, and caching.”<sup>67</sup> After applying the relevant statutory definitions to its understanding of the commercial arrangements for and technical elements of cable modem service, the FCC determined that “cable modem service as currently provided is an interstate information service, not a cable service, and that there is no separate telecommunications service offering to subscribers or ISPs.”<sup>68</sup>

The Commission’s finding that Internet access provided to end-user consumers via cable modem service constitutes an information service did not engender much controversy. Such services clearly consist of more than the “transmission, between or among points specified by the user, of information of the user’s choosing, without change in the form or content of the information as sent and received.”<sup>69</sup> Rather, the DNS services, protocol conversion, and other elements of cable modem service offer a “capability for generating, acquiring, storing, transforming, processing, retrieving, utilizing, or making available information.”<sup>70</sup>

However, the Commission’s determination that cable modem service does not involve a separate offering of telecommunications service was, and is, controversial. With respect to the cable modem service offered to end-user customers, the Commission found that the transmission capacity—the portion of cable modem service that can be considered

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65. *Id.* paras. 4–6.

66. *See generally id.* paras. 15–30 (showing that cable operators such as AOL Time Warner, Comcast, and AT&T had followed a multiple-ISP approach despite greater technical complexities in doing so, while Cox, Charter, and Cablevision each followed a business model involving the use of only one ISP).

67. *Id.* para. 17.

68. *Id.* para. 33.

69. 47 U.S.C. § 153(43) (2000).

70. 47 U.S.C. § 153(20) (2000).

telecommunications—is not separately offered and that this pipe therefore does not meet the statutory definition of telecommunications service.<sup>71</sup> As for the offering of pure transmission capacity on a wholesale basis to unaffiliated ISPs, the Commission noted that the cable operators making such capacity available had decided to deal with particular ISPs on an individual basis and therefore had determined on a case-by-case basis the terms on which they would deal with such ISPs.<sup>72</sup> In light of the FCC's interpretation of telecommunications service as equivalent to a common carrier service—which had been upheld by the U. S. Court of Appeals for the D. C. Circuit—the Commission found that, to the extent cable operators were making transmission capacity available to unaffiliated ISPs, they were not offering it to the public, but rather were doing so on a private carrier basis.<sup>73</sup>

The Commission's conclusion regarding the regulatory classification of cable modem service as provided to subscribers was more consistent with both *Computer II* and the 1996 Act. For example, an enhanced service under *Computer II* necessarily combined a basic service with computer processing.<sup>74</sup> Moreover, the Commission noted that under the 1996 Act, an information service is by definition provided via telecommunications.<sup>75</sup> The decision to classify cable modem service as an information service finds further support in the Commission's previous finding that information services and telecommunications services are mutually exclusive categories, as well as the fact that the Commission had never applied Title II regulation to cable operators.

Alternatively, the Commission's finding that the offering of transmission capacity to unaffiliated ISPs is not a telecommunications service is somewhat more difficult to justify. In many respects, such a service closely resembles the offering of capacity on the network of a wireline carrier. Moreover, there is clearly a tautological element in the Commission's reasoning. The Commission found that cable modem service was not properly classified as a telecommunications service largely due to the fact that the service was not provided on a common carrier basis.<sup>76</sup> In

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71. *Declaratory Ruling*, *supra* note 4, paras. 39–40.

72. *Id.* para. 55.

73. *Id.*; *see also* Virgin Islands Tel. Co. v. FCC, 198 F.3d 921, 926 (D.C. Cir. 1999).

74. *See supra* Part II.A. One distinction between services provided under the *Computer II* rules and cable modem service, which is not trivial, is that the enhanced service provider would not normally be a facilities-based carrier, but would instead lease capacity from AT&T for the purpose of selling value-added services. *See Brand X*, 125 S.Ct. at 2716–17 (Scalia, J., dissenting).

75. *Declaratory Ruling*, *supra* note 4, para. 39 (citations omitted).

76. *See Brand X*, 125 S.Ct. at 2714–18, n.7 (Scalia, J., dissenting).

so doing, the Commission reacted more to the business decisions the cable companies had already made and relationships those companies had already formed, than it focused on whether or not policy considerations warranted imposing Title II regulation on cable operators.

Notwithstanding the above weakness underlying the Commission's reasoning in the *Declaratory Ruling*, there are at least two reasons why the Commission was correct in its result. First, Title II regulation was intended from the beginning to govern traditional, monopolistic, wireline telephone companies. Despite the fact that cable modem service was becoming available on a commercial basis by late 1996,<sup>77</sup> nothing in the 1996 Act suggests that Congress intended to apply common carrier regulation to cable operators. Second, and more importantly, legal precedent enshrines the principle that a service provider is only a common carrier if it either chooses to hold itself out to the public as such or if it is under a legal obligation to do so.<sup>78</sup> Consequently, since the Commission determined that cable operators had not held themselves out to the public as common carriers and also found no legal obligation for cable operators to act as common carriers, it acted consistently with *NARUC I* in reaching its conclusion that transmission capacity for cable modem service is not a telecommunications service because it is not provided on a common carrier basis.<sup>79</sup>

#### IV. *BRAND X* AND IMMEDIATE AFTERMATH

##### A. *The Decisions*

##### 1. Court of Appeals Decision

Brand X Internet Services and other ISPs appealed the *Declaratory Ruling*, arguing that cable modem service comprises both a telecommunications service component and an information service component.<sup>80</sup> A three-judge panel of the Ninth Circuit Court of Appeals agreed with the appellants, finding that the Court's prior interpretation of the 1996 Act controlled its review of the *Declaratory Ruling*.<sup>81</sup>

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77. See Cable Digital News, Cable Modem Info Center, <http://www.cabledigitalnews.com/cmhc/cmhc1.html> (last visited Mar. 14, 2006).

78. See *National Ass'n of Reg. Utils. Comm'rs v. FCC*, 525 F.2d 630, 640 (D.C. Cir.), *superseded by statute as recognized by* 78 F.3d 842 (2d Cir. 1996).

79. See *Declaratory Ruling*, *supra* note 4, para. 55 (explaining the historic distinction between common carriage and private carriage, and finding that AOL Time Warner was "determining on an individual basis whether to deal with any particular ISP and [was] in each case deciding the terms on which it [would] deal with any particular ISP.").

80. *Brand X Internet Servs. v. FCC*, 345 F.3d 1120 (9th Cir. 2003).

81. *Id.* at 1132.

The court of appeals had previously addressed the issue of how to classify cable modem service in *AT&T Corp. v. City of Portland*, which it decided in 2000 in the absence of any definitive FCC pronouncements on the subject.<sup>82</sup> The *Portland* decision addressed the issue of whether local cable franchising boards could require AT&T to provide open access to its broadband facilities as a condition of local approval of the AT&T and TCI merger. The local authorities had premised their actions on the position that cable modem service is a cable service.<sup>83</sup> The court of appeals noted that a cable service under the 1996 Act is a one-way transmission of programming to subscribers generally and found that cable modem service did not fit this description; therefore, local authorities could not directly regulate cable modem service through their franchising authority.<sup>84</sup> The court went on to find that the pipeline provided by the cable modem operators was a telecommunications service and that the Internet access was an information service.<sup>85</sup> Because Section 541(b)(3)(B) of the 1996 Act provides that a franchising authority may not impose any requirement that has the effect of limiting the provision of telecommunications by a cable operator, the court concluded that the local franchise authorities were prohibited from conditioning the franchise transfer on AT&T's provision of open access to its broadband network.<sup>86</sup> In its decision, the court of appeals first described the *Portland* decision in detail and stated that its determination of the proper regulatory classification of cable modem service had been necessary to that decision, so the classification has precedential value.<sup>87</sup> In considering whether the *Declaratory Ruling* had any effect on the validity of its holding in *Portland*, the court noted that only an en banc panel would have the authority to issue a decision that overruled the precedent set in *Portland*.<sup>88</sup>

The court of appeals relied on its 1988 decision *Mesa Verde Construction Co. v. Northern California District Council of Laborers* in addressing the proper weight to give to the FCC's decision.<sup>89</sup> In *Mesa Verde*, the court had held that "if a panel finds that an [agency] interpretation of [its statute] is reasonable and consistent with [the law], the panel may adopt that interpretation even if circuit precedent is to the

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82. *AT&T Corp. v. City of Portland*, 216 F.3d 871 (9th Cir. 2000).

83. *Id.* at 875.

84. *Id.* at 876–77.

85. *Id.* at 878.

86. *See id.* at 878–79.

87. *Brand X*, 345 F.3d at 1130.

88. *Id.*

89. *Id.* (citing *Mesa Verde Construction Co. v. Northern California District Council of Laborers*, 861 F.2d 1124 (9th Cir. 1988)).

contrary.”<sup>90</sup> However, the Court had also qualified the holding in *Mesa Verde* by stating that an earlier panel decision could only be disregarded “where the precedent constituted deferential review of [agency] decisionmaking.”<sup>91</sup> The court in *Portland* was not faced with an agency’s construction of a statute that could require deference under the *Chevron* doctrine.<sup>92</sup> Rather, the court had to interpret what the court considered the plain language of the statute. The *Brand X* court found that *Mesa Verde* did not apply and that the court was therefore bound to follow *Portland*.<sup>93</sup> Accordingly, the court of appeals vacated the FCC’s determination that cable modem service was not a telecommunications service.

## 2. Supreme Court Decision

The Supreme Court released its eagerly anticipated *Brand X* decision in late June 2005. In a 6–3 opinion written by Justice Thomas, the Court disagreed with the Ninth Circuit’s application of the *Chevron* doctrine.<sup>94</sup> The Court overturned the court of appeals decision, holding that the *Declaratory Ruling* was a lawful construction of the 1996 Act under *Chevron* and the Administrative Procedure Act.<sup>95</sup>

The Court first examined the question of whether it should apply the *Chevron* doctrine to its review of the *Declaratory Ruling*. While the court of appeals had found that its interpretation of the 1996 Act in *AT&T Corp. v. City of Portland* trumped the FCC’s later interpretation in the *Declaratory Ruling*, the Court noted that nothing in *Portland* indicated that the court of appeals had found the statute unambiguous.<sup>96</sup> Observing that “*Chevron*’s premise is that it is for agencies, not courts, to fill statutory gaps,” the Court found that the court of appeals had erred in finding that *Portland* foreclosed the FCC from interpreting an ambiguous statute and that the court of appeals should instead have applied a deferential *Chevron* analysis to the *Declaratory Ruling*.<sup>97</sup>

Having determined that the *Chevron* framework applied to its review of the *Declaratory Ruling*, the Court then turned to the two-step procedure established by *Chevron*. The first part of the *Chevron* test is whether Congress has “directly address[ed] the precise question at issue.”<sup>98</sup> In

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90. *Mesa Verde*, 861 F.2d at 1136.

91. *Id.*

92. *Chevron U.S.A., Inc. v. Natural Res. Def. Council, Inc.*, 467 U.S. 837 (1984).

93. *Brand X*, 345 F.3d at 1131.

94. *Brand X*, 125 S.Ct. at 2699–2702.

95. *Id.* at 2695.

96. *Id.* at 2701–02.

97. *Id.* at 2700–01.

98. *Id.* at 2702 (quoting *Chevron*, 467 U.S. at 843).



applying this part of the *Chevron* analysis to the *Declaratory Ruling*, the Court found that “[t]he term ‘offer’ as used in the definition of telecommunications service . . . is ambiguous” because this definition does not clearly indicate whether a company that offers an integrated broadband Internet service is thereby offering a telecommunications service or is merely using telecommunications.<sup>99</sup> The Court looked to the language of the 1996 Act and the ordinary usage of the word “offer” in reaching this conclusion.<sup>100</sup> Further, the Court found that “[t]he Commission’s traditional distinction between basic and enhanced service also supports the conclusion that the Communications Act is ambiguous about whether cable companies ‘offer’ telecommunications with cable modem service” and noted that expanding Title II regulation to cover cable operators would have effected a major shift in Commission policy.<sup>101</sup>

In the second step of the *Chevron* analysis, a court defers to the agency’s interpretation if that construction is “a reasonable policy choice for the agency to make.”<sup>102</sup> The Court found that the Commission had acted reasonably and rejected the two central arguments made by the respondents. First, the Court found that the Commission’s interpretation of the 1996 Act would not allow communications providers to evade common carrier regulation simply by bundling a telecommunications service with an information service, despite the respondents’ arguments to the contrary.<sup>103</sup> The Court also concluded that the Commission had acted reasonably in finding that cable modem service is more than a transparent transmission path from an end-user perspective, and the Court noted the various functions provided by cable operators through a cable modem service, particularly DNS service.<sup>104</sup>

Finally, after completing the above *Chevron* analysis, the Court addressed the issue of whether the Commission’s decision to classify cable modem service differently from DSL service was “arbitrary and

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99. *Brand X*, 125 S.Ct. at 2704 (citations omitted). Justice Scalia strongly disagreed with the majority’s reasoning on this point and in a well-reasoned dissent argued that

[t]he relevant question is whether the individual components in a package being offered still possess sufficient identity to be described as separate objects of the offer, or whether they have been so changed by their combination with the other components that it is no longer reasonable to describe them in that way.

*Id.* at 2714 (Scalia, J. dissenting). However, while Justice Scalia’s argument is persuasive, the fact that nine Supreme Court justices could not agree on the proper interpretation of the 1996 Act in itself supports the notion that the statute is ambiguous.

100. *Id.* at 2704–05.

101. *Id.* at 2706–07 (citations omitted).

102. *Id.* at 2702 (quoting *Chevron*, 467 U.S. at 845).

103. *Id.* at 2708.

104. *Id.* at 2709–10.

capricious” as respondent MCI had argued.<sup>105</sup> The Court stated that “the Commission is free within the limits of reasoned interpretation to change course if it adequately justifies the change.”<sup>106</sup> Finding that the Commission had chosen to classify DSL service as a telecommunications service rather than an information service “based on . . . history, rather than on an analysis of contemporaneous market conditions,”<sup>107</sup> the Court found “nothing arbitrary about the Commission’s providing a fresh analysis” with respect to the cable industry.<sup>108</sup> However, the Court cautioned that it was expressing “no view on how the Commission should, or lawfully may, classify DSL service.”<sup>109</sup>

### B. *The Wireline Broadband Report and Order*

After the Supreme Court released the *Brand X* decision, the Commission immediately turned its attention to the issue of whether DSL service, the primary broadband alternative to cable modem service, also should be classified as an information service. The FCC had tentatively concluded in 2002 that DSL service should be so classified, but had not acted on its *Notice of Proposed Rulemaking*<sup>110</sup> in that proceeding pending resolution of the legal challenges to the *Declaratory Ruling*.<sup>111</sup> In August 2005, the Commission released the *Wireline Broadband Report and Order*, in which it adopted its previous, tentative conclusion that DSL service is appropriately classified as an information service.<sup>112</sup>

The Commission had little difficulty finding that DSL is an “information service.”<sup>113</sup> Specifically, the Commission found that DSL service involves “the offering of a capability for generating, acquiring, storing, transforming, processing, retrieving, utilizing, or making available information via telecommunications . . . .”<sup>114</sup> The Commission had made the same finding in the *Declaratory Ruling*<sup>115</sup> with respect to cable modem service, a conclusion that was not challenged in *Brand X*. As the

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105. *Brand X*, 125 S.Ct. at 2710.

106. *Id.*

107. *Id.* at 2711.

108. *Id.*

109. *Id.*

110. See *Appropriate Framework for Broadband Access to the Internet over Wireline Facilities, Notice of Proposed Rulemaking*, 17 F.C.C.R. 3019 (2002).

111. *Declaratory Ruling*, *supra* note 4.

112. *Wireline Broadband Report and Order*, *supra* note 11.

113. See *id.* paras. 12–17.

114. *Id.* para. 13.

115. See *supra* Part III.C; see also *Declaratory Ruling*, *supra* note 4, at 4821–22; *Brand X*, 125 S.Ct. at 2711 (noting that the Commission’s finding that cable modem service is an “information service” was not challenged).

characteristics of cable modem service that resulted in its classification as an information service are virtually indistinguishable from the characteristics of DSL service from a functional, end-user perspective, it is unlikely that this portion of the *Wireline Broadband Report and Order* will cause much controversy.

However, the key conclusion of the *Wireline Broadband Report and Order* is as controversial, or more so, than the *Declaratory Ruling*. Relying primarily on changed marketplace conditions, most notably the advent of intermodal competition, the Commission held that wireline carriers will no longer be required to “separate out the underlying transmission from wireline broadband Internet access service and offer it on a common carrier basis.”<sup>116</sup> Rather, the Commission concluded that carriers should be able to choose when to offer broadband transmission capacity and have a one-year transition period to decide whether to offer such capacity on a private carrier basis (i.e., not subject to Title II regulation) or as a common carrier.<sup>117</sup> Only in the latter case—where a carrier makes an affirmative choice to offer capacity on a common carrier basis—would the carrier be deemed to be offering telecommunications services.<sup>118</sup>

Interestingly, in reaching the decision that DSL transmission service would only be a telecommunications service to the extent carriers choose to offer it as such, the Commission failed to acknowledge the opposite conclusion it had reached in the *Advanced Services Order* and limited its discussion of that order to a single mention in a footnote.<sup>119</sup> One could easily conclude in reading the *Wireline Broadband Report and Order* that the Commission had never made an affirmative determination that DSL Internet access service is a telecommunications service and that *Brand X* and the *Declaratory Ruling* were the only recent, relevant precedent. The question of whether DSL service includes a separate offering of a telecommunications service is a more complex issue than whether cable modem service includes such an offering and requires a slightly different analysis. Notably, unlike cable operators, it is likely that providers of facilities-based DSL service have “made a stand-alone offering of transmission for a fee . . . to such classes of users as to be effectively

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116. *Wireline Broadband Report and Order*, *supra* note 11, para. 42.

117. *Id.* paras. 86–89.

118. *See id.* para. 90.

119. *See Wireline Broadband Report and Order*, *supra* note 11, para. 12 n.32 (stating that the Commission had “not been entirely consistent” with respect to the question of whether the “categories of ‘information service’ and ‘telecommunications service’ are mutually exclusive” without noting that in the *Advanced Services Memorandum Opinion and Order*, the Commission had in fact found these categories to be mutually exclusive but had also determined that DSL Internet access service consists of two separate services, an information service and a telecommunications service).

available directly to the public.”<sup>120</sup> Further, the wireline carriers that offer DSL service also offer traditional voice service (i.e., telecommunications services) directly to the public *using the same lines*.<sup>121</sup> The Supreme Court summarized the rationale underlying the *Declaratory Ruling* as follows: “[s]een from the consumer’s point of view, the Commission concluded, cable modem service is not a telecommunications offering because the consumer uses the high-speed wire always in connection with the information-processing capabilities provided by Internet access, and because the transmission is a necessary component of Internet access[.]”<sup>122</sup> Significantly, a DSL customer uses the same wire not only for DSL service, but also for voice service.<sup>123</sup>

In the *Wireline Broadband Report and Order*, the Commission did not fully address these distinctions and omitted any indication that in the *Declaratory Ruling* it had deemed the fact significant that cable modem service does not include an offering of telecommunications to ISPs.<sup>124</sup> While the Commission did not expressly indicate that it was giving decisional significance to this fact, one of the primary reasons the Commission gave for its decision in the *Declaratory Ruling* was that cable operators had not made stand-alone offerings of transmission for a fee, either to end users or to “such classes of users as to be effectively available directly to the public.”<sup>125</sup> The latter statement strongly suggested that the offering of capacity to ISPs on a common carrier basis would have entailed a different result (i.e., that cable modem service does include a separate offering of telecommunications service).

Given the high stakes surrounding the struggle for access by ISPs and competitive local exchange carriers (“LECs”) to incumbent LECs’

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120. See *Declaratory Ruling*, *supra* note 4, para. 40 (stating that the Commission is not aware of any cable modem service provider that has charged a transmission fee).

121. See, e.g., Verizon Web site, Frequently Asked Questions – DSL, at Technology 1–5, <http://www22.verizon.com/forhomedsl/channels/dsl/learnmore/faqs/> (last visited Mar. 14, 2006).

122. *Brand X*, 125 S.Ct. at 2703 (citing *Declaratory Ruling*, *supra* note 4, para. 39). The accuracy of this statement is debatable at best: a consumer uses the same “high-speed wire” for cable service as for cable modem service. In fact, a cable customer who elects not to purchase cable modem service at all, but whose cable system has been upgraded to allow the offering of such service, would *never* use this high-speed wire in connection with the information-processing capabilities provided by Internet access service.

123. Admittedly, one could argue that the “high-speed wire” in the DSL context includes only the high-frequency portion of the loop. However, as noted, the consumer uses the same physical wire for both DSL and traditional voice services. Further, consumers whose local loops have been conditioned to allow the provision of DSL, but choose not to subscribe to this service, use the line only for the transmission of telecommunications services.

124. *Declaratory Ruling*, *supra* note 4, para. 48.

125. See *id.* para. 40.

broadband facilities, it is all but certain that the *Wireline Broadband Report and Order* will be challenged in court. The Commission, apparently contemplating such a possibility, stated that it “is free to modify its own rules at any time to take into account changed circumstances.”<sup>126</sup> However, a court may set aside such an action upon a finding that the agency acted in a manner that was “arbitrary, capricious, an abuse of discretion, or otherwise not in accordance with law.”<sup>127</sup> When an agency changes an existing policy, it must “supply a reasoned analysis for the change beyond that which may be required when an agency does not act in the first instance.”<sup>128</sup> The parties that appeal the *Wireline Broadband Report and Order* will likely argue that the Commission failed to engage in reasoned decision making because it failed even to mention its previous classification of DSL services, much less provide evidence of the changes since 1999 that necessitated a change in course. Such arguments are not without merit.

The Commission chose not to exercise its forbearance authority under Section 10 of the 1996 Act, expressing confidence in its decision to reclassify DSL services.<sup>129</sup> Had the Commission elected to do so, it could have forborne from exercising Title II regulation on DSL services upon a finding that:

- (1) enforcement of such regulation or provision is not necessary to ensure that the charges, practices, classifications, or regulations by, for, or in connection with that telecommunications carrier or telecommunications service are just and reasonable and are not unjustly or unreasonably discriminatory;
- (2) enforcement of such regulation or provision is not necessary for the protection of consumers; and
- (3) forbearance from applying such provision or regulation is consistent with the public interest.<sup>130</sup>

Given the Commission’s previous decision in the *Advanced Services Memorandum Opinion and Order*, together with its apparent reluctance to acknowledge, much less explain, its change of course, a decision to forbear from exercising Title II regulation on DSL services arguably could have

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126. *Wireline Broadband Report and Order*, *supra* note 11, para. 81 (citing *Brand X*, 125 S.Ct. at 2699).

127. *Motor Vehicle Mfrs. Ass’n, Inc., v. State Farm Mut. Auto. Ins. Co.*, 463 U.S. 29, 41 (1983) (quoting 5 U.S.C. § 706(2)(A)).

128. *Id.* at 42.

129. *Wireline Broadband Report and Order*, *supra* note 11, paras. 81–82; *see also* 47 U.S.C. § 160 (2000). Note that the Commission did elect to forbear from imposing tariff requirements on those carriers that choose to offer DSL-based transmission capacity on a common carrier basis. *Wireline Broadband Report and Order*, *supra* note 11, paras. 91–94.

130. 47 U.S.C. § 160(a)(1)–(3) (2000).

been a safer approach in some respects. If the *Wireline Broadband Report and Order* is reversed on appeal, the Commission may wish to consider developing a record concerning the extent to which intermodal competition exists, particularly with respect to emerging technologies. Significantly, if the Commission determines that robust intermodal competition exists in the market for broadband services, it arguably could find that incumbent LECs are not required to offer identical prices for DSL transmission capacity to unaffiliated competitive LECs or ISPs. Notably, nothing in the Act prohibits price discrimination by common carriers, only “unjust or unreasonable” discrimination.<sup>131</sup> Since the FCC’s primary goal is to protect consumers, not competitors, one could argue that price discrimination is not unjustly or unreasonably discriminatory if such practices have no adverse impact on consumers due to the availability of competing forms of broadband Internet access. Other issues to consider in a forbearance analysis would include the extent to which incumbent LECs can be shown to have deferred investment due to regulatory considerations and economic analyses of requirements, such as interconnection and universal service contribution on the respective market shares of DSL service providers and cable modem service providers.

Whichever course of action the Commission takes regarding DSL, and regardless of whether or not the *Wireline Broadband Report and Order* is affirmed on appeal, the FCC will need to be mindful of the possibility that, as more and more services migrate to an Internet protocol-based platform, certain services it currently regulates as telecommunications services, particularly voice services, will likely one day be reduced to mere applications provided as part of a DSL package. As the Commission has already determined that the information service and telecommunications service elements of DSL are inseparable, it will be hard-pressed to develop a reasoned explanation of why an application riding on the network can be separated and regulated. Such convergence would undoubtedly strain the already burdened universal service mechanism past its breaking point and will also raise important issues in other areas of regulation, such as disability access.

### C. *The Ensign Bill*

On July 27, 2005, exactly one month after the Supreme Court decided *Brand X*, Senator John Ensign of Nevada introduced a bill “[t]o establish a market driven telecommunications marketplace, to eliminate government managed competition of existing communication service, and to provide

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131. 47 U.S.C. § 202(a) (2000).

parity between functionally equivalent services.”<sup>132</sup> While published reports suggest that the bill is not likely to pass,<sup>133</sup> its proposed elimination of the distinction between Title I and Title II services may foreshadow the direction of future legislation.

In the Ensign Bill, Basic Telephone Service (“BTS”) would retain a distinct regulatory classification. BTS would include single-line, flat-rate voice services within a local calling area, with access to 911, with touch-tone dialing, and with access to long distance.<sup>134</sup> The definition of BTS would exclude interexchange wireline service.<sup>135</sup>

The Ensign Bill would create a new category of service, a “communications service,” defined as:

any service enabling an end user to transmit, receive, store, forward, retrieve, modify, or obtain, voice, data, image, or video communications using any technology, including—(i) copper; (ii) coaxial cable; (iii) optical fiber; (iv) terrestrial fixed wireless; (v) terrestrial mobile wireless; (vi) satellite; (vii) power lines; or (viii) successor technologies; and . . . does not include (i) television or radio broadcasting; and (ii) any service that is not provided to the public or to a substantial portion of the public.<sup>136</sup>

The bill defines “broadband communications service” as a communications service with a capacity of greater than 64 kilobits per second.<sup>137</sup>

The new term “communications service” would essentially collapse the categories of “telecommunications service” and “information service” into a single category. Such services would be subject only to regulation in areas such as consumer protection, E911, consumer proprietary network information, access for persons with disabilities.<sup>138</sup> Notably, this would result in some additional regulation on services such as voice over Internet protocol even as the regulatory burden is reduced for traditional, circuit-switched voice services. This would help reduce the opportunities for regulatory arbitrage under the current regulatory scheme as noted above in Part IV.B.

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132. S. 1504, 109th Cong. Preamble (2005) [hereinafter *Ensign Bill*].

133. COMM. DAILY, Aug. 30, 2005, at 9.

134. *Ensign Bill*, *supra* note 132, § 4(a)(1).

135. *Id.*

136. *Id.* § 4(a)(4).

137. *Id.* § 4(a)(2). Other parties will undoubtedly comment upon the curious definition of broadband as anything above 64 kbps in what is otherwise a forward-thinking piece of legislation.

138. *Id.* § 8(a).

## V. CONCLUSION

As described in this Article, radical changes in communications technologies and the competitive environment over the past forty years have forced the Commission to rethink the manner in which it distinguishes between traditional, common carrier transmission services and newer applications that make use of such services. The *Declaratory Ruling* marked a conscious decision to refrain from imposing legacy economic regulation on new services that bore considerable resemblances to those services provided by the former monopoly carriers. Following the Supreme Court's affirmance of the *Declaratory Ruling* in *Brand X*, the Commission made a well-intentioned, but perhaps legally flawed, effort to level the playing field for similar services provided over different platforms. While some defenders of the *Wireline Broadband Report and Order* contend that this order promotes greater certainty for incumbent LECs, the great irony is that these carriers will likely face more uncertainty over the coming months, or years, in which the inevitable litigation surrounding this order runs its course. Looking forward, it is essential that the FCC and Congress both act in a manner that is even-handed and promotes competition, but also creates certainty for service providers while protecting consumers and advancing important social goals such as continued affordability of basic telephone service.



# Spread Spectrum Is Good—But it Does Not Obsolete *NBC v. U.S.*!

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## I. INTRODUCTION

This short Article addresses a popular misconception—that new technologies such as spread spectrum have eliminated the problem of radio interference. That is false. Spread spectrum is a great technology, but it does not eliminate the problem of interference. Similarly, although some have asserted otherwise, signals below the noise floor can create interference.

We first show that a number of authors have embraced these misconceptions in works addressing public policy—unfortunately, we are not attacking a strawman. Simplifying these authors' views somewhat, they argue technology has eliminated the problem of interference; therefore, the legal rationale for radio regulation under the Communications Act of 1934, affirmed in the 1943 *NBC* case,<sup>1</sup> must be reconsidered. On such reconsideration, the First Amendment trumps an obsolete theory of interference; therefore, the fundamental structure of the Communications Act of 1934 is invalid.

We then provide a nonrigorous (no equations!) explanation of the nature of interference created by spread spectrum signals or by signals below the noise floor. We also offer a few pointers to the technical literature for those who wish to understand these issues in more depth.

## II. PURPOSE AND APOLOGY

Scientific discoveries and technologies sometimes gain a cachet out of proportion to their value. Their names become buzzwords—and they are called on to explain problems far beyond their reach. Google the phrase *chaos theory* together with the word *politics* or Google the terms *quantum* and *finance*, and you will find a host of articles and Web pages that stretch the fabric of science far beyond its elastic limit.<sup>2</sup> Some authors merely use the science as simile, but others claim that the relevant science supports their analysis of politics, finance, or movie criticism.

A recent example of this phenomenon has occurred in telecommunications policy discussions in which analysts claim that new

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1. *NBC v. United States*, 319 U.S. 190 (1943).

2. We note that such overreaching papers are sometimes written by engineers. Back when information theory was a hot new topic, a famous editorial by Peter Elias lamented the repeated appearance of the generic paper *Information Theory, Photosynthesis, and Religion*, which “discusses the surprisingly close relationship between the vocabulary and conceptual framework of information theory and that of psychology (or genetics, or linguistics, or psychiatry, or business organization)” and suggested that the authors “give up larceny for a life of honest toil.” Peter Elias, *Two Famous Papers*, 4 IRE TRANSACTIONS ON INFO. THEORY 99, 99 (1958).

technology has solved the problems of radio interference.<sup>3</sup> Such claims have appeared in both the popular press and in academic journals.<sup>4</sup> The purpose of this Article is to examine two such claims and to match those claims with what we understand to be the capabilities of the technology. It is not our purpose here to engage in a discussion of spectrum policy—we (the Authors, collectively and individually) may agree with some of the policies advanced by these authors and disagree with others—rather, our purpose is to examine assertions regarding technology and to put those assertions into perspective.<sup>5</sup>

These technological claims are then used as the basis for arguing that the policy goals and legal basis of the Communications Act of 1934 are no longer valid.<sup>6</sup> For example, Benkler and Lessig state:

If the engineers are right—if the efficiency of an architecture of spread-spectrum wireless technology were even roughly equivalent to the architecture of allocated spectrum—then much of the present broadcasting architecture would be rendered unconstitutional. If shared spectrum is possible, in other words, then the First Amendment would mean that allocated spectrum—whether licensed or auctioned—must go.<sup>7</sup>

The Communications Act of 1934<sup>8</sup> incorporates large parts of the Radio Act of 1927<sup>9</sup> and, albeit amended many times, still governs use of the radio spectrum in the United States. The Supreme Court upheld the constitutionality of the Communications Act in *NBC*.<sup>10</sup> Justice Frankfurter, writing for the majority, upheld the challenged regulations and noted that interference justified regulation, “[u]nlike other modes of expression, radio

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3. Succinctly stated, interference occurs when one radio transmission impairs the reception of a second transmission. Properly defining *interference* and *harmful interference* can be a difficult task—one as rooted in economics and tort law as engineering. For the purposes of this Article, we assume that the reader will follow Justice Stewart’s approach to definitional issues and supply the definition he or she finds appropriate. Cf. *Jacobellis v. Ohio*, 378 U.S. 184, 197 (1963) (Stewart, J., concurring) (noting that despite the near impossible task of defining “hard-core pornography” he “[knew] it when [he] [saw] it”). For a discussion of interference, see generally R. Paul Margie, *Can You Hear Me Now?*, 2003 STAN. TECH. L. REV. 5, [http://stlr.stanford.edu/STLR/Articles/03\\_STLR\\_5/article\\_pdf.pdf](http://stlr.stanford.edu/STLR/Articles/03_STLR_5/article_pdf.pdf).

4. See *infra* Parts III.A and III.B.

5. Although we argue that some policy recommendations are based on reasoning from faulty premises, we acknowledge that those recommendations may, nonetheless, be valid.

6. Of course, there are attacks on the viability of NBC based on theories other than spread spectrum is like a magic pixie dust. See, e.g., Stuart Benjamin, *The Logic of Scarcity: Idle Spectrum as a First Amendment Violation*, 52 DUKE L.J. 1 (2002).

7. Yochai Benkler & Lawrence Lessig, *Net Gains: Will Technology Make CBS Unconstitutional?*, THE NEW REPUBLIC, Dec. 14, 1998 at 12, 14.

8. Communications Act of 1934, ch. 652, 48 Stat. 1064 (1934) (codified as amended in various sections of 47 U.S.C.).

9. Radio Act of 1927, ch. 169, 44 Stat. 1162 (1927), repealed by Communications Act of 1934, ch. 652, § 602(a), 48 Stat. 1064, 1102 (1934).

10. 319 U.S. 190.

inherently is not available to all. That is its unique characteristic, and that is why, unlike other modes of expression, it is subject to governmental regulation. Because it cannot be used by all, some who wish to use it must be denied.”<sup>11</sup> In dissent, Justice Murphy agreed with Justice Frankfurter on interference as the justification for regulation, “[o]wing to its physical characteristics radio, unlike the other methods of conveying information, must be regulated and rationed by the government. Otherwise there would be chaos, and radio’s usefulness would be largely destroyed.”<sup>12</sup>

Both the majority and the dissent in *NBC* accepted interference as the justification for regulation—that was not in debate. But, if spread spectrum eliminates interference, then that predicate is wrong.

We note that we hold in high regard many of the authors whose works are considered below and, if it were possible, would omit their names from our analysis. Unfortunately, it is hard to cite an article properly without using the author’s name.

We use the following approach. We state a proposition and follow that proposition with quotations from multiple sources showing how individual authors have expressed and accepted that proposition. We then analyze that proposition from the point of view of communications engineering. Our analysis is intended to be accessible—not mathematical. There are no equations, and mathematical jargon has been relegated to the footnotes.

### III. ANALYSIS

#### A. *Assertion One: Spread Spectrum Eliminates Interference*

This assertion appears in various forms in many publications. Below are several instances of this assertion.

- CDMA [a spread spectrum technology] modulation schemes *allow you to use spectrum without interfering* with others.<sup>13</sup>
- A variety of techniques, some dating back to the 1940s, allow two or more transmitters to coexist on the same frequency. The best-known of these is spread-spectrum. . . . The practical consequence is that no government regulator or property owner need decide which signal is entitled to use the frequency; *both of them can use it simultaneously*.<sup>14</sup>

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11. *Id.* at 226.

12. *Id.* at 228 (Murphy, J., dissenting).

13. George Gilder, *Telecosm: “Auctioning the Airwaves,”* FORBES ASAP, Apr. 11, 1994, at 99, 112 (emphasis added).

14. Kevin Werbach, *Supercommons: Toward a Unified Theory of Communications*, 82

- [N]ew technological developments, such as spread spectrum and ultra-wideband radio, make it possible for many users to use the same broad swath of spectrum simultaneously *without interference*.<sup>15</sup>
- The spread spectrum transmissions of multiple users occupy the same frequency band, but are treated by each other as manageable noise, *not as interference* that causes degradation of reception.<sup>16</sup>
- But the most important implication of spread spectrum technology for regulatory purposes is that it allows many users to use the same band of frequencies simultaneously. Because every signal is noise-like, the signal of each user is, to all the others, just part of the background noise. *The receiver ignores all signals but the one chosen for reception*, and “receives”—translates into humanly intelligible form—only those noise-like transmissions that carry the intended signal.<sup>17</sup>
- Using a variety of strategies, mostly known as spread spectrum, researchers in wireless technology have begun to demonstrate the viability of systems that allow many users to share the same slice of spectrum *without interfering* with one another.<sup>18</sup>
- *The problem of interference*, as real and serious as it was, like the problem of recouping the non-zero marginal cost of the book, *went away*.<sup>19</sup>
- With spread spectrum, a transmission is disassembled and sent out over a variety of frequencies, *without causing interference* to whatever else might be operating within those frequencies, and is reassembled on the other end . . . .<sup>20</sup>
- *With spread spectrum technologies, spectrum would not need to be allocated*, in the sense of giving one person an exclusive right to the

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TEX. L. REV. 863, 874 (2004) (emphasis added).

15. Stuart Buck, *Replacing Spectrum Auctions with a Spectrum Commons*, 2002 STAN. TECH. L. REV. 2, ¶ 6, [http://stlr.stanford.edu/STLR/Articles/02\\_STLR\\_2/article\\_pdf.pdf](http://stlr.stanford.edu/STLR/Articles/02_STLR_2/article_pdf.pdf) (emphasis added).

16. Yochai Benkler, *Overcoming Agoraphobia: Building the Commons of the Digitally Networked Environment*, 11 HARV. J.L. & TECH. 287, 324 (1997) (emphasis added).

17. *Id.* at 396 (emphasis added).

18. Benkler & Lessig, *supra* note 7, at 14 (emphasis added).

19. Eben Moglen, *Freeing the Mind: Free Software and the Death of Proprietary Culture*, Keynote Address at the University of Maine Law School’s Fourth Annual Technology and Law Conference, 13 (June 29, 2003), <http://moglen.law.columbia.edu/publications/maine-speech.pdf> (emphasis added).

20. Jesse Sunenblick, *Into the Great Wide Open*, COLUM. JOURNALISM REV. Mar.–Apr. 2005, at 44, 46 (emphasis added).

detriment of all others. With spread spectrum, broad swaths of the radio spectrum could be available for any to use, so long as they were using an approved broadcasting device. Spectrum would become a commons, and its use would be limited to those who had the proper, or licensed, equipment.<sup>21</sup>

These quotations came from *Forbes*, *Columbia Journalism Review*, *The New Republic*, three law review articles, and speeches by the authors. Those authors include professors at Stanford, New York University, Columbia, and the University of Pennsylvania. Another author is a practicing attorney who was a member of the *Harvard Law Review* and clerked for two federal circuit court judges.

Unfortunately, the fundamental assertion is incorrect. Actually, spread spectrum does not eliminate interference; rather, it changes the nature of interference.

Aquinas regarded arguments based on authority as the weakest form of proof.<sup>22</sup> Nevertheless, arguments regarding spread spectrum put forth by engineering experts would seem to carry more weight than those of the legal experts cited above. The reader can judge whether our contention that spread spectrum does not eliminate interference carries any weight. Others with substantial credentials support that same view. Consider Professor Andrew Viterbi, the Presidential Chair Professor in the Electrical Engineering Department at the University of Southern California and a member of both the National Academy of Engineering and the National Academy of Science. Viterbi explains the effect of spread spectrum on interference, saying: “[T]he main thrust of spread spectrum CDMA is to render the interference from all users and all cells, sharing the same spectrum, as benign as possible.”<sup>23</sup>

Professor James Spilker, Jr., Consulting Professor in the Electrical Engineering and Aeronautics and Astronautics Departments at Stanford University and a member of the National Academy of Engineering, summarizes spread spectrum well, saying:

It is often desired to provide a method by which multiple signals can simultaneously access exactly the same frequency channel with minimal interference between them. Spread spectrum signaling has the capability to provide a form of multiple access signaling called code division multiple access (CDMA) wherein multiple signals can be

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21. Lawrence Lessig, Code and the Commons, Keynote Address at Fordham Law School: Media Convergence, 7 (Feb. 9, 1999), <http://www.lessig.org/content/articles/works/Fordham.pdf> (emphasis added).

22. “Nam, locus ab auctoritate est infirmissimus.” THOMAS AQUINAS, SUMMA THEOLOGIAE, I<sup>a</sup> Q. 1, 8, available at <http://www.corpusthomicum.org/sth1001.html>.

23. Andrew J. Viterbi, *The Orthogonal-Random Waveform Dichotomy for Digital Mobile Personal Communications*, IEEE PERS. COMM., First Qtr. 1994, at 18.

*transmitted in exactly the same frequency channel with limited interference between users, if the total number of user signals  $M$  is not too large.*<sup>24</sup>

Let us back up a little, provide some background, and explain why spread spectrum does not eliminate interference. Spread spectrum is the name for a class of methods for impressing or modulating information on radio signals.<sup>25</sup> Spread spectrum has many advantages over earlier methods for transmitting information over radio such as AM and FM. A key advantage is that in many circumstances it is better at resisting interference than systems using most other radio modulation technologies. Depending on the circumstances, spread spectrum transmissions may generate either more or less interference to other communications systems than would modulation methods such as AM or FM.

An example may illustrate some of these properties. Consider a simplified world of radio communications in which there is a block of spectrum divided into ten radio channels. The radio channels are used for one-way communications from multiple groups of climbers communicating with their base camps in the valley below as illustrated in Figure 1. This example is constructed to remove some technical complications—e.g., all the transmitters are roughly equidistant from all the receivers. One can think of these radio channels as being 25 kHz blocks of spectrum. Communication using multiple individual frequency channels is defined as Frequency-Division Multiplexing (“FDM”),<sup>26</sup> and the process of accessing these channels is called Frequency-Division Multiple Access (“FDMA”).<sup>27</sup> An ideal frequency division multiplex system would permit a user to operate on any one of the ten channels without causing interference to users on the other nine channels. But, if two users tried to use a specific channel at the same time, the receivers in the valley would not be able to separate one signal from the other and interference would result.<sup>28</sup>

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24. 1 GLOBAL POSITIONING SYSTEM: THEORY AND APPLICATIONS 62 (Bradford W. Parkinson & James J. Spilker Jr., eds., 1996).

25. For an older, but still excellent, introduction to spread spectrum see Raymond L. Pickholtz, Donald L. Schilling & Laurence B. Milstein, *Theory of Spread-Spectrum Communications—A Tutorial*, 30 IEEE TRANS. ON COMM. 855 (1982), <http://mail.com.nthu.edu.tw/~jmwu/com5195/Schilling-DSSS-tutorial.pdf>.

26. ATIS Committee T1A1, ATIS Telecom Dictionary, frequency-division multiplexing (FDM), <http://www.atis.org/tg2k/> (scroll to frequency-division multiplexing (FDM), <http://www.networkdictionary.com/telecom/fdm.php> (last visited Mar. 23, 2006).

27. ATIS Committee T1A1, ATIS Telecom Dictionary, frequency-division multiple access (FDMA), <http://www.atis.org/tg2k/> (scroll to frequency-division multiple access (FDMA)), <http://www.networkdictionary.com/telecom/fdm.php> (last visited Mar. 23, 2006).

28. Recall that this is an idealized system. In the real world, the use of adjacent FDM channels often causes interference because real-world receivers cannot perfectly reject signals in adjacent channels.

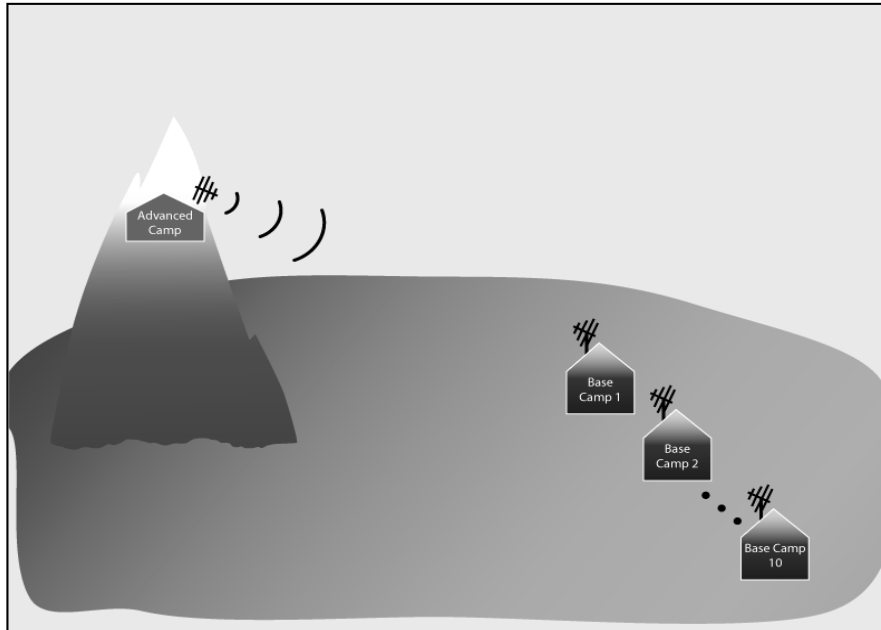
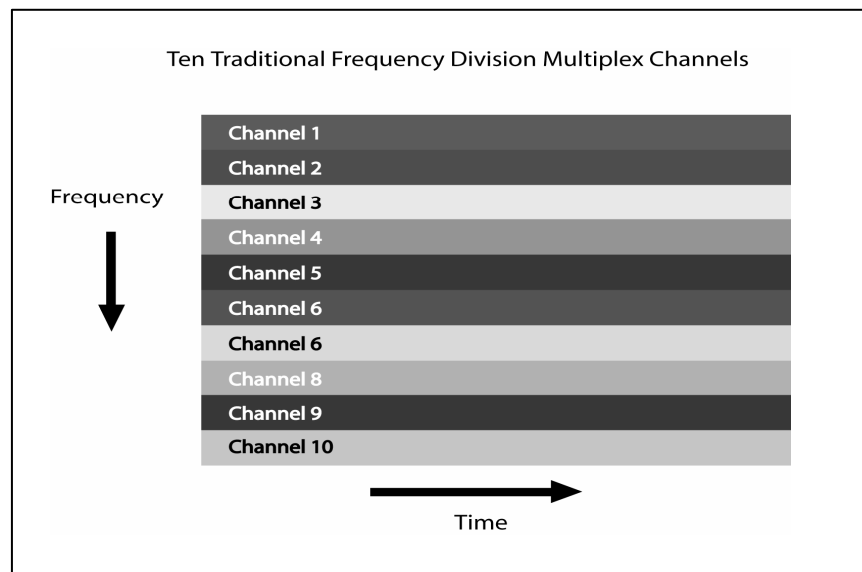
**Figure 1:** The Hypothetical Communications World**Figure 2:** Ten Separate Frequency Division Channels

Figure 2 shows the ten channels as a region or range of frequencies devoted to one use over time. Channel 1 is shown by the bar across the top of the figure.



In this technology, signals are not spread—rather, each signal occupies just the bandwidth it needs. Interference is a purely zero-one affair. If two users try to transmit on the same channel at the same time, each receives interference that makes the channel unusable. If two users transmit on different channels at the same time, there is no interference.

Figure 3 illustrates a hypothetical spread spectrum signal corresponding to the Channel 1 signal of the Figure 2 above. The intense signal that filled Channel 1 is now a weaker signal that covers all ten channels. The transmitted energy is scattered in both time and frequency in what appears to be a random fashion in accordance with what is called a spreading code. The process of multiplexing many signals on the same block of radio spectrum by using separate spreading codes for each user is called Code-Division Multiple Access (“CDMA”).

**Figure 3:** A Representation of a Spread Spectrum Signal

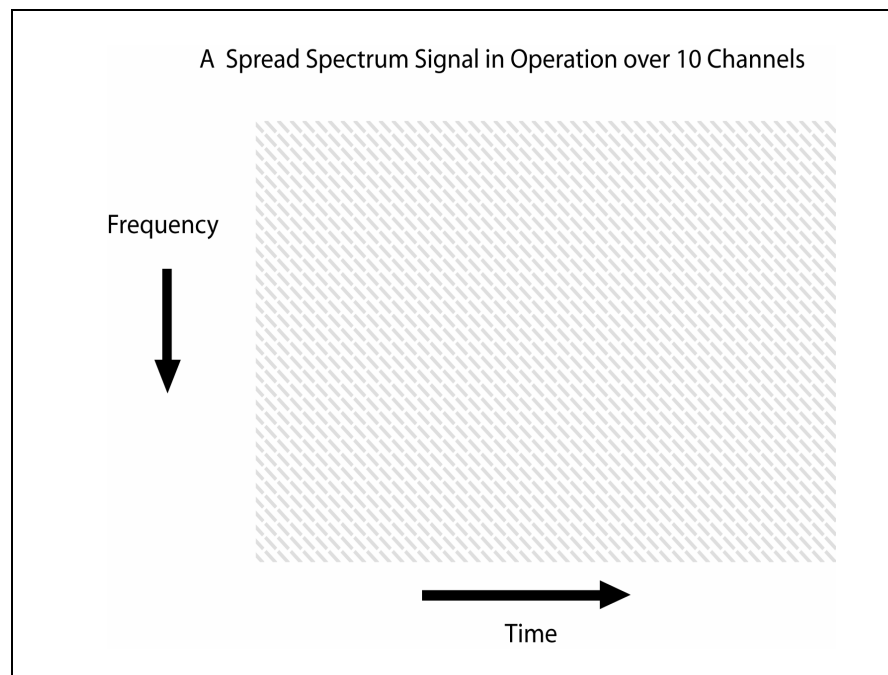


Figure 4 illustrates a different spread spectrum signal occupying all ten channels.

**Figure 4:** Representation of a Second Spread Spectrum Signal

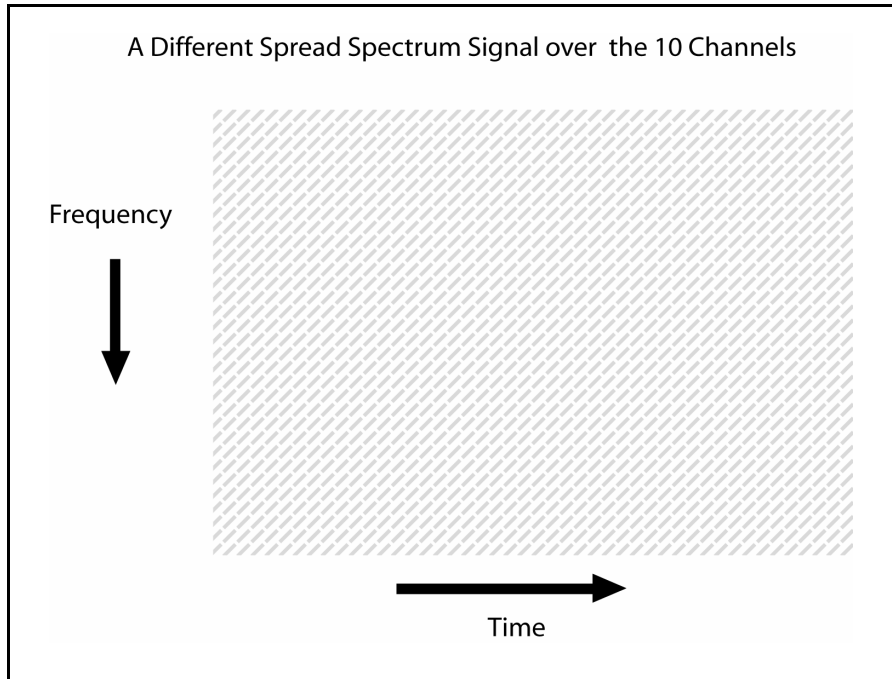
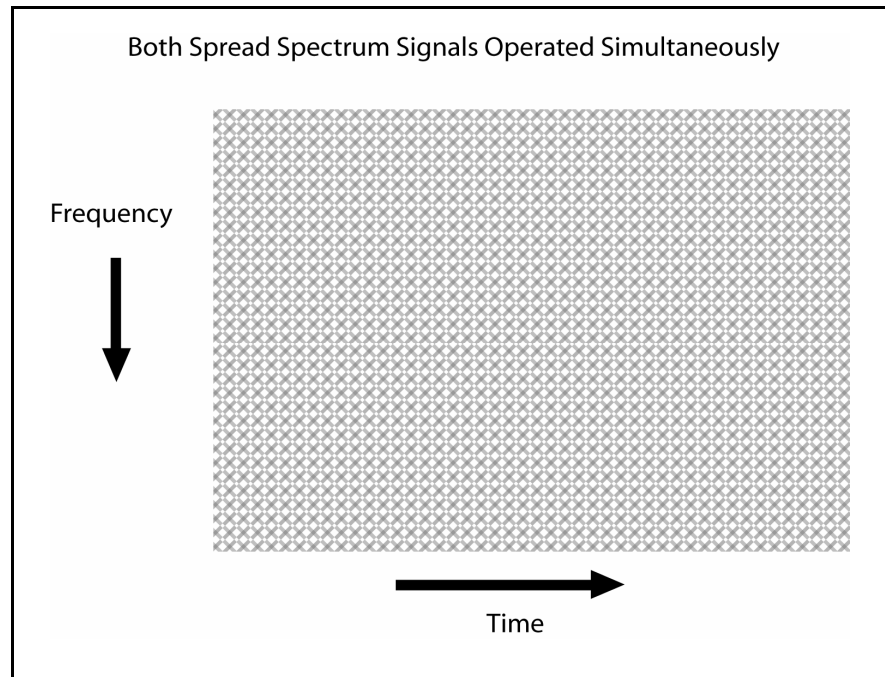


Figure 5 illustrates the operation of both spread spectrum signals simultaneously.

**Figure 5:** Representation of Two Spread Spectrum Signals



Those signals overlap in time and space. If one examines any small range of frequencies over a short period of time, one will find parts of both spread spectrum signals. However, the proper receiver can distinguish one spread spectrum signal from the other *sufficiently well*, making effective communication possible. Unlike the case with the earlier frequency-division channels, the receiver for one spread spectrum signal responds slightly to the other spread spectrum signal.<sup>29</sup> So, a spread spectrum system

29. Two caveats should be added here. First, recall that the perfect rejection of the adjacent channel signals in FDMA depended upon an ideal system. However, even in an ideal CDMA system, a receiver for one spreading code will respond (slightly) to a signal sent with a different spreading code. Second, there are some CDMA systems in which a receiver can perfectly separate two signals—such CDMA signals are as separate as the ten frequency-division multiplex channels considered above. But, there is no free lunch. If there is space for only ten frequency-division channels, there will be space for only ten perfectly separate CDMA signals with the same capacity. The sampling theorem shows that a waveform of bandwidth  $W$  and duration  $T$  has only  $2WT$  degrees of freedom. A system that uses ten orthogonal wideband spread spectrum signals puts one tenth of these degrees of

such as this could work acceptably if two or three users were operating. But, each additional user would increase the interference to all other active users. At some point, perhaps at about four to six users, interference would become so great that all users would lose service.

At this point, the nonengineering reader is probably willing to throw up his or her hands and ask, "What is the point of all this? You started with an ideal system that had no interference and replaced it with a system that has inescapable interference and supports fewer communications than were possible before!" The answer is that the utility of spread spectrum depends on the problem one is trying to solve. Assume that there are twenty groups of climbers on the mountain—more climbers than channels. Assume also that the climbers cannot coordinate channel use with one another or determine when another climbing party is using a channel, and only need to send requests back to their base camp occasionally—an average of two minutes per hour for each party. In the world with ten channels with zero-one interference, a climbing party would have to pick one of the ten channels, transmit their message, and hope that no other party was using that channel. In the spread spectrum world, there is an alternative solution. Each of the twenty climbing parties could be given a different spreading code and would use their individual code when transmitting. As long as no more than four or five climbing parties transmit at the same time, the mutual interference is low and all the messages are received. But, under these assumptions it is highly unlikely that more than four climbing parties will choose to transmit at the same time. This spread spectrum system provides efficient distributed access to a range of frequencies.<sup>30</sup> In the real world with pools of thousands of channels and millions of occasional users, the benefits of such distributed access would be even greater.

Of course, this example is an oversimplification—real-world applications include many other factors. One important factor is distance separation. In this example, the climbing parties were all roughly equidistant from the base camps. But, if one user were substantially closer to the base camps than were the others, that user's signal would be substantially stronger—consequently that user's signal would create more

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freedom into each spreading code. See JOHN G. PROAKIS, *DIGITAL COMMUNICATIONS* 160–68 (4th ed. 2001).

30. A rough calculation shows that in this example interference is approximately 100 times less likely with the CDMA system than with the traditional FDMA channels. This example parallels the data link in the Global Positioning System ("GPS") navigational satellite system in which each satellite uses a different spreading code to transmit its signal. The GPS data link works well with a dozen satellites in view by a receiver at any one time. But, the data link would fail if there were 200 satellites in view—mutual interference would overwhelm the desired signals. An excellent explanation of the GPS signaling system is the two-volume text (roughly 1400 pages) edited by Parkinson and Spikler. *GLOBAL POSITIONING SYSTEM*, *supra* note 24.

interference to other users. In a situation in which such near-far problems abound, the older separate channel system may be a preferable technology.<sup>31</sup>

In some circumstances, spread spectrum systems can share radio channels with older technologies without receiving or causing harmful interference. But, such sharing does not happen automatically. Rather, one must analyze the systems involved, calculate the performance impairments, and determine the highest power level at which the spread spectrum system can operate without creating unacceptable impairments. In 1991, Schilling and his coauthors provided an example of such a calculation and measurements.<sup>32</sup> They showed that a personal radio service, similar to today's Personal Communications Service ("PCS") that used wideband

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31. Real-world FDMA systems also suffer from this near-far problem—though usually not as severely as do CDMA systems. FDMA may be considered as an *orthogonal* multiple access technique for stationary communications so that, in theory, there is no interference (cross correlation is zero). The same can be said with orthogonal, direct sequence spread spectrum (e.g., Walsh codes) CDMA when there is no multipath (echoes or ghosts on the radio path). Multipath will deorthogonalize Walsh (or other orthogonal sequences), and Doppler spread will deorthogonalize FDMA signals. Doppler spread occurs when transmitters and receivers move relative to one another thereby shifting the received frequency slightly from the transmitted frequency. The two schemes are mathematical duals—by dual we refer to mathematical systems with symmetries that permit substituting one variable for another. See the discussion in the reference by Viterbi, *supra* note 23. For a discussion of time-frequency dualities, see Phillip Bello, *Time-frequency duality*, 10 IEEE TRANS. ON INF. THEORY 18–33 (1964). That is why, for highly time dispersive (e.g., multipath) channels with little or no Doppler spread, Orthogonal Frequency Division Multiplexing ("OFDM") performs well (the new IEEE 802.11g wireless Local Access Network ("LAN") standard takes advantage of this property). The tradeoff is that narrow subbands make multipath effects and InterSymbol Interference ("ISI") negligible. But, if the subbands are too narrow, Doppler spread deorthogonalizes the subbands and you get the dual of ISI—adjacent channel interference. Some respectable people now assert that they can get substantial capacity increases using coded OFDM. When one looks at it this way, there is both mutual Multiple Access Interference ("MAI") and Gaussian noise. Traditional thinking was that we want to eliminate MAI by first orthogonalizing and then working just above the noise floor (strictly speaking, at the lowest ratio of energy-per-bit to the noise density  $[E_b/N_0]$  as allowed by coding) in each "channel." This is the case in FDMA—a subdivision of spectrum so that each user gets a piece of "private" spectrum, if only for the allocation period. First generation IS-95 CDMA took a different philosophy by operating at the lowest  $E_b/(N_0+M*I_0)$ , where  $I_0$  is the MAI power density per user and  $M$  is the number of active, equally power-controlled users. As  $M$  gets large,  $N_0$  is no longer the floor; so first-generation CDMA is best thought of as an *interference-sharing* scheme. For larger spreading,  $I_0$  is reduced and you can allow more users—but you need more bandwidth to accommodate the increased spreading. CDMA also easily takes advantage of voice activity and actually uses the multipath to improve the Signal-to-Noise Ratio ("SNR") by diversity combining. Modern, 3G CDMA (e.g., cdma2000) uses more sophisticated coding but also allows for interference cancellation, i.e., MAI or Multi-User Detection ("MUD"), or space-time coding, each of which reduces the effective  $I_0$ .

32. Donald L. Schilling et al., *Broadband CDMA for Personal Communications Systems*, IEEE COMM. MAG., Nov. 1991, at 86–93.

spread spectrum could share spectrum with the microwave radio systems that were then in the 2 GHz band.<sup>33</sup> But this showing was conditional on the spread spectrum handsets not transmitting at powers above one thousandth of a watt and the acceptance of the authors' definition of impairment.<sup>34</sup> Alternatively, one could say that they showed that a personal radio service with handset power above one thousandth of a watt would create interference. They also calculated total system capacity (the number of mobile units that could be supported in a given region) taking into account the mutual interference of each mobile unit with all the others.<sup>35</sup> The system had a finite system capacity—albeit a capacity about three times larger than the capacity calculated for nonspread spectrum designs.

There is also substantial empirical evidence of interference to spread spectrum signals. One example is the strong protest that users of the GPS satellite signal (a spread spectrum system) raised against interference to the GPS signal from proposed Ultra Wideband ("UWB") systems.<sup>36</sup> Another example is the purchase of additional spectrum by the wireless carriers that use spread spectrum.<sup>37</sup> Relatedly, those wireless carriers using spread spectrum require their equipment suppliers to reduce the interference one handset generates to nearby handsets to a level a million times lower than that permitted by the Federal Communications Commission ("FCC").<sup>38</sup> It is hard to understand why these firms would spend money to reduce interfering signals unless those signals were harmful.

CDMA has built into it extensive capabilities for managing the power of signals transmitted from handsets so that those signals will all arrive at

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33. *Id.* at 86, 87, 92 n.5.

34. *Id.* at 92.

35. *Id.* at 90, 92.

36. See DAVID S. ANDERSON ET AL., U.S. DEP'T OF COMMERCE, ASSESSMENT OF COMPATIBILITY BETWEEN ULTRAWIDEBAND (UWB) SYSTEMS AND GLOBAL POSITIONING SYSTEMS (GPS) (2001), [http://www.ntia.doc.gov/osmhome/reports/uwbgps/NTIASP\\_01\\_45.pdf](http://www.ntia.doc.gov/osmhome/reports/uwbgps/NTIASP_01_45.pdf). See also Revision of Part 15 of the Commission's Rules Regarding Ultra-Wideband Transmission Systems, *First Report and Order*, 17 F.C.C.R. 7435 (2002), [http://hraunfoss.fcc.gov/edocs\\_public/attachmatch/FCC-02-48A1.pdf](http://hraunfoss.fcc.gov/edocs_public/attachmatch/FCC-02-48A1.pdf).

37. See, e.g., *Verizon Wireless Buys All NextWave for USD 3B*, MOBILE MONDAY, Nov. 5, 2004, <http://www.mobilemonday.net/mm/story.php?id=3893>.

38. See 3rd Generation Partnership Project 2, Recommended Minimum Performance Standards for cdma2000 Spread Spectrum Mobile Stations Release B, 3-113 (Dec. 13, 2002), [http://www.3gpp2.org/public\\_html/specs/cs0011-B\\_V1.0.pdf](http://www.3gpp2.org/public_html/specs/cs0011-B_V1.0.pdf) (setting the industry limit of -76 dBm on such emissions); see also 47 C.F.R. § 24.238(a) (2004) (limiting the existing PCS bands to -13 dBm). The CFR requires out-of-band emissions to be attenuated below the transmitting power by a factor of  $43 + 10 \log(P)$ . This is analogous to a speed limit sign that stated "slow down by (your current speed) - 35 miles/hour" So, if you are going 40 mph, you would slow down by 5 MPH (40 - 35) to 35 miles/hour. See *id.* The 63 dBm difference between the FCC permitted level and the industry standard is a factor of two million.

the cell tower at the same strength—thereby avoiding the near-far problem discussed earlier. If spread spectrum really eliminated interference, these capabilities would be unnecessary.

The unlicensed community is pressing for the release of more spectrum for unlicensed applications.<sup>39</sup> However, were interference not a problem, the current several hundred MHz of spectrum available for unlicensed systems would be sufficient to carry more data than any person would need.<sup>40</sup>

Spread spectrum is a great technology. When used in personal wireless systems, such as cellular and PCS, it increases capacity by a factor of two to ten over the earlier Time Division Multiple Access (“TDMA”) and FDMA technologies.<sup>41</sup> Used in the GPS system, it permits the efficient sharing of the satellite-to-earth radio channel.<sup>42</sup> Manufacturers and service providers have converged on the use of spread spectrum for third-generation wireless systems.<sup>43</sup> But, as good as spread spectrum is, it is not good enough to make the problem of interference go away.

*B. Assertion Two: Signals Below the Noise Floor Are Harmless*

- Spectrum below the noise floor is therefore not scarce, at least from the perspective of high-power systems above it, because these systems ignore radiation at that level.<sup>44</sup>
- For example, low-power UWB would be covered by this easement, to the extent that it operates under the noise floor and creates no

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39. See *Broadcast to Broadband: Completing the Digital Television Transition Can Jumpstart Affordable Wireless Broadband: Hearing Before the S. Comm. on Commerce, Science, & Transportation*, 109th Cong. (2005) (testimony of Michael Calabrese, Vice President and Director, Wireless Future Program, New America Foundation), [http://www.newamerica.net/Download\\_Docs/pdfs/Doc\\_File\\_2460\\_1.pdf](http://www.newamerica.net/Download_Docs/pdfs/Doc_File_2460_1.pdf). In his testimony, Mr. Calabrese states, “we also strongly recommend that roughly one-third (20 MHz) of the TV band spectrum reallocated for wireless services be reserved for shared, unlicensed wireless broadband . . .” *Id.*

40. Cf. *The Future of Spectrum Policy and the FCC Spectrum Policy Task Force Report: Hearing Before the S. Comm. on Commerce, Science, & Transportation*, 108th Cong. (2003) (testimony of Michael Calabrese, Director, Spectrum Policy Program, New America Foundation), [http://www.newamerica.net/Download\\_Docs/pdfs/Pub\\_File\\_1165\\_1.pdf](http://www.newamerica.net/Download_Docs/pdfs/Pub_File_1165_1.pdf) (noting the abundance of spectrum available to the public when regulations eliminate interference).

41. See CDMA Development Group, Technology, 2G - cdmaOne, <http://www.cdg.org/technology/2g.asp> (last visited Mar. 23, 2006).

42. See 1 Global Positioning System, *supra* note 24.

43. See CDMA Development Group, Technology, 3G-CDMA2000, <http://www.cdg.org/technology/3g.asp> (last visited Mar. 23, 2006).

44. Werbach, *supra* note 14, at 960.

interference.<sup>45</sup> An underlay easement would allow secondary unlicensed users to share licensed spectrum as long as they remain below the noise floor established by the license.<sup>46</sup>

The radio noise floor is the level of unavoidable radio static in the environment.<sup>47</sup> Such noise arises from different causes in different regions of the spectrum. In the AM band, the primary source of radio noise is either distant lightning (for someone on a rural road far from town) or nearby electrical equipment (for someone in town).<sup>48</sup> In the cellular and PCS bands, noise comes from the thermal microwave radiation in the environment, electronic equipment such as personal computers, and the out-of-band emissions of radio transmitters.<sup>49</sup> Satellite TV receivers see primarily the thermal microwave radiation from space—and because space is cold—this noise is lower than the noise seen by PCS receivers.<sup>50</sup>

When an external source adds noise to the environment, the total noise rises. Adding noise to the environment might be analogized to pouring more water in a bathtub—the level of the water in the bathtub rises. In contrast, if one pours more water into a river, the level of the water in the river stays the same.<sup>51</sup> Figure 6, taken from a presentation given by Kevin Werbach, illustrates this fallacy.<sup>52</sup> It shows a desired signal, the noise floor, and a signal below the noise floor (an underlay signal). As illustrated, there appears to be no problem.

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45. Gerald Faulhaber, *The Question of Spectrum: Technology, Management, and Regime Change* 11 (2005) (paper presented at the Economics, Technology, and Policy of Unlicensed Spectrum Conference, Michigan State University), <http://quello.msu.edu/conferences/spectrum/papers/faulhaber.pdf> (last visited Feb. 28, 2006). UWB radios spread their signals out over an enormous range of frequencies with little energy in any small range of frequencies.

46. William Lehr, *Dedicated Lower-Frequency Unlicensed Spectrum: The Economic Case for Dedicated Unlicensed Spectrum Below 3 GHz* 18 (New Am. Found., Spectrum Series Working Paper No. 9, 2004), available at [http://www.newamerica.net/Download\\_Docs/pdfs/Doc\\_File\\_1548\\_1.pdf](http://www.newamerica.net/Download_Docs/pdfs/Doc_File_1548_1.pdf).

47. See Rudholf F. Graf, *Modern Dictionary of Electronics* 505 (7th ed. 1999).

48. A. D. Spaulding & R. T. Disney, U.S. Dep't of Commerce, *Man-Made Radio Noise: Part I: Estimates for Business, Residential, and Rural Areas* 10–11 (1974), available at <http://www.its.bldrdoc.gov/pub/ot/ot-74-38/Ch1-3.pdf>.

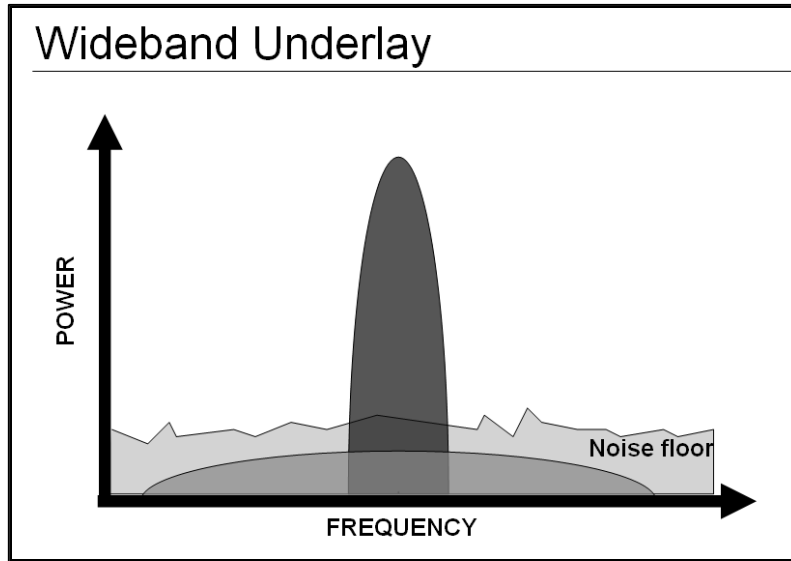
49. *Id.*

50. See GARY D. GORDON & WALTER L. MORGAN, *PRINCIPLES OF COMMUNICATIONS SATELLITES* 202–04, 220–21 (1993).

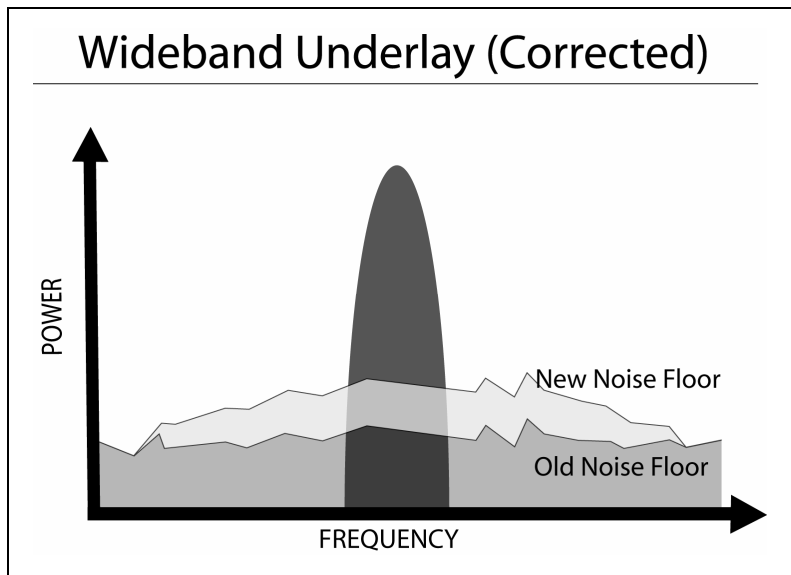
51. We ignore the transient rise in the river level while the added water works its way downstream.

52. Kevin Werbach, *The Open Spectrum Revolution*, Presentation to the Wireless Future Conference 9 (Mar. 23, 2004), [http://werbach.com/docs/wireless\\_future.ppt](http://werbach.com/docs/wireless_future.ppt).



**Figure 6:** Illustration of Underlay Signal

However, the drawing does not represent the physics observed in the real world. The proper illustration is shown in Figure 7.

**Figure 7:** Proper Illustration of Underlay Effects

The contrast is clear. In Werbach's diagram, the added noise or interference does not affect the total noise. In the revised diagram, the added noise or interference increases the total noise. That is how real-world systems work—akin to more water in a tub, not to more water in a river. An interfering signal reduces the margin against noise and interference.

This issue is not merely theoretical. Some modern radio systems can operate at signal levels sufficiently low that added noise or interference—even if below the noise floor—will noticeably degrade the performance of these systems.<sup>53</sup> For example, Superconductor Technologies sells cryogenically-cooled ultra-low noise amplifiers for use in cellular and PCS systems.<sup>54</sup> These amplifiers increase cell coverage by permitting the base station to hear signals that are too weak to hear with more conventional gear. Noise or interference at half the level of the noise floor would impair systems using such receivers.

#### IV. CONCLUSION

Radio interference remains a genuine problem—and neither using spread spectrum nor keeping the potentially interfering signal below the noise floor eliminates interference. We have tried to explain why interference remains a problem. We have also pointed to the behavior of spectrum users—users who could save billions if spread spectrum truly eliminated interference—as further evidence that our point is correct.

Although our purpose in this paper is to throw cold water on some unjustifiably optimistic views of radio technology, we conclude by noting that there is substantial cause for optimism regarding future use of the radio spectrum. Emerging technologies, such as Multiple-Input Multiple-Output (“MIMO”) and Multi-User Detection (“MUD”), will expand spectrum capacity several times over. Unfortunately, these technologies cannot be used in every radio application, and they may impose costs such as shorter battery life or higher prices. Technology has not eliminated interference, but the future for wireless communications is bright.<sup>55</sup>

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53. A short calculation shows why this is so. The Superconductor Technologies' SuperLink Rx 1900 has a noise figure of 1 dB. Thus, in an environment with an external noise temperature of 290 K, use of this device yields a system with total noise temperature of 365 K (1 dB higher). Adding noise power at a level of one half the noise floor (140 K) increases system noise temperature to 505 K. Thus, noise well below the noise floor increases system noise temperature by a factor of  $505/365 = 1.38$  or 1.4 dB. Such a 1.4 dB increase in noise will degrade the performance of modern wireless systems or will require compensating adjustments, such as a 38% increase in transmitted power.

54. See Superconductor Technologies Datasheet for SuperLink Rx 1900, [http://www.suptech.com/pdf/SuperLinkRx1900\\_web.pdf](http://www.suptech.com/pdf/SuperLinkRx1900_web.pdf) (last visited Mar. 23, 2006).

55. Technically speaking and in the interests of completeness, we note that MUD works by eliminating interference. Unfortunately, it can only eliminate some kinds of interference and, even then, is not perfect.

# Rethinking Reform of the FCC: A Reply to Randolph May

Russ Taylor\*

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## I. INTRODUCTION

Even the most strident opponents of regulation cannot fathom a world in which society does not—at some level—regulate the provision or consumption of information or communications. Even if markets function perfectly, we would still envision certain legal controls. A useful example

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of one such legal control is the First Amendment to the U.S. Constitution, which establishes firm boundaries on the government's ability to control information. Other forms of regulation may include the creation of a legal liability scheme if information is abused in some manner, such as libellous statements, copyright infringement, or identity theft. The absence of some form of regulation is unthinkable.

But as a society, we have gone much further in our attempt to regulate information than merely enacting prohibitions on certain government or private actions. Our federal, state, and local policymakers have created extensive regulatory structures that govern everything from the provision of cable and telecommunications services using public rights of way, satellite and wireless services that involve a high degree of international coordination or standardization, and various media services, with both positive and negative content regulation. Providers of media and communications services are licensed, subsidized, monitored, and sanctioned to specify just a few of the most commonly employed regulatory techniques. The problems and opportunities for which we see a regulatory role seem endless.

At the center of all this stands the Federal Communications Commission ("FCC"), a so-called independent federal regulatory agency that is composed of five commissioners, appointed by the President and confirmed by the Senate, not more than three of which are from the same political party.<sup>1</sup> The FCC is independent in the sense that, while it is subject to laws passed by Congress and court decisions, most of its actions cannot be directly overruled by the President through the administrative process. The FCC has an extensive array of responsibilities and obligations, a large budget and staff, and a prominent place in the heart of policymaking on media, technology, and communications. Further, because the FCC regulates several multibillion dollar industries that touch almost every aspect of our economic and social lives, its structure, remit, and activities are often subjected to severe scrutiny.

But some argue that having the FCC stand at the center of all this policymaking is the wrong approach. They make a compelling case in many respects. Why should five unelected officials establish forward-looking policies that govern media and communications in our republic? Would it not be better to remove the bureaucratic mystery surrounding policymaking and have these sometimes contentious issues resolved by the President or persons answering directly to the President? The President is accountable directly to the American public and is often regarded as a swift decision maker. If there is controversy, what better focal point than the

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1. 47 U.S.C. § 154 (2000).

President? It is in this intellectual climate that the *Administrative Law Review* recently published Randolph May's essay on opportunities for reform of the FCC.<sup>2</sup>

While this Article functions as a reply to May's essay, I salute May's many contributions to an important debate, namely, how best to structure society's control over the creation, distribution, and consumption of information. May's contributions are commendable as an initial matter for their very existence and nature. We should not regard our policymaking and regulatory structures as strictly bound by the idealist but perhaps unworkable principles of the past. If conditions change or our learning changes to such an extent that we believe a new regulatory structure is called for, then we should not hesitate to call for change. May does this.

My aim in this Article is to expand on May's recent call for consideration of FCC reforms, criticize his methodology to some extent,<sup>3</sup> and briefly present a framework within which reform of the FCC or any regulatory agency or organization can be evaluated. But my most important aim in this Article is to convey the following: Any discussion about reform of an agency with the size, importance, and history of the FCC should be based, in part, on empirical data about how regulators work, not anecdotal information that simply confirms our existing assumptions.<sup>4</sup> Just as carefully as we scrutinize the regulator, we should also carefully scrutinize our own assumptions about regulatory structures and the regulatory process, and the empirical or logical methods by which we test those assumptions.

## II. RANDOLPH MAY'S CALL FOR AGENCY REFORM

May offers two principal suggestions for reform of the FCC. He suggests (1) reducing the number of FCC commissioners from five to three

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2. Randolph J. May, *Recent Developments in Administrative Law: The FCC's Tumultuous Year 2003: An Essay on an Opportunity for Institutional Agency Reform*, 56 ADMIN. L. REV. 1307 (2004).

3. An important disclaimer is in order: May's essay does not generally claim to employ social science or similar investigatory techniques. Therefore, my criticism of May's approach is somewhat overstated—but purposely so. May asks for a debate and attempts to frame that debate by describing what he believes is an outdated regulatory structure and by drawing inferences from real-world situations he observes. Since his call for reform is based on a certain context established in his essay, it is appropriate to examine whether that context withstands careful scrutiny.

4. This Article tracks the claims contained in May's essay, which primarily calls for reform based on the need for more timely and coherent policies. This Article does not focus on doctrinal issues such as the questionable constitutional status of independent regulatory agencies or normative preferences about regulation or governance. In essence, this Article ignores the issues associated with agency reform and focuses exclusively on what one might call the *effectiveness* issue raised by May: Are there structural changes that, if implemented, would make the FCC more effective in accomplishing its mission?

or even one and (2) moving the FCC into the executive branch of government and removing its independent status.<sup>5</sup> As justifications for his reform proposals, May argues that “with a five-member agency, it is more likely that, as a result of compromises made in reaching a majority decision, the resulting order will lack clarity or even be internally contradictory.”<sup>6</sup> He also argues, “Along with increased political accountability, presidential supervision should lead to decisions that are timelier, more internally coherent, and generally more consistent with other executive branch initiatives.”<sup>7</sup>

When I first read May’s essay, I reacted quite strongly to these claims. This is not because I am an uncritical institutional supporter of the FCC or someone who otherwise fears change. My reaction is based primarily on what I perceive to be unexplored assumptions about regulation or governance of complex systems generally. My concern is not that we are *too critical* of issues surrounding agency reform. Instead, my concern is that we are *not thinking critically enough* about regulatory structures and processes. I will share my concerns and address them in this Article.

### III. EXPLORING THE NEED FOR AGENCY REFORM

As an initial matter we should explore whether, as May claims, conditions are ripe for reform of the FCC.<sup>8</sup> May’s argument that it is time to consider reform of the FCC stems from two assertions: (1) during the tumultuous year of 2003, the FCC poorly handled two important policy issues before it, and (2) convergence and rapid change significantly altered the marketplace environment.<sup>9</sup> I shall address each rationale in turn.

First, with respect to the year 2003, I agree with May that the FCC’s consideration of the two policy issues he discusses<sup>10</sup> was marked by

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5. May, *supra* note 2, at 1321.

6. *Id.* (citation omitted).

7. *Id.* at 1323 (citation omitted).

8. *Id.* at 1307–08.

9. *Id.* at 1309.

10. Those were the *Triennial Review* and the media ownership proceedings. For the *Triennial Review*, see Review of the Section 251 Unbundling Obligations of Incumbent Local Exchange Carriers, *Report and Order and Further Notice of Proposed Rulemaking*, 18 F.C.C.R. 16978 (2003) [hereinafter *Triennial Order*], *corrected by Errata*, 18 F.C.C.R. 19220 (2003), *aff’d in part and rev’d in part*, U.S. Telecom Assoc. v. FCC, 359 F.3d 554 (D.C. Cir. 2004) (reversing major portions of the FCC’s *Triennial Order*), *cert. denied*, 543 U.S. 925 (2004). For the media ownership proceedings, see 2002 Biennial Regulatory Review—Review of the Commission’s Broadcast Ownership Rules and Other Rules Adopted Pursuant to Section 202 of the Telecommunications Act of 1996, *Report and Order and Notice of Proposed Rulemaking*, 18 F.C.C.R. 13620 (2003), *aff’d in part and remanded in part*, Prometheus Radio Project v. FCC, 373 F.3d 372 (3d Cir. 2004) (remanding the FCC’s cross-media ownership limits decisions for justification or modification), *cert.*

squabbling, delay, and generally poor policymaking. Otherwise, I will not generally explore or critique May's description of those two FCC proceedings. However, subject to my earlier disclaimer, a broader, methodological critique surfaces: Are those two proceedings representative of the business before the agency during this time? Are they representative of a systematic agency pathology that requires a cure?<sup>11</sup> Here, I part company with May because the evidence appears anecdotal and highly subjective.<sup>12</sup>

Again, consistent with my initial disclaimer, we must realize that May is simply exploring opportunities for reform, albeit in a suggestive manner. But the criticism remains: Precisely why do the two selected proceedings, in May's words, "provide the opportunity and impetus" for considering reform of the FCC?<sup>13</sup> Why are they, again in May's words, "important for what [they say] about the functioning of the agency"?<sup>14</sup> In making these claims, we should first address the significant potential logical frailty in using two proceedings, from one year, out of the seventy years of the agency's existence and thousands of proceedings during that time. The two proceedings at issue may indeed say something larger about the structure of the FCC.<sup>15</sup> Alternatively, they may simply describe those two proceedings

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*denied*, 125 S.Ct. 2904 (2005).

11. Could it be possible that an agency with the particular reformed structure and characteristics advocated by May would have experienced a similarly tumultuous year in 2003? What would that tell us about structural reform? May claims that a bad 2003 for the FCC "increased the sense" that the regulatory regime needs updating, but before we discuss changing the FCC's structure, should we not first conduct a rigorous empirical analysis of the links between agency structure and policy outcomes? May, *supra* note 2, at 1309. May suggests that the FCC's structure contributes to poor outcomes. *Id.* However, we must be careful when alleging causation, particularly when there may be other confounding factors (e.g., confusing legislation) that could be the real cause of the poor policymaking outcomes.

12. While the two proceedings selected by May as examples of the FCC's poor track record were certainly important and controversial, there were many other important proceedings and activities before the FCC in 2003, including the DTV transition, public safety communications issues, and the World Radio Conference, to name but a few. *See generally* FCC ANNUAL PROGRAM PERFORMANCE REPORT (2003), available at <http://www.fcc.gov/Reports/ar2003.pdf> [hereinafter 2003 FCC Report].

13. May, *supra* note 2, at 1309.

14. *Id.* at 1313.

15. Certainly, there are many reasons for adopting this viewpoint. Study of an unusual or atypical case can teach us much about a larger issue. For example, the two proceedings at issue were quite large in terms of their social and economic impact on society. One might argue that, if the FCC fails in such important cases, it does not matter what the outcomes are in average cases. These two examples might serve as what Stake calls an "instrumental case study"—a study of the particular that offers insight into a larger phenomenon. ROBERT E. STAKE, *THE ART OF CASE STUDY RESEARCH* 3 (1995).

as statistical outliers, atypical of the agency's performance during 2003<sup>16</sup> and thus offer very little insight to those concerned with agency reform.

In any event, if we are to focus on one particular year, why not start with the FCC's critical assessment of its own performance during that year? Admittedly, an agency's self-appraisals will suffer from several problems such as insularity and bias. However, while painting a rather dismal portrait of an incompetent or unresponsive agency, May makes no mention of the FCC's annual self-appraisal reports ("Reports"), issued every year by the FCC and available to the public on its Web site.<sup>17</sup> The Reports track FCC performance in certain key areas such as spectrum, competition, homeland security, and modernization of internal practices. The Reports are exhaustive and specify data that illuminate the issues May addresses in his essay. For example, May criticizes the FCC for extraordinary delays in one particular rulemaking proceeding (a six-month delay),<sup>18</sup> but the FCC claims that, in Fiscal Year ("FY") 2003, the average time period between adoption of a decision and that decision's release to the public was a mere ten days.<sup>19</sup> The delay increased to fifteen days in FY 2004.<sup>20</sup> So, we are left with two accounts of the FCC's timeliness: May's qualitative account of the time delays associated with one or two particularly large and important proceedings, and the FCC's more quantitative account of its average speed of disposal of matters before it. Both accounts inform the debate. But calls for reform cannot be taken seriously unless they deal with both the illustrative and qualitative type of account and the exhaustive and quantitative type of account.

Not only does May criticize the FCC's timeliness in two proceedings, he also suggests that its decision-making ability is correlated with its number of commissioners, claiming that "it is more likely that, as a result of compromises made in reaching a majority decision, the resulting order will lack clarity or even be internally contradictory."<sup>21</sup> But May provides no further reasoning or data to support his otherwise contestable claim. Contrast the recent empirical studies that address this precise issue. For example, in one recent study, researchers compared the effectiveness of a

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16. A related methodological question: Why is the year 2003 representative? Longitudinal studies of the FCC's practices would likely offer a more realistic picture of how the agency's structure affects policy outcomes. This is particularly true because we are considering wholesale changes in the FCC's structure and not merely focusing on the introduction of a new regulatory technique or process.

17. See, e.g., 2003 FCC REPORT, *supra* note 12.

18. May, *supra* note 2, at 1314.

19. See 2003 FCC REPORT, *supra* note 12, at 30.

20. See FCC ANNUAL PROGRAM PERFORMANCE AND ACCOUNTABILITY REP. 67 (2004), available at <http://www.fcc.gov/Reports/ar2003.pdf>.

21. May, *supra* note 2, at 1321 (citation omitted).



five-member committee versus individual decision making on monetary policy issues. The study found that groups make better decisions than individuals.<sup>22</sup>

Even if one were to discard potentially unrealistic laboratory-style empirical work and simply focus on reported actual outcomes and comparisons, there is no evidence to suggest that multimember commissions perform worse than executive branch agencies. If one considers a reviewing court's rate-of-reversal of agency actions a proper measure of the quality of regulatory actions, then there exists ample data upon which to review real world outcomes. The answers from a 1992 review are not terribly surprising: (1) federal agencies tend to do well in court generally and (2) "there [is] no substantial difference . . . between the executive and independent agencies."<sup>23</sup>

I am not endorsing a particular viewpoint on whether the FCC would make better and timelier decisions if it was managed by one chairperson instead of a five-member commission. More study and consideration are clearly needed. I also suspect the answer would be highly contextual, depending on the precise nature of the issue in question and the affected parties. But one thing is certain, the concept of "less is more" in the context

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22. Claire Lombardelli, James Proudman & James Talbot, *Committees Versus Individuals: An Experimental Analysis of Monetary Policy Decision-making* (Bank of England, Working Paper No. 165, 2002), available at <http://ssrn.com/abstract=340560>. The Bank of England study also follows earlier empirical work which undercuts the notion that individuals make decisions in a timelier manner than groups. See Alan S. Blinder & John Morgan, *Are Two Heads Better Than One?: An Experimental Analysis of Group vs. Individual Decisionmaking* (Nat'l Bureau of Econ. Research, Working Paper No. 7909, 2000), available at <http://ssrn.com/abstract=242143>. But see David Schkade, Cass R. Sunstein & Daniel Kahneman, *Are Juries Less Erratic than Individuals?: Deliberation, Polarization, and Punitive Damages* (Univ. of Chicago Law School, John M. Olin Law & Econ. Working Paper No. 81, 1999), available at <http://ssrn.com/abstract=177368> (indicating that juries make more unpredictable and varied decisions than individuals when it comes to damage awards). Unlike juries, the Bank of England study employed economically-literate students from the London School of Economics in a policy environment, a setting more similar to the communications-literate FCC commissioners.

23. See Martha Anne Humphries & Donald R. Songer, *Law and Politics in Judicial Oversight of Federal Administrative Agencies*, 61 J. POL. 207, 210 (1999) (citation omitted) (describing a 1992 study covering federal agencies before U.S. Circuit Courts of Appeal for 1979, 1983, and 1987). Of course, we must be careful when we say that any statistic measures the quality of decision making. There could be factors other than the intellectual quality of an agency decision that result in success or failure in court. For example, federal agencies may have more litigation resources than private litigants. Also, as Humphries and Songer demonstrate, federal judges may let their own policy preferences influence their decisions. *Id.* Similarly, many provisions of federal law provide deference to administrative agencies' decisions. Finally, there may be procedural reasons (e.g., the doctrine of standing) why the quality of federal agency decisions are not tested at all.

of agency decision making has not been demonstrated with any degree of persuasiveness.

With respect to May's second rationale for reform—the current fast-changing state of the marketplace—nothing about this particular era of convergence and change warrants FCC reform in its own right. It is only the notion that the agency is out-of-step and unable to cope with the changed marketplace that would support the contention that reform is needed. But here again, I part company with those who claim that an agency born of New Deal thinking about problem solving is poorly suited to tackle problems in today's environment. At the very least, I look for more evidence.

I find a high degree of generational exceptionalism in May's description of the FCC as a once "sleepy backwater government agency" now confronting a new climate of "rapid technological change . . . propelled by the digital revolution" in which there are "rapid-fire business successes and failures" and resulting "breakdown of existing regulatory service distinctions."<sup>24</sup> While there are obviously changes afoot, they do not appear to be happening in such a rapid manner that the FCC cannot keep pace. There existed a similar environment of exceptionalism when then-Secretary of Commerce Herbert Hoover addressed the regulation of radio in 1924, ten years before the FCC was created:

There are certain minimum regulatory powers in the Department of Commerce. They are inadequate to meet the shifting situation that this developing art constantly presents. Nor could any legislation keep pace with the changes imposed by scientific discovery and invention now going on in radio. . . . With the development of the art this problem has become one of the most complex technical character ever presented to the Government for solution. At every succeeding conference we have had more and more difficult problems to solve, and those which we present today are of a complexity greater than ever before.<sup>25</sup>

But are these descriptions of change and complexity, renewed every generation it seems, really that authentic?<sup>26</sup> We must all fall victim to this

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24. May, *supra* note 2, at 1307–09.

25. Herbert Hoover, Secretary of Commerce, Address Before the Third National Radio Conference: Recommendations for Regulation of Radio (Oct. 6, 1924), *available at* <http://earlyradiohistory.us/1924conf.htm>.

26. Karl Popper wrote of this tendency, criticizing those scholars:

Contrasting their "dynamic" thinking with the "static" thinking of all previous generations, [and believing] that their own advance has been made possible by the fact that we are now "living in a revolution" which has so much accelerated the speed of our development that social change can be now directly experienced within a single lifetime. This story is, of course, sheer mythology.

KARL RAIMUND POPPER, *THE POVERTY OF HISTORICISM* 160 (2nd ed. 1960).

type of thinking at times—the thinking that ours is a unique age that requires new ideas and new structures for solving problems.

May also paints a portrait of the FCC and similar regulators as being born out of a flawed understanding of dispassionate regulatory expertise. He makes a very good point: we should not expect regulators to be insulated from the political process. But we cannot let our thinking about the silly ways that certain early regulators conceived themselves as dispassionate administrative scientists be equally as singular. Surely, the FCC possesses expertise in numerous areas covered by its statutory remit. Moreover, much of the FCC's work is accomplished in a nonpolitical environment and in a neutral manner. In other words, it was wrong during the New Deal era to place sheer faith in the concept of administrative science, just as it is wrong today to think there is no science to administration. So, while we should perhaps be interested in studying the use of “electioneering-style tactics” before the FCC,<sup>27</sup> we must also analyze how often and in what particular contexts those tactics are employed.

May takes dead aim at James Landis as the leading proponent of unrealistic thinking about the capabilities of the administrative state.<sup>28</sup> But Landis was more critical in his thinking about regulation than May credits him for. Landis was often severely critical of regulatory agencies. For example, in a report to President-elect Kennedy in 1960, Landis completely savaged the FCC, claiming that it “drifted, vacillated and stalled in almost every major area.”<sup>29</sup> Sounding almost like an earlier version of May, Landis further noted that the FCC “seems incapable of policy planning, of disposing within a reasonable period of time the business before it, of fashioning procedures that are effective to deal with its problems.”<sup>30</sup> Landis even advocated structural reforms remarkably similar to those advanced by May, calling on policymakers to increase the power of chairmen over collegial bodies and making those chairmen directly accountable to the President.<sup>31</sup> In fact, in his influential work on regulation, Justice Stephen Breyer noted that such structural approaches to agency reform (e.g., calls for single agency heads accountable to the President) are commonly advanced, and he cited similar reform proposals that go back as far as

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27. May, *supra* note 2, at 1317.

28. *Id.* at 1313.

29. STAFF OF S. COMM. ON THE JUDICIARY, 86th Cong., REPORT ON REGULATORY AGENCIES TO THE PRESIDENT-ELECT 53 (Comm. Print 1960) (James M. Landis, primary author).

30. *Id.*

31. *Id.* at 65.

1937.<sup>32</sup> Justice Breyer said of such proposals, “The major weaknesses in these and other similar proposals for structural change, however, is that they are designed to be policy neutral. They assume that improved agency structure will automatically bring about improved performance. Yet there is little evidence that this is so.”<sup>33</sup>

Further, the FCC may have been born during the New Deal era, but the agency that exists today is in numerous structural, procedural, and cultural ways not a New Deal agency. Since its birth, the FCC has, among other things, (1) had its structure changed in 1983 from seven commissioners to the present five,<sup>34</sup> (2) had its remit expanded, such as the addition of satellite communications in 1962,<sup>35</sup> (3) been subjected to new legal constraints such as the Administrative Procedure Act (“APA”) of 1946,<sup>36</sup> (4) seen the intellectual climate surrounding the field of regulation shift remarkably due to the influence of the “Chicago school” in developing the public choice theory of economic regulation,<sup>37</sup> and (5) been subject to more aggressive Presidential and Congressional oversight since the Reagan era.<sup>38</sup> And, of course, one cannot discount all the internal changes—some minor, some not so minor—that have occurred over the past seventy years. We should appreciate the significant differences from the agency that James Landis and Justice Felix Frankfurter would have recognized.<sup>39</sup>

May suggests that a regulator residing within a political branch of government is more accountable than an independent regulatory agency. He argues that “locating the FCC in the executive branch would introduce more political accountability for policymaking determinations.”<sup>40</sup> But precisely why does housing certain FCC policymaking functions in the executive branch increase accountability? The argument appears, on the surface, to be logical. One could imagine that, because the President is the only federal official voted on by all members of the electorate, his

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32. Stephen Breyer, *Regulation and Its Reform* 354 (1982).

33. *Id.* at 356.

34. Omnibus Budget Reconciliation Act of 1982, Pub. L. No. 97-253, 96 Stat. 805 (codified at 47 U.S.C. § 154(a) (2000)).

35. See Communications Satellite Act of 1962, 47 U.S.C. § 701 (2000).

36. See Administrative Procedure Act of 1946, 5 U.S.C. § 551 (2000).

37. Maxwell L. Stearns, *Restoring Positive Law And Economics: Introduction To Public Choice Theme Issue*, 6 GEO. MASON L. REV. 709, 720 (1998) (“[T]he earliest and perhaps most notable Chicago School contribution to public choice was to recast business regulation from an ‘imposed upon’ to an ‘acquired’ model.”).

38. See James F. Blumstein, *Regulatory Review By The Executive Office Of The President: An Overview And Policy Analysis Of Current Issues*, 51 DUKE L.J. 851, 858–60 (2001) (describing the far-reaching Reagan-era initiative that centralized presidential oversight of regulatory policy-making).

39. May, *supra* note 2, at 1312 (providing the perspective of J. Frankfurter).

40. *Id.* at 1322.

decisions on media and communications policy matters would be subject to great scrutiny by the press and public.

The concept of accountability stems from what concerns people and how those in power see themselves bound to address those concerns. So, how can we test May's claim? How can we judge whether an executive branch agency would be more accountable than an independent agency? And to whom would the agency be accountable? Do members of the public even realize that the FCC is today not directly controlled by the President? Does the public already *mistakenly* hold the President accountable for the actions of the FCC?<sup>41</sup> There are no polls of which I am aware that track popular beliefs about the independent nature of the FCC; although recent poll data suggest that a majority of the public ignores even the most heated media regulation debates.<sup>42</sup> So many questions remain unanswered that I cannot predict with confidence whether increased executive control over FCC policymaking would increase accountability.

We also must consider the follow-on effects, which may include further, not less, politicization of, and chaos in, the regulatory structures. As a prominent critic of presidential control over the regulatory process, Cynthia Farina points out:

The new presidentialism arms the President to insist that he, uniquely, possesses the constitutional prerogative, democratic mandate, and managerial competence to direct the administrative state. These claims of singular entitlement and ability to control the regulatory agenda establish a norm of confrontation, rather than collaboration. By raising the stakes for other actors in the system, such hegemonistic claims may trigger an oversight arms race. Indeed, many would say that this is exactly what happened in the 1980s, as Congress reacted to what it perceived as aggressive unilateral White House deregulatory initiatives

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41. It is this notion of an "accountability mismatch" that Mariana Prado innovated and conceptually explores in her recent paper. Prado notes that "the President can play with the electorate's perception. He may simply claim responsibility for popular policies and blame agencies for unpopular policies." Mariana Mota Prado, *Independent Regulatory Agencies and the Electoral Accountability of the President 11* (2004) (paper prepared for the SELA Conference, June 12, 2004) (citation omitted), <http://islandia.law.yale.edu/sela/SELA%202004/MotaPradoPaperEnglishSELA2004.pdf>.

42. Seventy-two percent of poll participants in July 2003 indicated that they had heard "nothing at all" about the FCC's media ownership proceeding. Twenty-three percent had heard "a little." Press Release, Pew Research Center for the People & the Press, *Strong Opposition to Media Cross-Ownership Emerges* (July 13, 2003), <http://people-press.org/reports/print.php3?PageID=721>. The number of people aware of the proceeding seems quite low and supports May's hypothesis that elevating media policy matters to the presidential level might increase public awareness and accountability. However, when contrasted with the polling status of executive branch departments on similar issues, the FCC might not fare so poorly. In other words, it is the *comparative* standing of the independent versus executive agencies we should be interested in, not simply the low standing of the independent regulatory agencies.

with a variety of equally aggressive countermeasures. . . . If we encourage political actors to regard regulatory oversight as a battle for the soul of the administrative state, we may be unpleasantly surprised at the weapons each turns out to have available in its arsenal.<sup>43</sup>

I do not necessarily endorse Farina's viewpoint, but her observation hits the proper methodological tone. The regulatory environment—that space or arena in which debates occur and decisions are taken—is not static. A legal shift of control over the FCC's policymaking functions to the executive branch would be followed by countershifts and not just from Congress. Regulatees, consumer groups, courts, and even FCC employees will likely react in different and perhaps unpredictable ways. I question whether we can predict policy outcomes, particularly successful policy outcomes, with any degree of certainty.

#### IV. EXPANDING THE CONTEXTUAL SETTING OF THE REFORM DEBATE

In this Part of the Article, I intend to abandon my overly harsh methodological critique of May's essay and instead champion his spirited call for fresh thinking about "reforming the original experiment."<sup>44</sup> But instead of focusing on the FCC and its experience in 2003, I will head in the opposite direction<sup>45</sup> and explore the FCC's regulatory environment in the context of other structures that affect policy.

Before we consider structural reform of the FCC, we should first critically examine the overall policy environment in which the agency operates. Otherwise, we run the danger of wrongly viewing regulation as merely an isolated, binary activity: the regulator acting on the regulatee. What are the factors—political, social, economic, and legal—that unduly constrain or overindulge the FCC? Perhaps, if reform is indeed required, we should first examine what some have called the "institutional endowments"<sup>46</sup> that, at least in some cases, can be predictive of regulatory

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43. Cynthia R. Farina, *Undoing the New Deal Through the New Presidentialism*, 22 HARV. J.L. & PUB. POL'Y 227, 235 (1998).

44. May, *supra* note 2, at 1312.

45. May's essay considers structural reform of the FCC at the agency level. Heading in a different direction, one could examine reform issues at a microlevel by reviewing the FCC's procedures and practices, or at a macrolevel, as this Article briefly attempts, by reviewing the regulatory and policy environment beyond the agency.

46. Brian Levy & Pablo T. Spiller, *The Institutional Foundations of Regulatory Commitment: A Comparative Analysis of Telecommunications Regulation*, 10 J.L. ECON. & ORG. 201, 205 (1994). Levy and Spiller describe five endowments: (1) executive and legislative institutions, (2) judicial institutions, (3) customs and broadly accepted norms that constrain behavior, (4) the contending social interests within a society, and (5) the administrative capabilities of the nation. *Id.* at 205–06. Levy and Spiller generally conclude that those governance structures which constrain administrative discretion and induce

success or failure. May mentions one and suggests others.<sup>47</sup> Combined, they raise the question of whether the FCC needs reform or whether we should first rethink other aspects of the regulatory and policy environment. Some elements of that larger environment include: previous FCC decisions, international organizations, Congress, and federalism.

#### A. *Previous FCC Decisions*

There is, perhaps, no greater constraint on FCC behavior and action than the agency's previous actions. We tend to think of the agency as an undifferentiated whole, but the FCC is composed of serial mini-administrations, each of which leave their stamp on media and communications policy. Even setting aside legal obligations for the FCC to follow precedent or explain its departures therefrom,<sup>48</sup> there exist practical reasons why previous FCC decisions are so constraining. Take, for example, the issue of standards setting. If the FCC sets a technological standard for a consumer device and then millions of those devices are sold in the marketplace, a subsequent mini-administration has little choice but to accommodate that standard for a period of time. Thus, the FCC's previous decisions have contributed to certain market structures that are difficult to undo or substantially amend through simple administrative reform.

#### B. *International Organizations*

Media and communications are global businesses. Increasingly, we are also seeing global regulatory structures, ranging from the trade-specific World Trade Organization ("WTO")<sup>49</sup> to the Internet Corporation for Assigned Names and Numbers ("ICANN").<sup>50</sup> Increasingly, the FCC may find itself unable to make policy in a particular area because that role has been assigned to another, more internationally-focused entity. Similarly, the FCC may be required to compromise its efforts in order to achieve

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private investment produce the best outcomes. *Id.* at 202–03.

47. May, for example, acknowledges that the FCC is often faced with "ill-defined and sometimes contradictory statutory mandates." May, *supra* note 2, at 1308. May also describes numerous court battles faced by the FCC, highlighting the fact that the agency does not always have the final say in policy matters. *Id.* at 1313.

48. See *Greater Boston Tel. Corp. v. FCC*, 444 F.2d 841, 852 (D.C. Cir. 1970).

49. The WTO is a multilateral trading system in which, for telecommunications purposes, member states agree to certain enforceable commitments, typically related to market access by foreign competitors. See World Trade Organization, <http://www.wto.org> (last visited Mar. 16, 2006).

50. ICANN says it is "responsible for coordinating the management of the technical elements of the [Domain Name System] to ensure universal resolvability so that all users of the Internet can find all valid addresses." ICANN Information, <http://www.icann.org/general/> (last visited Mar. 18, 2006).

some form of regulatory coordination with an international organization. This is an interesting area for those interested in reform, posing important questions: Are global regulatory structures more effective in an interconnected world? Do global regulatory structures impede the effectiveness of the FCC?

### C. Congress

The actions of Congress have an obvious effect on FCC performance. Normative policy preferences, for the most part, are established by Congress and merely implemented by the FCC. Similarly, the FCC's statutory remit can be expanded or narrowed by Congress, as can particular procedures<sup>51</sup> or legal standards or presumptions.<sup>52</sup> Particularly since the 1996 Act,<sup>53</sup> Congress specifies not only the policy goal, but also increasingly specifies the methods, timing, and legal standards by which the FCC seeks that goal.<sup>54</sup> Perhaps one area of reform to explore would be a loosening of these legislative constraints, applied in an *ex ante* fashion by Congress and often without serious study. This is particularly true in situations where—if you endorse May's viewpoint—we are experiencing a period of rapid technological change.

Another useful area for reform to explore would be a complete rewrite of the nation's laws pertaining to media and communications, particularly in light of the recent developments associated with wireless and Internet delivery of information. May's essay suggests that the laws which govern these industries are deficient from both a substantive and procedural perspective.<sup>55</sup>

### D. Federalism

States play a prominent role in both the media and communications sectors. For example, often subject to broad federal guidelines, state and local governments typically franchise cable operators and authorize telecommunications providers, and they specify the terms and conditions under which broadband and wireless facilities are emplaced. Perhaps

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51. See 47 U.S.C. § 160(c) (2000) (requiring the FCC to act on certain "forbearance" petitions within one year and ninety days of their submission).

52. See *id.* § 312(d) (putting the burden of proof in FCC license revocation proceedings on the Commission).

53. Telecommunications Act of 1996, Pub. L. No. 104-104, 110 Stat. 56 (codified at scattered sections of 47 U.S.C.).

54. See Sidney A. Shapiro & Robert L. Glicksman, *Congress, the Supreme Court, and the Quiet Revolution in Administrative Law*, 1988 DUKE L.J. 819, 820 (1988) (describing the congressional trend of narrowing administrative agency discretion).

55. May, *supra* note 2, at 1308 nn.3–4.



curbing the power of state and local authorities to make or impede certain media and communications policies would increase the effectiveness of the FCC.

Based on the foregoing, even a brief exploration of the environment in which the FCC operates reveals numerous areas where reform could proceed ahead of, or in conjunction with, institutional agency reform. But a review that solely focuses on the FCC, even if it is empirically rigorous, will be incomplete and perhaps misguided if it is not situated in the wider legal and policy context.

## V. OFCOM ON THE POTOMAC

Our review of models for reform should also not be limited to the United States. One useful model may be the United Kingdom's Office of Communications ("Ofcom"), a regulator with which I have some familiarity.<sup>56</sup> Ofcom was created on December 29, 2003, as a result of a complete structural overhaul of how the United Kingdom regulates the media and communications industries.<sup>57</sup> Ofcom replaced five other legacy regulators that previously governed differing industry sectors. Ofcom is therefore what some call a "converged regulator."<sup>58</sup>

Here is the comparison point for May's call for reform: Ofcom is not a collegiate policymaking body that functions in the same manner as the FCC. Ofcom has a more corporate structure. Ofcom has two leaders, called the "Chief Executive" and the "Chairman."<sup>59</sup> Ofcom is also not bipartisan or multipartisan like the FCC. By contrast, the appointment of Ofcom's Chief Executive is controlled by the government in power in the United

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56. In 2003, I cofounded OfcomWatch, a Web site that monitors the regulatory activities of Ofcom. As a comparatively new regulator, Ofcom is not well known within the United States. Ofcomwatch Home Page, <http://www.ofcomwatch.co.uk> [hereinafter *OfcomWatch*].

57. See generally Ofcom Communications, About Ofcom, [www.ofcom.org.uk/about](http://www.ofcom.org.uk/about) (last visited Mar. 18, 2006).

58. Ofcom was actually created by the Office of Communications Act of 2002 but was provided with greater structural clarity, remit, and procedures at the end of 2003. See Office of Communications Act 2002, ch. 11, <http://www.opsi.gov.uk/acts/acts2002/20020011.htm> (last visited Mar. 18, 2006); Communications Act 2003, ch. 21, Pt. 1, <http://www.opsi.gov.uk/acts/acts2003/20030021.htm> (last visited Mar. 18, 2006).

59. Ofcom's nine-member board differs from the FCC's five-member board for several reasons. First, the Ofcom board functions more like a corporate board and leaves the day-to-day media and communications regulation to the Chief Executive. Further, Ofcom's board adheres to a code of conduct in which all board members are deemed to have agreed to all decisions, and dissenting viewpoints are not revealed, either internally or externally. Finally, except for its current Chairperson, Lord Currie, the Ofcom board generally acts behind the scenes and is not a focal point for policy matters. See Office of Communications, The Ofcom Board: Functions and Role, [http://www.ofcom.org.uk/about/csg/ofcom\\_board/role/#acontent](http://www.ofcom.org.uk/about/csg/ofcom_board/role/#acontent) (last visited Mar. 18, 2006).

Kingdom, currently Tony Blair's New Labour government. So, Ofcom possesses the two structural characteristics—small leadership and part of the political branch—advanced by May for possible reform of the FCC.

The similarities between Ofcom and the model of structural reform May suggests for the FCC raise the questions: Is Ofcom more accountable, quick-acting, and coherent than the FCC? Would structuring the FCC to resemble Ofcom improve the U.S. media and communications regulatory system? I will attempt a brief answer to these questions, mindful of the dangers when comparing institutional structures across legal cultures.<sup>60</sup> I will also temporarily discard the methodological rigor that I applied to May's analysis of the FCC.

Because Ofcom was only created in December 2003, it is probably too soon to remark on whether Ofcom is an optimal regulator from an effectiveness standpoint. But in my opinion, by simply replacing five legacy regulators and serving as a single source for media and communications regulation, Ofcom represents a significant structural improvement over the legacy regulators. By having one regulator instead of five, citizens, consumers, and regulatees are probably more likely to know where to turn for information.

With respect to accountability, Ofcom is very responsible to New Labour and its key ministers who cover media and communications policy: Prime Minister Tony Blair, and Secretary of State for Culture, Media and Sport Tessa Jowell.<sup>61</sup> The links between Number 10 Downing Street and Ofcom are clear, and because there has never been a separation of powers in the United Kingdom, no person seriously questions whether New Labour directly controls media and communications policy. They do—despite occasional disclaimers to the contrary.<sup>62</sup>

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60. See ROGER COTTERRELL, *COMPARING LEGAL CULTURES* 13 (David Nelken ed., 1997) ("One of the enduring problems of comparative law has been its inability to demonstrate convincingly the theoretical value of doctrinal comparisons separated from comparative analysis of the entire political, economic and social (we might call it contextual) matrix in which legal doctrine and procedures exist."). In other words, Ofcom is part of a British policymaking establishment, aimed at British citizens and consumers, and acting within the British (and larger European) business and intellectual climate. A simple structural comparison to the FCC, while useful in some respects, ignores the many other variables that may explain policy preferences and outcomes.

61. See 10 Downing Street, Her Majesty's Government, <http://www.number-10.gov.uk/output/Page1371.asp> (specifying the United Kingdom cabinet ministers) (last visited Mar. 18, 2006).

62. Interestingly, Ofcom's executive, Stephen Carter, recently claimed that his agency is "unashamedly technocratic." Stephen Carter, Chief Executive Officer, Office of Communications, Address to Incorporated Society of British Advertisers Annual Conference: Ofcom Two Years On (Mar. 9, 2005), <http://www.ofcom.org.uk/media/speeches/2005/03/isba#content>.

But I have criticized Ofcom for a lack of accountability and transparency *to the public and regulatees* on numerous occasions. Ofcom's Web site is often confusing to the casual visitor.<sup>63</sup> Ofcom has no codified set of regulations. Ofcom has no rules governing *ex parte* presentations about contested or controversial matters. Ofcom does not permit reply comments in policy-making proceedings. Ofcom is overly secretive with respect to its documents, even in the face of the United Kingdom's Freedom of Information Act,<sup>64</sup> which was implemented in January 2005.<sup>65</sup> Ofcom regularly holds meetings with so-called stakeholders and does not invite or otherwise inform the public. Finally, Ofcom appears to "sell" already formulated policy answers to the public and regulatees, rather than consult in a meaningful way.<sup>66</sup>

Does Ofcom act in a timely manner? Because Ofcom is a new regulator, it may be much too soon to consider this question. I will offer one example, however, because it is the United Kingdom's comparison proceeding to the FCC's media ownership review.<sup>67</sup> This is Ofcom's strategic review of PSB. Ofcom's PSB review was initiated on November 6, 2003,<sup>68</sup> partially completed on February 8, 2005, with the release of Ofcom's Phase 3 report, and will continue into summer or autumn 2005 as the regulator continues to consult on matters related to the United Kingdom's distinct nations and regions.<sup>69</sup> The PSB review was initially supposed to be a twelve-month review, so it appears that Ofcom acted in an untimely manner.<sup>70</sup> In terms of comparing the timeliness of Ofcom as a

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63. Posting of Russ Taylor to <http://www.ofcomwatch.co.uk/2005/03/ofcom-v-fsa-on-complaints> (Mar. 29, 2005, 22:09 GMT) [hereinafter Posting 1].

64. Posting of Russ Taylor to <http://www.ofcomwatch.co.uk/2005/09/ofcom-should-publish-its-foi-decisions> (Sept. 7, 2005, 12:13 GMT).

65. Posting of Russ Taylor to <http://www.ofcomwatch.co.uk/2006/01/ofcom-2005-year-in-review> (Jan. 1, 2006, 17:02 GMT).

66. *OfcomWatch*, *supra* note 56; see also Posting 1, *supra* note 63.

67. The public service broadcasting ("PSB") review has three phases and attempts to answer some of the same basic questions as the FCC's media ownership proceeding. For example, it attempts to answer what marketplace solutions and governmental regulations will work together to best deliver quality media to citizens and consumers. The PSB review feeds into the United Kingdom government's 2006 review of the BBC Charter, a process that commenced in December 2003 and will not conclude until mid-2006. See U.K. Department of Culture, Media and Sport, BBC Charter Review Timetable, <http://www.bbccharterreview.org.uk/home/timetable.html> (last visited Mar. 18, 2006).

68. See Press Release, Office of Communications, Ofcom Commences Full Review of U.K. Public Service Broadcasting (Nov. 11, 2003), [http://www.ofcom.org.uk/media/news/2003/11/nr\\_20031106](http://www.ofcom.org.uk/media/news/2003/11/nr_20031106) (last visited Sept. 18, 2005).

69. See OFFICE OF COMMUNICATIONS, OFCOM REVIEW OF PUBLIC SERVICE TELEVISION BROADCASTING, PHASE 3 - COMPETITION FOR QUALITY 2 (Feb. 8, 2005), available at <http://www.ofcom.org.uk/consult/condocs/psb3/psb3.pdf>.

70. See Office of Communications, *supra* note 59.

regulator controlled by New Labour with one manager with the timeliness of the FCC as an independent agency with five commissioners, the PSB review only tells a small story, but it nevertheless probably stands for the proposition that, when you ask or raise important questions of public policy, resolution of those issues will take time. The particular structure of the agency may only be a small factor in determining the timing of policy measures.

We will know much more about Ofcom and its effectiveness in the coming years. Some of that knowledge may address the issues raised in May's essay—what are the connections, if any, between agency structure and successful policy outcomes? I suspect the answer will never be clear. The policymaking environment contains too many variables, both known and unknown (e.g., technological advancements), to enable us to fashion “a model agency for the digital age.”<sup>71</sup> Regulators—no matter what their structure—will likely continue to disappoint their critics.

## VI. CONCLUSION

May hits the right tone in his essay. We should consider reform of the FCC, and reform of all institutional structures that govern the media and communications sector. Consideration of reform, however, cannot proceed unless we first come to a consensus, based partly on empirical evidence, that reform is needed and that the FCC is the entity to which reforms should be targeted. Similarly, efforts to reform the FCC will be fruitless if they are not part of a comprehensive reform strategy that considers the wider legal and policy environment in which the FCC operates.

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71. May, *supra* note 2, at 1325 (quoting former FCC Chairman William Kennard).

# Cable Operators’ Fifth Amendment Claims Applied to Digital Must-Carry

**Nissa Laughner\***

**Justin Brown\*\***

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## I. INTRODUCTION

As we face the widespread transition from analog to digital television, arguments are being made with increasing frequency by organizations such as the National Cable Television Association (“NCTA”) that regulations like digital must-carry violate cable operators’ Fifth Amendment rights.<sup>1</sup>

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1. See, e.g., LAURENCE H. TRIBE, WHY THE COMMISSION SHOULD NOT ADOPT A BROAD VIEW OF THE “PRIMARY VIDEO” CARRIAGE OBLIGATION, Enclosure to Letter from David L.

These arguments have been made in the past, although most cases have failed to reach the Fifth Amendment claims by deciding the issues solely on First Amendment grounds.<sup>2</sup> And yet, without a clear understanding of the extent of the property rights held by cable operators, and the relationship between such property rights and speech rights, the legal analysis of such claims will remain incomplete.

Although such claims are nascent, they ultimately raise important policy implications for the future of cable regulation, particularly in the broadband era.<sup>3</sup> Property rights may form an alternative basis by which to limit must-carry and access regulations because property rights form the basis of takings and due process claims brought under the Fifth and Fourteenth Amendments. The Takings Clause, as incorporated through the Fourteenth Amendment, prohibits both state and federal governments from appropriating private property for public use without just compensation.<sup>4</sup> Similarly, the Due Process Clause prohibits state or federal deprivations of property without due process of law.<sup>5</sup> At least theoretically, a taking requires just compensation while a due process violation requires invalidation.<sup>6</sup> Differences between due process and takings analyses, however, have been historically muddled. The process beginning with the

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Brenner, Senior Vice President, NCTA, to Marlene H. Dortch, Sec'y, Federal Communication Commission (Jul. 9, 2002), [www.ncta.com/Pdf\\_Files/exparte\\_tribe.doc.pdf](http://www.ncta.com/Pdf_Files/exparte_tribe.doc.pdf) [hereinafter *TRIBE MEMORANDUM*].

2. See, e.g., *Turner Brdcast. Sys. v. FCC (Turner I)*, 512 U.S. 622 (1994). Justice O'Connor in *Turner I* noted that imposing common carrier like obligations on cable operators may raise Takings Clause questions. *Id.* at 684. In fact, the only case to date that has analyzed cable property rights in the access context was later vacated. *Berkshire Cablevision of Rhode Island, Inc. v. Burke*, 571 F. Supp. 976, 988–89 (D. R.I. 1983), vacated, 773 F.2d 382 (1985).

3. Yochai Benkler, commenting on the cable broadband access debate, in 2000, noted that “[t]he importance of the question of whether infrastructure is privately or publicly owned (or not owned at all) is partly dependent on our regulatory response to the question of the relationship between ownership over physical infrastructure and control over content.” Yochai Benkler, *Net Regulation: Taking Stock and Looking Forward*, 71 U. COLO. L. REV. 1203, 1236 (2000) (citation omitted).

4. U.S. CONST. amend. V. The Takings Clause of the Fifth Amendment provides: “[N]or shall private property be taken for public use, without just compensation.” U.S. CONST. amend. XIV. “No State shall make or enforce any law which shall abridge the privileges and immunities of the citizens of the United States . . . .”

5. U.S. CONST. amend. V & U.S. CONST. amend. XIV, § 1. The Due Process Clause of the Fifth Amendment provides that “nor [shall any person] be deprived of life, liberty, or property without due process of law . . . .” “The Due Process Clause of the Fourteenth Amendment states that “nor shall any State deprive any person of life, liberty, or property, without due process of law . . . .”

6. Danaya C. Wright, *Eminent Domain, Exactions, and Railbanking: Can Recreational Trails Survive the Court's Fifth Amendment Takings Jurisprudence?*, 26 Colum. J. Envtl. L. 399, 414 (2001).

1922 Supreme Court decision in *Pennsylvania Coal v. Mahon*, in which the majority announced that certain regulations can go too far in their interference with property rights, thus becoming the de facto equivalent of a direct taking.<sup>7</sup>

With respect to cable regulation, significant free speech implications may be muddying the waters further. Neither speech nor property rights are exclusive of one another. The degree to which cable historically has had autonomy over its facilities—as established through regulation and tradition—influences both speech and property rights. The legal ownership of particular channel space through obligations—such as public, educational, or government (“PEG”) channels, leased-access, and must-carry—influences the degree to which a cable company may have editorial control over those channels.<sup>8</sup> The degree to which a franchise creates property rights, and the degree to which those rights and agreements may be modified by local or federal law, may influence how a cable facility is used and who can use the facility.<sup>9</sup> While private property owners, in the traditional sense, may have the right to exclude unwanted and disruptive speakers from their property,<sup>10</sup> cable operators operate under significant regulation, but unlike many regulated businesses, cable operates in a field historically imbued with free speech values. If regulation limits the property-based claims of highly regulated businesses in fields that do not directly implicate free speech concerns,<sup>11</sup> then potentially, regulations

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7. 260 U.S. 393, 415 (1922); see also Carol M. Rose, *Mahon Reconstructed: Why the Takings Issue Is Still a Muddle*, 57 S. CAL. L. REV. 561 (1984) (discussing *Mahon* and its significance to the takings jurisprudence).

8. See, e.g., *Denver Area Educ. Telecomm. Consortium, Inc. v. FCC (Denver Area)*, 518 U.S. 727, 727 (1996) (plurality opinion) (explaining that cable companies may choose to permit the airing of sexually offensive material).

9. See, e.g., *Cox Cable Comm., Inc. v. United States*, 866 F. Supp. 553 (M.D.Ga. 1994); *Cox Cable Comm. Inc. v. United States*, 774 F. Supp. 633 (M.D.Ga. 1991); *Madison Cablevision, Inc. v. City of Morganton*, 1990 U.S. Dist. LEXIS 18794 (W.D.N.C., 1990); *Triad CATV, Inc. v. City of Hastings*, 1989 U.S. Dist. LEXIS 17617 (W.D.Mi. 1989); *City Comm., Inc. v. City of Detroit*, 650 F. Supp. 1570 (E.D.Mi. 1987); *Hopkinsville Cable TV, Inc. v. Pennyroyal Cablevision, Inc.*, 562 F. Supp. 543 (W.D.Ky 1982); *Telecomm. of Key West, Inc. v. United States*, 580 F. Supp. 11 (D.D.C. 1983); *Telecomm. of Key West, Inc. v. United States*, 757 F.2d 1330 (D.C. Cir. 1985); *Carlson v. Village of Union City*, 601 F. Supp. 801 (1985).

10. See *Loretto v. Teleprompter Manhattan CATV Corp.*, 458 U.S. 419 (1982); *Kaiser Aetna v. United States*, 444 U.S. 164, 180 (1979) (describing a historical basis for the right to exclude); *Lloyd Corp. v. Tanner*, 407 U.S. 551, 568 (1972) (stating that it never before “held that a trespasser or an uninvited guest may exercise general rights of free speech on property privately owned and used nondiscriminatorily for private purposes only. Even where public property is involved, the Court has recognized that it is not necessarily available for speaking, picketing, or other communicative activities.”).

11. See *Ruckelshaus v. Monsanto Co.*, 467 U.S. 986, 1010–11 (1984) (holding that businesses that operate in highly regulated fields may have limited reasonable expectations

designed to serve free speech values may significantly constrain the property-based claims of cable providers.

The recent resurgence of legal claims related to digital must-carry offers the opportunity to reconsider our approach to cable autonomy and to address the balance of these rights. Addressing this balance is particularly important given the programming diversity made available through digital innovation, which increases programming streams and scanning formats as well as cable capacity to transmit. The debate over digital must-carry must take into account the administrative and capacity burdens on a cable operator that attend such diversity, the concerns of local broadcasters in their attempt to reach cable subscribers, and the concerns of consumers over access to local broadcast programming. Conceptions of the property and free speech rights of cable operators influence each of these concerns.<sup>12</sup> While it may be easier to decide cable autonomy issues solely on First Amendment grounds, or to attempt to separate the speech and property concerns, a more holistic picture of cable autonomy rights may only be possible with the development of a hybrid analysis that looks at the intersection of speech and cable property rights.

By identifying the legal and policy implications of property rights in the digital must-carry issue, this Article identifies underlying points of confusion associated with cable autonomy—a confusion that arises out of cable’s quasi-public, quasi-private status. Absent such analysis, this confusion may create an inconsistent and unpredictable regulatory and legal regime in which ever-expanding notions of property may silently and slowly encroach on prevailing notions of access or, alternatively, buttress speaker rights. Part II of this Article will begin with a review of must-carry regulations, including the recent policy debate over dual and multicast carriage. Part III will present a traditional Fifth Amendment analysis of must-carry. Part IV will address some of the free speech implications of this property-based analysis. Finally, Part V will conclude by showing how these property-based claims may influence future cable regulatory policies.

## II. MUST-CARRY AND RETRANSMISSION CONSENT RULES

The Federal Communications Commission (“FCC”) faces numerous concerns regarding must-carry and retransmission consent in the digital

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of property claims in light of current and potential regulation).

12. Even though the FCC in 2005 ruled that cable operators only have to carry either an existing analog or digital-only television station, this debate is far from settled. Broadcasters have vowed to contest the FCC’s decision. Drew Clark, *FCC Sides with Cable Industry in ‘Multicasting’ TV Debate*, NATIONAL JOURNAL’S CONGRESSDAILY, Feb. 11, 2005.



context,<sup>13</sup> most notably the calculation of cable channel capacity,<sup>14</sup> the definitions of “primary video”<sup>15</sup> and “program-related[ness],”<sup>16</sup> and the preservation of digital signal quality (e.g., material degradation).<sup>17</sup> Part of the FCC’s dilemma in applying the must-carry rules to digital television is that initial rules were written in an analog environment when each station delivered programming in the same signal format<sup>18</sup> (NTSC, 525 lines, 4x3 aspect ratio) and in the same amount of channel space (6 MHz).<sup>19</sup> In a digital environment, however, each station can transmit in eighteen different scanning formats and may send up to six simultaneous digital streams of programming. As a result, the application of the must-carry rules in the digital environment creates a policy quagmire.

#### A. Analog Must-Carry

The original must-carry rules are found in the Cable Television Consumer Protection and Competition Act of 1992 (“1992 Cable Act”), which amends the Communications Act of 1934.<sup>20</sup> The 1992 Cable Act prohibits cable operators and other multichannel video programming distributors from retransmitting commercial and low-power television signals, as well as radio broadcast signals, without the broadcaster’s consent. This permission is commonly referred to as retransmission consent.<sup>21</sup> When a broadcast station chooses to negotiate a retransmission consent agreement, the cable operator will compensate the station for the placement of its programming on the cable system.<sup>22</sup> Network-affiliated broadcasters are better positioned to negotiate retransmission agreements because of the popularity and ratings of their programs. Without these

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13. For an overview of the constitutional issues of applying the must-carry rules to digital television (“DTV”), see Albert N. Lung, Note, *Must-Carry Rules in the Transition to Digital Television: A Delicate Constitutional Balance*, 22 CARDOZO L. REV. 151 (2000).

14. See Carriage of Digital Television Broadcast Signals, *First Report and Order and Further Notice of Proposed Rule* [sic] *Rulemaking*, 16 F.C.C.R. 2598, paras. 124–27 (2001) [hereinafter *DTV Must-Carry*].

15. *Id.* paras. 50–57.

16. *Id.* para. 122.

17. *Id.* paras. 70–72.

18. See Carriage of Digital Television Broadcast Signals, *Notice of Proposed Rulemaking*, 13 F.C.C.R. 15092, para. 18 (1998).

19. *Id.* para. 9.

20. Cable Television Consumer Protection and Competition Act of 1992, Pub. L. No. 102-385, 106 Stat. 1460 (codified in scattered sections of 47 U.S.C.).

21. See generally Charles Lubinsky, *Reconsidering Retransmission Consent: An Examination of the Retransmission Consent Provision (47 U.S.C. § 325(b)) of the 1992 Cable Act*, 49 FED. COMM. L.J. 99 (1997) (providing an overview of cable television and retransmission content regulation).

22. 47 U.S.C. § 325(b)(10) (2000).

stations on their cable lineup, the cable system is likely to lose many customers. Estimates demonstrate that about 80% of commercial television broadcasters chose retransmission consent over must-carry in the 1993–96 election cycle.<sup>23</sup>

Under the 1992 Cable Act, however, a station may elect the must-carry option when its carriage does not financially benefit the cable system. Section 4 of the 1992 Cable Act requires cable operators to carry “the signals of local commercial television stations and qualified low power stations . . . .”<sup>24</sup> If a cable operator has twelve or fewer usable activated channels, the cable operator must carry only three local commercial stations, selected at the cable operator’s discretion. Cable operators, however, may not select a low-power station over a local affiliate and, if the cable operator elects to carry a local affiliate of a network, it must carry the affiliate that is nearest to the area served by the cable system. If a cable operator has more than twelve usable activated stations, however, then this operator must carry local commercial stations as requested, up to one-third of all channel capacity.<sup>25</sup>

Section 5 of the 1992 Cable Act also gives noncommercial (i.e., public) television stations authority to demand carriage.<sup>26</sup> Cable systems consisting of 12 or fewer channels are required to carry the signal of one qualified local noncommercial educational station.<sup>27</sup> Systems with thirteen to thirty-six channels are required to carry at least one but not more than three stations,<sup>28</sup> and cable systems with more than thirty-six channels are required to carry the signal of three noncommercial, educational stations.<sup>29</sup> In order to be considered a qualified noncommercial station, a station either must be licensed as such and “owned and operated by a public agency, nonprofit foundation, corporation, or association[.]”<sup>30</sup> or be owned and operated by a municipality transmitting “predominantly noncommercial

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23. Stuart N. Brotman, *National Cable Television Association*, “Priming The Pump”: *The Role of Retransmission Consent in the Transition to Digital Television*, October 1999, available at [http://brotman.com/whatsnew\\_article\\_priming\\_content.html](http://brotman.com/whatsnew_article_priming_content.html) (follow link to Retransmission’s Consent Track Record).

24. 47 U.S.C. § 534(a) (2000).

25. 47 U.S.C. § 534(b)(1)(B) (2000).

26. *Id.* § 535. Some commentators suggest the must-carry provisions protecting public television were singled out separately from commercial stations because more public stations had been dropped absent must-carry rules. Yet, the courts have failed to treat Section 4 or 5 of the 1992 Cable Act discriminately. Monroe E. Price & Donald W. Hawthorne, *Saving Public Television: The Remand of Turner Broadcasting and the Future of Cable Regulation*, 17 HASTINGS COMM. & ENT. L.J. 65, 83 (1994).

27. 47 U.S.C. § 535(b)(2)(A).

28. *Id.* § 535(b)(3)(A)(i).

29. *Id.* § 535(e).

30. *Id.* § 535(l)(1)(A)(i).

programs for educational purposes.”<sup>31</sup> Noncommercial stations rely exclusively on must-carry and, unlike their commercial counterparts, are not able to seek compensation under the retransmission consent provisions.<sup>32</sup>

In the findings section of the 1992 Cable Act, Congress cited many justifications for the must-carry and retransmission rules. Congress found the cable industry to be highly concentrated and worried that this concentration could lead to barrier-of-entry problems for new programmers and a reduction of media outlets (i.e., diversity) available to consumers.<sup>33</sup> Congress also contended the cable industry is increasingly vertically integrated consisting of common ownership among cable operators and cable programmers, and thus, operators favor affiliated programmers.<sup>34</sup> This integration made it “more difficult for noncable-affiliated programmers to secure carriage on cable systems.”<sup>35</sup> Most importantly, Congress found there was “substantial governmental and First Amendment interest in promoting a diversity of views provided through multiple technology media.”<sup>36</sup> As laid out in Section 307(b) of the 1934 Communications Act, Congress articulated an important governmental interest in the carriage of local stations because such carriage was necessary to provide a “fair, efficient, and equitable distribution of broadcast services.”<sup>37</sup> Local origination of programming was seen as a “primary objective” of must-carry regulation because local broadcast stations are an “important source of local news and public affairs programming” vital to “an informed electorate.”<sup>38</sup>

Given all the praise for local broadcasting, Congress found it necessary to promote the availability of free, over-the-air television to the public. Realizing the shift in audiences from broadcast to cable programming, Congress acknowledged that some advertising revenues would be reallocated to cable. In effect, cable systems carrying local broadcast stations were competing for advertising revenues on their own systems, and theoretically, cable operators had an economic incentive to terminate the retransmission of broadcast signals. Congress contended that

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31. *Id.* § 535(l)(1)(B).

32. 47 U.S.C. § 325(b)(2)(A) (2000).

33. Cable Television Consumer Protection and Competition Act of 1992, 102 Pub. L. No. 385, §2(a)(2)–(4), 106 Stat. 1460, 1460 (1993).

34. *Id.* § 2(a)(5).

35. *Id.*

36. *Id.* § 2(a)(6).

37. *Id.* § 2(a)(9).

38. *Id.* § 2(a)(11).

absent must-carry, there was a strong likelihood that “additional local broadcast signals will be deleted, repositioned, or not carried.”<sup>39</sup>

*B. Analog Must-Carry Rules Are Constitutional*

In 1997, by a five-to-four vote, the Supreme Court ruled the must-carry rules to be constitutionally valid under intermediate scrutiny as specified by the *O’Brien* test.<sup>40</sup> The Court examined the two inquiries left open during its prior review in *Turner I*: first, whether the factual record developed by the three-judge district court “supports Congress’ predictive judgment that the must-carry provisions further important governmental interests[.]”<sup>41</sup> and second, whether the rules did “not burden substantially more speech than necessary to further those interests.”<sup>42</sup>

In answering its first question, the Court reasserted that the rules furthered three important, interrelated governmental interests: (1) preserving the benefits of free, over-the-air local broadcast television, (2) promoting the widespread dissemination of information from a multiplicity of sources, and (3) promoting fair competition in the market for television programming.<sup>43</sup>

Combining these elements, the Court determined the must-carry rules aided in preserving a multiplicity of broadcast outlets, a substantial governmental objective. In reaching this conclusion, the Court exhaustively elaborated on predicted threats that existed absent any must-carry requirements. The increasing trends of vertical and horizontal integration in cable provided operators with the incentive and ability to give preferential treatment to their affiliated-programming services.<sup>44</sup> Moreover, when cable subscription percentages leveled off, cable operators were expected to compete more aggressively with broadcasters for advertising revenue.<sup>45</sup> The Court also demonstrated that a significant number of broadcasting

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39. *Id.* § 2(2)(a)(15). In light of the frequency with which retransmission consent is invoked, many researchers and commentators criticize the findings in the 1992 Cable Act and the Supreme Court’s use of these findings to uphold the rules. *E.g.*, Nancy Whitmore, *Congress, the U.S. Supreme Court and Must-Carry Policy: A Flawed Economic Analysis*, 6 COMM. L. & POL’Y 175, 177, 223–24 (2001); Thomas W. Hazlett, *Digitizing “Must-Carry” Under Turner Broadcasting v. FCC*, 8 SUP. CT. ECON. REV. 141, 195, 201 (2000).

40. *Turner Brdcast. Sys. v. FCC (Turner II)*, 520 U.S. 180, 185 (1997) (citing *United States v. O’Brien*, 391 U.S. 367 (1968)).

41. *Id.*

42. *Id.*

43. *Id.* at 189 (quoting *Turner I*, 512 U.S. at 662).

44. *Id.* at 197 (“Horizontal concentration was increasing as a small number of multiple system operators (MSO’s) acquired large numbers of cable systems nationwide.”).

45. *Turner II*, 520 U.S. at 203.

stations had been dropped during periods without must-carry rules,<sup>46</sup> placing some stations in financial disarray.<sup>47</sup> Accordingly, the Court found the provisions to be consistent with the first prong of *O'Brien*.<sup>48</sup>

Next, the Court examined the additional prong of *O'Brien*—namely whether the must-carry rules were broader than necessary to accomplish Congress’s objective. Upon reviewing the evidence adduced on remand, the Court found “cable operators have not been affected in a significant manner by must-carry.”<sup>49</sup> The Court cited many statistics to support its finding: 87% of the time cable operators had been able to meet must-carry requirements through previously unused channel capacity, 94.5% of cable systems nationwide did not drop any programming to fulfill their obligations, and cable operators carry an average of 99.8% of the programming they carried before enactment of must-carry.<sup>50</sup> The Court conceded that a majority of stations continue to be carried without must-carry. The Court also noted that the 5,880 broadcast channels, which appellants contended would be dropped absent any legal obligations, only placed a small burden on cable systems. In turn, “[b]ecause the burden imposed by must-carry is congruent to the benefits it affords,”<sup>51</sup> the Court concluded the provisions are narrowly tailored to meet its objective of preserving “a multiplicity of broadcast stations for the 40 percent of American households without cable.”<sup>52</sup>

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46. *Id.* at 202.

47. *Id.* at 208–09. Although contrary evidence was presented, the Court clarified its role, which was determining whether the legislative conclusion was supported by the record before Congress, not “reweigh[ing] the evidence *de novo*,” or “replac[ing] Congress’ factual predictions with [its] own.” *Id.* at 211 (quoting *Turner I*, 512 U.S. at 666).

48. *See id.* at 196.

49. *Id.* at 214.

50. *Id.* While cable operators contended these figures were overblown, the Court believed the results of must-carry spoke for themselves and stated, “It is undisputed that broadcast stations gained carriage on 5,880 channels as a result of must-carry. While broadcast stations occupy another 30,006 cable channels nationwide, this carriage does not represent a significant First Amendment harm to either system operators or cable programmers . . . .” *Id.* at 215.

51. *Turner II*, 520 U.S. at 215. The Court analyzed and rejected several proposed alternatives to the current must-carry rules, including: (1) the use of an A/B input selector switch, (2) a leased-access regime system, (3) subsidy mechanisms to support financially weak stations, and (4) antitrust enforcement or anticompetitive administrative procedures. *See id.* at 219, 221–22. Even though such alternatives placed less strain on cable operators, the Court articulated that “content-neutral regulations are not ‘invalid simply because there is some imaginable alternative that might be less burdensome on speech.’” *Id.* at 217. (quoting *United States v. Albertini*, 472 U.S. 675, 689 (1985)).

52. *Id.* at 216.

### C. *Digital Must-Carry*

Provisions in the Telecommunications Act of 1996 address advanced television,<sup>53</sup> a new system of broadcast television commonly referred to as digital television. In the legislative history, Congress stated that it did not intend to “confer must carry status on advanced television or other video services offered on designated frequencies” and added that the “issue is to be the subject of a Commission proceeding under section 614(b)(4)(B) of the Communications Act.”<sup>54</sup> Furthermore, according to the House Conference Report’s interpretation of the 1992 Cable Act, when the FCC adopts new standards for broadcast television signals, such as the authorization to broadcast in high definition, the FCC must conduct a proceeding to make any changes to signal carriage requirements.<sup>55</sup> Thus, the must-carry laws seem to be flexible enough to cover technological improvements,<sup>56</sup> and the FCC has authority to conduct a proceeding to determine in what way these laws should apply.

In 2001 the FCC established must-carry for digital-only television stations by providing for carriage of a digital station that returns its analog spectrum.<sup>57</sup> The FCC found that the 1992 Cable Act “neither mandates nor precludes the mandatory simultaneous carriage of both a television station’s digital and analog signals (‘dual-carriage’).”<sup>58</sup> The FCC also ruled that Congress intended the term “primary video” in the digital context to “mean[] a single programming stream and other program-related content”<sup>59</sup> and not the multicast streams that local broadcasters may offer.<sup>60</sup> As a result, the digital-only station must elect which programming stream is its primary video, and the cable operator must provide mandatory carriage to

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53. 47 U.S.C. § 336(a)(1)–(2) (2000).

54. BENTON FOUND., LEGISLATIVE BACKGROUND: DIGITAL TELEVISION AND CABLE TV, <http://www.benton.org/publibrary/policy/tv/legislation.html> (last visited Mar. 23, 2006).

55. H.R. CONF. REP. NO. 102-862, at 67 (1992).

56. To further demonstrate its authority to reinterpret the must-carry rules in the digital context, the FCC referred to the legislative history of the 1992 Cable Act. *DTV Must-Carry*, *supra* note 14, para. 8. The FCC stated:

[T]he relevant language states that when the FCC adopts new standards for broadcast television signals, such as the authorization of broadcast high definition television (HDTV), it shall conduct a proceeding to make any changes in the signal carriage requirements of cable systems needed to ensure that cable systems will carry television signals complying with such modified standards in accordance with the objectives of this section.

*Id.* n.25 (quotation omitted).

57. *DTV Must-Carry*, *supra* note 14.

58. *Id.* para. 2.

59. *Id.* para. 57.

60. *See id.* para. 55.

the broadcaster's primary video stream.<sup>61</sup> The FCC allowed stations flexibility to negotiate for full or partial carriage of its digital TV signal.<sup>62</sup> In addition, the FCC also allowed a commercial station that negotiates retransmission consent of its analog signal to tie carriage of its digital signal to carriage of its analog signal.<sup>63</sup>

Despite acknowledging the substantial governmental interests in preserving free television, a multiplicity of information sources, and fair competition in the programming market,<sup>64</sup> the FCC tentatively concluded that dual carriage places an undue burden on cable operators and therefore violates their First Amendment rights.<sup>65</sup> Presently, cable operators are "required to carry local television stations on a tier of service provided to every subscriber and on certain channel positions designated in the [1992 Cable] Act."<sup>66</sup> However, under the 1992 Cable Act, cable operators "are not required to carry duplicative signals or video that is not considered primary."<sup>67</sup> During the temporary transition from analog to digital broadcasting, an "increasing redundancy of basic content between the analog and digital signals as the Commission's simulcasting requirements are phased in."<sup>68</sup> If the FCC imposed a dual-carriage requirement, cable operators would be required to carry identical digital and analog television signals, and because of lessened channel capacity, cable operators could be forced to drop other programming services.<sup>69</sup> To make a final determination on dual-carriage, the FCC raised numerous questions regarding the seven DTV proposals<sup>70</sup> and requested further comment on

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61. *Id.* para. 57. For further analysis on the meaning and importance of "primary video" within the digital must-carry debate, see Michael M. Epstein, "Primary Video" and Its Secondary Effects on Digital Broadcasting: Cable Carriage of Multiplexed Signals Under the 1992 Cable Act and the First Amendment, 87 MARQ. L. REV. 525 (2004).

62. *DTV Must-Carry*, *supra* note 14, para. 27.

63. *Id.* para. 30.

64. *Id.* para. 4.

65. *Id.* para. 3. For further analysis of dual and multicast carriage, see Joel Timmer, *Broadcast, Cable and Digital Must Carry: The Other Digital Divide*, 9 COMM. L. & POL'Y 101 (2004).

66. *DTV Must-Carry*, *supra* note 14, para. 6 (citing 47 U.S.C. § 534(b)(6)–(7), § 535(g)(5), (h)).

67. *Id.* (citing 47 U.S.C. § 534(b)(3)(A), (b)(5), § 535(b)(3)(C), (g)). While the broadcast industry urged the FCC to impose a dual-carriage requirement during the transition period to "ensure that viewers have continued access to all available local television programming[.]" cable operators argued that dual carriage would create blank screens on their channel line-up, since "most consumers will not have digital television receivers or converters allowing them to display digital signals on analog sets." *Id.* para. 10 (citations omitted).

68. *Id.* para. 9.

69. *Id.*

70. See Carriage of the Transmissions of Digital Television Broadcast Stations, *Notice*

other digital must-carry concerns, including evaluating digital carriage agreements, retransmission consent, and market forces;<sup>71</sup> calculating cable system channel capacity;<sup>72</sup> and identifying and applying program-relatedness.<sup>73</sup>

In February 2005, the FCC reaffirmed its earlier decisions in its *Second Report and Order and First Order on Reconsideration*.<sup>74</sup> Specifically, the FCC reconsidered and ruled against the dual must-carry requirement.<sup>75</sup> The FCC also reconsidered and ruled primary video only constitutes one programming stream, not the full bit stream of a local digital broadcast station's combined multicast signals.<sup>76</sup> The FCC refuted that a number of governmental interests would not be met absent a dual-carriage requirement during the digital television transition. In light of the *Turner I* and *Turner II* decisions and the application of intermediate scrutiny, the FCC examined whether or not dual carriage would preserve free over-the-air television and promote "widespread dissemination of information from a multiplicity of sources."<sup>77</sup> The FCC concluded that the interests of viewers who wish to see local, over-the-air broadcast stations are not clearly threatened without dual must-carry. Cable carriage is not needed to ensure that noncable households have access to a digital broadcast station, and nearly all local analog stations are carried under retransmission consent or must-carry. In addition, "[t]he absence of a dual carriage requirement might in fact encourage broadcasters to produce a 'rich mix of over-the-air programming' in order to convince cable operators to voluntarily carry their digital signal."<sup>78</sup> Dual carriage also promotes duplicative programming—the same program in both analog and digital—and therefore does not promote the widespread dissemination of information from a multiplicity of sources.<sup>79</sup>

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of *Proposed Rulemaking*, 13 F.C.C.R. 15092, paras. 40–50 (1998) [hereinafter *Carriage of DTV*].

71. *DTV Must-Carry*, *supra* note 14, para. 130.

72. *Id.* para. 123.

73. *Id.* para. 122.

74. *Carriage of Digital Television Broadcast Signals, Second Report & Order and First Order on Reconsideration*, 20 F.C.C.R. 4516, paras. 2–3 (2005) [hereinafter *DTV Must-Carry II*].

75. *Id.* para. 27.

76. *Id.* para. 44.

77. *Id.* para. 14 (citation omitted).

78. *Id.* para. 18.

79. *Id.* para. 19. Furthermore, evidence suggests dual carriage would not necessarily expedite the DTV transition. *See id.* As of the beginning of 2005, cable operators offer an HDTV program package option in 184 of the 210 designated market areas ("DMAs") and carry more than 500 local DTV stations nationwide. Eighteen cable networks now offer some form of HDTV programming during part of their schedule. *Id.* para. 24. As a result,



After striking down dual carriage, the FCC examined what the must-carry policy should be after the digital television transition is completed for local stations who engage in multicasting. Even though the Congressional intent is unclear regarding the meaning of what constitutes primary video in the digital context,<sup>80</sup> the FCC examined whether an alternative interpretation would further the important governmental interests of free over-air-television—“widespread dissemination of information from a multiplicity of sources”<sup>81</sup> and facilitation of the digital television transition.<sup>82</sup> According to the FCC, Congress and the broadcast industry have failed to demonstrate that free local broadcasting would be jeopardized without multicast carriage. With the single program stream carriage requirement, a local broadcaster will still have a presence on the local cable system and requiring additional broadcast streams from the same broadcaster “would not promote diversity of information sources” and “arguably diminish the ability of other, independent voices to be carried on the cable system.”<sup>83</sup> The FCC believes that high quality digital programming will best facilitate the transition, including cable operators’ desire to carry local HDTV broadcast content, a scenario still possible under the single program stream carriage requirement.<sup>84</sup>

Currently, the only viable regulatory alternative that exists for the industry is to work within the parameters set forth by the FCC’s *DTV Must-Carry Report and Order and Further Notice of Proposed Rulemaking* and the FCC’s *Second Report and Order and First Order on Reconsideration*. Until the digital transition is complete,<sup>85</sup> or until a local station returns its analog spectrum voluntarily ahead of schedule, a local broadcaster may

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the FCC believes that the above trends will be more likely to spur the sales of DTV sets than the imposition of a dual-carriage requirement. *Id.* para. 25.

80. *Id.* para. 33.

81. *Id.* para. 37 (citation omitted).

82. *Id.* paras. 37–41.

83. *Id.* para. 39.

84. *Id.* para. 40.

85. To facilitate the timely recovery of analog spectrum, Congress and the FCC adopted an aggressive policy requiring broadcasters to convert to digital so it could reallocate and auction part of the existing spectrum utilized by analog broadcasting. The Balanced Budget Act of 1997 provides an exception for the termination of analog services. A station may extend its analog operation beyond 2006 if the television market in which it is operating has not received an 85% penetration in DTV viewership. Otherwise, analog operation will end when 85% of households in a given market can receive a digital signal. See Balanced Budget Act of 1997, Pub. L. No. 105-33, § 3003, 111 Stat. 251, 265 (codified at 47 U.S.C. § 309(j)(14)(B)). Congress changed the 85% rule to a hard date of February 18, 2009, when broadcasters must return their analog spectrum to the government, effectively shutting down analog TV broadcasting. See Digital Television Transition and Public Safety Act of 2005, Pub. L. No. 109-171, § 3002, 120 Stat. 4 (2006) (codified in scattered sections of 47 U.S.C.).

only elect must-carry for its analog signal. When a station returns its analog spectrum, then a station may invoke must-carry for the single, primary video program—whether in HDTV or standard-definition—that they elect. Unless otherwise specified in the future,<sup>86</sup> the plan only provides a mandatory right for a station's single, primary video signal. As a result, retransmission consent bargaining and market forces are undoubtedly key variables to examining viable policy alternatives, both during and after the digital broadcast transition. Because more than sixty percent of all households receive their local television broadcast signals through cable systems,<sup>87</sup> significant progress needs to take place in reaching additional retransmission consent agreements if the public at large is to reap the potential benefits of digital broadcasting.

### III. CABLE FIFTH AMENDMENT CLAIMS

Because the FCC ruled against dual and multicast carriage, the FCC declined to explore and reach any conclusions on the merits of the Fifth Amendment Takings Clause arguments brought by cable operators.<sup>88</sup> Because of the FCC's most recent *Order*,<sup>89</sup> cable operators may no longer face the prospect of significant must-carry burdens in the form of dual or multicast carriage of multiple channel streams.<sup>90</sup> Rather, as noted earlier, the FCC ruled that "primary video" in the digital context meant only "a single programming stream and other program-related content,"<sup>91</sup> Nevertheless, broadcasters are likely to challenge the FCC's most recent

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86. Based upon the DTV policy model employed in Germany, Ferree and Powell believe the down-converting plan would expedite the transition because existing cable and satellite subscribers who receive local stations may be included in the 85% rule calculation. In addition, such a policy would nullify any need for a dual-carriage requirement for analog and digital signals during the transition. Ted Hearn, *Powell Floats a Rigid DTV Switchover*, MULTICHANNEL NEWS, Mar. 15, 2004, at 50; Ted Hearn, *Powell Pushes Back on DTV Plan*, MULTICHANNEL NEWS, Apr. 5, 2004, at 26. For more specific details and analysis of the Berlin plan and its utility in the United States, see *German DTV Transition Differs from U.S. Transition in Many Respects, But Certain Key Challenges Are Similar: Testimony Given Before Subcomm. on Telecommunications and the Internet of the H. Comm. on Energy and Commerce*, REP. NO. GAO-04-926T (2004) (statement of Mark L. Goldstein, Director, Physical Infrastructure Issues). In addition, the FCC deferred the issue of program-relatedness in the context of digital must-carry for a subsequent report and order. See *DTV Must-Carry II*, *supra* note 74, para. 44.

87. See Annual Assessment of the Status of Competition in the Market for Delivery of Video Programming, *Twelfth Annual Report*, FCC 06-11, para. 37 (2006), [http://hraunfoss.fcc.gov/edocs\\_public/attachmatch/FCC-06-11A1.pdf](http://hraunfoss.fcc.gov/edocs_public/attachmatch/FCC-06-11A1.pdf). As of June 2005, 65.4 million of the nation's 109.6 million television households subscribed to cable television service. *Id.*

88. *DTV Must-Carry II*, *supra* note 74, paras. 26, 42.

89. See *id.*

90. See *supra* notes 72–82 and accompanying text.

91. *DTV Must-Carry*, *supra* note 14, para. 57.

order on constitutional grounds or urge Congress to pass specific digital must-carry legislation.<sup>92</sup> Furthermore, the FCC has extended a basic, single program must-carry regime into the digital era.<sup>93</sup> Cable operators may view the transition as an opportunity to gain more control over their facilities by challenging any carriage and advocating for a regime based primarily on retransmission consent.

Cable operators and their advocates are developing their Fifth Amendment arguments. Lawrence Tribe, a law professor at Harvard Law School, for example, was commissioned by the National Cable Television Association (“NCTA”) to write a report about digital must-carry in 2003. In this report, he argued that multichannel must-carry violated the Fifth Amendment.<sup>94</sup> More specifically, he argued that multichannel must-carry is a form of actual, physical invasion that takes advantage of the substantial investments made by cable operators in upgrading their facilities for digital transmission, a *per se* violation of the Takings Clause.<sup>95</sup> Legal representatives for public broadcasting have responded to Tribe’s arguments by emphasizing that since must-carry was upheld by the Supreme Court in the *Turner* litigation, the issue of multichannel carriage does not raise Fifth Amendment implications.<sup>96</sup>

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92. See *supra* note 13 and accompanying text. The National Association of Broadcasters (“NAB”) “will be working to overturn today’s anti-consumer FCC decision in both the courts and Congress.” Todd Shields, *It’s Official: Must-Carry is Out*, MEDIAWEEK, Feb. 14, 2005, at 7, [http://www.mediaweek.com/mw/search/article\\_display.jsp?schema=&vnu\\_content\\_id=1000798343&WebLogicSession=QhcqraUzNNyuPtU9fouOTEtLUzcQnEGa1PIJfhqEbMcJQP1ar6Da%7C1399616429770259426/181605430/6/7005/7005/7002/7002/7005/-1](http://www.mediaweek.com/mw/search/article_display.jsp?schema=&vnu_content_id=1000798343&WebLogicSession=QhcqraUzNNyuPtU9fouOTEtLUzcQnEGa1PIJfhqEbMcJQP1ar6Da%7C1399616429770259426/181605430/6/7005/7005/7002/7002/7005/-1) (quoting Eddie Fritts, Chairman & CEO of the National Association of Broadcasters). The NAB also asked the FCC to reconsider its second order concerning digital must-carry. See Carriage of Digital Television Broadcast Signals, *Petition for Reconsideration of the National Association of Broadcasters and the Association for Maximum Service Television, Inc.*, CS-Docket No. 98-120, April 21, 2005, available at <http://www.nab.org/Newsroom/PressRel/Filings/ReconPetitionCarriage42105.pdf>.

93. See Clark, *supra* note 12.

94. TRIBE MEMORANDUM, *supra* note 1.

95. See *generally id.* (discussing the Takings Clause and the government’s inability to avoid the clause when the government takes a business and continues its operation). The mere fact that cable operators may retain “title to and bare possession of the tangible real and personal property necessary to provide programming,” in the view of Tribe, does not make the government’s commandeering of the channel capacity any less blatant. *Id.* at 15 (citation omitted). Although Tribe acknowledged that must-carry obligations only occupy a small portion of the cable operators’ total bandwidth capacity, he stressed “[t]here is no constitutional exception that allows the government to avoid the Takings Clause by taking one strand of property at a time.” *Id.* (citation omitted).

96. See Letter from Lonna M. Thompson et al., Vice President and General Counsel, Ass’n of Public Television Stations, to Marlene H. Dortch, Sec’y, FCC, 7 n.8 (Mar. 4, 2004), available at [http://www.aptv.org/members/legal/public/loader.cfm?url=/commonspot/security/getfile.cfm&pageid=6352\\_1.pdf](http://www.aptv.org/members/legal/public/loader.cfm?url=/commonspot/security/getfile.cfm&pageid=6352_1.pdf).

But because neither *Turner* decision directly addressed the Fifth Amendment implications of must-carry,<sup>97</sup> such claims remain open as an alternative basis for relief. The Fifth Amendment implications of digital must-carry will likely be complex—more so than outlined in the debate thus far. Following a typical Fifth Amendment analysis, this Part looks first to whether must-carry qualifies as a *per se* taking, an actual physical invasion, and then proceeds with an analysis of whether must-carry is a regulation that goes too far in its interference with property rights, thus giving rise to just compensation under a traditional regulatory takings analysis.

#### A. *Physical Appropriation*

Must-carry may be characterized as a physical taking because the provision authorizes local broadcasters to physically invade cable channel capacity.<sup>98</sup> State action that authorizes a permanent physical invasion constitutes a *per se* taking, automatically giving rise to just compensation, even if the economic impact of the regulation on the property owner is negligible. This rule, formed from a long line of precedent,<sup>99</sup> was summarized and succinctly announced in the 1982 decision of *Loretto v. Teleprompter Manhattan CATV Corp.*,<sup>100</sup> when the Court invalidated a state statute that authorized the attachment of cable boxes to tenant housing.<sup>101</sup> Ignoring the *de minimis* nature of the space occupied by the cable box,<sup>102</sup> the Court emphasized that any state-compelled, permanent occupation gives rise to “a historically rooted expectation of compensation.”<sup>103</sup>

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97. In *Turner I*, however, Justice O'Connor noted that there may be Fifth Amendment implications to must-carry. Unfortunately, the argument was not developed. See *Turner I*, 512 U.S. at 684 (O'Connor, J., concurring in part and dissenting in part).

98. See *supra* notes 24–31 and accompanying text. If a station elects retransmission consent, then the cable operator compensates the station for programming. Such compensation is dependent on market factors. See *supra* notes 21–23 and accompanying text. As such, no Fifth Amendment implications arise.

99. See, e.g., *Loretto v. Teleprompter Manhattan CATV Corp.*, 458 U.S. 419 (1982); *Kaiser Aetna v. United States*, 444 U.S. 164, 179–80 (1979) (“We hold that the ‘right to exclude’ so universally held to be a fundamental element of the property right, falls within this category of interests that the Government cannot take without compensation.”) (citation omitted); *Int’l News Serv. v. Assoc. Press*, 248 U.S. 215, 250 (1918) (Brandeis, J., dissenting) (“An essential element of individual property is the legal right to exclude others from enjoying it.”).

100. 458 U.S. 419 (1982).

101. *Id.*

102. *Id.* at 436–37.

103. *Id.* at 441 (noting that an occupation is “qualitatively more intrusive than perhaps any other category of property regulation.”).

However, the Court cautioned that the *per se* rule did not extend to “restrictions upon the owner’s use of his property.”<sup>104</sup> Had the statute, for example, simply required the landlord to provide cable service to requesting tenants, the landlord would have retained sufficient control over cable installation and the *per se* rule would have been inapplicable.<sup>105</sup> Indeed, the right to exclude, as used in the *Loretto* decision, seems closely related to trespass.<sup>106</sup> The state statute in *Loretto* allowed individual cable installers to enter the landowner’s property at will.<sup>107</sup> The *Loretto* Court noted that “an owner suffers a special kind of injury when a *stranger* directly invades and occupies the owner’s property.”<sup>108</sup> Thus, a regulation that did not completely and permanently divest an owner of this right to exclude would not be a *per se* taking.<sup>109</sup> It would be a restriction on use, a restriction more appropriately analyzed under a traditional regulatory takings analysis.

Determining how and when a regulation governs a use of a property and when a regulation authorizes an actual, physical occupation may be a bit tricky in the must-carry context. Does must-carry authorize an actual, physical invasion of channel space, or does must-carry require cable operators to offer local broadcast channels to subscribers in a convenient manner? Many cable operators face pre-existing limitations on their use of channel space per their historical development as a quasi-public, quasi-private entity subject to limited public interest obligations.<sup>110</sup> Is must-carry a permanent invasion in the same way that the attachment of a cable box is permanent, or is it more analogous to the temporary invasion of speakers in a mall environment? Does must-carry compel a physical invasion in physical space by taking cable bandwidth, or does must-carry merely modify a use of a property by mandating limited relationships with local broadcasters?

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104. *Id.* Such powers included the right to impose “affirmative duties on the owner.” *Id.* at 436.

105. *Id.* at 440–41 n.19.

106. See Dennis H. Long, Note, *The Expanding Importance of Temporary Physical Takings: Some Unresolved Issues and An Opportunity for New Directions in Takings Law*, 72 IND. L.J. 1185, 1198–99 (1997) (citation omitted).

107. See *Loretto*, 458 U.S. at 423 n.3.

108. *Id.* at 436.

109. In *Dolan v. City of Tigard*, the Court further drew a distinction between a permanent “occupation” and a temporary “use.” 512 U.S. 374 (1994). The Court agreed that landowners would issue “time, place, and manner” restrictions on speech activities so as to ensure that such speech does not disrupt commercial functions. See *id.* at 394 (citing *PruneYard Shopping Center v. Robins*, 447 U.S. 74, 83 (1980)).

110. See *Midwest Video Corp. v. FCC*, 440 U.S. 689, 701 (1979) (determining that cable could not be made into “pro tanto common carriers”).

*Loretto* suggests that *per se* analysis only applies in situations involving a pre-existing, historically-based right to exclude.<sup>111</sup> The Court has traditionally protected real property interests with great zeal because of the certain historical expectations associated with the development and use of real property.<sup>112</sup> Property-based protections for business interests fell into disfavor after the demise of *Lochner*-era substantive due process review in the 1930s because such protections tended to equate laissez-faire economics with constitutional protection.<sup>113</sup> While the Fifth Amendment continues to protect business interests and equipment against regulations that go too far, less of a historical basis exists on which to base reasonable expectations. As a result, the right to exclude and the *per se* test may not extend to all forms of tangible and intangible property.

If this were so, claimants could require compensation by simply couching their claims in terms of an actual, physical invasion. For instance, a bank might allege that a regulation requiring a bank to divest for fraudulent practices was a compelled, physical invasion of their shareholders' profits.<sup>114</sup> A company might allege that a settlement deduction for the use of a governmental tribunal was a compelled, physical occupation of the settlement.<sup>115</sup> However, to borrow a term from the Supreme Court, these examples show an "extravagant extension of *Loretto*."<sup>116</sup> In such circumstances, the *Loretto* rule would usurp contract remedies and other forms of relief; any person who faced economic harm from a regulation would be able to claim an actual, physical invasion and entitlement to just compensation. The cost of regulation would be

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111. See *Loretto*, 458 U.S. at 435 (citation omitted).

112. See Molly S. McUsic, *The Ghost of Lochner: Modern Takings Doctrine And Its Impact on Economic Legislation*, 76 B.U. L. REV. 605, 612–14.

113. See *id.* at 610. See also *West Coast Hotel Co. v. Parrish*, 300 U.S. 379, 392 (1937) ("Liberty implies the absence of arbitrary restraint, not immunity from reasonable regulations . . .") (quoting *Chicago, B. & Q. R. Co. v. McGuire*, 219 U.S. 549, 567 (1911)).

114. In *Golden Pacific Bancorp v. United States*, 15 F.3d 1066 (Fed. Cir. 1994), the court of appeals faced a Fifth Amendment claim by the Golden Pacific Bank that was based in part on a claim there was a *per se Loretto* taking and in part on the *Penn Central* balancing test. See *id.* at 1071–72. In this case, the Comptroller of Currency began an investigation of Golden Pacific, the bank, for insolvency. Rumors of the investigation of the bank lead to a run on the bank; the Comptroller then, based in part on this run, declared that the bank was insolvent. See *id.* at 1069. The bank alleged that this was a physical invasion of the bank's property, asserting that the action was a taking of the value of the stock for the stockholders. See *id.* at 1073 (diminishing the value of the stock was not a physical invasion). The court held however that there was no "historically rooted expectation of compensation," and that because the bank was operating in a highly regulated field it had "less than the full bundle of property rights." *Id.* at 1073–74 (citations omitted).

115. *United States v. Sperry Corp.*, 493 U.S. 52, 62 (1989).

116. *Id.* at 62 n.9.

prohibitive.<sup>117</sup> In essence, a deregulatory mandate would be encrypted into the Constitution.

As a result, in those few cases that have looked at access to telecommunication facilities from a property-based perspective, the courts have avoided a direct application of the *per se* rule.<sup>118</sup> For example, in *Qwest Corp. v. United States*,<sup>119</sup> a federal claims court determined there was no permanent physical invasion when a law required incumbent local telephone services to carry the signals of competing local telephone service providers on an unbundled, nondiscriminatory basis.<sup>120</sup> The *Qwest* court distinguished *Loretto* by emphasizing that the statute gave cable operators control over the installation process itself,<sup>121</sup> but the telephone interconnection law gave incumbent phone companies power over installation and service of equipment as well as the interconnection process.<sup>122</sup> *Qwest* argued that physical occupation of the telephone wires existed in terms of “flow of electrons.”<sup>123</sup> The court rejected this argument, emphasizing that *Loretto* applied to invasion by physical objects that invade physical space,<sup>124</sup> that the regulation governed not real property but

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117. *McUsic*, *supra* note 112, at 655 (“Economic interests, such as personal property, trade secrets, copyright, and money, are all recognized by the Court as ‘property’ under the Fifth Amendment, but receive little protection against government regulation.”) (citation omitted).

118. *See, e.g.*, *Qwest Corp. v. United States*, 48 Fed. Cl. 672 (2001); *Berkshire Cablevision of Rhode Island, Inc. v. Burke*, 571 F. Supp. 976 (D.R.I. 1983), *vacated*, 773 F.2d 382 (1st Cir. 1985).

119. 48 Fed. Cl. 672 (2001).

120. *Id.* at 675 (citing 47 U.S.C. § 251(c)(3)).

121. *Id.* at 691.

122. *Id.*

123. *Id.* at 693. Specifically, *Qwest* argued that there was physical occupation of its loops, the telephone wire that comes into the home and is connected to a central office switch—also known as the “first and last mile.” *Id.* at 695.

124. *Id.* at 694. The physical and virtual collocation requirements in the Communications Act were slightly more problematic. Physical collocation allowed competing access providers to enter the physical offices of local exchange carriers and to “install and operate its circuit terminating equipment” in this space, which virtual collection, allows the local exchange carriers to mandate the equipment used by competing access providers and “to string . . . cable to a point of interconnection . . .” *Id.* at 691–92 (citation omitted). A prior but noncontrolling decision had found physical collocation to be in violation of *Loretto*. *Id.* (citing *GTE Northwest, Inc. v. PUC*, 900 P.2d 495 (1995), *cert. denied*, 517 U.S. 1155 (1996)). The *Qwest* court emphasized that three main factors determinative in these decisions—there is a direct physical attachment; a third party owns the material to be attached; and, attachment is mandatory—would also be determinative if *Qwest* were directly challenging a competing exchange carrier’s physical collocation without just compensation. *Id.* at 692. The holdings were not determinative, however, with regard to the loops, since none of the factors were truly satisfied. *See id.* at 693.

closely regulated equipment,<sup>125</sup> and that interconnection regulated the use of property by mandating a lessor/lessee relationship.<sup>126</sup>

In the context of highly regulated equipment—particularly when no direct, physical, and tangible attachment is made—regulations may almost always be construed as constituting property use rather than a physical invasion. While *Loretto* stressed that the *de minimis* nature of the cable box did not alter the nature of the invasion,<sup>127</sup> a *de minimis* exception does seem to exist for intangible property and functional equipment. A fundamental difference can be seen between digital and analog signals passing to and fro along the cable lines and actual individuals passing to and fro on a person's land. The latter instance is "qualitatively more intrusive," thus justifying the application of a *per se* rule.<sup>128</sup> To refuse a distinction would be to create a constitutional matrix that prioritized property rights to such an extent that many other rights would be crippled. The exception would subsume the rule, traditional takings analysis, and even, as will be discussed *infra*, First Amendment analysis.

Furthermore, even in situations involving tangible, real property invasions, it is unclear whether a pre-existing right to exclude continues to exist regardless of the property's current use. In 1980, just two years before *Loretto*, the Supreme Court in *PruneYard Shopping Center v. Robins*<sup>129</sup> determined that California could, pursuant to its state constitution, require mall owners to allow peaceful public speech on the premises.<sup>130</sup> The Court had previously stated that the First Amendment did not limit private property rights by extending public speech rights on private property.<sup>131</sup> Nevertheless, the Court held that state legislatures could extend greater speech protection than that afforded by the First Amendment by limiting state-created property rights.<sup>132</sup> The Court thus suggested that the invasion in *PruneYard* was not egregious because the mall owner profited by creating a sense of public space.<sup>133</sup>

In *Loretto*, the Court distinguished *PruneYard* by emphasizing that the invasion in *Loretto* was permanent, while the invasion in *PruneYard* was only temporary and limited.<sup>134</sup> It is unclear, however, whether the

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125. *See id.* at 694–95.

126. *See id.* at 695.

127. *See Loretto v. Teleprompter Manhattan CATV Corp.*, 458 U.S. 419, 436–37 (1982).

128. *Id.* at 441.

129. 447 U.S. 74 (1980).

130. *Id.* at 83.

131. *Lloyd Corp. Ltd. v. Tanner*, 407 U.S. 551 (1972).

132. *See PruneYard*, 447 U.S. at 82–83.

133. *Id.* at 83–84.

134. *See Loretto v. Teleprompter Manhattan CATV Corp.*, 458 U.S. 419, 434 (1982).



Court would continue to view a right of access for speech purposes as a temporary invasion. For example, *in dicta* from *Nollan v. California Coastal Comm'n* the Court explained that when “individuals are given a permanent and continuous right to pass to and fro” on private property by an act of government, a violation of *Loretto* is likely.<sup>135</sup> How do we distinguish between a right of access to pass to and fro and a right of access to speak, as with must-carry?

The initial decision to open the property to the public in *PruneYard* made the speech access right qualitatively less intrusive.<sup>136</sup> The Court further developed this distinction in *Yee v. City of Escondido*,<sup>137</sup> upholding a rent control law against an allegation of invasion because the landowner made the initial decision to enter the rental market. Determining how regulations that give access to particular channels modify historical

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The distinction between a permanent and temporary invasion, particularly in the must-carry context, is further discussed in the context of regulatory takings. See Danaya C. Wright & Nissa Laughner, *Shaken, Not Stirred: Has Tahoe-Sierra Settled or Muddied the Regulatory Takings Waters?* 32 E.L.R. 11177, 11180–82 (2002). The time component adds a dimension to the question of how to define the relevant property right being regulated. Per the current analysis, permanence seems to refer to the fact that in the malls, speakers may come and go. In the context of must-carry, however, the channels are more permanently occupied by broadcasters.

135. *Nollan v. California Coastal Comm'n*, 453 U.S. 827, 832 (1987).

136. In *Lloyd Corp., Ltd. v. Tanner*, however, a plurality of the Court reversed an injunction against a mall owner preventing the owner from interfering with peaceful demonstrations on the mall property. The Court reasoned that

[a]lthough accommodations between the values protected by [the First, Fifth, and Fourteenth] Amendments are sometimes necessary, and the courts properly have shown a special solicitude for the guarantees of the First Amendment, this Court has never held that a trespasser or an uninvited guest may exercise general rights of free speech on property privately owned and used nondiscriminatorily for private purposes only. Even where public property is involved, the Court has recognized that it is not necessarily available for speaking, picketing, or other communicative activities.

407 U.S. at 567–68.

The Court also stressed that property remains private even if the “public is generally invited to use it for designated purposes,” such as commerce. See *id.* at 569. However, in the dissenting opinion joined by Justices Douglas, Brennan, and Stewart, Justice Marshall spoke of the implications of too strongly expanding property rights in this context:

As governments rely on private enterprise, public property decreases in favor of privately owned property. It becomes harder and harder for citizens to find means to communicate with other citizens. Only the wealthy may find effective communication possible unless we . . . continue to hold that “[t]he more an owner, for his advantage, opens up his property for use by the public in general, the more do his rights become circumscribed by the statutory and constitutional rights of those who use it.

*Id.* at 586 (quoting *Marsh v. Alabama*, 326 U.S. 501, 506 (1946)).

137. 503 U.S. 519, 531 (1992).

expectations, and whether cable operators, like landlords, make the initial decision to open their properties creates imperfect analogies.

Such imperfection is reflected in the fractured *Denver Area* decision<sup>138</sup> in which the Court was asked to determine the extent of cable control over leased and PEG channels. Some Justices, for example, determined that PEG access channels were a historical and pre-existing limitation on cable franchises,<sup>139</sup> while other Justices would have required a consistent and formal property-like demand of PEG channels by local authorities in order to find such a pre-existing limitation.<sup>140</sup> With respect to leased access channels, Justices in *Denver Area* argued that the leased grant did not guarantee freedom from cable editorial control,<sup>141</sup> and with respect to both leased and PEG channels, three Justices argued that cable operators were the original owners in much the same way booksellers own and control bookstores and the materials sold therein.<sup>142</sup>

Analogizing must-carry to either PEG or leased channels is also imperfect. Historically, early cable television systems did carry broadcast channels almost exclusively until the FCC, through the origination rules, required cable to produce original programming.<sup>143</sup> Unlike PEG channels, however, which were negotiated by local authorities in exchange for franchise rights to use local rights-of-way, must-carry is not the result of negotiation, but of a government mandate to carry when negotiation, in the form of retransmission consent, fails.<sup>144</sup> While the initial decision of cable operators to offer cable communications may historically have included an expectation of carriage,<sup>145</sup> the primary purpose of cable operators is to offer their own programming and to offer channel space on a competitive basis to nonaffiliated programmers.<sup>146</sup> Additionally, must-carry does not

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138. 518 U.S. 727 (1996).

139. *See id.* at 760–64 (plurality opinion).

140. *See id.* at 828 (Thomas, J., joined by Rehnquist, C.J., and Scalia, J., concurring in judgment in part and dissenting in part) (emphasizing that a public forum analysis, the basis of the analysis for a historical and pre-existing limitation on cable channel control, would require, in the least, “property in which the government has held at least some formal easement or other property interest permitting the government to treat the property as its own in designating the property as a public forum.”) Justice Thomas distinguished PEG access channels as a regulatory restriction, not the appropriation of a formal property interest. *See id.*

141. *See id.* at 746–52, 771 (Stevens, J., concurring), 824–27 (Thomas, J., concurring in judgment in part and dissenting in part).

142. *Id.* at 824–27.

143. *See United States v. Midwest Video*, 406 U.S. 649, 655–56.

144. *See supra* notes 24–31 and accompanying text.

145. *See Midwest Video*, 406 U.S. at 655–56.

146. The vertical program limit, however, stipulates that cable operators may air no more than 40% of programming that they have an affiliated ownership interest in. *See Time*

mandate a lessor/lessee relationship because broadcasters are not required to pay for connection to the cable facility.<sup>147</sup>

Nevertheless, it is unlikely that the actual, physical invasion rule would protect a cable company's ability to offer channel space on a competitive basis to nonaffiliated programmers completely, particularly since cable has historically been subject to public interest obligations. Indeed, cable operators are limited in assuming a historically-based right to exclude because they serve a uniquely public function and because of particularly technological characteristics. In *Turner I*, the Court reasoned that while cable operators were speakers for First Amendment purposes, they may be subject to limited, viewpoint-neutral regulations like must-carry because of their detrimental impact on free over-the-air programming.<sup>148</sup> The Court was concerned with the ability of cable operators to "restrict, through the physical control of a critical pathway of communication, the free flow of information and ideas."<sup>149</sup> Unlike other forms of mass communication like newspapers, cable operators were uniquely positioned to prevent other speakers from reaching cable subscribers—unless such speakers were able to contract for space on the cable facility.<sup>150</sup> In the property context, such gatekeeping might suggest that a physical takings analysis is inappropriate.<sup>151</sup>

In sum, the utility of the *per se* permanent, physical occupation test in the context of digital must-carry is doubtful. Access for speech purposes is considered a limitation on the right to exclude that is constitutionally valid

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Warner Entm't v. FCC (*Time Warner*), 240 F.3d 1126 (D.C. Cir. 2001) (remanding the FCC's national household penetration cap and affiliated program channel limits to the FCC for factual justification). The FCC is in the process of revising both the horizontal and vertical ownership rules that apply to cable systems. See The Commission's Cable Horizontal and Vertical Ownership Limits and Attribution Rules, *Further Notice of Proposed Rulemaking*, 16 F.C.C.R. 17312 (2001); The Commission's Cable Horizontal and Vertical Ownership Limits, *Second Further Notice of Proposed Rulemaking*, 20 F.C.C.R. 9374 (2005).

147. See 47 U.S.C. §534(b)(10) (2000).

148. See *Turner I*, 512 U.S. at 656–57.

149. *Id.* at 657 (citation omitted).

150. *Id.* at 656–57.

151. In some respects, must-carry may be viewed as analogous to an easement by necessity, a common law doctrine allowing a right of passage across surrounding private property if a parcel is completely encapsulated. See *Quinn v. Holly*, 146 So. 2d 357, 359 (Miss. 1962). An easement by necessity seems to be an historical exception to a general right to exclude that evolves out of practical necessity and public policy. Similarly, access, if historically necessary to reach cable subscribers, may be an historical exception to a general right of cable systems to exclude speakers. See Harold Feld, *Whose Line Is It Anyway? The First Amendment and Cable Open Access*, 8 COMM.LAW CONSP. 23, 24 (2000) (suggesting that, with respect to broadband open access, "an open access requirement amounts to a 'virtual easement' over the cable plant.").

unless, as the Court in the later decision of *Dolan* explained, such restriction unqualifiedly and unreasonably impairs the primary value or use of the property.<sup>152</sup> An actual, physical invasion requires that there be an actual, historical right to exclude based on both the nature and the function of the property. Thus, even though the *Loretto* test, as a *per se* analysis, is based on a lower evidentiary standard than that used in traditional regulatory takings analysis, the application of this *per se* rule is limited.<sup>153</sup> Even if the *Loretto* rule does not apply, must-carry may certainly be viewed as a regulation on the use of the property and thus may be analyzed under a traditional regulatory takings analysis.

### B. Regulatory Takings

The traditional test for regulatory takings emerged in *Penn Central Transp. Co. v. New York* (“*Penn Central*”).<sup>154</sup> *Penn Central* involved a claim against the designation of the Penn Central Station as a state historic landmark, thus prohibiting its owners from developing the air space above the monument. The Court utilized a three-prong, ad-hoc analysis that considered the following: (1) the character of the governmental action; (2) the economic impact of the action; and (3) the extent to which such action interferes with the claimant’s reasonable investment backed expectations.<sup>155</sup> In general, the more intrusive the governmental action, the greater the negative economic impact of the regulation on the plaintiff, and the more reasonable the plaintiff’s reasonable investment backed expectations, the more likely a regulatory taking has occurred.<sup>156</sup>

Based upon the three-part test articulated above, *Penn Central* could not prevail on its regulatory takings claim. First, the character of governmental action in *Penn Central*—the historical landmark designation—was not a direct physical invasion or motivated by a “uniquely public function[.]”<sup>157</sup> Second, in terms of economic impact of the historic landmark designation, *Penn Central* gained transfer development rights and still had the ability to use the airspace above the

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152. See 512 U.S. at 393 (citation omitted).

153. See Wright & Laughner, *supra* note 134, at 11180.

154. 438 U.S. 104 (1978).

155. *Id.* at 124. This test may not be applicable to facial challenges. See Andrea L. Peterson, *The Takings Clause: In Search of Underlying Principles, Part I—A Critique of Current Takings Clause Doctrine*, 77 CAL. L. REV. 1301, 1361 (1989). Some courts have suggested that a facial challenge requires that the mere enactment of the legislation may deprive the owner of “all economically viable use.” See *id.*

156. *Penn Central*, 438 U.S. at 127–28.

157. *Id.* at 128.

terminal.<sup>158</sup> Third, because the regulation did not interfere directly with the use of the station as a station, Penn Central still retained investment-backed expectation interests.<sup>159</sup>

Particularly egregious violations of any one of the *Penn Central* factors may cause a court to award just compensation. For instance, an actual, physical invasion may be a particularly egregious form of government action because permanent, physical occupations interfere with several property rights concurrently. Similarly, the Supreme Court has determined that denial of economically viable use of a property is a taking.<sup>160</sup> Absent these two limited circumstances, one of the most determinative factors in regulatory takings analysis is the reasonableness of the investment.<sup>161</sup> Such reasonableness is measured in terms of historical protection of the uses affected by the regulation<sup>162</sup> as well as in terms of the regulatory regime under which the owner does business.<sup>163</sup> The Court has repeatedly stated that “mere unilateral expectations” and “abstract need” do not translate into reasonable expectations.<sup>164</sup>

Doing business in a highly regulated field raises the bar for cable operators hoping to show reasonable expectations.<sup>165</sup> In highly regulated industries, the reasonableness of any expectation is significantly curtailed. In *Ruckelshaus v. Monsanto Co.*,<sup>166</sup> for example, the Court identified a traditional property interest in trade secrets—a taking would not occur when disclosure of that trade secret is not prohibited by law.<sup>167</sup> Two years later, the Court in *Connolly v. Pension Benefit Guaranty Corp.*<sup>168</sup> emphasized that federal law could disregard or destroy existing contract rights in highly regulated fields without violating either the Due Process or

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158. *See id.* at 136 (noting that obstructions to Penn Central’s use of the airspace were not known to the Court).

159. *Id.* at 138 (holding that Penn Central retained the ability to improve the property).

160. *See Lucas v. S.C. Coastal Council*, 505 U.S. 1003, 1016 (1992).

161. *Penn Central*, 438 U.S. at 109 (assessing the constitutionality of the New York City’s Landmarks Preservation Law in terms of the “reasonable return” that was still possible on the property owner’s investment).

162. *See Lucas*, 505 U.S. at 1016 n.7.

163. *See Monsanto*, 467 U.S. at 1011–12.

164. *See Webb’s Fabulous Pharmacies, Inc. v. Beckwith*, 449 U.S. 155, 160 (1980); *Board of Regents of State Colleges v. Roth*, 408 U.S. 564, 578 (1972) (finding an abstract concern, but an insufficient property interest).

165. *See generally Monsanto*, 467 U.S. at 986 (assessing whether “reasonable investment-backed expectation” existed with trade secrets, warranting just compensation for the government taking them).

166. *Id.*

167. *See id.* at 1004–08.

168. 475 U.S. 211 (1986).

Takings Clause.<sup>169</sup> As a result, when a property owner does business in a highly regulated field, the owner may only have a viable Fifth Amendment claim against federal law affecting the final use, and only when there is an explicit federal guarantee protecting such a use.<sup>170</sup>

The statutory framework governing cable operators has never included an express guarantee that regulators will not impinge on the cable company's use of its franchise, but preserved the right to encourage competition and protect the public interest.<sup>171</sup> In *United States v. Midwest Video*, the Court held that the FCC had ancillary jurisdiction over cable for the purpose of enhancing television services.<sup>172</sup> Historically, cable has been subject to a dual regulatory regime, where local authorities issue franchises, the terms of which are curtailed by both federal legislation and the First Amendment.<sup>173</sup> As a result of this history, cable operators have difficulty arguing that they have reasonable expectations in any given regulatory regime.<sup>174</sup> Furthermore, cable operators may be hard pressed to find an explicit federal guarantee protecting expectancies against must-carry. One such guarantee may come in the form of a federal prohibition that prevents the regulation of cable as a common carrier.<sup>175</sup> Common carriers are federally required to carry the speech of others on a nondiscriminatory basis.<sup>176</sup> While the issue was raised in first *Turner* decision by dissenting Justice O'Connor,<sup>177</sup> in neither *Turner* decision did the Court hold that must-carry contravened the federal prohibition against regulating cable as a common carrier.<sup>178</sup>

169. *See id.* at 223–24.

170. *See Monsanto*, 467 U.S. at 1011.

171. *See* 47 U.S.C. 253(a)–(d) (2000).

172. *See* 406 U.S. at 665–66.

173. *Capital Cities Cable, Inc. v. Crisp*, 467 U.S. 691, 702 (1984) (citing the *Cable Television Report and Order*, 36 F.C.C.2d 143, 207 (1972)).

174. *See, e.g., Cox*, 866 F. Supp. at 556–59 (explaining that there were no property interests in a contract and thus no takings).

175. 47 U.S.C. § 541(c) (2000) (“Any cable system shall not be subject to regulation as a common carrier or utility by reason of providing any cable service.”).

176. *See* 47 U.S.C. § 153 (10) (2000). *See also* MICHAEL K. KELLOGG, JOHN THORNE, & PETER W. HUBER, *FEDERAL TELECOMMUNICATIONS LAW* 11–15 (2d ed. 1999).

177. *Turner I*, 512 U.S. at 684 (1994) (O'Connor, J., dissenting). Justice O'Connor stated:

Congress might also conceivably obligate cable operators to act as common carriers for some of their channels . . . . Setting aside any possible Takings Clause issues, it stands to reason that if Congress may demand that telephone companies operate as common carriers, it can ask the same of cable companies; such an approach would not suffer from the defect of preferring one speaker to another.

*Id.*

178. *See id.*; *see also Turner II*, 520 U.S. 180.

Furthermore, the Telecommunications Act of 1996 authorizes the FCC to hold a hearing to determine whether the extension of must-carry to digital technologies is appropriate.<sup>179</sup> As in *Monsanto*, it would seem that protecting property rights in this instance would have the result of interfering with federal flexibility in instituting a regulatory plan.<sup>180</sup> Absent interference with a fundamental property right, or an outright appropriation of the entire cable facility, cable seemingly has limited reasonable expectancies in control over certain channels. Admittedly, however, *Monsanto* involved the protection of trade secrets as a property right,<sup>181</sup> and intellectual property may not receive the same degree of protection as more tangible property and equipment, such as the channel space commandeered for must-carry channels.

Nevertheless, given the extensive regulatory treatment of cable, it appears unlikely that cable would be able to prove reasonable investment-backed expectations to be free from access regulations, such as digital must-carry. If the FCC had imposed a dual or multicast must-carry regime, or if such a regime were to come into effect in the future, the added burdens associated with digital must-carry—including the added administrative costs—would make cable claims to reasonable investment stronger. Under the current history in which reasonable expectations are limited, however, cable operators may not be able to sustain a regulatory takings claim because of *Penn Central*.<sup>182</sup>

If, however, a court did find reasonable expectancies, it would balance such expectancies against the nature of the governmental action and the economic impact of the regulation. The central goal of this balancing is to determine whether the regulation is merely adjusting benefits and burdens of social welfare<sup>183</sup> or “forcing some people to bear public burdens which, in all fairness and justice, should be borne by the public as a whole.”<sup>184</sup> The central goal of evaluating the “character of government action” is to “prevent unfair forms of redistributions [of

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179. See *supra* notes 53–54 and accompanying text.

180. See *Monsanto*, 467 U.S. at 1008. In *Monsanto*, the Court emphasized that “the Trade Secrets Act is not a guarantee of confidentiality to submitters of data, and, absent an express promise, Monsanto had no reasonable, investment-backed expectation that its information would remain inviolate in the hands of EPA.” *Id.* Similarly, the mandate that the FCC hold a hearing to determine whether or not to extend must-carry, as authorized by federal law, may limit the reasonable expectancies in complete channel space ownership.

181. *Id.* at 1003–04.

182. See *Penn Central*, 438 U.S. at 135 (setting the test to determine whether a regulation is a taking requiring just compensation).

183. See *id.*

184. See *Armstrong v. United States*, 364 U.S. 40, 49 (1960) (Harlan, J., dissenting).

wealth].”<sup>185</sup> An egregious government action, like an actual, physical invasion, favors the property owner,<sup>186</sup> while preventative measures, such as those prohibiting a nuisance, favor the regulator.<sup>187</sup>

The *Penn Central* Court further distinguished situations in which the government is “acting in an enterprise capacity, has appropriated part of . . . [a] property for some strictly governmental purpose” and situations in which the government is regulating in favor of public welfare.<sup>188</sup> When public welfare concerns arise, the government action is better justified—even when regulations substantially interfere with the value or use of a property.<sup>189</sup> If an entire property interest or an essential right<sup>190</sup> is destroyed, the government action, regardless of its public welfare purpose, is constitutionally suspect.

In the case of cable operators, regulation is usually limited to actions designed to serve the public interest and, as *Turner* emphasized, to balance unequal technological and economic advantages that cable operators possess.<sup>191</sup> The cable industry is controlled by several large companies and

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185. See Jeremy Paul, *The Hidden Structure of Takings Law*, 64 S. CAL. L. REV. 1393, 1433–34 (1991). Generally, fairness is based on (1) historical protections for the autonomy of the landowner and (2) the necessity of balancing property rights against communal interests. Two significant considerations that impact a court’s analysis of the “character of the governmental action,” are the reason for, or purpose of, the action, and the degree to which the action interferes with property rights. For instance, government reallocation of property rights is likely to be viewed more negatively than reallocation for public interest purposes. See *id.*; see also *Webb*, 449 U.S. at 160–61.

186. See *Kaiser Aetna*, 444 U.S. at 180; *Loretto*, 458 U.S. at 433.

187. See *Lucas*, 505 U.S. at 1022–23 (noting that there is no right to use property in a manner “akin to public nuisances,” even if in denying the landowner the right to commit a nuisance, the regulation destroys all economically viable use of the property).

188. See *Penn Central*, 438 U.S. at 135.

189. See *id.* at 131.

190. See *Hodel v. Irving*, 481 U.S. 706, 717 (1987); but see *Andrus v. Allard*, 444 U.S. 51, 65 (1979). In *Andrus*, the Court refused to hold that a complete abolition of the right to sell eagle feathers was a taking, since the property owner had not one “strand” in the “full bundle” of property rights. *Id.* at 65–66. The Court noted that the owners could give the feathers away or devise them. *Id.* Additionally, the Court noted that the “loss of future profits” from the sale of the feathers is a “slender reed upon which to rest a takings claim.” *Id.* at 66. The burden in this case was to “secure the ‘advantage of living and doing business in a civilized community.’” *Id.* at 67 (citation omitted). It is difficult to reconcile *Andrus* with *Hodel*, except the Court in *Hodel* noted that the regulation seemed overbroad for its purpose, and because the Native American land in that case was so fractionalized, it had no real resale value. *Hodel*, 481 U.S. at 718.

191. See *Turner I*, 512 U.S. at 632–33. The Court stated:

Congress found that the physical characteristics of cable transmission, compounded by the increasing concentration of economic power in the cable industry, are endangering the ability of over-the-air broadcast television stations to compete for a viewing audience and thus for necessary operating revenues. Congress determined that regulation of the market for video programming was necessary to correct this competitive imbalance.



faces little competition in a given market area.<sup>192</sup> A competing cable company would likely be dissuaded from overbuilding by the high cost of entry and the economies of scale.<sup>193</sup> Furthermore, cable has the ability to gatekeep through its physical control over the first and last mile.<sup>194</sup> Because of this physical control, information is funneled through a cable bottleneck, and thus, cable can prevent broadcasters and other programmers from reaching cable subscribers.<sup>195</sup> These concerns, if reasonable, would seem to be sufficient to end any inquiry into the social-welfare purpose of the government regulation.

Nevertheless, if certain regulations interfere with a substantial property right to a significant degree, such interference, regardless of its overarching social-welfare purpose, violates fundamental property protection. Thus, the character of government action in the context of must-carry may favor the cable company if a cable company can show that a fundamental or entire property right is taken. This question raises a common problem in takings jurisprudence: the characterization of the relevant property interest. Such a problem would not arise if, for example, the government completely and directly appropriated a fundamental property interest or an entire parcel.<sup>196</sup> Regulations, however, are seldom so sweeping.

Courts measure the governmental action and the economic impact of a regulation, not only in terms of the extent to which property rights are modified, but also in terms of how much of the property is affected.<sup>197</sup> For

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*Id.*

192. *Id.* at 633.

193. *Id.*

194. *Id.* at 656.

195. *Id.* For more analysis on how this bottleneck metaphor emerged within intermediate scrutiny, see generally *Whitmore*, *supra* note 39.

196. *Loretto*, 458 U.S. at 436 (“constitutional protection for the rights of private property cannot be made to depend on the size of the area permanently occupied”); *Tahoe-Sierra Pres. Council, Inc. v. Tahoe Reg’l Planning Agency*, 535 U.S. 302, 331–32 (2002), where the Court stated:

An interest in real property is defined by the metes and bounds that describe its geographic dimensions and the term of years that describes the temporal aspect of the owner’s interest. Both dimensions must be considered if the interest is to be viewed in its entirety. Hence, a permanent deprivation of the owner’s use of the entire area is a taking of ‘the parcel as a whole,’ whereas a temporary restriction that merely causes a diminution in value is not.

*Id.* (citation omitted).

197. See Benjamin Allee, Note, *Drawing the Line in Regulatory Takings Law: How a Benefits Fraction Supports the Fee Simple Approach to the Denominator Problem*, 70 *FORDHAM L. REV.* 1957, 2006 (2002) (“Substantiality [as an approach by which to evaluate the effect of a regulation on the property rights of a landowner] deals with losses to conceptually independent parcels of land.”).

this reason, claimants attempt to make regulations appear more egregious by narrowly characterizing the affected property—limiting it to a particular property interest that is directly regulated.<sup>198</sup> Cable operators, for instance, may claim that access or must-carry regulations essentially condemn the affected bandwidth rather than merely a portion of their entire capacity to transmit.<sup>199</sup> In this way, the character of the governmental action and the economic impact of the regulation appear more intrusive.

In order to determine the relevant property right, courts often look to the substantiality of the alleged taking—both in qualitative and quantitative terms.<sup>200</sup> The *Loretto* Court, for example, determined that the actual, physical invasion was more significant than the minimal size of the property affected because the regulation had a permanent impact on a fundamental property right—the right to exclude.<sup>201</sup> Permanence, however, may not be required to invoke Fifth Amendment protection.

The Court in *First English Evangelical Lutheran Church of Glendale v. County of Los Angeles*<sup>202</sup> held that a temporary regulation could constitute a taking just as in older cases where temporary wartime appropriation of businesses, such as steel plants, were takings.<sup>203</sup> In these cases, the temporary nature of the invasion did not mitigate the Fifth Amendment implications of the invasion.<sup>204</sup> In the must-carry context, cable operators may argue by analogy that the cable company's decision to enter the cable business cannot be conditioned on the occupation of channel space by broadcasters and other competitors.<sup>205</sup>

Wartime appropriation, however, took over the entire business and thus today might be a denial of all economically viable use<sup>206</sup> and a direct interference with historical protections for the right to exclude<sup>207</sup>—both

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198. See Andrew S. Gold, *The Diminishing Equivalence Between Regulatory Takings and Physical Takings*, 107 DICK. L. REV. 571, 616–17 (2003).

199. See, e.g., Complaint at 78–81, *Comcast Cablevision v. Broward Co.* (S.D.Fla. 1999) (No. 99-6934-CIV), <http://www.techlawjournal.com/courts/broward/19990720.htm>.

200. See Allee, *supra* note 197; see also *Tahoe-Sierra Pres. Council*, 535 U.S. at 331–32.

201. *Loretto*, 458 U.S. at 433 (citation omitted).

202. 482 U.S. 304 (1987).

203. *Id.* at 317–18; see also *Wright & Laughner*, *supra* note 134, at 11184.

204. *Id.* at 318 (“Though the takings were in fact ‘temporary,’ there was no question that compensation would be required for the Government’s interference with the use of the property . . . .”) (citation omitted).

205. See Daniel F. Spulber & Christopher S. Yoo, *Access to Networks: Economic and Constitutional Connections*, 88 CORNELL L. REV. 885, 940 n.220 (2003) (noting that even a partial and temporary occupation of private property, as per access to network regulations, requires just compensation because such access requirements prevent the business owner from creating new facilities.).

206. See *Lucas*, 505 U.S. at 1016–19.

207. See *Loretto*, 458 U.S. at 419 (citation omitted).

constitute *per se* takings.<sup>208</sup> More importantly, to read *First English*<sup>209</sup> consistently with *PruneYard*,<sup>210</sup> *Yee*,<sup>211</sup> and other access cases, it seems that the importance of the permanence of the invasion is indirectly proportional to the size of the entire property interest affected. Thus, the relative permanence of the invasion seems somewhat dependent on the definition of the relevant property interest in quantitative terms.

Courts use federal and state laws to define the relevant property interest<sup>212</sup> unless, of course, a *per se* violation is implicated.<sup>213</sup> Franchise agreements set the terms of cable service. Such agreements are modifiable by federal regulation and local ordinance.<sup>214</sup> Thus, while must-carry provisions do take bandwidth,<sup>215</sup> it is unlikely that the court would find the particularly affected bandwidth to be the relevant property interest. As the physical appropriation discussion makes clear, it is also doubtful that the court would find must-carry to be a permanent invasion because only a relatively small portion of the bandwidth is taken, much like a temporary easement.<sup>216</sup> Even if multicast must-carry is ultimately implemented, the anticipated six-fold increase in carriage burdens that result from multiple broadcast streams is relatively small in comparison to the overall channel capacity of a cable provider, and the six-fold increase will not change the overall amount of bandwidth occupied.<sup>217</sup> Thus, must-carry may not be a particularly egregious form of governmental action since cable operators retain significant editorial control over a majority of their facility.<sup>218</sup>

The final factor in the traditional *Penn Central* regulatory takings analysis looks at the “economic impact of the regulation.”<sup>219</sup> Just as the

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208. See Wright & Laughner, *supra* note 134, at 11184.

209. 482 U.S. 304.

210. 447 U.S. 74.

211. 503 U.S. 519.

212. See *Monsanto*, 467 U.S. at 1001.

213. See *Loretto*, 458 U.S. at 436–37 (“[C]onstitutional protection for the rights of private property cannot be made to depend on the size of the area permanently occupied.”).

214. See 47 U.S.C. 545 (2000); see also *Tribune–United Cable Company v. Montgomery County*, 784 F.2d 1227 (4th Cir. 1986).

215. See Complaint, *supra* note 199, para. 81.

216. See *Loretto*, 458 U.S. at 433 (finding that a temporary easement is not a *per se* taking).

217. See Epstein, *supra* note 61, at 562–63 (citations omitted). Epstein explains that “[a]lthough a digital signal may be split into up to six sub-channels, the amount of signal bandwidth remains the same as it was as an analog signal, 4.3 Mhz.” *Id.* at 563 (citation omitted). Epstein also notes that there has been a “large increase in cable programming on most analog cable systems in the last decade”—an increase likely to make the must-carry burden seem proportionally less burdensome. See *id.*

218. *Denver Area*, 518 U.S. at 828–29 n.11.

219. *Penn Central*, 438 U.S. at 124.

character of government action becomes more egregious when it substantially affects the entire property interest, so too does the economic impact become more egregious when economic loss “relative to the particularly affected property” is proportionally greater.<sup>220</sup> In *Penn Central*, the Court noted that mere diminution in property value did not tip the balance in favor of the claimant, particularly with respect to speculative land uses.<sup>221</sup> Instead, the Court looked exclusively at the regulation’s impact on the present use of the property, not on the prospective use of airspace above the station.<sup>222</sup> Just as there is no constitutional guarantee preventing the passage of regulations that would ultimately and incidentally diminish the value of corporate stock, there is likewise no guarantee embedded in the Fifth and Fourteenth Amendments that would guarantee property against regulations that might harm resale value.<sup>223</sup> To the extent the cable operators allege the government is appropriating their future profits and market share, it is unlikely they would fair any better than *Penn Central* did when alleging that a historic preservation statute appropriated airspace.<sup>224</sup>

This is particularly true with respect to access-type cable regulations like must-carry. As one lower court has noted, Fifth Amendment protections do not include “eternal monopolistic, industry-wide protection from competition.”<sup>225</sup> Must-carry, however, differs from leased-access in that carriage is mandated and no money changes hands.<sup>226</sup> Cable operators may be able to argue that they no longer have the channel space to carry independent public interest programming, such as C-SPAN, PEG channels, or local public television stations because of must-carry burdens to carry local broadcast stations.<sup>227</sup> While the FCC’s denial of multicasting obligations may lessen these costs and burdens, cable operators may experience a loss in revenue represented by the channel space now occupied by must-carry channels that would otherwise be open to

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220. See Paul, *supra* note 185, at 1501.

221. *Penn Central*, 438 U.S. at 131 (citations omitted).

222. *Id.* at 136–37.

223. See Wright & Laughner, *supra* note 134, at 11188 (citation omitted).

224. See *Penn Central*, 458 U.S. at 138.

225. See *Cox*, 866 F. Supp. at 559.

226. See *supra* notes 24–25 and accompanying text.

227. See, e.g., Carriage of Digital Television Broadcast Stations, *Comments of A&E Television Networks*, FCC CS Docket No. 98-120, at 14–18 (2001), [http://gulfoss2.fcc.gov/prod/ecfs/retrieve.cgi?native\\_or\\_pdf=pdf&id\\_document=6512569255](http://gulfoss2.fcc.gov/prod/ecfs/retrieve.cgi?native_or_pdf=pdf&id_document=6512569255); Letter from Glenn Moss, Sr. V.P. for Business Affairs & Affiliate Relations, Courtroom Television Network, to Marlene H. Dortch, Secretary, FCC, (2002), [http://gulfoss2.fcc.gov/prod/ecfs/retrieve.cgi?native\\_or\\_pdf=pdf&id\\_document=6513291503](http://gulfoss2.fcc.gov/prod/ecfs/retrieve.cgi?native_or_pdf=pdf&id_document=6513291503).

independent programmers.

In summary, cable operators face an uphill battle in making a traditional regulatory takings claim against the current digital must-carry requirements. However, if multicast obligations are legislatively imposed, or if broadcasters successfully challenge the limited must-carry order, then cable operators may be in a slightly stronger position to show that digital must-carry infringes on their reasonable investment-backed expectations. Further, digital must-carry has a greater economic impact on cable operators, particularly if dual and multicast carriage requires them to abandon independent and cable network programming. Even if greater digital must-carry burdens were imposed, the ultimate fate of a regulatory takings claim would depend on the characterization of cable's regulatory history, cable's ability to anticipate heavier must-carry burdens in light of digital technology, and the relative amount of channel space occupied by any digital must-carry burdens. In light of these concerns, one may argue that the cable industry could anticipate some increased must-carry burden because of the technological innovation associated with digital broadcasting (e.g., efficiency of bandwidth) and changing expectations of the public with respect to free over-the-air broadcasting.<sup>228</sup>

But even if the bottleneck argument is no longer as persuasive because of increased competition and innovation of digital broadcast television and direct-broadcast satellite ("DBS"), it nevertheless could be established that retransmission consent is more consistent with cable property rights than mandatory carriage—a point thoroughly discussed in Part IV.

#### IV. COMPELLED SPEECH AND PROPERTY IN THE CABLE CONTEXT

As mentioned previously, cable is a quasi-public entity that is protected as a speaker under the First Amendment<sup>229</sup> and, yet, subject to limited public-interest regulations because of its ancillary effect on broadcasting.<sup>230</sup> When discussing the gatekeeping control inherent to the cable industry, the *Turner* Court emphasized that cable subscribers could be denied access to a certain type of programming.<sup>231</sup> At the time *Turner I* was decided, cable service may have been the only service available in certain areas.<sup>232</sup> Now, alternatives like DBS are more prevalent.<sup>233</sup>

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228. See Epstein, *supra* note 61, at 560 (emphasizing that broadcaster's must-carry needs do not remain static in light of changing technology).

229. See *Turner I*, 512 U.S. at 650, 656.

230. *Id.* at 650–52.

231. See *id.* at 656.

232. *Id.* at 633.

233. See Annual Assessment of the Status of Competition in the Market for the Delivery

Nevertheless, concern over gatekeeping was not focused on the ability of cable to reach consumers when other television providers could not.<sup>234</sup> Rather, the Court focused on the ability of cable to block access to cable subscribers.<sup>235</sup> Because of this ability to drown out other speakers, the *Turner I* Court distinguished must-carry regulations from situations involving compelled speech—when a state actively forces individuals to advocate for, or associate with, a particular speaker or viewpoint.<sup>236</sup>

Gatekeeping control can also influence a property-based analysis. For example, when the government compelled a utility service to include a competitor's views in its billing statements, there was a question as to whether the law interfered with the public utility's property right in its envelopes.<sup>237</sup> The Court in *Pacific Gas and Electric Company v. Public Utilities Commission of California* found that First Amendment rights were not contingent on ownership, though the envelopes were property of Pacific Gas.<sup>238</sup> Applying a First Amendment analysis, the *PG&E* Court held that the regulation was content-based because it prioritized the speech of a particular point of view—a difference the Court used to distinguish *PruneYard*.<sup>239</sup>

How might the space in a billing envelope and space on channel capacity compare? Per the common description, property describes a series of rights associated with ownership, such as the right to exclude, the right to alienate, and the right to develop. If property encompasses a series of rights, is there a way to draw a practical distinction between the right to exclude unwanted speakers from space on a letter and to exclude unwanted speakers from space on a channel? The Court has increasingly extended property based protections for more nebulous economic and contractual rights,<sup>240</sup> and a significant possibility remains that a regulatory takings

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of Video Programming, *Tenth Annual Report*, 19 F.C.C.R. 1606, paras. 7, 69 (2004), available at [http://hraunfoss.fcc.gov/edocs\\_public/attachmatch/FCC-04-5A1.pdf](http://hraunfoss.fcc.gov/edocs_public/attachmatch/FCC-04-5A1.pdf).

234. See *Turner I*, 512 U.S. at 656.

235. *Id.* (“[S]imply by virtue of its ownership of the essential pathway for cable speech, a cable operator can prevent its subscribers from obtaining access to programming it chooses to exclude.”).

236. *Id.* at 653.

237. See *Pac. Gas & Elec. Co. v. Pub. Util. Comm’n (PG&E)*, 475 U.S. 1, 17–18 (1986).

238. *Id.*

239. See *id.* at 12.

240. See McUsic, *supra* note 112, at 624–26. McUsic emphasizes that in the late 1970s and 1980s, the Court began to combine a broad definition of property that incorporated reference to economic rights and tests that smacked of traditional due process analysis, such as the fragmentation of property interests and the means/end test used in *Dolan*, 512 U.S. at 374. This trend has been well documented by legal scholars.

analysis might raise constitutional implications with respect to access-type regulations like must-carry.

On the surface it would seem that where compelled speech and property intersects, a due process analysis may be the appropriate framework. Under such a lens, the issue becomes whether the government is illegally overstepping its bounds by interfering with a fundamental constitutional right like property. To analyze space in an envelope as a form of property subject to Takings, however, would import such an expansive reading of property rights into the Takings and Due Process clauses that it would be difficult to envision a social welfare regulation that would be able to pass Fifth Amendment scrutiny in the absence of just compensation. Such a broad reading of property would essentially have the same effect that the *Lochner* era substantive due process review had on social welfare legislation.<sup>241</sup> In essence, it would tie the hands of regulators and legislators hoping to promote the public interest by defining public interest to mean laissez-faire economic policies and private interests superseding public rights.<sup>242</sup>

Despite problems associated with defining how to set limits on property, however, property rights help establish the degree of association between the speaker and the allegedly compelled message. In the presence of strong, traditional property rights—such as real property interests—compelled speech and property strengthen one another in terms of the association between the property owner and the speaker. In the absence of private property rights, such an association is difficult to establish. With respect to PEG access channels, for example, courts have considered a limited public fora analysis, which would prevent cable operators and the local governments from claiming that mandatory carriage of broadcast

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241. See McUsic, *supra* note 112, at 614 (discussing the impact of *Lochner*); The reasons such review is disfavored was succinctly stated by the Court in *Williamson v. Lee Optical of Oklahoma*, 348 U.S. 483 (1955), where it noted that:

The day is gone when this Court uses the Due Process Clause . . . to strike down . . . laws, regulatory of business and industrial conditions, because they may be unwise, improvident, or out of harmony with a particular school of thought . . . . We emphasize what Chief Justice Waite said in *Munn v. State of Illinois* . . . [f]or protection against abuses by the legislatures the people must resort to the polls, not to the courts.

*Id.* (citation omitted).

242. See Cass R. Sunstein, *A New Deal For Speech*, 17 HASTINGS COMM. & ENT. L.J. 137 (1994); See McUsic, *supra* note 112, at 624–25. It would seem that too strong of a reliance on property rights would have the regulatory effect of returning us to a pre-New Deal public interest philosophy viewing corporate rights as virtually synonymous with public rights. See LOUISE M. BENJAMIN, FREEDOM OF THE AIR AND THE PUBLIC INTEREST: FIRST AMENDMENT RIGHTS IN BROADCASTING TO 1935 4–6 (2001).

signals via must-carry requirements compel speech.<sup>243</sup> Such an analysis also limits any assertion of a property-based right to exclude because the property owner benefits from making his or her property publicly available.<sup>244</sup>

Both rights also are modified by necessity when balancing multiple constitutional rights. A landowner cannot prevent workers from gathering information about their legal rights by alleging that the transmission of information across the property is a form of invasion or trespass.<sup>245</sup> The rights of the individual on the property to receive information in these circumstances are paramount to the property rights of the landowner.<sup>246</sup> Similarly, in the compelled speech cases, nonviewpoint specific regulations that prevent businesses from walling off subscribers and listeners do not violate the First Amendment rights of the provider. In *Red Lion Broadcasting v. FCC*, the right of the public to a variety of information on a public medium was paramount to the broadcasters' right of editorial control.<sup>247</sup> In *Turner I*, the right of the cable subscriber to receive broadcast television without having to change his or her home technology configuration through a broadcast switch was effectively paramount to the

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243. *Horton v. City of Houston*, 179 F.3d 188, 192–94 (5th Cir. 1999), *cert denied*, 528 U.S. 1021 (1999). In *Horton*, the court considered but did not determine whether PEG access channels were public fora. *See id.* at 190–93. It noted, however, that the Supreme Court has said that the “the public forum doctrine should not be extended in a mechanical way to the very different context of public television-broadcasting.” *Id.* at 192 (citing *Arkansas Educ. Television Comm. v. Forbes*, 523 U.S. 666 (1998)). And that the majority of justices in *Denver Area* refused to consider Justice Kennedy’s argument that access channels are a public forum. *Id.*; *See also Denver Area*, 518 U.S. 780–81 (Kennedy, J., concurring in part, concurring in judgment in part, and dissenting in part); *Denver Area*, 518 U.S. at 749–50 (Breyer, J.) (refusing to consider public forum doctrine); *Denver Area*, 518 U.S. at 826–30 (Thomas, J., concurring in the judgment in part and dissenting in part) (arguing that PEG channel is not a public forum)).

244. *See PruneYard*, 447 U.S. at 83–84.

245. *See New Jersey v. Shack*, 277 A.2d 369 (N.J. 1971).

246. *See id.* at 373–74. The Supreme Court of New Jersey determined that by law, an attorney and health care worker could enter private property to inform migrant workers of their rights without raising Fifth Amendment right to exclude concerns since the interests of the migrant worker outweighed the values supported by private property in this context. *Id.*

247. 395 U.S. 367, 387 (1969). Although the *Red Lion* decision was based in part on the now defunct and much criticized fairness doctrine, two aspects of the *Red Lion* decision are particularly germane to this analysis. First, the Court in *Red Lion* noted that “[t]he right of free speech of a broadcaster, the user of a sound truck, or any other individual does not embrace the right to snuff out the speech of others.” *Id.* (citing *Assoc. Press v. United States*, 326 U.S. 1 (1945)). The right of a broadcast license had not conveyed a right to monopolize the use of a scarce resource, but only the right to use the medium as a proxy for the public interest. Second, the *Red Lion* Court noted that there were countervailing interests at stake: the “right of the viewers and listeners,” an interest that was “paramount” to the broadcast licensee’s right to engage in “unlimited private censorship . . . in a medium not open to all.” *Id.* at 390, 392.



cable operators' right to be free from broadcasters' views.<sup>248</sup> In *Miami Herald v. Tornillo*, the Court upheld the right of newspapers to exclude unwanted speakers because of historical protections associated with a free and vibrant press.<sup>249</sup> As explained in *Turner I*, because newspapers cannot prevent delivery of alternative views in a separate publication, newspapers have no control over the mailbox or the public.<sup>250</sup>

With respect to Fifth Amendment takings claims to must-carry, such challenges must account for the technological changes that may make gatekeeping a less-than-persuasive argument. In light of the anticipated success of local digital broadcasting multicast services and robust DBS competition, cable may no longer be a technological gatekeeper. Absent gatekeeping control, and in light of the Supreme Court's recognition of cable as speakers, must-carry may violate the First Amendment because cable subscriber rights to receive information would not be directly implicated. Concurrently, property rights in such channels would be strengthened.

To the degree that gatekeeping concerns continue to focus on the right of cable subscribers to receive local broadcast programming, neither the digital broadcast transition nor increased competition from DBS are particularly persuasive. Instead, the analysis would depend on whether gatekeeping concerns are reconceptualized from focusing narrowly on cable subscribers and broadly on a general video audience. The question remains whether the government could show a continued substantial interest—that is, whether must-carry is necessary to preserve broadcasting and whether, as emphasized in *Turner II*, must-carry continues to pose a proportionally limited burden on cable operators.<sup>251</sup> Therefore, the ultimate question with respect to must-carry and gatekeeping concerns, whether from a First or a Fifth Amendment perspective, hinges on whether limiting cable autonomy rights is necessary to preserve access to the information and diversity that local broadcast stations provide to the public.

## V. CONCLUSION

The idea that the First Amendment protects against compelled speech but does not protect those that would drown out others is not a novel concept. Such a view was expressed by the Supreme Court in *Associated*

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248. See *Turner I*, 512 U.S. at 656–57.

249. 418 U.S. 241, 256 (1974) (“A responsible press is an undoubtedly desirable goal, . . . press responsibility is not mandated by the Constitution and like many other virtues, it cannot be legislated.”).

250. *Turner I*, 512 U.S. at 656 (“A cable operator, unlike speakers in other media, can thus silence the voice of competing speakers with a mere flick of the switch.”).

251. See *supra* notes 49–52 and accompanying text.

*Press v. United States*<sup>252</sup> when it stated that “[f]reedom of the press from governmental interference under the First Amendment does not sanction repression of that freedom by private interests.”<sup>253</sup> The idea that the Fifth Amendment does not protect against easements by necessity and against rights of access for legal counseling is also not new.<sup>254</sup> And yet, pressure to allow such drowning in favor of private rights seems to be mounting. Furthermore, when private interests seek to repress alternative voices, reliance on property rights and Fifth Amendment claims seems to be growing, particularly as private property protections expand.<sup>255</sup>

Fifth Amendment claims against digital must-carry represent only one of many takings challenges in today’s telecommunications landscape, each of which has its own set of permutations. Admittedly, this analysis only begins to explore property implications associated with telecommunications policy issues. For example, it also may be anticipated that property-based claims may be used in the future to influence regulatory policies concerning Interactive Television Services (“ITV”). Digital technology allows for the development and use of new interactive television services that will provide subscribers with the ability to select and input information related to, or in addition to, the video programming available. Currently, however, questions exist as to whether a nondiscrimination rule should prevent cable from discriminating in favor of the ITV enhancements of affiliated programmers and from discriminating against the enhancements of independent programmers and local broadcasters.<sup>256</sup> Such a nondiscrimination rule would likely raise similar First Amendment and Fifth Amendment concerns expressed here with respect to digital must-carry.

The possibility remains that public rights may be paramount when necessary to receive information and may modify the historical and reasonable expectations of the property owner. This possibility is influenced on those factors emphasized by the Supreme Court in its approach to the First Amendment rights of cable, newspapers, and

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252. 326 U.S. 1 (1945).

253. *Id.* at 20.

254. *Shack*, 277 A.2d at 373.

255. Professors Norman Dorsen and Joel Gora in an article analyzing the way property rights influenced First Amendment rights during the Burger Court reached this conclusion. They emphasized that “when free speech claims are weighed in the balance, property interests determine on which side of the scales ‘the thumb of the Court’ will be placed.” Mark Cordes, *Property and the First Amendment*, 31 U. RICH. L. REV. 1, 2 (1997) (quoting Norman Dorsen & Joel M. Gora, *Free Speech, Property, and the Court: Old Values, New Balances*, 1982 SUP. CT. REV. 195).

256. See, e.g., Nondiscrimination in the Distribution of Interactive Television Services Over Cable, *Notice of Inquiry*, 16 F.C.C.R. 1321, para. 6 (2001).

broadcasters: technology, particularly gatekeeping control and historical public use and tradition, as argued in this analysis.

In all of the cases mentioned herein, and as this must-carry property analysis demonstrates, competing and overlapping First and Fifth Amendment concerns create ambiguities. In the context of cable and property rights, Fifth Amendment doctrine and takings law seems to be isolated from First Amendment doctrine and even from more traditional takings analysis.<sup>257</sup> While analogies can be drawn between real property takings and intellectual property cases, courts seem to be reluctant to draw these analogies. The process of drawing such analogies is important, however, to understand the meaning of private property rights in a quasi-public business.<sup>258</sup> Indeed, with respect to many forms of communication providers, such as common carriers, property rights jurisprudence remains ambiguous;<sup>259</sup> such ambiguity is naturally extended to cable technologies.

If, as Commissioner Abernathy suggests, the regulation of certain services, such as cable broadband services, is motivated by assumptions about protecting personal property rights in order to encourage innovation and development,<sup>260</sup> this cable property analysis of must-carry may provide the foundation for overcoming speculative assumptions about cable property rights. Subsequently, this understanding may help prevent the misuse of property-based rhetoric to inappropriately harm competition or limit the scope of must-carry or other access regulation. Indeed, if must-carry has become a policy quagmire because it was written for an analog world, it is also a legal quagmire with respect to the property and speech rights implicated by any regulatory approach. As shown, cable property arguments against must-carry are riddled with ambiguities and weakness. Nevertheless, these arguments may influence regulatory policy and indirectly contribute to a loss of public access to the benefits of digital broadcast television, if and when market forces fail to allow for negotiation.

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257. See, e.g., *PruneYard*, 447 U.S. at 88.

258. See Eric R. Claeys, Assistant Professor of Law, St. Louis University, *The Telecommunications Act of 1996, The Takings Clause, and Tensions in Property Theory*, Paper Presented Before the Conference Avoiding a Tragedy of the Telecomms: Finding the Right Property Rights Regime for Telecommunications (Mar. 18, 2004), at 2, [http://www.manhattan-institute.org/pdf/cde5-17-04\\_claeys.pdf](http://www.manhattan-institute.org/pdf/cde5-17-04_claeys.pdf).

259. *Id.* at 26.

260. Kathleen Q. Abernathy, Commissioner, FCC, *The Role of Property Rights in Understanding Telecommunications Regulation* (May 17, 2004), at 2, [http://hraunfoss.fcc.gov/edocs\\_public/attachmatch/DOC-247332A1.pdf](http://hraunfoss.fcc.gov/edocs_public/attachmatch/DOC-247332A1.pdf) (“Policymakers seldom focus explicitly on property rights, and yet such a discussion can shed light on how regulation affects investment incentives and the behavior of firms in the marketplace.”).

Beyond the must-carry context, the unraveling and understanding of cable operators' Fifth Amendment claims have significant public-policy implications. Compared to other facilities-based competitors like DBS or local exchange carriers, the cable industry is arguably in the best market and technological position to provide households with a bundled array of services that include video programming, ITV, high-speed Internet access, and affordable telephone service, as evidenced through its recent rollout of Voice-over-Internet Protocol.<sup>261</sup> While Congress or the FCC may pass laws or rules in the public interest to curb the cable industry as it continues expand into new offerings, recent trends suggest the industry will continue to challenge such measures under First and Fifth Amendment claims. Although used predominantly as a current rhetorical device to influence policymakers, it is only a matter of time before cable operators' Fifth Amendment claims will further develop in court and serve as another check and balance to curb government regulation.

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261. See generally Annual Assessment of the Status of Competition in the Market for the Delivery of Video Programming, *Eleventh Annual Report*, FCC 05-13 (2005), available at [http://hraunfoss.fcc.gov/edocs\\_public/attachmatch/FCC-05-13A1.pdf](http://hraunfoss.fcc.gov/edocs_public/attachmatch/FCC-05-13A1.pdf) (documenting trends in the market place and competition for the delivery of video programming).

# An Economic Approach to the Regulation of Direct Marketing

Daniel R. Shiman\*

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## I. INTRODUCTION

In the last thirty years of the twentieth century, the volume of direct marketing received through the traditional channels of mail and telephone increased rapidly.<sup>1</sup> More recently, new electronic media for communications have developed, such as fax, e-mail, and instant messaging, and new personal communications devices have appeared, such as wireless phones and e-mail devices, which have made communications easier, cheaper, and more immediate. The growth of direct marketing in traditional and new media has raised concerns about an important privacy issue, the right to not be intruded upon or annoyed by unsolicited mail, telephone calls and electronic messages (i.e., the “right to be let alone”). As a result there has been a substantial increase in the demand for legislation to regulate direct marketing in recent years. In the last two decades, legislation has been passed by Congress and state legislatures to regulate direct marketing in various media, including the establishment of do-not-contact lists for some media (e.g., telemarketing), and the outright ban of unsolicited commercial messages for other media (e.g., unsolicited commercial faxes).

Policymakers have had to balance the benefits derived from direct marketing (and firms’ free speech rights) with receivers’ rights to privacy. While direct marketing can improve the flow of information about products available to consumers, and therefore provides a benefit to buyers, it also generates a negative externality, since nonbuyers are also forced to expend time, effort, and sometimes money processing advertising messages. A large volume of poorly-targeted direct marketing messages can therefore place a significant burden on consumers’ time, patience, and resources. Indeed, if the volume of advertising messages on a particular communications medium is heavy enough, consumers may be deterred from using that medium for their communications needs. Thus, direct marketing can affect the usefulness, and even the viability, of a communications medium.

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1. See Daniel R. Shiman, *The Nature and Causes of the Increase in Direct Mail Volume in the Last Half of the Twentieth Century* (Feb. 2001) (unpublished manuscript), <http://ssrn.com/abstract=547042> (scroll down to SSRN Electronic Paper Collection and download).

This Article demonstrates how economic social welfare analysis can provide guidance to policymakers who are considering whether to regulate direct marketing in various media, and what forms of regulations are most effective. The key factors that determine where the problem is likely to be greatest are identified and analyzed to help determine in which media the intrusion of direct marketing on receivers' privacy is likely to be the most troublesome. The Article discusses how the recent rise in complaints about direct marketing and demands for regulation is caused mostly by changes in the technological environment, which have increased the volume of direct marketing sent out and lowered direct marketing's value to consumers, thus raising its total cost to receivers. Of particular importance are the development of new inexpensive means of communication, such as e-mail and electronic messaging, the use of mobile personal communications devices, which increase the immediacy of communications, and improvements in information technology, which have lowered the cost and increased the profitability of conducting a mass direct marketing campaign. The Article also discusses the various solutions available, which can be deployed by receivers, senders, or imposed by the government or the organization or firm that controls the communications medium.

## II. THE GROWTH OF DIRECT MARKETING

The use of direct marketing by advertisers has grown rapidly in the last few decades. Much of this growth occurred in the traditional direct marketing outlets, such as direct mail and telemarketing. In the late 1970s and 1980s the volume of direct mail increased rapidly, as shown in Figure 1. Between 1975 and 1988 in particular, the number of direct mail pieces received per capita jumped by 133%.<sup>2</sup> The likely causes of this increase are the fall in information technology and communication costs, the general increase in demand for advertising, and the increased information firms have about consumers.<sup>3</sup> In 2003, 54% of the total mail volume received by households was direct mail advertising and fundraising, about thirteen pieces per week per household.<sup>4</sup> (See *infra* Figure 1.)

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2. *Id.* at 3.

3. *Id.* at 11–12.

4. See UNITED STATES POSTAL SERVICE, THE HOUSEHOLD DIARY STUDY 3, 38 (2003), available at [http://www.usps.com/householddiary/\\_pdf/HDS2003.pdf](http://www.usps.com/householddiary/_pdf/HDS2003.pdf). The 54% is derived by dividing the total number of advertising by the total mail sent to households in 2003. See *id.* See also UNITED STATES POSTAL SERVICE, THE HOUSEHOLD DIARY STUDY 8, 38 (2004), available at [http://www.usps.com/householddiary/\\_pdf/HDS2004.pdf](http://www.usps.com/householddiary/_pdf/HDS2004.pdf) [hereinafter HOUSEHOLD DIARY STUDY 2004].

Telemarketing grew even more rapidly in this time period than direct mail. Expenditures on outbound telemarketing increased annually by 10.3% from 1978 to 1996, versus 5.7% for direct mail.<sup>5</sup> By 1998, more was being spent by marketers on outbound (from firms to consumers) telemarketing, \$58.9 billion, than on direct mail advertising, \$39.7 billion.<sup>6</sup>

Direct marketers have been quick to utilize new communications and information technologies to help them advertise their products directly to potential and existing customers. As fax machines became common in commercial establishments, firms attempted to advertise their products by sending unsolicited faxes.<sup>7</sup> Advertising on the Internet has grown rapidly, much of it in the form of Unsolicited Commercial Emails (“UCE” or “spam”). It has been estimated that about 80% of all e-mail was spam in 2004.<sup>8</sup> There has also been substantial posting of advertisements on Internet forums and bulletin boards and on Usenet,<sup>9</sup> Internet mailing lists,<sup>10</sup> and discussion groups.<sup>11</sup> Some countries in Asia and Europe where Short

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5. Annual growth rate calculated using natural logarithm, deflated by GDP price deflator (e.g., if growth over T years from  $X_0$  to  $X_T$ , growth rate  $= \ln(X_T/X_0)/T$ ). See WHARTON ECON. FORECASTING, ECONOMIC IMPACT: U.S. DIRECT & INTERACTIVE MARKETING TODAY 1997 (Direct Mktg. Ass’n 1997); DIRECT MAIL MKTG. ASS’N, FACT BOOK ON DIRECT RESPONSE MARKETING 51–52 (1980); Data from Universal McCann U.S. Advertising reports provided by Robert J. Coen, McCann-Erickson, N.Y. (August 2004) [hereinafter Coen U.S. Advertising Report] (on file with Author and *FCLJ*). The GDP price deflator is extracted from the U.S. COUNCIL OF ECONOMIC ADVISORS, ECONOMIC REPORT OF THE PRESIDENT tbl. B-3 (2004), available at <http://www.gpoaccess.gov/usbudget/fy05/sheets/b3.xls>.

6. *Direct Marketing Flow Chart*, DIRECT MKTG., Nov. 1999, at 3. Statistics on telemarketing expenditures since the implementation of the FTC’s Do-Not-Call list are not available.

7. See *Stop Me Before I Fax Again*, ECONOMIST, May 27, 1989, at 29. See generally Andrea Gerlin, *Businesses Tired of Faxed Ads Sue the Senders*, WALL ST. J., May 9, 1995, at B1 (detailing efforts of several companies trying to curb advertising rates).

8. Tom Zeller, Jr., *Law Barring Junk E-Mail Allows a Flood Instead*, N.Y. TIMES, Feb. 1, 2005, at A1.

9. Usenet is a collection of special-interest discussion groups called newsgroups that can be easily accessed on the Internet. Usenet newsgroups are set up like bulletin boards, such that participants can post a message at no cost for others to read. See ROSALIND RESNICK & DAVE TAYLOR, THE INTERNET BUSINESS GUIDE: RIDING THE INFORMATION SUPERHIGHWAY TO PROFIT 16–22 (1994); Wikipedia, Mailing List, [http://en.wikipedia.org/wiki/Mailing\\_list](http://en.wikipedia.org/wiki/Mailing_list) (last visited Mar. 29, 2006).

10. An Internet mailing list (often called a Listserv mailing group) allows members to communicate with the group by sending in messages to a central list server, which then distributes the messages by e-mail to subscribers. Many mailing lists allow anyone to easily and freely subscribe and unsubscribe. See RESNICK & TAYLOR, *supra* note 10, at 9–16 (1994); Wikipedia, Mailing List, [http://en.wikipedia.org/wiki/Mailing\\_list](http://en.wikipedia.org/wiki/Mailing_list) (last visited Mar. 29, 2006).

11. Julie Chao, *Internet Pioneers Abandon World They Created*, WALL ST. J., June 7, 1995, at B1. It has even reached the comment sections on bloggers’ Web sites. See Matt Hicks, *Microsoft Bloggers Face Search Spam Pinch*, EWEEK, Dec. 21, 2004,



Message Service ("SMS") text messaging is heavily used have seen large volumes of unsolicited advertising appear on text messages to mobile devices.<sup>12</sup> There are now predictions that commercial advertising will soon appear on instant messaging ("spim"),<sup>13</sup> IP telephony,<sup>14</sup> and telemarketing calls to wireless phones.<sup>15</sup>

#### A. Public Reaction to Direct Marketing

The growth of unsolicited advertising in the traditional channels of direct mail and telemarketing, and the new channels of advertising by fax, e-mail, Internet forums, and electronic messaging, has attracted public attention and concern. There has been an increase in the number of articles on direct marketing in the news media, including newspaper editorials and magazine cover stories.<sup>16</sup> Public opinion surveys suggest that the public is quite concerned about the volume of direct marketing received. The number of people who wish they received less advertising mail rose from 30% in 1987 to 49% in 1998 to 63% in 2003.<sup>17</sup> In 1994, 86% of the public said they wished they got fewer telemarketing calls.<sup>18</sup> Meanwhile 90% of Internet users responding to a survey in November 2003 said they found UCE annoying, and 74% wanted it banned.<sup>19</sup> Large numbers of Web sites have been created to protest direct marketing, and organizations have been

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[http://www.eweek.com/print\\_article2/0,2533,a=141476,00.asp](http://www.eweek.com/print_article2/0,2533,a=141476,00.asp).

12. DoCoMo in Japan reported that 84% of i-Mode traffic was spam around 2002. John L. Guerra, *Wireless Spam: Coming to a Cell Phone Near You?*, BILLING WORLD AND OSS TODAY, Mar. 2004, available at <http://www.billingworld.com/archive-detail.cfm?archiveId=7454&hl#>.

13. Celeste Biever, *Spam Being Rapidly Outpaced by 'Spim'*, NEWSIDENTIST.COM, Mar. 26, 2004, <http://www.newscientist.com/article.ns?id=dn4822>.

14. This was called "spit" by one observer. Celeste Biever, *Move Over Spam, Make Way for "Spit"*, NEWSIDENTIST.COM, Sept. 24, 2004, <http://www.newscientist.com/channel/info-tech/electronic-threats/dn6445>.

15. See Guerra, *supra* note 12; CBSNews.com, *Telemarketers Eye Cell Phones*, Dec. 17, 2004, <http://www.cbsnews.com/stories/2004/12/17/eveningnews/consumer/main661811.shtml>.

16. Joseph E. Phelps et al., *Press Coverage and Public Perception of Direct Marketing and Consumer Privacy*, J. DIRECT MKTG., Spring 1994, at 9, 15-16 (1994). See, e.g., *Revolt of the Junk Receivers*, ECONOMIST, Sept. 29, 1990, at 24 (1990); Brad Edmondson, *Death to Junk Mail!*, AM. DEMOGRAPHICS, Sept. 1992, at 2; Susan Headden, *The Junk Mail Deluge*, U.S. NEWS & WORLD REP., Dec. 8, 1997, at 40-41.

17. See U.S. POSTAL SERVICE, THE HOUSEHOLD DIARY STUDY III-29, tbl. 3-11 (1999) [hereinafter HOUSEHOLD DIARY STUDY 1999]; HOUSEHOLD DIARY STUDY 2003, *supra* note 4, tbl. A4-10.

18. U.S. POSTAL SERVICE HOUSEHOLD DIARY STUDY (1994) (unpublished survey results on file with the Author and the FCLJ).

19. HUMPHREY TAYLOR, THE HARRIS POLL, HARRIS INTERACTIVE, SPAM KEEPS ON GROWING (2003), [http://www.harrisinteractive.com/harris\\_poll/index.asp?PID=424](http://www.harrisinteractive.com/harris_poll/index.asp?PID=424).

set up to encourage legislation that would regulate telemarketing and spam.<sup>20</sup>

Policymakers have responded by conducting hearings, passing legislation, and implementing new rules, to regulate some forms of direct marketing.<sup>21</sup> Yet some forms of direct marketing have received more attention and legislation and are heavily regulated (or even banned), while other forms have appeared to spark less concern and have been less regulated. For example, despite the attention given in the media<sup>22</sup> and in congressional hearings,<sup>23</sup> direct mail has not been regulated, and there appears to be little public pressure to regulate it in the near future.<sup>24</sup>

Telemarketing, on the other hand, has been heavily regulated at the state and federal levels, and the strength of the regulations is increasing. Initially, just the hours and methods of contact were regulated.<sup>25</sup> More recently, new legislation and regulations have made it easier for consumers to completely opt-out of receiving unsolicited telemarketing calls. Many states have passed "asterisk bills," which prohibit unsolicited telephone

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20. Leslie Gornstein, *Telemarketer-bashing Spreads Across Internet*, FORT WORTH STAR-TELEGRAM, Apr. 3, 1997, at 1. For example, an organization dedicated to stopping the use of UCE called the Coalition Against Unsolicited Commercial Email ("CAUCE") claims to have over 21,000 members as of early 2005, and is pressing Congress to pass legislation restricting unsolicited e-mail. CAUCE Coalition Against Unsolicited Commercial Email, CAUCE Membership Statistics, <http://www.cauce.org/members/stats/index.phtml> (last visited Mar. 18, 2006) [hereinafter CAUCE].

21. For example, Congress has conducted hearings on direct mail, and passed the Telephone Consumer Protection Act to regulate telemarketing, and the CAN-SPAM Act of 2003 to regulate direct marketing on the Internet. *Oversight Hearing on the Use of Mailing Lists in Direct Marketing: Hearing Before the Subcomm. on Postal Operations and Serv. of the H. Comm. on Post Office and Civil Serv.*, 102nd Cong. (1991) [hereinafter *Oversight Hearing*]; ARTHUR WINSTON, *DIRECT MARKETING AND THE LAW: WHAT MANAGERS NEED TO KNOW 194-195* (1993); Press Release, Federal Trade Commission, The CAN-SPAM Act: Requirements for Commercial Emailers, Apr. 2004.

22. See, e.g., *Revolt of the Junk Receivers*, *supra* note 16; Edmondson, *supra* note 16; Headdon, *supra* note 16.

23. See *Oversight Hearing*, *supra* note 21.

24. There is some self-regulation in the form of a do-not-mail list called the Mail Preference Service ("MPS"), which is maintained by the industry trade group the Direct Marketing Association ("DMA"). See DIRECT MKTG. ASS'N, *PRIVACY PROMISE MEMBER COMPLIANCE GUIDE* (2003), [http://www.the-dma.org/privacy/Privacy\\_Promise.pdf](http://www.the-dma.org/privacy/Privacy_Promise.pdf) [hereinafter COMPLIANCE GUIDE].

25. Telemarketers were required to register with state authorities in many states, and the large majority of states have regulated the use of Automatic Dialing Recorded Message Players ("ADRMPs") and the permitted hours of making calls. Congress passed the Telephone Consumer Protection Act ("TCPA") in 1991, which restricted the hours of calling, required that telemarketers maintain do-not-call lists, and prohibited the use of ADRMPs. See WINSTON, *supra* note 21, at 186-87; DIRECT MKTG. ASS'N, *COMPENDIUM OF GOVERNMENT ISSUES AFFECTING DIRECT MARKETING IN 1998*, 65-69 (Elizabeth Scanlon ed., 1999) (on file with author and FCLJ).

sales calls to people who have requested that an asterisk be placed next to their name in the telephone directory, or have required that telemarketers honor do-not-call lists.<sup>26</sup> The most significant impact has come from the national Do Not Call registry imposed by the FTC in 2003. Sixty-two million phone numbers were signed up just one year later, about 60% of respondents to a survey.<sup>27</sup>

Commercial advertising both to fax machines and using text messaging to mobile phones has been banned.<sup>28</sup> Notably, both methods of advertising cost the receivers money. There were significant complaints about unsolicited fax messages in the 1980s, especially since faxes consumed receivers' toner and paper, and tied up their fax machines.<sup>29</sup> Unsolicited fax advertising was banned by the Telephone Consumer Protection Act of 1991 ("TCPA").<sup>30</sup> Meanwhile, phone companies in the United States usually charge a per message fee for sending and receiving text messages.<sup>31</sup> The FCC prohibited the sending of unsolicited commercial messages to mobile phones in 2004 as part of the implementation of the CAN-SPAM act.<sup>32</sup>

Telemarketing to wireless phones has become controversial, and it too incurs a cost for receivers.<sup>33</sup> While not illegal, it has been limited by a combination of self-restraint by telemarketers following the rules issued by the industry trade group, the Direct Marketing Association ("DMA"), and legal restrictions.<sup>34</sup> The FTC's Do Not Call registry accepts wireless phone

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26. WINSTON, *supra* note 21, at 186–87; DIRECT MKTG. ASS'N, *supra* note 25. About forty states have regulations concerning honoring do-not-call lists, and many of these maintain their own list. See Direct Mktg. Ass'n, Where Marketers Can Obtain State Do-Not-Call Lists, <http://www.the-dma.org/government/donotcalllists.shtml> (last visited Mar. 18, 2006).

27. Press Release, FTC, National Do Not Call Registry Celebrates One-Year Anniversary (June 24, 2004), <http://www.ftc.gov/opa/2004/06/dncanny.htm>. The FTC also reported that 87% of those who signed up said they received fewer calls. *Id.*

28. WINSTON, *supra* note 21, at 194; Rules and Regulations Implementing the Controlling the Assault of Non-Solicited Pornography and Marketing Act of 2003, *Order*, 19 F.C.C.R. 15927, paras. 1, 13–19 (2004) [hereinafter Non-Solicited Pornography].

29. See *Stop Me Before I Fax Again*, *supra* note 7; Gerlin, *supra* note 7; R.A. Spinello, *Ethical Reflections on the Problem of Spam*, 1 ETHICS & INFO. TECH. 185, 187 (1999).

30. Telephone Consumer Protection Act of 1991, 47 U.S.C. § 227, 227(d) (2000); WINSTON, *supra* note 21, at 194.

31. For example, Verizon Wireless charges \$0.10 for each message sent or received with packages available that allow unlimited text messages with other Verizon Wireless customers for a monthly fee. See Verizon Wireless, Personal, Plans, <http://www.verizonwireless.com> (select "Individual Plans"; click "TXT messaging") (last visited Mar. 28, 2006).

32. Non-Solicited Pornography, *supra* note 28.

33. CBSNews.com, *supra* note 15.

34. See COMPLIANCE GUIDE, *supra* note 24; Press Release, Direct Mktg. Ass'n, Unsolicited Marketing Calls to Cell Phones Are Illegal—With or Without a Cell Phone

numbers, and the TCPA's prohibition on the use of automatic telephone dialing equipment, which the FCC now interprets to include the commonly used predictive dialers, for calling wireless numbers significantly reduces the incentive for telemarketers to call wireless phones.<sup>35</sup>

The rapid growth of UCE (i.e., spam) has generated many complaints from users and Internet Service Providers ("ISPs") (which incur added costs from carrying it on their servers) and attracted policymakers' attention. Many states have passed laws to regulate UCE, or are considering legislation to restrict its use.<sup>36</sup> Congress passed the CAN-SPAM Act of 2003, which requires that commercial e-mail clearly indicates who sent it and what its purpose is, and be labeled as advertising in the subject line.<sup>37</sup> The volume of spam e-mail has continued to rise since passage, however.<sup>38</sup>

### B. *The Literature on Direct Marketing*

The evident rise in public concern about direct marketing has yet to be fully explained in the formal literature. Kielbowicz<sup>39</sup> argues that the controversy surrounding "junk mail" was manufactured by newspapers in order to raise third class postal rates and hinder the development of direct mail, a traditional competitor to newspapers for advertising. Yet the strength of the public's reaction against direct marketing in media other than mail suggests that the public has substantial concerns about the direct marketing that it receives.<sup>40</sup>

Some privacy experts have analyzed this issue as an encroachment on individual privacy. Privacy experts have recognized that two kinds of individual privacy are affected by direct marketing: the right to be left alone, and the right to control information about oneself.<sup>41</sup> Yet most of the

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Directory (Dec. 10, 2004), <http://www.the-dma.org/cgi/disppressrelease?article=609>.

35. See Joseph Sanscrainte, *Wireless Number Portability: The Compliance Conundrum*, CONNECTIONS MAG., June 2004, available at <http://www.connectionsmagazine.com/articles/4/043.html>.

36. See CAUCE, *supra* note 20.

37. FEDERAL TRADE COMMISSION, THE CAN-SPAM ACT: REQUIREMENTS FOR COMMERCIAL EMAILERS (2004), available at <http://www.ftc.gov/bcp/online/pubs/buspubs/canspam.pdf>.

38. Zeller, *supra* note 8.

39. Richard B. Kielbowicz, *Origins of the Junk-Mail Controversy: A Media Battle over Advertising and Postal Policy*, 5 J. POL'Y HIST. 248, 249 (1993).

40. See *supra* Part I.A (describing public reaction).

41. See Ellen R. Foxman & Paula Kilcoyne, *Information Technology, Marketing Practice, and Consumer Privacy: Ethical Issues*, 12 J. PUB. POL'Y & MARKETING 106, 107 (1993); Cathy Goodwin, *Privacy: Recognition of a Consumer Right*, J. PUB. POL'Y & MKTG 149, 150 (1991); Mary Gardiner Jones, *Privacy: A Significant Marketing Issue for the 1990s*, J. PUB. POL'Y & MKTG 133, 135 (1991).

discussion on direct marketing's impact on privacy, in the academic literature and the popular press, has concentrated on consumers' loss of control over information about themselves, i.e. their loss of "informational privacy."<sup>42</sup> However, the volume problem, which involves the "right to be left alone," is fundamentally different from the informational privacy problem. While informational privacy can easily be compromised by a single incident of personal information being improperly obtained or used,<sup>43</sup> the volume problem as discussed here relates to the aggregate volume of advertising received. Therefore, the key issues here are not individual incidents and how to prevent them, but the basic conditions determining the volume and relevance of advertising received by consumers, and how burdensome this advertising is for consumers to process. Thus, the volume problem must be studied differently, and the solutions needed will differ in nature from those proposed to protect informational privacy.<sup>44</sup>

Much of the literature on the volume problem has tended to focus on either the ethical<sup>45</sup> or legal<sup>46</sup> issues concerning direct marketing's impact

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42. See, e.g., Paul N. Bloom, et al., *Avoiding Misuse of New Information Technologies: Legal and Societal Considerations*, 58 J. MKTG 98, 100 (1994); Jones, *supra* note 41; Kevin F. McCrohan, *Information Technology, Privacy, and the Public Good*, 8 J. PUB. POL'Y & MARKETING 265, 265-266 (1989); John Morse & Suzanne Morse, *Teaching Temperance to the 'Cookie Monster': Ethical Challenges to Data Mining and Direct Marketing*, 107 BUS. & SOC'Y REV. 76, 76 (2002); Glen J. Nowak & Joseph Phelps, *Understanding Privacy Concerns: An Assessment of Consumers' Information-Related Knowledge and Beliefs*, J. DIRECT MKTG., Autumn 1992, at 28; Glen J. Nowak & Joseph Phelps, *Direct Marketing and the Use of Individual-Level Consumer Information: Determining How and When 'Privacy' Matters*, J. DIRECT MKTG, Summer 1995, at 46; Phelps et al., *supra* note 16, at 17-18 (noting that of 435 newspaper stories from five major newspapers that were examined for 1984-1992, 71% contained references to the gathering and/or use of information about consumers, while only 30% concerned the intrusion of uninvited advertising messages).

43. Cf. Goodwin, *supra* note 41, at 150-52.

44. The volume problem does not encompass all possible violations of an individual's right to be left alone. A single incident, such as a fraudulent telemarketing call or a harassing call, can intrude on this other form of privacy. These potential violations of individual privacy fall outside the scope of this Article.

45. See, e.g., Spinello, *supra* note 29; Foxman & Kilcoyne, *supra* note 41; George Milne & Mary Ellen Gordon, *Direct Mail Privacy-Efficiency Trade-offs Within an Implied Social Contract Framework*, 12 J. PUB. POL'Y & MARKETING 206 (1993).

46. See, e.g., Jonathan Byrne, *Squeezing Spam Off the Net: Federal Regulation of Unsolicited Commercial E-mail*, 2 W. VA. J.L. & TECH. 1.4 (1998), <http://www.wvu.edu/~law/wvjolt/Arch/Byrne/Byrne.htm>; Michael W. Carroll, *Garbage In: Emerging Media and Regulation of Unsolicited Commercial Solicitations*, 11 BERKELEY TECH. L. J. 233 (1996), available at [http://fringe.davesource.com/Fringe/NonZen\\_Companies/Spammers/Legal\\_Analysis.html](http://fringe.davesource.com/Fringe/NonZen_Companies/Spammers/Legal_Analysis.html); Franklyn S. Haiman, *Speech vs. Privacy: Is There a Constitutional Right Not to be Spoken to?*, 67 NW. U. L. REV. 153 (1972); David E. Sorkin, *Unsolicited Commercial E-Mail and the Telephone Consumer Protection Act of 1991*, 45 BUFF. L. REV. 1001 (1997); WINSTON, *supra* note 21.

on consumers' privacy. Some authors have proposed or discussed particular solutions to the problem.<sup>47</sup> The direct marketing trade press has also discussed the issue, often providing advice to direct marketers on how to avoid angering consumers or policymakers with their marketing.<sup>48</sup>

There is recent economics literature that analyzes the issues of call externalities<sup>49</sup> and information overload<sup>50</sup> discussed in this Article. Some of this literature focuses on pricing issues and on finding the welfare-maximizing price that achieves the optimal level of message-sending.<sup>51</sup>

However, there has been little attempt to provide an overarching framework to be used by policymakers for analyzing the problem in many communications media using a microeconomic perspective. Such a framework would help us understand how serious the problem is, or is likely to become, for different media, and how it is affected by various economic and technological factors. It would also help policymakers better evaluate the impact of various possible regulations that could be used to reduce the problem where it exists.

This Article analyzes the volume problem generated by direct marketing, using a theoretical framework that is based on microeconomic social welfare analysis. This framework allows for a multichannel approach to regulation, such that the decision to regulate direct marketing in any particular media would take into consideration the opportunities for firms to advertise their products using other, more suitable, media. This approach complements traditional legal and ethical analysis. The problems of informational privacy, consumer fraud, and free speech are not considered here (except tangentially), since they fall outside the scope of

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47. See, e.g., Ian Ayres & Matthew Funk, *Marketing Privacy*, 20 YALE J. ON REG. 77 (2003); Thede Loder, Marshall Van Alstyne & Rick Wash, An Economic Response to Unsolicited Communication (2005), available at <http://web.si.umich.edu/tprc/papers/2005/443/spam-tprc.pdf>; Lorrie Faith Cranor & Brian A. LaMacchia, *Spam!*, COMM. ASS'N COMPUTING MACHINERY, Aug. 1998, at 74; Goodwin, *supra* note 41; Milne & Gordon, *supra* note 45; Mark S. Nadel, *Rings of Privacy: Unsolicited Telephone Calls and the Right of Privacy*, 4 YALE J. ON REG. 99 (1986).

48. See, e.g., Karl Dentino, *Taking Privacy Into Our Own Hands*, DIRECT MKTG., Sept. 1994, at 38; Phil Herring, *Life Beyond the Spreadsheet*, DIRECT MKTG., Feb. 1992, at 49; Donna Loyle, *Do's & Don'ts in the Privacy Era*, TARGET MKTG., Nov. 2003, at 30.

49. Call externalities are the benefits gained by the recipient of a message sent by someone else. Benjamin E. Hermalin & Michael L. Katz, *Sender or Receiver: Who Should Pay to Exchange an Electronic Message?*, 35 RAND J. ECON. 423, 423 (2004).

50. See, e.g., Timothy Van Zandt, *Information Overload in a Network of Targeted Communication*, 35 RAND J. ECON. 542 (2004).

51. See, e.g., Daniel R. Shiman, *When E-Mail Becomes Junk Mail: The Welfare Implications of the Advancement of Communications Technology*, 11 REV. INDUS. ORG. 35 (1996); Hermalin & Katz, *supra* note 49; Loder, Van Alstyne & Wash, *supra* note 47.

the framework presented. Those interested in these issues should consult the extensive literature concerning them.<sup>52</sup>

This Article next describes the basic framework for analysis, and shows how the value of direct marketing can vary using a mathematical model and some examples. It focuses in the initial analysis on two key factors: the sending and receiving costs associated with a particular communications medium. The following Part discusses how to apply the framework to the various media available for direct marketing. It then discusses how to take into consideration other factors that could affect the value of direct marketing in particular media, and how these factors may change over time. Next, the kinds of solutions that are available to reduce the cost of direct marketing to consumers and society are examined. The final Part provides some concluding remarks.

### III. THE FRAMEWORK FOR ANALYSIS OF THE VOLUME PROBLEM

This Article is concerned with the kind of direct marketing that involves firms sending unsolicited advertising messages directly to selected consumers. This advertising benefits consumers by informing them about products they might want to buy. However, it also imposes a cost on consumers, regardless of whether they buy the product. This cost includes the time and effort used in processing the message (reading the letter or answering the telephone and hearing the sales pitch), and determining the appropriate response. For example, if a consumer receives a letter from a marketer advertising encyclopedias, the consumer benefits by hearing about the encyclopedias, but at a cost of having to open, read, and dispose of the letter. If the consumer does not purchase the encyclopedias, the time spent examining the letter will likely have been wasted.<sup>53</sup> While the cost of processing each message may be small, large numbers of messages may impose a significant burden on consumers' time and patience. With some kinds of messages (e.g., fax and SMS text messages) there is also a financial cost incurred by the recipient for receiving a message. Because there is a cost from these messages imposed on receivers which is incurred regardless of whether a purchase is made, this market for messages generates a negative externality. When negative

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52. See, e.g., Bloom et al, *supra* note 42; Byrne, *supra* note 46; Carroll, *supra* note 46; Foxman & Kilcoyne, *supra* note 41; Goodwin, *supra* note 41; Milne & Gordon, *supra* note 45; Morse & Morse, *supra* note 42; Sorkin, *supra* note 46.

53. The benefits a consumer might derive from reading about the product are discussed later.

externalities exist, market mechanisms do not typically lead to efficient results.<sup>54</sup>

This Article utilizes microeconomic social welfare analysis in a framework developed in a previous paper by the author.<sup>55</sup> Social welfare analysis is employed here to analyze the value (and potential harms) to consumers and society of receiving advertising messages and to assess the impact of various organizational, technological, and regulatory options that could be implemented.<sup>56</sup>

A microeconomic approach usually requires the identification of the benefits and costs of the market action, in this case the sending and receiving of direct advertising messages. Firms use direct marketing to attempt to sell their products directly to customers they have identified as likely purchasers.<sup>57</sup> They will send an advertising message to every consumer for whom the expected (i.e., average) revenue gained from sending the message exceeds the cost of sending the message, such that the firm earns a positive expected profit from sending the message. The expected net benefit the consumer gets from a message equals the difference between the expected benefit of hearing about the product and the cost of processing the message. The expected net benefit to society (i.e., the welfare gained) from sending a message is then the expected net benefit to the consumer of receiving the message, plus the net benefit to the firm of

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54. Externalities occur when some of the costs or benefits from a market action are not borne by the market participants. DENNIS W. CARLTON & JEFFREY M. PERLOFF, *MODERN INDUSTRIAL ORGANIZATION* 82 (3d ed. 2000). In market transactions without externalities, those who incur costs associated with the transaction (usually by the producer of the good) are compensated by payments (usually from buyers). In this case, there is a cost created by the sending of a message (i.e., the cost of processing the message) that is imposed on third parties, which are the people who receive and process the message but do not buy the good.

55. Shiman, *supra* note 51. Microeconomic social welfare analysis examines the costs and benefits to society from the operation of a market. Markets that are operating efficiently maximize the net benefits (called social welfare) society gains from that market. Social welfare analysis is often used by economists to determine the extent of market failure in a particular market, whether caused by structural characteristics of the industry, externalities, or government regulations and taxes. They also use it to analyze the impact of a policy action on a market. *See generally* CARLTON & PERLOFF, *supra* note 54, ch. 3.

56. Oftentimes social welfare analysis involves separately determining the impact of the market and the market failure on consumers (called consumer surplus) and producers (called producer surplus) to find each group's net benefit, and then summing the two groups' net benefits to calculate the impact on welfare. CARLTON & PERLOFF, *supra* note 54, at 71–72. In this Article the analysis focuses on senders and receivers of messages. Note that while message senders are usually sellers of a good, most recipients do not buy the good, so the correspondence is not identical to the usual model of sellers and buyers of goods.

57. According to one survey, the industries that use direct mail the most are mail order firms, publishers, department stores, specialty stores, and credit card companies, in that order. HOUSEHOLD DIARY STUDY 1999, *supra* note 17, at VI-7.



sending it (i.e., the firm's profit). If firms send out messages which provide a negative expected net benefit to society, then this Article will call these messages "Welfare-Reducing Marketing" messages or WRM. Society would be better off if WRM messages were not sent, since the cost to consumers to receive and process these messages is greater than the expected benefit to consumers from hearing about the product plus the expected profit to firms from sending the message.

The expected benefit to the consumer of hearing about the product depends on, among other factors, the likelihood that the consumer will purchase the product. This in turn depends on how carefully the sending firm has targeted likely buyers. Firms maintain or acquire lists of consumers classified according to the consumers' personal characteristics such as demographics, lifestyles, subscriptions, and past purchases. For each offer of a particular product, price and sales pitch, firms are able to test each list with sample mailings of 5,000–10,000 names to determine that list's response rate, which is the proportion of people on the list that respond to each mailing. Each list is used in a direct marketing campaign only if it generates a high enough response rate to produce sufficient revenue to at least cover the cost of the mailings to that list.<sup>58</sup>

Low message sending costs make it profitable for a firm to send advertising to lists with low response rates. In effect, the low cost of contacting consumers reduces the incentive for marketers to target their advertising carefully, because the cost of wasting advertising on nonbuyers is low. The consumers receiving this advertising, however, may place a low value on it, because of the low probability of their purchasing the good. For example, if a firm uses lists with a 1% response rate, only 1 in 100 recipients will be interested, and the other recipients might consider the mailing unwelcome, even before examining it.<sup>59</sup>

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58. See BOB STONE, *SUCCESSFUL DIRECT MARKETING METHODS* ch. 9 (5th ed. 1994). For example, if a firm has three lists of potential customers, call them lists A, B, and C, then the firm might try test mailings to three samples of 10,000 names, one sample drawn from each list. If in response to the test mailing 100 people on list A, 500 people on list B, and 2,000 people on list C purchase the firm's good, then the predicted response rate for list A is  $100/10,000 = 1\%$ , for list B is  $500/10,000 = 5\%$ , and for list C is  $2,000/10,000 = 20\%$ . If the firm determines that a 10% response rate is required for the mailing to be profitable, then the firm would consider engaging in a full direct marketing campaign, with a mailing sent to all names on the list, only for list C.

59. Note the expected benefit is determined *ex ante*, before the receiver has processed the message and decided whether to respond. WRM can therefore occur for *all* consumers who receive the message, even those who *ex post* find it useful. This would be akin to forcing people to buy a \$2 lottery ticket, with a 1% chance of winning \$100, yielding an expected net benefit of -\$1. Even though there are a few happy winners in the short run, if this purchase occurs repeatedly, everyone will likely be worse off in the long run.

Thus an advertising message is more likely to be considered undesirable by receivers if it is poorly targeted, and if the cost of processing the message (both financial and in time and effort) is high. Those media with low costs of sending messages, and that have a high cost of receiving and processing messages are therefore more likely to have welfare-reducing messages.

In some media the sending costs may be sufficiently low, and receiving costs sufficiently high, that advertising on the whole yields a negative net benefit to recipients. If recipients are unable to distinguish, before processing the messages, between advertising messages that yield a positive net benefit and those that yield negative net benefit, then they may prefer to receive no advertising at all. Thus for media where all messages look alike *ex ante* (before they are processed), and the net benefit of processing advertising is negative, consumers will have an aversion to all marketing on these media, which we will call "Marketing Aversion." When Marketing Aversion exists, consumers may avoid processing all advertising messages, if possible, or may urge policymakers to ban all advertising.<sup>60</sup>

Indeed, if consumers cannot distinguish *ex ante* between advertising and personal messages, and the net benefit to consumers of processing all messages received (including nonadvertising messages) were negative, then consumers would want to ignore all messages received. Thus it would not be worthwhile to answer the telephone, or read one's mail, e-mail, or Internet forum postings. If this occurred for most users of a medium, the medium would collapse as a means of communicating with others, which we will call "Medium Failure." Direct marketing thus can affect the viability of a medium.<sup>61</sup>

If the net benefit to all senders and recipients of all marketing messages is negative, then there is "Negative Welfare from Marketing." If it proves impossible to reduce the harms from marketing or to block just the welfare-reducing marketing messages, then the government may want

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60. In this case marketers using low response rate lists to send WRM impose a negative externality not just on receivers, but also on other marketers that are targeting more carefully, since recipients might equally ignore all advertising.

61. There are likely a number of media that have collapsed because of this problem, especially on the Internet, which has extremely low message sending costs. For example, many unmonitored Usenet groups and Internet forums have disappeared. See Molly Wood, *Eulogy for Usenet*, ZDNET.COM, Jan 25, 2005, [http://reviews-zdnet.com.com/4520-6033\\_16-5622511-1.html](http://reviews-zdnet.com.com/4520-6033_16-5622511-1.html) ("After all, the AOL hordes, by many accounts, ushered in the decline of Usenet, including the arrival of the spam that would eventually overwhelm the neighborhood."); see also John C. Dvorak, *Googlepedia: The End is Near*, PCMAG.COM., Feb. 14, 2005, <http://www.pcmag.com/article2/0,1895,1764757,00.asp> ("Usenet has fallen out of favor and been largely marginalized over the past several years, as spammers helped ruin it.").

to consider banning all unsolicited direct marketing on this medium. Note that direct marketing may, as a whole, provide positive net benefits to society even if consumers have Marketing Aversion, if the profits to firms (plus any external benefits)<sup>62</sup> outweigh the costs to consumers from the marketing.<sup>63</sup>

#### A. *The Mathematical Model*

This Part outlines the mathematical model that demonstrates the conditions for when some or all firms' direct marketing will be welfare-reducing.<sup>64</sup> Readers who are not interested in the mathematics may skip this Subsection. Let the firm's cost of sending an advertising message to each consumer be  $s$  for a particular communications medium. The price it charges for the good is  $P$ , and the cost of producing and shipping the good, excluding advertising costs, is  $C$ . The firm sends messages to each list for which the expected revenue from responses exceeds the sending costs. The expected economic profit per message sent to a person on list  $i$  is

$$(\text{Eq. 1}): \pi_i = (P - C) \theta_i - s \text{ where } \theta_i \text{ is the response rate for list } i.$$

The firm sends advertising to all lists for which  $\pi_i > 0$ , and therefore all lists with response rate  $\theta > s/(P - C)$ . The list with the lowest response rate  $\theta_m$  to be contacted is then

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62. One external benefit might be financial support for providing the medium. For example, the U.S. Postal Service relies significantly on direct marketing for revenues. Thus a ban on direct mail would likely force postal rates up for noncommercial users. Similarly, some broadcast media (which do not involve direct marketing) likely have the equivalent of Marketing Aversion, but most consumers accept the advertising messages to be a necessary evil, since the messages support the other uses of the medium. For example, programming on advertiser-supported television and radio broadcasts is supported by consumers having to view advertisements during the programs.

63. Whether policymakers want to include sellers' profits in the analysis depends on whether they prefer to focus on total social welfare or on consumer surplus. Economic theory has traditionally assumed that side payments between economic actors and groups can be arranged, such that winners (those that gain from a policy) can compensate losers for their losses. Thus, social welfare analysis usually has the goal of choosing the policy that maximizes the total gain to society as a whole, and assumes that the gains can be redistributed as necessary to make everyone happy. If such side payments are not feasible, then policymakers must choose how to weigh the various parties' gains and losses according to political tastes and, possibly, considerations of long-term dynamic implications (e.g., economic growth and technological development).

64. This model was first outlined in Shiman, *supra* note 51, and further developed in Daniel R. Shiman, *The Impact of Firms' Increased Information about Consumers on the Volume and Targeting of Direct Marketing* (Aug. 1997) (unpublished manuscript), available at <http://ssrn.com/abstract=555646> (scroll down to SSRN Electronic Paper Collection and download).

$$(\text{Eq. 2}): \theta_m = s/(P - C).$$

As  $s$  falls, lists with lower response rates will get advertising.

Meanwhile, consumers who receive messages incur a cost  $r$  for processing each message. Assume that those consumers that choose to buy the good value it at  $B$ , if they are offered it, such that they receive value of  $B - P$  if they buy it.<sup>65</sup> The *ex ante* expected utility or benefit to consumers of receiving each message, often called the consumer surplus, is the probability of buying the good multiplied by the benefit if purchased, minus the receiving cost.<sup>66</sup> So if consumers on list  $i$  have probability  $\theta_i$  of buying the good, let their expected utility from each advertising message be

$$(\text{Eq. 3}): u_i^a = (B - P)\theta_i - r.$$

The social welfare gained from each message is the sum of the expected benefits to senders and receivers, plus any external costs or benefits to third parties.<sup>67</sup> Assume that the external cost or benefit to third parties, call it  $E$ , is constant for each message.<sup>68</sup> Then the social welfare

65. We assume that consumers have a linear additively separable utility function such that for each message received, their *ex post* utility is

$$u = \begin{cases} (B - P) - r & \text{if } B \geq P \\ -r & \text{if } B < P. \end{cases}$$

Note that the cost of receiving messages rises linearly with the number of messages such that twice as many messages are considered twice as burdensome to consumers. This may understate the actual increase in cost if consumers feel there is an annoyance factor to receiving more advertising messages, particularly for messages advertising goods that are not purchased.

66. Note that we assume that the receiver benefits from the message only if he or she buys the good advertised. Some consumers may benefit from seeing advertised prices for competing goods from multiple prices, even if they intend to purchase just one good. Or they may enjoy "window shopping" by browsing catalogs, either because they have an interest in the products or in the manner of presentation (such as Sharper Image). These benefits gained from just receiving the message can be incorporated into the analysis either by adjusting the receiving cost  $r$ , if all messages are of interest or if only some messages are of interest, by assuming that  $B$  incorporates the utility from consuming both the message and the good. In the latter case, not all positive benefits  $B > P$  lead to a purchase, and consumers may actually want more mail than they receive. The market solution to this latter case is simple: the advertiser may require payment for its advertising if no purchases are made, as some catalog companies have appeared to do by putting a price on the catalog.

67. See CARLTON & PERLOFF, *supra* note 54, ch. 3. We assume for simplicity there are no taxes.

68.  $E$  could represent the impact of an advertising letter or catalog on a landfill, or the burden on an ISP of passing along an e-mail in which case the value of  $E$  would be negative. Note that whether a message is responded to will not likely change the message's impact on the environment and on message intermediaries, so its cost or benefit does not

gained from each message sent to list  $i$  would be

$$\begin{aligned} \text{(Eq. 4): } W_i &= \pi_i + u_i^a + E \\ &= [(P - C)\theta_i - s] + [(B - P)\theta_i - r] + E \\ &= (B - C)\theta_i - s - r + E. \end{aligned}$$

A message is welfare reducing if  $W_i < 0$ . Observe that  $\pi_i$  can be positive, while  $u_i^a$  and even  $W_i$  can be negative if  $r$ ,  $P$ , and  $E$  are large enough.<sup>69</sup> This means that the firm may find it profitable to send messages to some consumers while those consumers and society, including third parties, gain negative benefit from receiving the messages. This is because  $r$  and  $E$  are externalities, which are costs to consumers and society that are not directly paid for by producers and buyers during the transaction. To simplify the analysis for now,  $E$  will be assumed to be zero. From (Eq. 2), (Eq. 4), and the fact that  $W_i$  is increasing in  $\theta_i$  in (Eq. 4), we find<sup>70</sup> that WRM messages will be sent, meaning that  $W_i < 0$  for some lists  $i$ , only if

$$\text{(Eq. 5): } s/(P - C) < r/(B - P).$$

For this analysis it is assumed that  $B$ ,  $P$ , and  $C$  are constant. While they will vary among products, firms, and consumers, it seems unlikely that they will vary much by medium for any given product, and therefore the focus is on how changes in receiving cost  $r$  and sending cost  $s$ , especially large order-of-magnitude changes, affect social welfare. Consequently, WRM messages are more likely to be sent in media with low sending costs and high receiving costs. Consumers will not want to receive any WRM messages since for those messages  $u_i^a < 0$ .

If all advertising messages look alike *ex ante*, it is possible for the negative utility obtained by consumers for those messages to outweigh the positive benefits from other advertising messages received. Thus, summing the utilities for all advertising messages  $j$  received by a consumer, if

$$\text{(Eq. 6): } \sum_j u_j^a < 0$$

then there is Marketing Aversion.

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vary with  $\theta_i$ .  $E$  could also be positive. For example, the pictures of missing children placed on some advertising mail may aid in their return.

69. Here  $E$  is assumed to be negative and “large” in absolute value terms.

70. See Shiman, *supra* note 51, at 39.

Medium Failure occurs when receivers are unable to distinguish *ex ante* between advertising and personal messages, and the net benefit of receiving all messages is negative. If consumers receive personal messages, each yielding utility  $u_k^p$ , then they will ignore all messages received if the messages all look alike *ex ante*, and if

$$(\text{Eq. 7}): \sum_j u_j^a + \sum_k u_k^p < 0.$$

Negative Welfare from Marketing occurs when the net benefit to society, including senders and receivers, of all marketing messages is negative. Thus summing the welfare,  $W_i$ , gained from each message over all lists  $i$  and all people  $m_i$  on each list, direct marketing in a particular medium is generally harmful to society if total social welfare ("SW") is negative, or

$$(\text{Eq. 8}): SW = \sum_i \sum_{m_i} W_i = \sum_i m_i [(B - C)\theta_i - s - r + E] < 0.$$

### B. An Example of Welfare-Reducing Marketing

A simple example will illustrate how the value of direct marketing can vary by communications medium. Assume that a firm wants to advertise its good using direct marketing. The firm has three lists of consumers with a different response rate, or the percentage of people on the list that purchase the good, for each list. Let the high, medium, and low response rate Lists be H, M, and L, respectively, with corresponding response rates  $\theta_H = 25\%$ ,  $\theta_M = 5\%$ , and  $\theta_L = 1\%$ . For this example, assume that the cost of producing and shipping the good is  $C = \$20$ , exclusive of advertising expense, and the price that it sets is  $P = \$30$ , yielding a profit per good sold, excluding advertising costs, also known as the "allowable margin" or "net order contribution," of  $P - C = \$10$  per unit sold. Meanwhile, consumers who receive messages incur a cost for processing the message  $r$ , which is assumed to be \$0.25. Also assume that those consumers who choose to buy the good value it at  $B = \$32$ . Thus, they receive value of  $B - P = \$2$  if they buy it.

We can see what happens when the sending cost  $s$  falls, from \$2 to \$0.40 to \$0.01, as marketers switch to lower cost media or as communications costs fall within a medium. The payoffs received per message, by firms, consumers, and society, are shown in Table 1 for Media 1, 2, and 3. (See *infra* Table 1.)

So for Medium 1 and List H in Table 1, there is a 25% probability that each message will result in a sale for the firm, which combined with a \$10 allowable margin per sale, generates \$2.50 expected (average) revenue

per message. After subtracting out the \$2 cost of a message, this yields a net expected profit,  $\pi$ , per message of \$0.50. Meanwhile, consumers on List H have a probability of 25% of receiving a benefit of \$2 from buying the good, for an expected benefit of \$0.50 of hearing about the good, which with a cost of the equivalent of \$0.25 in effort to process each message, yields a net expected benefit of \$0.25 per message. Expected social welfare gained by society is then the \$0.50 benefit (profit) to firms plus the \$0.25 benefit (i.e., consumer surplus or “CS”) to consumers, or \$0.75 for each message sent. It is assumed here that there are no costs or benefits to message intermediaries or the environment. If there were such, the estimated social welfare would be adjusted accordingly.

In Medium 1, because of the high sending cost, it is only profitable for a firm to send messages to List H. Meanwhile, Medium 2's lower sending cost makes it profitable to also contact List M, and in Medium 3, List L is contacted as well. Although the mailing to List H generates positive benefits to consumers and society in every medium, the mailing to list List M in Medium 2 yields negative consumer surplus and social welfare, and therefore, those messages are WRM messages. Consumers and society would be better off without this mailing.

In Medium 3 there is not just WRM for List L. If a consumer does not know which list he or she is on, and has equal probability of being on each list,<sup>71</sup> then the expected benefit of receiving a message is -\$0.04 per message<sup>72</sup> such that the cost to the consumer of receiving all unsolicited advertising outweighs the benefit of hearing about the products offered. The consumer would then prefer to receive no advertising, and there would be Marketing Aversion. Medium 3 would be a candidate for Medium Failure if consumers were equally likely to be on Lists H, M, and L,<sup>73</sup> and the gain from getting personal messages was less than the loss from receiving advertising messages.

Medium 4 demonstrates how an increase in the receivers' cost of processing messages can affect their attitude towards direct marketing. The rise in receiving cost relative to Medium 1 now makes receivers much worse off.<sup>74</sup> And even though messages are better targeted in Medium 4,

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71. Note that not knowing which list you are on means not knowing how the product's attributes relate to your personal characteristics, rendering you unable to determine your likelihood of purchase before processing the message and learning about the product.

72. See *infra* Table 1, rightmost column.

73. In fact, since direct marketing is usually used for niche-type goods, consumers are much more likely to be on lists with low response rates such as L and M. With a higher probability of being on List M and especially L, the average consumer benefit from receiving unsolicited advertising will be even lower for Media 2 and 3.

74. A rise in receiving costs can occur for a number of reasons, such as an increase in the value of a receiver's time, or the use of new media in which immediate processing of a

receivers in that medium are worse off there than in Medium 2. Thus, the extent of the volume problem depends on the combination of  $r$  and  $s$  for a particular medium. Observe also that a ban on all advertising messages sent would increase social welfare in Medium 4 since that medium has Negative Welfare from Marketing. However, even though consumers may advocate a ban in Medium 3, such a ban would not be welfare maximizing.

#### IV. APPLYING THE BASIC FRAMEWORK

A rough determination of which media are more likely to have WRM messages and Marketing Aversion can be made by examining the estimated sending and receiving costs for each medium. The results for a variety of media, using roughly estimated sending and receiving costs, are graphically displayed in Figure 2.<sup>75</sup> Direct marketing messages from media that are characterized by both high receiving costs, such that the messages are costly for consumers to process, and low sending costs, such that the messages are more poorly targeted, will be less desirable to receivers. Hence, in the diagram, consumers should prefer advertising from media in the lower left, while media that are in the upper right are more likely to have WRM, Marketing Aversion, and Medium Failure. (See *infra* Figure 2.)

This diagram demonstrates why some media have been regulated more quickly and heavily than others, particularly among older media. Despite complaints about the increased volume of direct mail received, mail's characteristics probably give it the highest value of consumer surplus, which helps explain why it has remained unregulated. Telemarketing's higher receiving cost has led to increasing regulation, while fax advertising's combination of low sending costs and high receiving costs is probably the reason why it was quickly banned.

It is also clear from the diagram that the problems of WRM, Marketing Aversion, Medium Failure, and Negative Welfare from Marketing are potentially far more serious for the newer communications

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message is needed, such as for a cell phone. These examples also demonstrate how technological changes can improve the situation. Changes that lower the cost of receiving messages (i.e., going from Medium 4 to Medium 1) will increase receivers' net benefits from direct marketing.

75. While estimates can be easily developed for sending costs, estimating receiving costs for the average recipient is much more difficult. It was assumed here that receiving costs depend on how long it takes to process a message (e.g., e-mail can be quickly scanned and discarded), whether a message demands immediate attention or not (e.g., phone calls and messages to mobile devices are usually attended to quickly), whether there is a cost charged for receiving a message (e.g., wireless calls use up minutes of a plan; senders and receivers pay for each SMS message), and whether the receiver's physical resources are used (e.g., faxes consume paper and ink).



media, compared to the traditional media of mail and wireline calls. The use of electronic communications and the Internet has significantly lowered the cost of sending out messages, often by several orders of magnitude. Meanwhile, the use of personal mobile devices to allow consumers to communicate whenever they want, no matter what they are doing, and to immediately send and receive important messages, has increased the disruption caused by receiving low value messages.<sup>76</sup> Thus, the problems caused by direct marketing are likely to be quite significant for calls and text messages to wireless phones and for e-mail and instant messaging on the Internet. This helps explain why there has been an increased interest by the public and policymakers in regulating direct marketing, and why the option of banning direct marketing for particular media is increasingly discussed.<sup>77</sup>

The potential for trouble would appear to be greatest for personal wireless devices if e-mail from the Internet is allowed to reach wireless phones as SMS text messages.<sup>78</sup> With near-zero costs of sending, and a significant disruption caused to recipients, the potential harm caused by direct marketing here is very large.<sup>79</sup> The FCC has imposed a ban on sending unsolicited commercial messages to the Internet e-mail addresses for wireless devices.<sup>80</sup>

## V. THE IMPACT OF OTHER FACTORS ON THE ANALYSIS

While overall sending and receiving costs are key determinants of the existence and extent of WRM and Marketing Aversion, other factors, such as how individuals vary in their preferences for direct marketing, the impact of direct marketing on the environment and on message intermediaries, changes in technology and receivers' value of time, the impact of the recent increase in volume of direct marketing received, and the existence of alternative direct marketing channels, also play a significant role. This Article discusses here how policymakers could take these factors into consideration when considering what kind of regulations, if any, are needed to regulate direct marketing within a particular medium.

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76. This, and the fact that the consumers pay for minutes of use, explains why many people do not want to have their cell phone numbers published. See CBSNews.com, *supra* note 15.

77. See Part II.A, *supra*.

78. While in Europe such a connection has not been enabled, some U.S. carriers are starting to provide a gateway between Internet e-mail and SMS text messages. In Japan, DoCoMo already blocks as spam about 80% of the one billion e-mails it receives from the Internet for its SMS customers. Guerra, *supra* note 12.

79. Guerra, *supra* note 12.

80. Non-Solicited Pornography, *supra* note 28, at 15927, para. 1.

A. *Variation by Individual in Direct Marketing's Impact*

Individual characteristics of consumers play a crucial role since consumers are heterogeneous in the direct marketing they will receive and their reaction to it. Consumers will vary in two key dimensions. First, the receiving cost will vary by individual. Some people place a higher value on their time or find intrusions on some media more irritating. Others, however, may like the convenience of being directly notified of available products through direct marketing or may enjoy looking through catalogs even if they don't buy. Second, people with certain characteristics may be more likely to be targeted by direct marketers. Mailing lists of consumers who make frequent purchases, have high incomes, or have recently had a baby are considered particularly valuable, and these consumers generally get more direct advertising.<sup>81</sup> Some consumers might even find themselves placed on inappropriate mailing lists. One person complained that buying a baby gift for someone else put her on a mailing list for parents, and she was subsequently inundated by advertisements for baby products.<sup>82</sup> To the extent that consumers are heterogeneous in their reaction to direct advertising, policymakers may want to give consumers the choice of not receiving direct advertising.

B. *Variation in Impact According to the Source and Type of Direct Marketing*

Some sources and types of direct marketing may provide less irritation than others, even if the response rates are similar. For example, consumers may not mind receiving direct marketing from firms of which they are currently customers. Surveys show that consumers are much more likely to read mail from firms with which they have had a past relationship.<sup>83</sup> In addition, many consumers benefit from receiving and perusing catalogs, even if they make no purchase. They may enjoy keeping up with fashions and technology. They may also find their ability to get the lowest price improves with the receipt of multiple catalogs. Low response

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81. *Oversight Hearing*, *supra* note 21. Important and famous people also tend to receive a large volume of unsolicited personal messages and "fan mail," creating a similar kind of burden, similar because the sender imposes a cost on the receiver of processing the unsolicited message. *Id.*

82. *Oversight Hearing*, *supra* note 21.

83. Jean Li Rogers, *Mail Advertising and Consumer Behavior*, 13 PSYCH. & MKTG, 211, 224-25 (1996); See HOUSEHOLD DIARY STUDY 1999, *supra* note 17, at VI-59. This effect falls outside the framework described above only if it is not the result of house lists having higher response rates. Note that solicited direct marketing messages are excluded from this Article's analysis.

rates for these kinds of advertising might be misleading as to their value to consumers.

*C. Impact on Third Parties*

A full economic analysis of the problem should take into account not only the impact on consumers and firms of direct marketing, but also other externalities as well. First, direct mail and fax advertising may have an impact on the environment from the disposal of unwanted messages. Direct mail in particular has provoked complaints about the large quantity of solid waste created, and the burden on landfills it creates.<sup>84</sup> In response, the U.S. Postal Service initiated a "Greening the Mail" Task Force to study methods of reducing environmental waste and improving recycling of mail, and about half of all direct mail marketers reported using recycled paper in their promotions.<sup>85</sup>

Second, unsolicited advertising may have an impact on message intermediaries that have to deliver the messages. These intermediaries may find it harmful or beneficial to transmit the advertising messages, depending on the cost of handling the message and whether they receive compensation for passing it along. Telephone companies and the U.S. Postal Service receive payment for transmitting advertising and encourage it with volume discounts, as do TV and radio stations, which depend on advertising for their revenue.<sup>86</sup> ISPs, on the other hand, receive no payment for messages sent or received, and unsolicited commercial e-mail has become a significant burden on their systems.<sup>87</sup>

*D. Impact of Economic and Technological Factors on Sending and Receiving Costs*

Economic and technological factors can have a significant impact on sending and receiving costs, and therefore on whether direct marketing should be regulated for a particular medium. The development of new electronic media for communication is the most obvious factor to take into consideration. These media usually have much lower sending costs, which

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84. DIRECT MKTG. ASS'N, *supra* note 25, at 57.

85. *Id.* at 55–58.

86. For example, the U.S. Postal Service offers discounts for large quantities of advertising mail, with additional discounts depending on the size and weight of the mail and whether it is presorted. USPS Web site, <http://pe.usps.com/text/dmm300/243.htm> (last visited Feb. 24, 2006). See also HAROLD L. VOGEL, ENTERTAINMENT INDUSTRY ECONOMICS, ch. 6 (4th ed., 1998).

87. Barry D. Bowen, *Controlling Unsolicited Bulk E-Mail: Who's Taking Action? What's Being Done?*, SUNWORLD, Aug. 1997, <http://sunsite.uakom.sk/sunworldonline/swol-08-1997/swol-08-junkemail.html>.

increases the likely volume of poorly-targeted direct marketing received. In some cases, the cost of sending has dropped by several orders of magnitude.<sup>88</sup>

Receiving costs have also been affected by economic and technological factors. Time appears to have become an increasingly valuable commodity to consumers, so the cost of processing a message in a particular medium may be increasing. In addition, as people develop busy schedules, the ability to avoid or postpone handling low priority messages becomes more important and raises the cost of messages on media that require immediate handling, such as phone calls.<sup>89</sup> Meanwhile, new technological advances have not just lowered sending costs, but receiving costs as well. The use of answering machines, voice mail, caller ID, and anonymous call rejection have lowered the receiving cost of telemarketing calls, just as spam filters have lowered the cost to receivers from e-mail advertising. In addition, it is important to recognize that the development of electronic messaging has not only lowered the cost of sending a message in comparison to phone calls, but also made it easier for receivers to scan the subject and contents of the message, and to delay processing the message until it is convenient.

#### *E. Impact of Changes in Volume and Targeting in Traditional Channels*

Recently, the volume of direct mail and telemarketing calls has dramatically increased, as discussed above and seen in Figure 1. The reasons for this include a decline in sending costs, (especially in telemarketing) and businesses' increased demand for advertising.<sup>90</sup> The development of geodemographic and psychographic databases, with their extensive information about individual consumers, has also played a major factor in direct marketing's growth.<sup>91</sup> The use of these databases has helped direct marketers to better identify likely buyers and has increased the volume of direct marketing sent to these buyers.<sup>92</sup>

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88. See Figure 2, *infra*.

89. These factors may help explain the recent push to help consumers avoid telemarketing calls.

90. Shiman, *supra* note 1. See also DICK SHAVER, THE NEXT STEP IN DATABASE MARKETING: CONSUMER GUIDED MARKETING 228-29 (1996).

91. SHAVER, *supra* note 90, at 229-30; Shiman, *supra* note 1.

92. SHAVER, *supra* note 90, at 228-31; see Shiman, *supra* note 1. The explanation for why better targeting *increases* the volume of direct marketing, which might seem counterintuitive if it is expected that it eliminates mailings to likely nonbuyers, is that increased information makes it profitable to conduct mailings that were hitherto unprofitable. For example, a firm might not find it profitable to advertise encyclopedias in a mailing to the whole population because of the low response rate, but might find it

The growth of direct marketing in traditional channels has drawn the attention of the public and the media and spurred adoption of a national do-not-call list. Yet, whether consumers are actually made worse off by this growth depends on the cause of the increase. To the extent that use of these databases helps improve the targeting of direct marketing, consumers may be better off because more of their mail and telemarketing calls will be useful, and they will receive fewer offers they do not want. However, the increase in volume may make consumers worse off, for two reasons. First, if lists with lower response rates are being used (due to a fall in sending costs), WRM is more likely, as already discussed. Second, the marginal benefit of receiving each additional message is likely to fall as more messages are received for competing products. The first credit card offer may be considered valuable, but the tenth such offer will probably be of little marginal value, since it is unlikely to be offering significantly higher benefits than earlier messages. On the other hand, for some products, more competing offers should mean increased competition and lower prices.<sup>93</sup>

#### *F. Viewing Communications Media as Alternative Marketing Channels*

Rather than independently examining each medium to determine the extent of WRM on that medium, one could instead view all of the media available as just alternative means of delivering the same advertising message to consumers. If all consumers were identical, and available media only differed in their sending and receiving costs, then the problem can be defined for policymakers as finding the optimal medium in which to allow direct marketing to be distributed, while banning unsolicited advertising on all other channels, on which advertising would be redundant. However, since consumers are heterogeneous in their tastes and in the attention they pay to different media, and because of strong legal concerns about limiting free speech, policymakers are unlikely to fully adopt this viewpoint. Yet, this approach could play an important part in the evaluation of the problem of WRM in various media and the appropriateness of different solutions under consideration.

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worthwhile to do a direct mailing to a list of parents of school-age children. A theoretical demonstration and analysis of this effect is provided in Shiman, *supra* note 64.

93. For example, competition between multiple credit card companies to gain customers might cause them to lower the price of obtaining a credit card. Thus the annoyance to consumers of getting more direct marketing could be outweighed by the drop in prices from the increase in competition.

## VI. AVAILABLE SOLUTIONS TO THE PROBLEM

In addition to the basic conditions described above, the extent and seriousness of WRM observed in a medium depends as well on the technological, organizational, and physical solutions that are available for dealing with the problem. A variety of innovative methods have been used to solve the problems of WRM messages and Marketing Aversion. This Article, discusses, in turn, those solutions that receivers can adopt for themselves, those that can be adopted by advertisers singly or through an industry association, and those that government (or if it exists, an organization or message intermediary that controls message sending on a particular medium) can impose. Many of these solutions have been discussed in the literature on direct marketing.<sup>94</sup>

A typology of the major types of solutions that have been used is presented in Table 2. While not a comprehensive list, most solutions employed fit into one of these types. These solutions generally have a goal of either eliminating poorly targeted advertising messages, reducing the cost of processing messages, or giving consumers the ability to avoid receiving some or all advertising. (See *infra* Table 2.)

### A. Receiver-Deployed Solutions

Many consumers have found ways to scan messages, in order to determine their value quickly, instead of processing them fully.<sup>95</sup> Scanning includes checking the source of the message (e.g., from the envelope, the "From:" field on an e-mail, or Caller ID), skimming the message, or using an answering machine to screen calls. While these methods generally lower the cost of processing messages, they increase the likelihood of missing potentially valuable offers or important messages that are accidentally filtered out. Scanning is made easier for consumers when advertising is well labeled, so government-imposed labeling requirements can be beneficial.

Another method used to handle WRM is to have someone screen incoming messages. Screening can be costly, and is employed, for instance, by people whose high value of time justifies paying a receptionist to answer telephone calls and read the mail. On the Internet, many forums are moderated, meaning someone has volunteered to screen out undesirable

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94. See, e.g., Ayres & Funk, *supra* note 47; Cranor & LaMacchia, *supra* note 47; Goodwin, *supra* note 41; Milne & Gordon, *supra* note 45; Nadel, *supra* note 47.

95. According to a 1998 survey, only 12.4% of households usually read their advertising mail, while 38.8% usually scan it, 37.2% read some of it, and 11.5% usually do not read it. Household Diary Study 1999, *supra* note 17, at III-27.

messages.<sup>96</sup> This often involves a significant investment of time by the moderator.<sup>97</sup> Filtering, which is similar, involves automatically rejecting messages depending on their type or source. E-mail, for example, can be filtered by software.<sup>98</sup>

Limiting access can be implemented either by individual receivers, who can decide to receive messages only from people they know, or by a central decision maker who restricts communications to the group to those sent by approved members. Many Internet forums try to restrict marketers' access to the group by limiting discussion to members.<sup>99</sup> Some early users of Internet forums formed small private groups to continue their discussions uninterrupted by low-quality commercial and noncommercial messages.<sup>100</sup>

### B. Industry-Deployed Solutions

A variety of solutions can be deployed by direct marketers that reduce the problem of WRM. Voluntary restraints are often recommended by industry groups and adopted by firms to forestall government regulation, to avoid offending potential customers, and to avert retaliation by unhappy recipients. For example, business is supposed to learn the proper "netiquette" for advertising on the Internet.<sup>101</sup> Firms have been advised to avoid being obtrusive, to learn about and be respectful of the culture of the Internet, to tailor their messages to their audience, and to use more interactive methods of advertising.<sup>102</sup> Offended consumers can quickly spread the word about a company's transgressions,<sup>103</sup> which makes large

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96. See RESNICK & TAYLOR, *supra* note 9, at 16.

97. One academic listserv group's moderator, who normally does not filter out postings from subscribers, said he receives "many requests to post advertisements for new lists, new servers, new journals, old journals, dozens of conferences, and on and on. If I forward them all, you would want to unsubscribe." Posting of Samuel H. Williamson, Executive Director, The Cliometric Society, Miami University, SWILLIAM@sba-laws.sba.muohio.edu, to econhist@cs.muohio.edu (Nov. 30, 1994) (on file with Author and *FCLJ*).

98. Microsoft Outlook and many antivirus and firewall software packages now provide filters that attempt to remove UCE.

99. Chao, *supra* note 11. Of course, for large public Internet forums, it can be difficult to identify marketers or people who have engaged in inappropriate marketing in the past and should be excluded because of the anonymity of the Internet. It is usually quite easy to create a new identity in these forums without divulging personal information.

100. *Id.*

101. See Raj Mehta & Eugene Sivadas, *Direct Marketing on the Internet: An Empirical Assessment of Consumer Attitudes*, J. DIRECT MKTG., Summer 1995, at 21, 22; RESNICK & TAYLOR, *supra* note 9, at 152-55; MARY J. CRONIN, *DOING BUSINESS ON THE INTERNET: HOW THE ELECTRONIC HIGHWAY IS TRANSFORMING AMERICAN COMPANIES* (1994).

102. See Mehta & Sivadas, *supra* note 101, at 22-24.

103. For example, one entrepreneur tried to market beauty cream to a business librarian newsgroup on the Internet, and later apologized to the group for the intrusion when he

companies in particular very careful in how they market on the Internet, since they have more to lose from offending current customers than to gain by adding a few new ones.<sup>104</sup>

Many firms maintain their own in-house "do-not-contact" lists.<sup>105</sup> Some firms put check-off boxes on their mailings, order forms, and Web sites that allow their customers to indicate that they do not want any advertising from the firm, and that they do not want their name shared with others. Telemarketers are required by law to maintain lists of consumers who ask for no further calls from the telemarketer.<sup>106</sup> This solution, sometimes called an "opt-out option" or "negative option," allows consumers to designate more specifically the advertising they do not want, thus reducing the burden that WRM places on consumers.<sup>107</sup>

Industry "do-not-contact" lists, which allow consumers to opt out of receiving all advertising, are the solution offered by the DMA.<sup>108</sup> For example, there is a Mail Preference Service ("MPS"), which maintains a "do-not-write" list of people who have requested that they not receive any unsolicited direct mail.<sup>109</sup> All marketers are expected to refrain from sending direct mail to people on this list.<sup>110</sup> Similarly, the Telephone Preference Service ("TPS") and the E-mail Preference Service ("e-MPS") maintain "do-not-call" and "do-not-email" lists. The DMA requires that all members honor these lists.<sup>111</sup> This solution is particularly appropriate when consumers differ in their reaction to direct marketing, such that some have Marketing Aversion, while others want to receive some advertising.

Offering inducements or rewards to process messages, such as coupons, prizes or lottery drawings, is a method some firms use to effectively lower the consumer's cost of processing the message. It also increases the consumer's likelihood of not discarding the message when scanning it.

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received a flurry of angry messages instead of orders. MARY J. CRONIN, *DOING BUSINESS ON THE INTERNET: HOW THE ELECTRONIC HIGHWAY IS TRANSFORMING AMERICAN COMPANIES* 117 (1994).

104. See Mehta & Sivadas, *supra* note 101, at 24; Bowen, *supra* note 87. Unfortunately, there are small firms that care little about their reputation and are willing to offend many consumers in their hunt for a few buyers. Because of the very low cost of sending e-mail messages, even a small number of such firms can create a significant problem with spam.

105. Goodwin, *supra* note 41, at 104.

106. 47 U.S.C. § 207(c)(3) (2000).

107. See Jeff Sovern, *Opting In, Opting Out, or No Options at All: The Fight for Control of Personal Information*, 74 WASH. L. REV. 1033, 1069–82, 1092–94 (1999).

108. COMPLIANCE GUIDE, *supra* note 24, at 11.

109. *Id.*

110. *Id.*

111. *Id.*



Voluntary restraints may not be successful in media to which many firms have open access. Too many firms sending out poorly-targeted messages can lead to widespread Marketing Aversion and even to Medium Failure, in which consumers stop paying attention to the medium. In this case no single firm bears the full cost of sending out too many messages, thus leading to a free-rider problem where each firm has inadequate incentive to reduce its own message sending, despite the benefit if all do so. Consumer enforcement of rules may also be ineffective. For example, netiquette has often been enforced by users themselves, who have “flamed” or sent rude messages back at those who break the understood rules of the Internet.<sup>112</sup> Yet, some aggressive marketers are willing to brave this “flame war,” if it is profitable. According to one marketer, a typical mailing is sent out to about 250,000 addresses at a time and yields a 0.5% positive response rate, with flames trashed automatically.<sup>113</sup> Voluntary self-regulation will be effective only if four conditions hold: (1) the regulations are strong enough to solve the problem for consumers; (2) existing firms agree to the regulations; (3) entry into the industry is difficult for small unscrupulous firms that ignore the regulations; and (4) those abuses that do occur are not very costly to consumers.

*C. Solutions Imposed by a Government, Message Intermediary, or Controlling Organization*

In some media there is a controlling organization (that controls the content of the messages sent) or a message intermediary, (which carries messages but does not generally decide on content), which has an incentive to reduce WRM and avoid Medium Failure, especially if its income depends on consumers paying attention to the messages received, or if transmitting the messages is costly and unprofitable.<sup>114</sup> In other media government regulation may be the only way to reduce or eliminate WRM and avoid Medium Failure. In addition to making opt-out programs, (such as the FTC’s Do Not Call Registry), and labeling requirements mandatory, government, message intermediaries, and controlling organizations have other methods available for reducing the problem of WRM.

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112. See Milne & Gordon, *supra* note 45, at 209.

113. Bowen, *supra* note 87.

114. For example, television and radio stations are controlling organizations that limit the amount of advertising they broadcast in order to avoid driving viewers away. Too much advertising leads to the equivalent of Medium Failure in which consumers stop paying attention to the medium by changing the channel. ISPs attempt to eliminate spam, partly because of the cost of carrying it and also because of their customers’ dislike for it. Bowen, *supra* note 87.

Charging a fee or tax for sending messages is one method of reducing WRM. With higher message-sending costs, senders will have an incentive to use only lists with high response rates. Since senders already know the message, it might be socially desirable and economically efficient to make them determine for whom the message will be valuable.<sup>115</sup> The socially optimal fee was derived in Shiman, *When E-Mail Becomes Junk Mail*.<sup>116</sup> One variant of this solution that has recently gained popularity in the scholarly press would require senders of unsolicited advertising to offer to pay receivers to receive messages, at a price to be set by the receiver.<sup>117</sup> It has been argued that this will achieve the optimal level of message sending and eliminate the negative externality that unsolicited messages impose on receivers.<sup>118</sup>

To reduce the intrusiveness and receiving cost of some messages, limitations are often placed on how and when messages are sent. Restrictions have been placed on telemarketers to prohibit calling late at

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115. Similarly, low-quality messages can often be discouraged by charging a fee, as some refereed journals do for submitted papers and college admissions offices do for applications.

116. Shiman, *supra* note 51, at 39.

117. See, e.g., BILL GATES ET AL., *THE ROAD AHEAD* 173–74 (1995); Ayres & Funk, *supra* note 47, at 80–81.

118. See, e.g., Ayres & Funk, *supra* note 47, at 80–81; Loder, Van Alstyne & Wash, *supra* note 47, 6–8. Since senders have to pay for the processing costs they impose on receivers, this proposal effectively internalizes the externality, and the higher sending costs induce senders to better target their messages to consumers who are likely to purchase the good. However, a potential problem with this proposal that is not addressed by advocates is that many receivers may attempt to game this system in order to maximize the revenue gained from senders. Receivers interested in increasing their income may want to misrepresent their likelihood of purchasing to try to increase the messages they get paid for receiving. Thus, many consumers will want to provide false information about their characteristics to surveys and questionnaires to make themselves look likely to purchase expensive goods. For example, a low-income respondent could describe herself as a wealthy boat owner in order to attract and be paid for receiving direct marketing messages attempting to sell boats or accessories. This could cause significant problems for poll-takers, market researchers, and the Census, for whom it is essential that respondents have no financial interest in providing untruthful answers. Note that proposals that require consumers to read the messages before being paid could be foiled by software that pretends to read the message. For an example of proposals that require consumers to read messages before being paid, see GATES ET AL., *supra* note 117, at 173–74. Alternative schemes of charging senders can be devised that avoid this incentive for misrepresentation, but they would not likely achieve the optimal level of message sending. For example, consumers could be allowed to set their price for receiving a message, but would only be compensated if they purchase the good. They would not then want to attract messages for goods they would not buy, and the higher price set by some receivers would discourage senders from sending messages to them. Alternatively, the senders' payments could go to another entity (e.g., the carrier providing the communications service) rather than the receiver. The higher sending costs would induce senders to better target their messages, and receivers would not have an incentive to attract messages for goods they are unlikely to buy.

night, to prevent the tying up of emergency police and ambulance lines, and to stop telemarketing equipment holding on to the line after the recipient has hung up.<sup>119</sup>

Government or a message intermediary may decide to implement a total ban on unsolicited advertising, such as was imposed by the government on unsolicited fax advertising.<sup>120</sup> Such a policy would be desirable if there is Negative Welfare from Marketing. For example, in Table 1 a ban on all advertising would be beneficial to society in Medium 4. A policy banning the sending of advertising unless consumers grant permission is sometimes called “opt-in.” The Internet has had a culturally-understood ban on bulk mailings of UCE, with ISPs attempting to enforce the ban through “acceptable use” policies that users are required to abide by.<sup>121</sup> Once detected, bulk e-mailers usually have had their access to the Internet revoked by their ISP; however, they have been able to regain access through ISPs that are less vigilant or more cooperative, or by use of subterfuge.<sup>122</sup> Unregulated media suffering from WRM, Marketing Aversion, or Medium Failure might, however, evolve into controlled media, which are controlled by a single organization and are often able to deal more effectively with the problems caused by unsolicited advertising (and the related problem of the broadcast of low-quality noncommercial messages). For example, moderated forums and newsgroups have often replaced open forums on the Internet.<sup>123</sup>

## VII. CONCLUDING REMARKS

Policymakers should be concerned about the economic inefficiencies and harms to privacy potentially caused by some forms of direct marketing. But before making a decision as to whether and how direct marketing should be regulated, policymakers should carefully assess the characteristics of a medium, employing economic analysis such as was used in the framework presented in this Article. This is in addition to a careful examination of the legal and ethical considerations involved, such as firms’ right to free speech and individuals’ right to privacy. Policymakers should keep in mind five important points while performing

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119. 47 U.S.C. § 227(b).

120. *Id.*

121. Bowen, *supra* note 87.

122. See Zeller, *supra* note 8. See Raymond B. Everett, Guerilla Warfare: A System Administrator’s Perspective on Unsolicited Commercial E-Mail, testimony submitted to the FTC Workshop on Unsolicited Commercial E-Mail (1997), <http://www.ftc.gov/bcp/privacy/wkshp97/comments2/reverett.htm> (stating that ISPs have very little incentive in the marketplace to invest in technology that would prevent spammers from sending unsolicited commercial e-mails via their ISPs).

123. Chao, *supra* note 11.

this analysis: (1) microeconomic social welfare analysis provides a useful framework for assessing the volume problem; (2) sending as well as receiving costs in a particular medium should be considered, since the former determines the degree of targeting; (3) in some media, consumers will differ in their valuation of receiving direct marketing, and the solution chosen should be sensitive to these differences; (4) the existence of alternative media will affect the value of unsolicited advertising on a particular medium to consumers and society; and (5) organizational, economic, and technological developments may reduce or increase the need for regulation of direct marketing.

When WRM is present, consumers and message intermediaries may need help in managing the flow of advertising received. The most desirable solution for consumers would be to make it easier for them to process messages. This would lower receiving costs, and would allow consumers to process more information about products available and thus make better purchasing decisions. This can sometimes be achieved with relatively unobtrusive regulations, such as requiring marketers to label the sources and purposes of messages and banning deceptive practices. These measures would also help consumers to prioritize processing of their messages.

Opt-out and opt-in programs give control to consumers of whether advertising messages are sent to them. These methods are crude in the sense that consumers cannot determine whether individual offers are worth examining, but can be useful for many consumers when Marketing Aversion is widespread. Opt-out programs, whether company-specific or medium-wide, allow consumers to determine when a particular source of advertising is yielding positive utility, although the burden is on consumers to find out about the programs and sign up for them. They may also benefit marketers by giving low-interest consumers, who are unlikely purchasers, the ability to remove themselves from the mailing lists. These programs are more effective when they are well publicized and all direct marketing firms have to honor them, such as with the FTC's Do Not Call registry.

Many solutions can be implemented by industry, and thus government intervention is not needed in all media with WRM. However, voluntary restraints do not always work.<sup>124</sup> Whether industry can develop effective regulations for itself is unclear since some firms will ignore

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124. For example, the DMA's attempt to reduce the public's concerns about spam by requiring marketers to obey the e-mail preference service, and include a valid means of opting out on their solicitations, has generally been unsuccessful. See COMPLIANCE GUIDE, *supra* note 24, at 14 (stating that if a member of the DMA fails to adhere to the Privacy Promise, the DMA can take action against the company, which at most includes being expelled from the DMA).

voluntary guidelines. As one observer pointed out, “bad guys don’t self-regulate.”<sup>125</sup>

It is possible that media with open access to marketers and widespread Marketing Aversion will be supplanted by controlled media, with one organization controlling or monitoring content, if that organization proves able to deal effectively with unsolicited advertising. A competitive market for media could develop, with open and controlled media competing for consumers’ attention. In addition, new technologies may develop to help consumers handle unsolicited advertising, (as answering machines and Caller ID have done, and filtering software may do).

The development of new electronic media poses a major challenge to policymakers who desire to protect these new forms of communication for the benefit of consumers. The significantly lower sending costs of some media, such as e-mail and instant messaging, and the higher receiving costs of communications using mobile devices, increases the potential burden on consumers, and welfare lost to society, caused by direct marketing. It should be kept in mind that if the sending costs are low enough, the resulting flood of poorly-targeted marketing means that virtually all recipients will place a negative value on receiving direct marketing. Medium Failure is possible if users become deluged with direct marketing and abandon the medium. Thus, if other solutions turn out to be ineffective, a complete ban on direct marketing may be needed (if it is even feasible to implement) to maintain the viability of the medium. While it is possible that technology will reduce or eliminate the problem, the outlook is not hopeful for e-mail and similar forms of electronic messaging. The cost of sending messages is too low, entry is too easy and anonymous for small firms, regulations on content and labeling are impossible to perfectly enforce on the Internet, and spammers will likely always find a way to get around anti-spam filters by making their messages look legitimate.<sup>126</sup> Already spam has been found by one study to have cost the United States \$17 billion in 2003 from lost productivity.<sup>127</sup>

Further research is needed to determine the existence and extent of WRM and Marketing Aversion in various media, how well various solutions ameliorate the negative externalities generated by direct marketing, and the heterogeneity of consumer responses to direct

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125. Dentino, *supra* note 48, at 40.

126. The Internet has two key characteristics that make controlling WRM particularly difficult: (1) the marginal cost of sending messages is essentially zero, so bulk e-mailings can be profitable; and (2) senders can connect easily and anonymously so that identifying them in order to block access or prosecute them can be extremely difficult.

127. Zeller, *supra* note 8.

marketing in each medium. While it may prove impossible to precisely quantify the costs involved, particularly receiving costs, a general assessment should be possible through the use of public opinion surveys, rough estimations of costs involved, and analysis of the technologies available.

**TABLE 1**

Payoffs Per Message to Firms, Consumers, and Society for Direct Marketing As  
Sending Costs Fall

	Lists of Consumers and Their Associated Response Rate			Average <sup>a</sup> (per consumer contacted)
	H (= 25%)	M (= 5%)	L (= 1%)	
Medium 1, s=\$2, r=\$0.25:				
Firm profit ( $\pi$ )	0.50 *	-1.5	-1.9	0.5
Consumer benefit (CS)	0.35 *	-0.15	-0.23	0.25
Social welfare (SW)	1.35 *	-1.65	-2.13	0.75
Medium 2, s=\$0.4, r=\$0.25:				
Firm profit ( $\pi$ )	2.10 *	0.10 **	-0.3	1.1
Consumer benefit (CS)	0.25 *	-0.15 **	-0.23	0.05
Social welfare (SW)	2.35 *	-0.05 **	-0.53	1.15
Medium 3, s=\$0.01, r=\$0.25:				
Firm profit ( $\pi$ )	2.49 *	0.49 *	0.09 **	1.02
Consumer benefit (CS)	0.25 *	-0.15 *	-0.23 **	-0.04
Social welfare (SW)	2.74 *	0.34 *	-0.14 **	0.98
Medium 4, s=\$2, r=\$2:				
Firm profit ( $\pi$ )	0.50 **	-1.5	-1.9	0.5
Consumer benefit (CS)	-1.50 **	-1.9	-1.98	-1.5
Social welfare (SW)	-1.00 **	-3.4	-3.88	-1

\* Lists that receive a marketing message because they are profitable for marketers ( $\pi > 0$ )

\*\* Lists that receive welfare-reducing marketing (WRM) messages, for which  $SW < 0$ .

<sup>a</sup> Assumes consumers are evenly divided among all three lists. The numbers are calculated only for those lists contacted and are averages per message.

**TABLE 2**

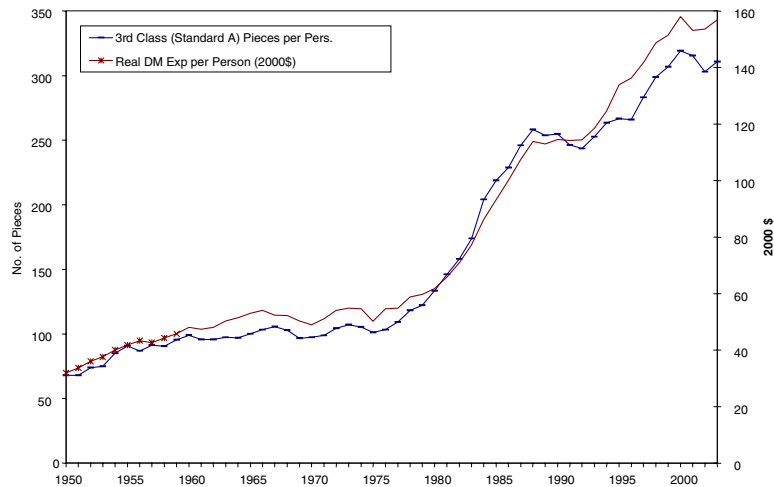
Types of Solutions to the Problem of Welfare-Reducing Marketing

	<b>Brief Name</b>	<b>Description</b>
1	Scanning	Receiver quickly determines source or content of message (made easier if message is properly labeled)
2	Screening & Filtering	Messages screened by another person (receptionist or moderator) or automatically (filtering software)
3	Limited Access	Access to the medium, group, or receiver is restricted to approved senders only
4	Company-specific opt-out=Firm Do-not-contact list	Receiver can put name on list requesting no advertising from a specific firm
5	Medium opt-out=Industry Do-not-contact-list	Receiver can put name on list requesting no advertising messages on that medium
6	Rewards	Sender offers inducement for a receiver to process message
7	Fee	Sender charged for sending message
8	Restrictions on sending	Restrictions imposed on how and when messages are sent
9	Total ban or opt-in only	No advertising messages permitted, or allowed only with express permission of receiver



FIGURE 1

Third Class Pieces of Mail Received per Person, and Inflation-Adjusted Direct Mail Expenditures per Person, 1950–2004

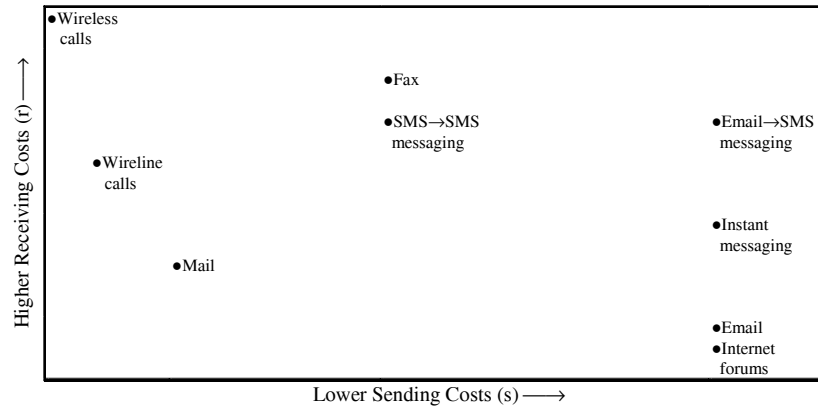


Third class pieces per person are actual number of pieces received per year. Real direct mail expenditures per person are in thousands of (base year 2000) dollars per person, adjusted for inflation.

Sources: Total Population for per person calculation is derived from the U.S. COUNCIL OF ECONOMIC ADVISORS, ECONOMIC REPORT OF THE PRESIDENT tbl. B-34 (2004), available at <http://www.gpoaccess.gov/usbudget/fy05/sheets/b34.xls>. (1) Third Class (Standard mail) Pieces per Person: BUREAU OF THE CENSUS, U.S. DEPARTMENT DEPT. OF COMMERCE, HISTORICAL STATISTICS OF THE UNITED STATES: COLONIAL TIMES TO 1970 (1975), at 806; U.S. POSTAL SERV., ANNUAL REPORT OF THE POSTMASTER GENERAL (various years) (on file with the Author); Bureau of the Census, U.S. Dept. of Commerce, Statistical Abstract of the United States (various years). Third Class is now called Standard mail. Standard mail is a discounted rate reserved for bulk (large volume) advertising mail. The USPS reported that in 2003 about 76% of advertising mail was Standard (third class) mail. HOUSEHOLD DIARY STUDY 2004, *supra* note 4. (2) Real Direct Mail Expenditures per Person, deflated using the GDP price index: Coen U.S. Advertising report, *supra* note 5; ECONOMIC REPORT OF THE PRESIDENT, *supra* note 5. The Direct Mail Expenditures were divided by the U.S. population estimates and by the GDP implicit price deflator (with the year 2000 set to 1).

FIGURE 2

## Key Characteristics of Various Communications Media



Placement on both axes is estimated. Placement on horizontal axis according to 1/s.

*Sources:* For receiving costs, rough estimates of relative values by medium have been used, according to various factors, such as time it takes to process, flexibility in when to process, ability to scan and identify the message's sender and subject, and can vary by individual. For further discussion on receiving costs, see Part III, *supra*, text for discussion. The sending costs include both the cost of acquiring lists of consumers' addresses and telephone numbers, and the cost of creating and sending the message. Notes on how sending costs  $s$  and some receiving costs  $r$  were determined:

(1) Mail:

$s$ : Approximate cost of \$0.35–\$0.40 per piece of doing a direct mailing of an advertisement for one product, assuming typical format. DIRECT MKTG ASS'N, STATISTICAL FACT BOOK 1995, at 262.

(2) Wireline and Wireless calls (telemarketing):

$s$ : Range of \$1–4 for outbound mail sent to consumers cost per decision-maker contact given in Stone, *supra* note 58, at 338. See also DIRECT MKTG ASS'N, STATISTICAL FACT BOOK 1995, at 144 (showing cost of \$4–5 per call on its sample outbound telemarketing cost worksheet). Wireless telemarketing would likely be more costly because of the greater difficulty in obtaining wireless phone numbers.

(3) Fax:

$s$ : Cost of approximately \$0.02–\$0.04 per page for a high volume broadcast fax campaign. Faxts Telysis, Inc., <http://www.faxbroadcasters.com> (last visited Mar. 30, 2006); NBS, <http://www.narabroadcastingservices.com/Rates%5BNBS%5D.htm> (last visited Mar. 30, 2006)

$r$ : Will likely include \$0.02–\$0.08 per page for cost of printing the fax on a laser or inkjet printer. See CONSUMERS UNION, CONSUMER REPORTS BUYING GUIDE 137 (2006).

(4) E-mail:

$s$ : Some advertised rates are \$100 for list of three million addresses and \$400 for a complete e-mail campaign to two million addresses. Americaint, Email Marketing Campaigns, <http://www.americaint.com/email-marketing-campaigns/email-marketing-services.html> (last visited Mar. 28, 2006); Americaint, Email Lists, <http://www.americaint.com/bulk-email-lists/buy-email-lists.html> (last visited Mar. 28, 2006).

$r$ : Includes cost of transmitting, storing, and downloading for consumer and ISPs.

(5) Internet Forums, including Usenet Groups and Listservers:

$s$ : Very low cost of writing and posting to a group with many readers.

(6) SMS text messaging for messages sent to wireless phones:

$s$ : The cost of sending one SMS message (SMS→SMS) to an SMS receiver (i.e., SMS to SMS) is approximately \$0.05–\$0.10, based on wireless phone plans; however, monthly plans with bundles of SMS messages included are available, which would lower the average cost to \$0.01 per message. Short Message Service, WIKIPEDIA, [http://en.wikipedia.org/wiki/Short\\_message\\_service](http://en.wikipedia.org/wiki/Short_message_service) (last visited Mar. 28, 2006). The cost of sending Internet e-mail to SMS Messaging users (i.e., e-mail to→SMS) is the same as e-mail.

*r*: Wireless plans usually charge \$0.02–\$0.10 to receive each message. Lisa W. Foderaro, *Young Cell Users Rack Up Debt, a Message at a Time*, N.Y. TIMES, Jan. 9, 2005, available at <http://www.nytimes.com/2005/01/09/technology/09message.html?ei=5088&en=3c2813c28094e8b0&ex=1262926800&partner=rssnyt&pagewanted=all&position> (last visited Mar. 28, 2006).



# Rethinking Regulation of Advertising Aimed at Children

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# I. INTRODUCTION: A BRIEF HISTORY OF THE REGULATION OF ADVERTISING AIMED AT CHILDREN

In the 1970s, both the Federal Communications Commission ("FCC")<sup>1</sup> and the Federal Trade Commission ("FTC")<sup>2</sup> completed extensive examinations of advertising directed at children. The FCC issued a policy statement asking networks to voluntarily limit the amount of commercial time aired during programs directed at children.<sup>3</sup> The FTC compiled a staff report stating that it was fundamentally unfair for advertisers to direct commercials at children and issued a *Notice of Proposed Rulemaking* in 1978 that proposed major regulation of advertisements aired during children's television.<sup>4</sup> The FTC received harsh

1. Children's Television Report and Policy Statement, *Decision and Report*, 50 F.C.C.2d 1 (1974) [hereinafter *Children's Television Report*].

2. See J. Howard Beales III, Remarks at the George Mason Law Review 2004 Symposium on Antitrust and Consumer Protection: Competition, Advertising, and Health Claims: Legal and Practical Limits on Advertising Regulation 6–8 (Mar. 2, 2004), <http://www.ftc.gov/speeches/beales/040312childads.pdf>.

3. Children's Television Report, *supra* note 1, paras. 40–45.

4. The staff proposed either: (1) a complete ban on advertising directed at children eight and under; (2) a ban of all ads for foods linked to poor dental health directed at children twelve and under; or (3) a requirement that ads for foods linked to poor dental health contain disclosures of the health effects of the foods. Children's Advertising,

political and public response to this proposed rulemaking. The Washington Post called the proposal “a preposterous intervention that would turn the FTC into a great national nanny.”<sup>5</sup> Congress responded to the FTC’s proposal not only by passing legislation limiting the FTC’s power to enforce any rule relating to children’s advertising, but also by failing to renew the FTC’s funding, in effect shutting down the agency temporarily.<sup>6</sup> After the FTC’s unsuccessful attempt to regulate advertising aimed at children, there was not much governmental involvement in the area until 1990, when Congress passed the Children’s Television Act (“CTA”),<sup>7</sup> which instructed the FCC to enforce certain requirements for television broadcasters. At this time, the FCC was still opposed to government involvement in this area and preferred to let the market regulate itself.<sup>8</sup>

The two main requirements of the CTA are: (1) the FCC must establish standards for broadcasters regarding the amount of children’s television programming aired;<sup>9</sup> and (2) broadcasters must limit the amount of commercial time aired during children’s television programs to 10.5 minutes per hour or less on weekends and 12 minutes per hour or less on weekdays.<sup>10</sup> This commercial limit applies to over-the-air commercial television broadcasters, as well as cable<sup>11</sup> and digital television suppliers.<sup>12</sup> The FCC adopted its rules to enforce the CTA in 1991<sup>13</sup> and revised these rules in 1996.<sup>14</sup> Neither of these actions affected the substantive nature of the commercial limits, and dealt mainly with methods of enforcing the rules.

While some members of Congress objected to the government

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*Proposed Trade Regulation Rulemaking*, 43 Fed. Reg. 17967, 17969 (Apr. 25, 1978); Beales, *supra* note 2, at 7.

5. Editorial, *The FTC as National Nanny*, WASH. POST, Mar. 1, 1978, at A22.

6. See Beales, *supra* note 2, at 10.

7. Children’s Television Act of 1990, Pub. L. No. 101-437, 104 Stat. 996 (1990) (codified at scattered sections of 47 U.S.C.).

8. H.R. REP. NO. 101-385, at 4 (1991).

9. The FCC requires broadcasters to air three hours of “core” children’s programming per week. Policies and Rules Concerning Children’s Television Programming, *Report and Order*, 11 F.C.C.R. 10660, para. 4 (1996) [hereinafter *Policies Concerning Programming*].

10. 47 U.S.C. § 303a(b).

11. FCC Consumer Facts, <http://www.fcc.gov/cgb/consumerfacts/childtv.html> (last visited Mar. 12, 2006).

12. Children’s Television Obligations of Digital Television Broadcasters, *Notice of Proposed Rule Making*, 15 F.C.C.R. 22946, para. 12 (2000), [http://hraunfoss.fcc.gov/edocs\\_public/attachmatch/FCC-00-344A1.pdf](http://hraunfoss.fcc.gov/edocs_public/attachmatch/FCC-00-344A1.pdf).

13. Policies and Rules Concerning Children’s Television Programming, *Memorandum Opinion and Order*, 6 F.C.C.R. 5093 (1991) [hereinafter *Children’s Memo*].

14. *Policies Concerning Programming*, *supra* note 9, para. 1.

imposing these commercial limitations,<sup>15</sup> these limitations are much less stringent than those in place in other countries that have used legislation to address advertising to children. Sweden has banned all advertising aimed at children twelve and under.<sup>16</sup> Norway and Finland have banned companies from sponsoring children's television shows.<sup>17</sup> Belgium has banned commercials from appearing five minutes before, during, and five minutes after children's programs.<sup>18</sup> Strict regulations appear to be forthcoming in England, where one of its major broadcasters, the British Broadcasting Corporation, has banned the use of cartoon characters in fast food ads.<sup>19</sup>

This Note does not address the overall effectiveness of the CTA and the FCC regulations made pursuant to the CTA, or the validity of the underlying premise that children benefit from the availability of a large amount of television programming aimed at them,<sup>20</sup> and will only discuss the effectiveness of the CTA's commercial limits. This Note will examine the potential harms of advertising to children and will analyze the effectiveness of the CTA under the Supreme Court's test for determining the constitutionality of restrictions on commercial speech.<sup>21</sup> This Note will conclude that the commercial limitation of the CTA is probably constitutional. However, an analysis of the CTA under the Court's test will find that the CTA is not as effective as other regulations that could be adopted. Finally, this Note will suggest alternative regulations of commercials that would more effectively deal with the harms caused by advertising to children.

## II. THE SCOPE OF THE CTA AND THE GOVERNMENT'S GENERAL PURPOSE IN PRESCRIBING COMMERCIAL LIMITS FOR CHILDREN'S TELEVISION PROGRAMS

Although the FCC and Congress's purpose for the three-hour mandate was to increase the amount of beneficial television available to children,<sup>22</sup> the increased amount of television aimed at children correspondingly

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15. See H. R. REP. NO. 101-385, at 22.

16. THE KAISER FAMILY FOUND., THE ROLE OF MEDIA IN CHILDHOOD OBESITY 8 (2004), <http://www.kff.org/entmedia/upload/The-Role-Of-Media-in-Childhood-Obesity.pdf> [hereinafter KAISER REPORT].

17. *Id.*

18. *Id.*

19. *Id.*

20. For a discussion of the negative effects of children viewing large amounts of television see *id.* at 9 (indicating that the Surgeon General and the American Academy of Pediatrics recommend limits on the amount of television that children watch).

21. See *Cent. Hudson Gas & Elec. Corp. v. Pub. Serv. Comm'n*, 447 U.S. 557 (1980).

22. See S. REP. NO. 101-66, at 1 (1991).



increases the amount of advertising aimed at children.<sup>23</sup> This increased exposure includes not only direct advertisements, but also instances in which companies use popular TV characters to promote their products.<sup>24</sup> In all, the average child sees 40,000 television ads per year.<sup>25</sup> Also, over half of American children have television sets in their rooms, indicating that many children are watching a significant amount of television without direct parental supervision.<sup>26</sup>

In addition to the evidence that children view large amounts of commercial material, considerable evidence indicates that children have difficulty distinguishing a commercial from the program that they are watching.<sup>27</sup> Congress recognized that children who cannot distinguish between commercials and programs will be harmed by excessive exposure to commercials; children who do not know they are watching a commercial “certainly cannot be expected to react aversively to an excessive amount of advertising by changing the channel or turning off the television.”<sup>28</sup> A 2004 study by the American Psychological Association (“APA”) supports this congressional finding. The study found an inverse relationship between children who understand the nature of commercials and children who trust all commercials and want to acquire all the products they see advertised on television.<sup>29</sup>

While the overall goal of the CTA is to improve television for children sixteen and under, the commercial limitation aims to protect only younger children, whom Congress thought were being adversely affected by commercials.<sup>30</sup> Thus, the definition of “child” for the purpose of commercial limits differs from the definition in other areas of FCC regulation. For the purposes of other FCC regulations, “children” are considered sixteen and under, but for the purposes of identifying shows that

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23. See DALE KUNKEL ET AL., AM. PSYCH. ASS'N, REPORT OF THE APA TASK FORCE ON ADVERTISING AND CHILDREN: SECTION: PSYCHOLOGICAL ISSUES IN THE INCREASING COMMERCIALIZATION OF CHILDHOOD 2-3 (2004), available at <http://www.apa.org/releases/childrenads.pdf> [hereinafter APA TASK FORCE].

24. *Id.*

25. *Id.* at 1-2.

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

27. See, e.g., Policies and Rules Concerning Children's Television Programming, *Report and Order*, 6 F.C.C.R. 2111, para. 3 n.13 (1991) [hereinafter *Children's Programming Report*]; APA TASK FORCE, *supra* note 23, at 5-8 (finding that children below ages four and five cannot distinguish between programs and commercials and that children up to ages seven and eight do not recognize that the purpose of commercials is to convince viewers to buy the product).

28. H. R. REP. NO. 101-385, at 6.

29. APA TASK FORCE, *supra* note 23, at 17.

30. *Children's Programming Report*, *supra* note 27, para. 15.

face commercial limitations, “children” are considered twelve and under.<sup>31</sup>

For air time to be classified as “commercial” the broadcaster must have received consideration from the company that is advertising a product or service, and the announcement must have a promotional purpose.<sup>32</sup> Thus, public service messages sponsored by nonprofit organizations, promotions for other television programs, or educational or “spot” announcements that are introduced by the speaker saying “sponsored by [a company]” are not considered commercial material for the purposes of the limitation.<sup>33</sup> In fact, the FCC seeks to encourage such announcements.<sup>34</sup>

Particularly worrisome to the FCC and Congress are “program-length commercials,” programs in which a commercial for a product associated with the program airs during the program or within 60 seconds of its beginning or end.<sup>35</sup> If a broadcaster airs such a commercial during a program or within the 60-second window, the entire program will be considered commercial material.<sup>36</sup> For example, if a commercial for Burger King that featured characters from the cartoon “SpongeBob SquarePants” aired during or within 60 seconds of a “SpongeBob SquarePants” episode, the entire 30-minute program would count as a commercial. The FCC rejected the Action for Children’s Television (“ACT”) request to expand the scope beyond the 60-second window and found that “the short attention spans of children, particularly younger children most likely to confuse program and commercial material,” justified permitting commercials for products associated with television shows to be aired outside of the 60-second window.<sup>37</sup>

The FCC indicated that when enforcing the CTA it would consider single and accidental violations of the act de minimis, but would assess penalties for “willful or repeated” violations.<sup>38</sup> The result of this policy is that neither the broadcaster’s intent nor its overall compliance with the CTA is the FCC’s primary concern. For example, an FCC investigation revealed that Oceanic-Time Warner Cable of Hawaii had aired thirty-one half hour programs during which commercials for products associated with the program also aired, but that all the violations were inadvertent.<sup>39</sup> The

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31. *Id.*

32. *Children’s Memo*, *supra* note 13, para. 11 (1991).

33. *Id.* para 9.

34. *Children’s Programming Report*, *supra* note 27, para. 7 (1991).

35. *Id.* paras. 44–45.

36. *Id.* para. 46.

37. *Id.* para. 45.

38. *Id.* para. 39 (citation omitted).

39. The commercials were aired due to flawed computer design and human error. Int’l Family Entm’t Inc., *Order*, 19 F.C.C.R. 20789, para. 4 (2004), *available at*

FCC also found that Oceanic had not benefited financially by airing these commercials during the programs.<sup>40</sup> Still, the FCC required that International Family Entertainment, who had provided Oceanic with the programming, make a “voluntary contribution” of \$500,000 for the thirty-one inadvertent violations.<sup>41</sup> In another proceeding, although Viacom, over its Nickelodeon channel, aired less than the maximum time of commercial material 85% of the time, and although its violations of the CTA were unintentional and due to “flawed internal procedures and human error,”<sup>42</sup> the FCC still entered into a consent decree that required Viacom to not only fix the problems that resulted in violations, but also make a “voluntary contribution” to the U.S. Treasury of one million dollars.<sup>43</sup>

### III. THE HARMS CAUSED BY ADVERTISING TO CHILDREN AND THE NEED FOR FURTHER GOVERNMENTAL REGULATION

While the government states its purposes for protecting children in general terms—children are easily influenced and cannot tell advertising from regular programming—there are some specific and real harms that advertising can inflict upon children. Two of these harms, increased materialism and reinforcement of racial stereotypes, probably are not so substantial as to warrant governmental intervention. However, a growing amount of evidence indicates that advertising directed at children is a direct cause of obesity and health problems in children, making the issue of advertising directed at children a problem that the government should address with regulation.

While children may already want many of the products advertised to them, children who view commercials for such products exhibit a “statistically significant [increase in their] desire for the advertised merchandise.”<sup>44</sup> Also, when considering the effect of advertising on children, one must consider both the immediate effect of making children want the advertised product and the cumulative effect of children developing general habits.<sup>45</sup> That is, not only do toy and junk food commercials influence children to want those items featured in the commercials, they also influence children to want more toys and junk food in general.

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[http://hraunfoss.fcc.gov/edocs\\_public/attachmatch/DA-04-3259A1.pdf](http://hraunfoss.fcc.gov/edocs_public/attachmatch/DA-04-3259A1.pdf).

40. *Id.*

41. *Id.* para. 12.

42. Viacom Int’l Inc., *Order*, 19 F.C.C.R. 20802, para. 4 (2004), available at [http://hraunfoss.fcc.gov/edocs\\_public/attachmatch/DA-04-3260A1.pdf](http://hraunfoss.fcc.gov/edocs_public/attachmatch/DA-04-3260A1.pdf).

43. *Id.* para. 12.

44. APA TASK FORCE, *supra* note 23, at 10.

45. *Id.* at 9.

### A. *Advertising's Effect on Children's Health*

The majority of advertisements directed at children are for food products, and most of these foods are unhealthful.<sup>46</sup> The number of ads directed at children has steadily increased over the last twenty years, and has roughly doubled since the 1970s.<sup>47</sup> The number of ads aired for foods such as frozen dinners, which are typically high in fat and sodium, has more than doubled in the last twenty years.<sup>48</sup> During this same period, the rate of obesity in children has more than tripled, rising from roughly 4% to roughly 15%.<sup>49</sup> Studies have found a relationship between this increase in ads for unhealthful foods and obesity in children.<sup>50</sup> Also, it appears that ads for food may have an even greater effect on children who are already overweight.<sup>51</sup> Thus, exposure to advertisements for unhealthful foods may lead otherwise healthy children to develop unhealthful eating habits and become overweight and already overweight children to further exacerbate their weight problem.

Not only are there far more ads for unhealthful foods than for healthful foods, but also the influence of ads for unhealthful foods seems to be stronger than the influence of ads for healthful foods.<sup>52</sup> These numerous food advertisements influence children to prefer particular candies, sodas, or fast food restaurants and to generally prefer candy, soda, and fast food over more healthful foods.<sup>53</sup>

Studies have found that commercials not only influence children to eat more of the foods that they do not need, but also cause them to eat less of the foods that they do need. A study that showed one group of children ads for fruit and fruit juice and another group of children ads for candy and

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46. KAISER REPORT, *supra* note 16, at 5.

47. *See id.* at 4.

48. *Id.* at 5.

49. *Id.* at 1.

50. APA TASK FORCE, *supra* note 23, at 12 (citing W. Dietz, *You Are What You Eat—What You Eat Is What You Are*, 11 J. ADOLESCENT HEALTH CARE 76 (1990); K.B. Horgan, et al., *Television Food Advertising: Targeting Children in a Toxic Environment*, in THE HANDBOOK OF CHILDREN AND MEDIA 447–62 (D.G. Singer & J.L. Singer eds., 2001); R.P. Toriano & K.M. Flegal, *Overweight Children and Adolescents: Description, Epidemiology and Demographics*, PEDIATRICS, 101, 497 (1998)).

51. *See* Jason C.G. Halford et al., *Effect of television advertisements for foods on food consumption in children*, 42 APPETITE 221, 224 (2004) (finding that obese children remembered commercials for foods more frequently than other children and that “exposure to the TV food ads exaggerated already distinctive patterns of food choice.”).

52. APA TASK FORCE, *supra* note 23, at 12 (citations omitted).

53. *See* Gerard Hastings, Martine Stead & Laura McDermott, *How Food Promotion Influences Children*, EDUC. J., July 2004, at 14; Danny Kucharsky, *Targeting Kids*, MARKETING MAG., July 12, 2005, at 6 (citing a study that found a correlation between the amounts of sugary cereals consumed and viewing of commercials for these cereals).

Kool-Aid found a significant correlation between the ads the children watched and their food and drink choices.<sup>54</sup> Another study indicated that viewing ads for unhealthful foods may lead children to eat fewer fruits and vegetables.<sup>55</sup>

The increase of obesity in children is a serious concern and should not be ignored by the government. Obesity causes health problems for children, and 80% of overweight children become overweight adults.<sup>56</sup> Currently, two-thirds of U.S. adults and nine million children in the United States are either overweight or obese.<sup>57</sup> Obesity is much more than a cosmetic problem. The health effects of obesity may be more severe than those of cigarette smoking.<sup>58</sup> Indeed, bad eating and exercise habits caused 400,000 deaths in the United States in 2000.<sup>59</sup> In addition to the deaths caused by obesity, obesity costs the American health care system seventy billion dollars per year.<sup>60</sup> The American Academy of Pediatrics states that the price of childhood obesity is “staggering.”<sup>61</sup>

### *B. Advertising's Effect on Children's Materialistic Nature*

While the health effects of advertising to children are apparent and serious, commercials aimed at children also influence children to be more materialistic. The APA found a correlation between the amount of television a child watches and the child's number of requests for products.<sup>62</sup> A study that compared children in Sweden, where advertising directed at children is illegal, to children in Great Britain, found that children in Great Britain requested more products than children in Sweden.<sup>63</sup> In addition to this increased materialism, the APA also found a

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54. APA TASK FORCE, *supra* note 23, at 12.

55. See KAISER REPORT, *supra* note 16, at 5.

56. *Id.* at 1.

57. Bruce Nixon, *Advertising and Marketing to Children: Everybody's Business*, INT'L J. OF ADVER. & MKTG TO CHILDREN, Apr.–June 2004, at 19–20.

58. KAISER REPORT, *supra* note 16, at 1 (referring to a report from the Surgeon General).

59. Nixon, *supra* note 57, at 20.

60. Dan Glickman, Agric. Sec'y, USDA, Remarks at USDA Symposium on Childhood Obesity: Causes and Prevention 62, 63 (Oct. 27, 1998), <http://www.usda.gov/cnpp/Seminars/obesity.PDF>.

61. The American Academy of Pediatrics Committee on Nutrition, *Policy Statement: Prevention of Pediatric Overweight and Obesity*, 112 PEDIATRICS 424, 425 (2003).

62. APA TASK FORCE, *supra* note 23, at 11; see also Karen J. Pine & Avril Nash, *Dear Santa: The effects of television advertising on young children*, 26 INT'L J. BEHAV. DEV. 529, 539 (2002) (“[Research] finds that increasing amounts of commercial television watched are matched by an increase in the overall amount of toys requested by children, and an increase in the number of branded products requested.”).

63. Pine & Nash, *supra* note 62, at 536.

correlation between the amount of television advertising observed and children's "acceptance of materialism."<sup>64</sup> Thus, exposure to advertisement influences not only children's behavior, but also their value system.

A problem related to the materialistic values adopted by children arises when parents deny these children's requests for products. Children generally become angry or upset with their parents when parents deny a request for a product that the child saw advertised on television.<sup>65</sup> The APA found that "the frequent purchase requests associated with children's advertising exposure may place strain on parent-child interaction."<sup>66</sup>

### C. Advertising's Role in Re-Enforcing Racial Stereotypes

While the advertising industry has made significant improvements in racial hiring practices over the last thirty years, advertisements aimed at children also can encourage racist tendencies or reinforce existing stereotypes. The "cultivation theory" indicates that "if children are repeatedly exposed to certain portrayals of an ethnic group, they may develop corresponding beliefs about the group."<sup>67</sup> The Children's Advertising Review Unit ("CARU")<sup>68</sup> recognized the power of advertisements to reinforce stereotypes and set guidelines indicating that advertisers should "incorporate minority and other groups in advertisements in order to present positive and pro-social roles and role models whenever possible."<sup>69</sup>

While studies conducted over the previous thirty years revealed underrepresentation of minorities and placement of minorities in commercials for mainly low-cost products, a 2000 study showed improvement in the representation of minorities in advertisements aimed at children.<sup>70</sup> However, this study found that minorities were still underrepresented in toy commercials, and that this underrepresentation "may cultivate a belief that Black children are not 'mainstream' enough to

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64. APA TASK FORCE, *supra* note 23, at 11 (citation omitted).

65. *Id.* (citations omitted).

66. *Id.*

67. Hae-Kyong Bang & Bonnie B. Reece, *Minorities in Children's Television Commercials: New, Improved, and Stereotyped*, 37 J. CONSUMER AFF. 42, 43 (2003).

68. The National Advertising Review Council, an alliance between the Better Business Bureau and the advertising industry, created CARU "to promote responsible children's advertising and to respond to public concerns." BETTER BUS. BUREAU, SELF REGULATORY GUIDELINES FOR CHILDREN'S ADVERTISING 2, <http://www.caru.org/guidelines/index.asp> [hereinafter CARU Guidelines]. The CARU attempts to set guidelines so that the advertising industry may regulate itself.

69. *Id.* at 3.

70. Bang & Reece, *supra* note 67, at 46-47.

appear in all types of commercials.”<sup>71</sup> The study also found that minorities were rarely shown in a home or family setting, possibly contributing “to a stereotype that many Black people do not have strong family ties or that many Asian American parents are too busy at their workplace to have family time at home.”<sup>72</sup> Also, minority adults were underrepresented in children’s commercials, possibly contributing to the stereotype “that the absence of adults in minority children’s life is quite widespread.”<sup>73</sup>

While advertisers should continue to adjust their practices to ensure that they are not communicating messages to children that reinforce or create racial prejudices, advertisers seem to be making significant progress in this area and are legitimately attempting to regulate themselves. And though materialism and parent-child conflict are not normally considered desirable, these problems are not serious enough, by themselves, to warrant a reconsideration of the current government regulation of advertising aimed at children. However, the growing rate of obesity in America should be a governmental concern because of the cost it is inflicting on the health care system and the government’s general interest in improving Americans’ health. Because advertising directed at children has been shown to contribute to obesity, it is important to not only examine the constitutionality of the CTA, but also explore more effective ways in which the government could constitutionally regulate advertising aimed at children.

#### IV. A CONSTITUTIONAL ANALYSIS OF THE CTA

Speech regulated by the CTA is subject to lesser First Amendment protection because the speech is: (1) commercial in nature; (2) broadcast; and (3) aimed at children. Considering these characteristics, the CTA’s commercial restriction does not violate current First Amendment jurisprudence.

##### A. *The Lesser First Amendment Protection Given to the Speech Regulated by the CTA*

Television commercials directed at children fall into the category of commercial speech because they are “related solely to the economic interests of the speaker and its audience.”<sup>74</sup> The government is given an

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71. *Id.* at 62.

72. *Id.*

73. *Id.* at 63.

74. *Central Hudson*, 447 U.S. at 561 (citations omitted). Even commercials aimed at children that, in addition to promoting a product, contain messages or information of a noncommercial nature are considered commercial speech. *See Bd. of Trs. v. Fox*, 492 U.S. 469, 474–75 (1989).

“ample scope of regulatory authority”<sup>75</sup> to regulate commercial speech and such speech has “a limited measure of protection, commensurate with its subordinate position in the scale of First Amendment values.”<sup>76</sup>

The Court, in *Central Hudson Gas & Electric Corp. v. Public Service Commission*, developed a four-prong test for regulations of commercial speech: (1) for the speech to be subject to First Amendment protection it must not mislead the consumer or promote unlawful acts; (2) the government must have a substantial interest in regulating the speech; (3) the regulation of speech must directly and substantially advance the government’s interest; and (4) the regulation of speech must not be more extensive and broad than necessary.<sup>77</sup>

The first prong of the *Central Hudson* test gives the government power to regulate speech that it does not have in other contexts. Under this prong, the government can restrict commercial speech that does not “accurately inform the public about lawful activity.”<sup>78</sup> The rationale for treating commercial speech differently and allowing the government to suppress misleading statements is “the importance of avoiding deception and protecting the consumer from inaccurate or incomplete information in a realm in which the accuracy of speech is generally ascertainable by the speaker.”<sup>79</sup> Moreover, “[F]alse or misleading speech in the commercial realm also lacks the value that sometimes inheres in false or misleading political speech.”<sup>80</sup> Because of this lack of value, the Court has expressed its approval of statutes that ban forms of commercial speech that are “fraudulent, deceptive, or coercive.”<sup>81</sup> The FTC has developed a test to determine whether or not an advertisement is deceptive or misleading.<sup>82</sup> In

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75. *Fox*, 492 U.S. at 477.

76. *Ohralik v. Ohio State Bar Ass’n.*, 436 U.S. 447, 456 (1978).

77. *Central Hudson*, 447 U.S. at 566. Some current Justices have indicated that they feel the *Central Hudson* test is applied in inappropriate circumstances. See *Thompson v. W. States Med. Ctr.*, 535 U.S. 357, 367 (2002). For example, Justice Thomas has consistently expressed his displeasure with the use of the *Central Hudson* test when “the government’s asserted interest is to keep legal users of a product or service ignorant in order to manipulate their choices in the marketplace.” *Greater New Orleans Brdcast. Ass’n v. United States*, 527 U.S. 173, 197 (1999) (Thomas, J., concurring) (internal quotations omitted). Justice Scalia has indicated that he has “discomfort with the *Central Hudson* test, which seems to me to have nothing more than policy intuition to support it.” *44 Liquormart, Inc. v. Rhode Island*, 517 U.S. 484, 517 (1996) (Scalia, J., concurring).

78. *Central Hudson*, 447 U.S. at 563.

79. *Rubin v. Coors Brewing Co.*, 514 U.S. 476, 493 (1995) (Stevens, J., concurring).

80. *Id.* at 496.

81. *Edenfield v. Fane*, 507 U.S. 761, 768 (1993). The *Edenfield* Court noted that statutes that encompass not only this misleading speech but also legitimate, nonmisleading speech would have to satisfy the remaining three prongs of the *Central Hudson* test. *Id.* at 769.

82. For the complete statement, see *Cliffdale Assoc., Inc.*, 103 F.T.C. 110, 176 (1984).



general, for a commercial to be considered deceptive, and thus outside of the scope of the First Amendment, the commercial must contain a representation that could mislead a reasonable consumer and affect that consumer's decision to purchase a product.<sup>83</sup>

In addition to its ability to restrict misleading or deceptive commercial speech, Congress empowered the FTC to restrict unfair speech.<sup>84</sup> For commercial speech to be unfair, the speech must be "likely to cause substantial injury to consumers which is not reasonably avoidable by consumers themselves and not outweighed by countervailing benefits to consumers or to competition."<sup>85</sup> The FTC may consider public policy, but may not make it the primary basis for finding a practice unfair.<sup>86</sup> When challenging a practice as unfair, the government must demonstrate that a regulation of the practice will reduce the harm caused; such an effect will not be presumed.<sup>87</sup>

Also, the Court has allowed regulations that protect children to stand, when in other contexts the regulations would violate the First Amendment.<sup>88</sup> The Court held in *FCC v. Pacifica Foundation* that the government may protect the "well-being of its youth" through the "regulation of otherwise protected expression," by restricting indecent speech on the radio that children are likely to hear.<sup>89</sup> When passing the CTA, Congress considered the Court's willingness to limit speakers' First Amendment protections in order to allow the government to protect children.<sup>90</sup>

Also, broadcast speech receives less First Amendment protection than other forms of speech.<sup>91</sup> The Court has recognized the FCC's authority and power to regulate a broadcaster's speech if the regulation "would serve 'the

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83. *Id.* at 168–70.

84. 15 U.S.C. § 45(a)(1) (2000) ("[U]nfair or deceptive acts or practices in or affecting commerce, are hereby declared unlawful.").

85. § 45(n).

86. *Id.*

87. *See 44 Liquormart*, 517 U.S. at 505.

88. *See Ashcroft v. Free Speech Coal.*, 535 U.S. 234, 250–51 (2002) (holding that while the government may ban actual child pornography, it may not ban virtual child pornography, because virtual child pornography does not harm children in the way that actual child pornography does (citation omitted)); Dennis Crouch, Comment, *The Social Welfare of Advertising to Children*, 9 U. CHI. L. SCH. ROUNDTABLE 179, 186 (2002) (citing *New York v. Ferber*, 458 U.S. 747 (1982)).

89. *FCC v. Pacifica Found.*, 438 U.S. 726, 749 (1978) (citing *Ginsberg v. New York*, 390 U.S. 629, 639–40 (1968)).

90. *See H.R. REP. NO. 101–385*, at 8 (1991).

91. *See Reno v. ACLU*, 521 U.S. 844, 868 (1997); *Action for Children's TV v. FCC*, 58 F.3d 654, 659 (D.C. Cir. 1995) (citing *Pacifica*, 438 U.S. at 748).

public interest, convenience, and necessity.”<sup>92</sup> The *Pacifica* Court put forth two rationales for giving broadcast speech less protection than speech communicated over other mediums. First, broadcast speech is heard by people in their own homes, and in the home, “the individual’s right to be left alone plainly outweighs the First Amendment rights of an intruder.”<sup>93</sup> Second, broadcast speech is “uniquely accessible to children.”<sup>94</sup> Both these rationales apply to commercials directed at children; these advertisements are viewed by children within their homes and are aired during programs to which children generally have access.

*B. An Analysis of the CTA Under Central Hudson’s Four-Prong Test*

Keeping in mind the lesser protection given to the speech regulated by the CTA based on the speech’s commercial nature, its direction at children, and the broadcast media over which it is aired, the Note will analyze the CTA under the four prongs of the *Central Hudson* test.

1. Prong One: Are Commercials Aimed at Children Misleading?

When determining if advertisements aimed at children are misleading or deceptive, advertisements should be looked at from the perspectives of the children at whom the advertisements are aimed. Thus, the “limited ability of children to detect exaggerated or untrue statements” will be considered.<sup>95</sup> The FTC typically challenges advertisements that lead to harms that “parents themselves generally cannot prevent or control.”<sup>96</sup> Thus, advertisements found to be unfair have included those that show toys performing actions that they cannot perform or those that advertise 900 numbers that children can call to talk with characters from television shows.<sup>97</sup> However, J. Howard Beales, former FTC Director of Consumer Protection, expressed the view that “Kids’ pestering their parents with demands for ‘junk foods’ may be annoying and aggravating, but it is not unfair or deceptive under the FTC Act.”<sup>98</sup>

On the other hand, the APA believes that advertising aimed at

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92. *Pacifica*, 438 U.S. at 748 (quoting 47 U.S.C. §§ 309(a), 312(a)(2)).

93. *Id.* at 748 (citing *Rowan v. Post Office Dept.*, 397 U.S. 728 (1970)).

94. *Id.* at 749.

95. Roscoe B. Starek, III, FTC Commissioner, *The ABCs at the FTC: Marketing and Advertising to Children*, Summary of Prepared Remarks (July 25, 1997) (citation omitted), <http://www.ftc.gov/speeches/starek/minnfin.htm>.

96. FTC, *ADVERTISING TO KIDS AND THE FTC: A REGULATORY RETROSPECTIVE THAT ADVISES THE PRESENT* 5 (2004), [www.ftc.gov/speeches/beales/040802adstokids.pdf](http://www.ftc.gov/speeches/beales/040802adstokids.pdf).

97. *See id.*

98. Beales, *supra* note 2, at 7.

children is inherently unfair.<sup>99</sup> The APA based this opinion on research that revealed: (1) children generally cannot distinguish between a commercial and a program until the age of 4–5;<sup>100</sup> (2) children generally do not realize that the purpose of a commercial is to persuade the viewer to buy the advertiser's product until the age of 7–8;<sup>101</sup> and (3) even with training, children of this age generally cannot develop the ability to comprehend the persuasive purpose of commercials.<sup>102</sup> Legislation requires that when a company advertises its products, the company must identify itself and make it clear that the company has paid for the advertisement.<sup>103</sup> The purpose of this requirement is to ensure that commercial viewers realize that what they are viewing has been paid for and know the identity of the person or company paying for the advertisement.<sup>104</sup> Based on this purpose, the APA opined: "If it is unfair and deceptive to seek to bypass the defenses that adults are presumed to have when they are aware that advertising is addressed to them, then it must likewise be considered unfair and deceptive to advertise to children in whom these defenses do not yet exist."<sup>105</sup> The American Academy of Pediatrics also found that "advertising directed toward children is inherently deceptive and exploits children under 8 years of age."<sup>106</sup> Not only do psychologists feel that advertising aimed at children is inherently deceptive, a survey of youth marketers found that 91% of these marketers think that companies advertise products to children in ways that children do not realize that they are being targeted.<sup>107</sup>

In addition to the inability of children to distinguish between advertisements and television, it is increasingly common for advertising agencies to employ psychologists to help develop ads that will influence children to buy products.<sup>108</sup> Some psychologists believe that their colleagues who work with advertisers violate the mission of the APA, and are basically "helping [advertisers] manipulate children."<sup>109</sup> The APA Task Force, which extensively investigated advertising directed at children, agreed that the use of psychological research to develop commercials that

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99. APA TASK FORCE, *supra* note 23, at 22.

100. *Id.* at 6.

101. *Id.* at 8.

102. *Id.* at 15.

103. 47 U.S.C. § 317(a) (2000).

104. National Broadcast Company Concerning Sponsorship Identification, 27 F.C.C.2d 75, 75 (1970).

105. APA TASK FORCE, *supra* note 23, at 21.

106. KAISER REPORT, *supra* note 16, at 8 (citation omitted).

107. Daren Fonda & Eric Roston, *Pitching it To Kids*, TIME, June 28, 2004, at 52–53.

108. APA TASK FORCE, *supra* note 23, at 20.

109. Rebecca A. Clay, *Advertising to children: Is it Ethical?*, 31 MONITOR ON PSYCH. 8, (2000), available at <http://www.apa.org/monitor/sep00/advertising.html>.

will be particularly effective and will take advantage of the limited abilities of children is unfair, but noted that some psychological research in the area was acceptable.<sup>110</sup> However, there is little that can be done to prevent advertisers from using research to exploit children's tendencies. Even if psychologists were to refuse to work directly with companies, it would be nearly impossible to prevent advertisers from using existing psychological publications or research to help them design their ads to take advantage of the limited abilities of children.<sup>111</sup>

The capacity of ads to mislead children is demonstrated by a study that found that 70% of children thought that fast food was healthful.<sup>112</sup> Another study showed children unhealthful foods and healthful foods and asked them to indicate which food was healthful; the more television that children watched, the more likely they were to choose the unhealthful food.<sup>113</sup>

If one believes the studies and opinions of groups such as the APA, the Kaiser Foundation, and the American Academy of Pediatrics—reputable groups whose opinions are highly valued on many subjects—then advertisements mislead children. The House Committee on Energy and Commerce made findings similar to those of the APA regarding the ability of children to discern and interpret advertisements and concluded that children “tend to place indiscriminate trust in television advertising.”<sup>114</sup> When determining whether or not commercial speech aimed at children is inherently misleading and thus not subject to First Amendment protection, the Court would consider evidence that shows commercials do in fact mislead children.<sup>115</sup> Thus, the studies and reports of the APA, the Kaiser Foundation, and the American Academy of Pediatrics would be relevant and should be persuasive. The Court would also consider relevant children's relative lack of knowledge when deciding whether advertising aimed at them is misleading.<sup>116</sup>

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110. APA TASK FORCE, *supra* note 23, at 22.

111. *See* Clay, *supra* note 109.

112. KAISER REPORT, *supra* note 16, at 5–6 (citation omitted).

113. *Id.* at 6 (citation omitted).

114. H.R. REP. NO. 101-385, at 6 (1991).

115. *In re R.M.J.*, 455 U.S. 191, 200 n.11 (1982), which stated:

The commercial speech doctrine is itself based in part on certain empirical assumptions as to the benefits of advertising. If experience proves that certain forms of advertising are in fact misleading, although they did not appear at first to be “inherently” misleading, the Court must take such experience into account.

(citations omitted).

116. *See* *Bates v. State Bar of Ariz.*, 433 U.S. 350, 383 (1977) (noting that when considering whether restrictions on advertising by lawyers was misleading, because “the public lacks sophistication, concerning legal services, misstatements that might be

Because of their misleading nature, advertisements aimed at children should be considered outside the protection of the First Amendment under *Central Hudson*. Thus, the CTA does not violate the First Amendment and even more restrictive regulation would also be constitutional.

Despite the strong likelihood that advertisements directed at children deserve no protection from the First Amendment, an analysis of the CTA under the remaining three prongs of *Central Hudson* helps examine how the CTA advances its goal of protecting children. Moreover, if the Court finds that advertising to children is not inherently misleading, the government would merely be prohibited from completely banning advertising directed at children. If the Court finds that advertising to children is not inherently misleading, but merely has the potential to mislead, the state could still regulate advertising aimed at children subject to the *Central Hudson* test.<sup>117</sup>

## 2. Prong Two: Does the Government Have a Substantial Interest in Protecting Children from Advertising?

The CTA meets the second prong of the *Central Hudson* test because the government has a substantial interest in protecting children from the harms associated with advertising. As the House Bill accompanying the CTA indicated, “[I]t is difficult to think of an interest more substantial than the promotion of the welfare of children.”<sup>118</sup> Courts have also found that the protection of children is a substantial state interest.<sup>119</sup>

There is also substantial evidence that advertising harms children. The government must present evidence that advertising harms children in order to meet the second prong of *Central Hudson*; that is, the government cannot merely claim that something harms children without offering proof.<sup>120</sup> However, the government does not need to show absolute certainty or agreement within the scientific community that a certain type of speech harms children.<sup>121</sup> The studies mentioned above linking

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overlooked or deemed unimportant in other advertising may be found quite inappropriate in legal advertising.” (citation omitted)). Therefore, because different audiences have different degrees of sophistication and knowledge, “different degrees of regulation may be appropriate in different areas.” *Id.* at 384 n.37.

117. See *Peel v. Att’y Registration & Disciplinary Comm’n of Ill.*, 496 U.S. 91, 110 n.17 (1990).

118. H.R. REP. NO. 101-385, at 11 (1991).

119. E.g., *Pacifica*, 438 U.S. at 757–58.

120. *Edenfield*, 507 U.S. at 771 (indicating that when regulating commercial speech, the government “must demonstrate that the harms it recites are real and that its restriction will in fact alleviate them to a material degree.”).

121. Indeed, when dealing with the regulation of indecent speech, “the Supreme Court has never suggested that a scientific demonstration of psychological harm [to children] is

childhood obesity and resulting health problems to advertising aimed at children should give the government ample evidence to satisfy the Court that commercial speech aimed at children is harmful and that the government has a substantial interest in preventing these harms.

### 3. Prong Three: Does the CTA Substantially Protect Children from the Harms of Advertising?

A restriction on commercial speech “may not be sustained if it provides only ineffective or remote support for the government’s purpose.”<sup>122</sup> So, to satisfy the third prong of *Central Hudson*, the CTA must substantially protect children from the harms caused by advertising. A possible problem with finding that the CTA significantly reduces children’s exposure to advertising is that children are already exposed to numerous advertisements through billboards, print media, and the Internet. However, television advertisements reach more children than any other form of media, and advertisers rely on television ads more than ads through other mediums.<sup>123</sup> Thus, the existence of advertising over other mediums would probably not preclude a finding that regulating advertisements on television substantially protects children from advertising.

In addition to overtly advertising, companies also reach children through television by placing their products or brand names in television programs. Currently, there are no restrictions on products or brand names appearing on television programs.<sup>124</sup> The prominent placement of a product in a program could produce a persuasive effect on children similar to that of a commercial for that product featuring a character from the currently airing program. That is, a child viewing a show in which a character uses a certain product may think that the character endorses this product and thus assumes positive qualities about that product. However, while this possibility exists, no proof exists that producers or advertisers purposely employ this tactic.<sup>125</sup> While the FCC does not currently restrict the use of brand name products within a show, it has indicated that “[s]hould abuses occur . . . [it] will not hesitate to revisit this issue.”<sup>126</sup>

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required . . .” *Action for Children’s TV*, 58 F.3d at 661–62. The D.C. Circuit relied on *Ginsberg v. New York*, 390 U.S. at 642–43, in which the Court stated that the government did not need to show complete agreement within the scientific community that obscenity harms children in order to regulate indecent speech.

122. *Central Hudson*, 447 U.S. at 564.

123. See APA TASK FORCE, *supra* note 23, at 4.

124. *Children’s Programming Report*, *supra* note 27, para. 41 (reasoning that such a restriction would inhibit the creativity of writers).

125. See *id.* paras. 5, 41–42. “[A] program’s relationship to products is not necessarily indicative of commercial intent.” *Id.* para. 41.

126. *Id.* para. 44.

A more serious problem with the constitutionality of the CTA arises when one considers whether limiting the amount of commercial time aired during programs aimed at children substantially reduces the amount of commercial material viewed by children. Significant numbers of children are watching television after 10:00 p.m.,<sup>127</sup> the time before which the FCC requires that stations air their core children's television programs.<sup>128</sup> These children are likely watching television that is not aimed at children and is thus not subject to commercial limitations.<sup>129</sup> The concept of "children's grazing" through channels while watching television also makes it difficult to control or know what children actually watch.<sup>130</sup> Thus, for the premise to hold true that limiting the amount of commercial time during individual shows aimed at children substantially limits the amount of commercial material that children view, children would have to watch primarily shows aimed at children and not flip through channels and view commercials during this "grazing." This premise is difficult to accept. Children under eight generally do not really understand the point of commercials, and children five and under cannot even tell the difference between a commercial and a program.<sup>131</sup> Also, children who view television without parental supervision may view significant amounts of television not aimed at them. Cartoons such as Fox's "The Family Guy," Comedy Central's "South Park," or cartoons that are part of The Cartoon Network's "Adult Swim," are not aimed at children. However, children may simply come across these shows and watch them because they are cartoons.

Even if it could be demonstrated that the CTA actually reduced the amount of commercial material viewed by children, there is a lack of evidence that reducing the quantity of commercials substantially reduces the effect of commercials on children.<sup>132</sup> In fact, evidence indicates that children may develop a preference for a particular brand or product after seeing a commercial only one time.<sup>133</sup>

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127. *Action for Children's TV*, 58 F.3d at 657.

128. FCC Consumer Facts, <http://www.fcc.gov/cgb/consumerfacts/childtv.html> (last visited Mar. 12, 2006).

129. See H.R. REP. NO. 101-385 at 16 (1991); cf. *infra* Part V.B.2. (discussing children's familiarity with characters that do not appear in programming aimed at children).

130. *Action for Children's Television*, 58 F.3d at 668.

131. APA TASK FORCE, *supra* note 23, at 5-7.

132. See H.R. REP. NO. 101-385, at 19-20 (1991) (indicating a disagreement among experts over whether harm was caused by "too many" commercials).

133. APA TASK FORCE, *supra* note 23, at 10 (adding that increased exposure may make it more likely for such a preference to develop); KAISER REPORT, *supra* note 16, at 5 (describing a study in which children developed preferences for advertised products after seeing only one program containing commercials).

Other obstacles the CTA, as enforced by the FCC, faces with meeting the third prong are the FCC's exceptions to the commercial limitations.<sup>134</sup> The FCC's provision that "public service" and educational announcements do not count towards the total amount of commercial time makes sense and does not frustrate the purpose of the statute. However, the provision that excludes time spent on advertisements for other shows does not conform to the statute's purpose. If children are persuaded to watch more television, they will also view more ads. The Court has found that "[t]here is little chance that [an act] can directly and materially advance its aim, while other provisions of the same Act directly undermine and counteract its effects."<sup>135</sup> By exempting ads that encourage children to watch more television, and thus more commercials, the CTA, as enforced by the FCC, undermines its goal of reducing children's exposure to advertising.

Another exception in the CTA is its unexplained distinction between weekend television, during which broadcasters may only air 10.5 minutes of commercial material per hour, and weekday television, during which broadcasters may air 12 minutes per hour.<sup>136</sup> Data available at the time of the passage of the CTA indicated that children watch more television on weekdays than on weekends.<sup>137</sup> Because the purpose of the CTA is to reduce children's exposure to commercials, it would make more sense to set a higher commercial time limit for television broadcast on the weekends when fewer children are watching television. Thus, the higher limit of commercial material for weekday television cannot be justified in accordance with the overall purpose of the statute, and undermines the government's interest.

#### 4. Prong Four: Is the CTA More Extensive Than Necessary to Achieve the Government's Goals?

The CTA passes the fourth prong of the *Central Hudson* test because it is not more extensive than necessary. The Court has clarified that this prong does not require that the government's regulation be the "least restrictive means" but only that it be "one whose scope is 'in proportion to

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134. Cf. *Rubin v. Coors Brewing Co.*, 514 U.S. 476, 489 (1995) (noting that exceptions to a statute prohibiting alcoholic beverage manufacturers from displaying the alcohol content on labels "bring into question the purpose of the labeling ban"); *Valley Brdcast. Co. v. United States*, 107 F.3d 1328, 1334-35 (9th Cir. 1997) (stating that the numerous exceptions to a statute banning advertising for gambling made it difficult for the statute to substantially advance its goal of reducing participation in gambling).

135. *Rubin*, 514 U.S. at 489.

136. See H.R. REP. NO. 101-385, at 20 (1991).

137. See *id.*



the interest served’”<sup>138</sup> or that it is “narrowly tailored to achieve the desired objective.”<sup>139</sup>

Before the passage of the CTA, market forces already kept the amount of commercial material aimed at children at a level near or below those levels prescribed by the CTA.<sup>140</sup> A survey conducted by the National Association of Broadcasters two years before Congress passed the CTA indicated that broadcasters aired an average of eight minutes and thirty-eight seconds of commercial material per hour during children’s programming,<sup>141</sup> an amount significantly below the limits set by the CTA. Only 7.6% of children’s programs in the top twenty markets averaged more than thirteen minutes of commercial material per hour.<sup>142</sup> Thus, the CTA’s commercial limitation caused broadcasters to adjust their commercial allowances for less than 10% of their children’s programs, an insignificant adjustment considering that most broadcasters air much more programming aimed at adults than at children. While broadcasters also had to ensure that they did not air commercials featuring characters from the shows during which the commercials air, this restriction is less burdensome and extensive than other restrictions of commercial speech approved by the Court.<sup>143</sup>

Indeed, the CTA has not caused much difficulty for broadcasters, perhaps explaining why broadcasters did not immediately challenge the CTA. The inconsistencies in the amount of time allowed and the exception for commercials for other programs benefit broadcasters in two ways. First by allowing them to air more commercials during shows that more children watch, and second by allowing them to air ads for their own television shows that do not count towards the commercial limits, boost their own ratings, and increase the amount of money that advertisers pay for advertising spots. While these inconsistencies and exceptions are primary reasons that the statute should fail the third prong of *Central Hudson*, it would make little sense for broadcasters to bring a claim challenging the CTA based on an inconsistency or exception that benefits them.

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138. *Fox*, 492 U.S. at 480 (quoting *In re R.M.J.*, 455 U.S. at 203).

139. *Id.*

140. See H.R. REP. NO. 101-385, at 6–7 (1991).

141. *Id.* at 7.

142. *Id.*

143. See, e.g., *United States v. Edge Brdcast. Co.*, 509 U.S. 418 (1993) (permitting a complete ban of commercials promoting gambling in a state where gambling was illegal, even though the commercials reached a significant number of people in a state where gambling was legal); *Posadas de Puerto Rico Assocs. v. Tourism Co.*, 478 U.S. 328 (1986) (upholding a law that banned Puerto Rican casinos from advertising themselves to residents of Puerto Rico even though casino gambling was legal in Puerto Rico). The reasoning behind the *Posadas* decision has been questioned by the Court, but the Court has not stated that the result in the case was erroneous. 44 *Liquormart*, 517 U.S. at 509–11.

## V. BETTER WAYS TO ACHIEVE THE GOAL OF PROTECTING CHILDREN FROM THE HARMS CAUSED BY ADVERTISING AIMED AT CHILDREN

While the CTA has not overly burdened broadcasters, it has done little to protect children from the harms of advertising. Indeed, the amount of advertising directed at children continues to grow as does the amount of television watched by children.<sup>144</sup> Because the government has solidly accepted the premise that television viewing benefits children, and because parents increasingly place their children in front of the television or other electronic media through which advertisers can reach children instead of sending them outside to play or handing them a book, this trend seems likely to continue.<sup>145</sup>

Thus, it is time to rethink the more extensive regulation of advertising directed at children that the FCC and FTC considered in the 1970s and that is currently in place in other countries. While several things must be done to address the harms caused by advertising, an important step is for the government to change the fundamental nature of its regulation of children's advertising and regulate content instead of quantity.

### A. *The Reluctance of the FTC to Initiate Further Regulation*

The FTC seems reluctant to completely ban advertising aimed at children, as countries such as Sweden have done. This reluctance stems from two factors: (1) the past failure of the FTC to regulate advertising aimed at children; and (2) the political views of FTC commissioners. Former FTC Commissioner Orson Swindle feels that in this area, the government should stay uninvolved and allow the industry to regulate itself.<sup>146</sup> Former FTC Chairman Timothy Muris also felt that the government should not regulate this advertising, and that advertising is not the primary cause of childhood obesity.<sup>147</sup> Former Commissioner J. Howard Beales indicated that the ramifications of the FTC's attempt to regulate advertising aimed at children in the 1970s will dictate the FTC's current policies and that the FTC "will tread very carefully when responding to calls to restrict truthful advertising to children."<sup>148</sup>

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144. KAISER REPORT, *supra* note 16, at 1.

145. *See id.* (indicating that children spend roughly 5.5 hours per day in front of some sort of media).

146. Orson Swindle, Commissioner, FTC, Advertising Issues Before the Federal Trade Commission (Apr. 28, 2004), <http://www.ftc.gov/speeches/swindle/040428aaf.htm>.

147. Kucharsky, *supra* note 53 (quoting Timothy Muris, "I think banning marketing is a distraction. Even our dogs and cats are fat . . . and it's not because they're watching too much advertising.").

148. Beales, *supra* note 2, at 14.

However, the FTC and other governmental organizations have regulated ads for tobacco and alcohol.<sup>149</sup> Former Commissioner Swindle indicated that the FTC was willing to regulate tobacco and alcohol because, “[i]f children purchase and consume alcohol or tobacco, it creates serious health risks for them—risks that they may well not fully comprehend.”<sup>150</sup> This distinction between the harms caused by advertising alcohol or tobacco to children and the harms caused by advertising in general to children may have made sense at one time.<sup>151</sup> However, deaths and health problems caused by obesity, to which advertising directed at children substantially contributes, are now nearly as serious and costly as those caused by the use of tobacco.<sup>152</sup> Also, similarly to how children do not completely understand the consequences of alcohol and tobacco use, they also do not fully comprehend the consequences of making poor nutritional decisions.<sup>153</sup> While the harms caused by children drinking and smoking may be more obvious, the harms caused by children developing poor eating habits are no less serious.

*B. The Government Should Regulate the Content Instead of the Amount of Commercial Material Aimed at Children*

In the commercial context, the content of speech can be regulated.<sup>154</sup> Such content-based regulation does not have to pass the strict scrutiny analysis the Court usually applies to content-based regulations,<sup>155</sup> but need only pass the four-prong *Central Hudson* test for commercial speech. Some content-based regulation of commercials aimed at children already exists. For example, the FCC prohibits “host-selling,” the practice of using a character in a television show to appear in an advertisement that airs during

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149. See Orson Swindle, Commissioner, FTC, Remarks at the Aggressive Advertising and the Law Workshop (Feb. 22, 1999), [www.ftc.gov/speeches/swindle/osbdaspc.htm](http://www.ftc.gov/speeches/swindle/osbdaspc.htm) [hereinafter Aggressive Advertising Remarks]; Nixon, *supra* note 57, at 19.

150. Aggressive Advertising Remarks, *supra* note 149.

151. When the FTC issued its staff report in 1978, childhood obesity was at a much lower rate than it is today. KAISER REPORT, *supra* note 16, at 1. At the time the FTC issued its report, the primary harm of advertising to children was thought to be tooth decay. See Beales, *supra* note 2, at 6.

152. KAISER REPORT, *supra* note 16, at 1.

153. See *supra* Part III; see generally APA TASK FORCE, *supra* note 23; KAISER REPORT, *supra* note 16.

154. *Central Hudson*, 447 U.S. at 561 n.6.

155. For a government regulation to be constitutional regarding speech that is given full First Amendment protection, the regulation “must be narrowly tailored to promote a compelling Government interest.” *United States v. Playboy Entm’t Group*, 529 U.S. 803, 813 (2000). “If a less restrictive alternative would serve the Government’s purpose, the legislature must use that alternative.” *Id.* (citation omitted).

the character's show.<sup>156</sup> Also, statutes aimed at limiting children's exposure to advertisements for alcoholic beverages have been held constitutional because of the state's interest in preventing minors from drinking.<sup>157</sup>

As Justice Stevens indicated, "[A]ny description of commercial speech that is intended to identify the category of speech entitled to less First Amendment protection should relate to the reasons for permitting broader regulation: namely, commercial speech's potential to mislead."<sup>158</sup> Because commercial speech aimed at children is misleading, all commercial speech aimed at children could be proscribed. Thus, content regulation of this speech would not cause the dangers inherent in other types of content-based regulation. As the Court said in *R.A.V. v. City of St. Paul*, "When the basis for the content discrimination consists entirely of the very reason the entire class of speech at issue is proscribable, no significant danger of idea or viewpoint discrimination exists."<sup>159</sup>

It is not the number or duration of commercials that misleads children; it is the content of commercials. Thus, a regulation of content seems a more effective and logical angle from which to approach the problems caused by advertising to children. Market forces should usually prevent broadcasters from airing more commercial material than currently allowed by the CTA.<sup>160</sup> Moreover, regulation of content instead of amount would prevent broadcasters from being penalized for inadvertent violations of the time restrictions or program-length commercial proscription with which they have made good faith efforts to comply.<sup>161</sup>

#### 1. Commercials Aimed at Children Should Be Required to Contain Additional Information That Would Reduce the Commercials' Tendency to Mislead.

In the commercial context, the government may often "require[] affirmative disclosures that the speaker might not make voluntarily."<sup>162</sup> The Supreme Court has acknowledged that the general trend in federal policy is to require companies to make more disclosures than they might

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156. *Children's Programming Report*, *supra* note 27, para. 44 n.147.

157. *See, e.g., Anheuser-Busch, Inc. v. Schموke*, 101 F.3d 325, 327 (4th Cir. 1996) (upholding a constitutional ban on billboard advertising of alcoholic beverages in certain parts of Baltimore).

158. *Rubin*, 514 U.S. at 494 (Stevens, J., concurring).

159. 505 U.S. 377, 388 (1992).

160. *See* H.R. REP. NO. 101-385, at 7 (1991) (indicating that at the time the CTA was enacted, most stations aired less commercial material per hour than the CTA allows).

161. *See* discussion *supra* Part II.

162. *Rubin*, 514 U.S. at 492 (Stevens, J., concurring) (citations omitted).

make on their own.<sup>163</sup> Indeed, the Court has indicated that with potentially misleading speech, an appropriate remedy is to require the speaker to clarify the speech by including additional information such as a disclaimer.<sup>164</sup>

One way to effectively regulate the content of commercials would be to require advertisers to include certain information about their products in their commercials. Most commercials aimed at children do not provide product information, instead attempting only “to associate the product with fun and happiness.”<sup>165</sup> A 1997 study indicated that approximately only 2% of food commercials contained nutritional information.<sup>166</sup> A good place to start regulating commercials aimed at children would be to require that food companies disclose information about their products, such as fat content or high sodium levels.

Such disclosures may prove beneficial and lead children to make better nutritional decisions. Requirements that companies include nutritional information on product labels have led to a decrease in consumers’ fat intake.<sup>167</sup> Also, a study indicated that when restaurants included nutritional information on their menus, customers ordered foods with lower amounts of fat and cholesterol.<sup>168</sup> While children may not comprehend nutritional information as completely as adults, a study indicated that children ages 4–7 “possess the ability to comprehend abstract concepts such as energy, a strong heart, that good foods keep germs out of the body, and that low fat keeps the heart healthy.”<sup>169</sup> Advertisements aimed towards children emphasizing the value of choosing healthful foods and lifestyles have been effective.<sup>170</sup> Also, regardless of children’s comprehension of nutritional information, disclaimers about the nutritional value of foods would help parents discuss the healthfulness of advertised foods with their children.<sup>171</sup>

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163. *See id.* at 484 (citing Nutrition Labeling and Education Act of 1990, Pub. L. No. 101-535, 104 Stat. 2353, as amended (requiring that companies include nutritional information on the labels of food products)).

164. *Peel*, 496 U.S. at 116 (Marshall, J., concurring) (citation omitted).

165. *See* APA TASK FORCE, *supra* note 23, at 4–5 (using the examples of McDonald’s ads featuring Ronald McDonald and cereal ads featuring Tony the Tiger).

166. *See* Aya Kuribayashi et al., *Actual Nutritional Information of Products Advertised to Children and Adults on Saturday*, 30 CHILDREN’S HEALTH CARE 309, 318 (2001).

167. *Id.* (citations omitted).

168. *Id.* (citation omitted).

169. Susan Sharaga Swadener, *Nutrition Education for Preschool Age Children: A Research Review*, <http://www.nal.usda.gov/fnic/usda/preschoolne.html> (citation omitted).

170. KAISER REPORT, *supra* note 16, at 9 (citation omitted). A media campaign that encouraged adults and children to use 1% or skim milk resulted in sales of 1% milk going up 21% and sales for skim milk going up 11%.

171. *Cf. Fatty Meals, Advertising Linked to Youth Obesity*, NATION’S HEALTH, Apr.

When making these disclaimers, advertisers should be required to use language that children can understand. Children do not understand the real meaning of phrases such as “some assembly required,” or “part of a balanced breakfast.”<sup>172</sup> Instead, advertisers should use language such as “you have to put it together,”<sup>173</sup> or “be sure to eat Frosted Flakes along with milk, orange juice, and a banana.” Including such language in commercials aimed at children would help reduce commercials’ misleading nature.<sup>174</sup>

## 2. Cartoon Characters and Celebrities Should Not Appear in Commercials Aimed at Children

A second way in which the government could regulate commercials aimed at children would be to ban the use of cartoon characters and celebrities in these commercials. While the Court generally indicates that restrictions on speech should be as limited as possible, the Court has found that some bans on certain methods of advertising would be acceptable. In the context of advertising of professional services, the Court has held that “when the particular content or method of the advertising suggests that it is inherently misleading or when experience has proved that in fact such advertising is subject to abuse, the States may impose appropriate restrictions. Misleading advertising may be prohibited entirely.”<sup>175</sup> Two of the three justifications identified by the Court for allowing such restrictions justify a proscription of celebrities and cartoon characters in commercials aimed at children. The Court identified “[t]he public’s comparative lack of knowledge[] [and] the limited ability of the professions to police themselves” as relevant.<sup>176</sup> The studies discussed above have indicated the limited ability of children to interpret commercial messages. While the establishment of the CARU guidelines does present an attempt at self-regulation, advertisers have made no attempt to restrict the use of cartoon characters and celebrities in advertisements for children’s products. Indeed, many companies currently use characters from popular children’s

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2004, at 7. Some restaurants have begun printing nutritional information on their menus in order to help children make informed decisions. Sen. Tom Harkin (D-Iowa) and Rep. Rosa DeLauro (D-Conn.) have introduced bills that would require restaurants to print nutritional information on their menus. In support of his bill, Harkin said, “Nutrition information on menus will help parents guide their kids food choices and their own as well.” *Id.*

172. APA TASK FORCE, *supra* note 23, at 5.

173. *Id.*

174. *Cf. Peel*, 496 U.S. at 115 (Marshall, J., concurring) (“Facts as well as opinions can be misleading when they are presented without adequate information.”).

175. *In re R.M.J.*, 455 U.S. at 203. This decision was unanimous.

176. *Id.* at 202. The third justification, “the absence of any standardization in the ‘product,’” does not apply to products advertised to children. *Id.*

television in their ads.<sup>177</sup> This widespread use of these characters in advertising indicates that companies realize the persuasive effect that these characters have over children.

Studies also show that the use of cartoon characters or celebrities increases commercials' influence over children.<sup>178</sup> Children certainly recognize and retain images of cartoon characters—even those that do not appear in children's shows—used in advertisements. A 1996 study revealed that nine and ten-year-olds were able to identify the Budweiser Frogs nearly as often as they were able to identify Bugs Bunny.<sup>179</sup> This fact is even more significant when one considers that these frogs do not even appear in commercials aimed at children. Thus, at least in theory, children should not have significant exposure to these commercials. Similarly, a 1991 study showed that as many six-year-olds could identify Joe Camel, the cartoon camel formerly used by Camel cigarettes, as could identify the Disney Channel logo.<sup>180</sup> In light of evidence of the influence that cartoons and celebrities hold over children, several British broadcasters have banned their use in food commercials aimed at children in an attempt to fight that country's problem with childhood obesity.<sup>181</sup>

Congress recognized the persuasive effect of characters in children's shows when it found that the practice of airing commercials during shows whose characters appear in the commercials "take[s] unfair advantage of the inability of children to distinguish between programming and commercial content."<sup>182</sup> The FCC has also indicated its awareness of the power wielded by the characters that appear in children's television programs by banning host-selling. Significantly, these studies that indicate children's ability to recognize and recall characters undermine the FCC's rationale for allowing commercials featuring characters to air sixty seconds before or after a show featuring that character.<sup>183</sup>

More support for the constitutionality of such a ban comes from the Court's view that, in some instances, the secondary effects of speech may be considered when upholding a ban on speech that does not receive full

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177. See KAISER REPORT, *supra* note 16, at 6 (describing Burger King's use of Teletubbies, Rugrats, Shrek, Pokemon, and SpongeBob SquarePants).

178. APA TASK FORCE, *supra* note 23, at 10 (citations omitted).

179. *Id.* at 13 (citation omitted).

180. *Id.*

181. KAISER REPORT, *supra* note 16, at 8; see also Jeremy Lee, *Cartoon characters to face child food ad ban*, CAMPAIGN (UK), July 30, 2004, at 10.

182. H.R. REP. NO. 101-385, at 16-17 (1991).

183. The FCC used children's short attention span to justify the sixty-second window. See *Children's Programming Report*, *supra* note 27, para. 45.

First Amendment protection.<sup>184</sup> Because commercials aimed at children that use cartoon characters or celebrities are commercial speech, aimed at children, and broadcast, they are subject to limited First Amendment protection. Thus, the secondary effects of these commercials—namely, the prevalence of childhood obesity—could be considered when determining the constitutionality of a ban of such commercials.

### 3. Regulation Should Apply to All Commercials Aimed at Children Instead of Only Commercials That are Aired During Programs Aimed at Children

In addition to changing its focus from regulating the amount of commercial material to the content of commercial material, the government should regulate all commercials that are aimed at children, not only commercials aired during shows aimed at children. The CTA's commercial limitation applies only to "programs originally produced and broadcast primarily for an audience of children twelve years old and under."<sup>185</sup> The limitation does not apply to "programs originally produced for a general or adult audience which may nevertheless be significantly viewed by children."<sup>186</sup> This distinction does not make sense. The House members who voiced dissenting opinions on the content of the CTA noted the irrationality of this distinction and asserted, "if you accept the premise of this legislation, commercial time limits should be applied to all programs, not just to those which are deemed to be 'children's programs.'"<sup>187</sup>

In addition to making more logical sense, regulating commercials aimed at children, and not just those aired during shows aimed at children, would conform to the Court's policy against restricting the content of speech available to adults in order to make the speech appropriate for children.<sup>188</sup> A ban on the use of cartoon characters and celebrities in commercials *aimed at children* would not present the same issues that the Court found impermissible in cases such as *Lorillard Tobacco*, because such a ban would not significantly deny adults access to truthful information concerning commercial decisions.<sup>189</sup> Indeed, the ban would not

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184. See *R.A.V. v. St. Paul*, 505 U.S. 377, 388–89 (1992) (citations omitted).

185. H.R. REP. NO. 101-385, at 16 (1991).

186. *Id.*

187. *Id.* at 21.

188. *Lorillard Tobacco Co. v. Reilly*, 533 U.S. 525, 564 (2001) ("[T]he governmental interest in protecting children from harmful materials . . . does not justify an unnecessarily broad suppression of speech addressed to adults.") (quoting *Reno v. ACLU*, 521 U.S. 844, 875 (1997)).

189. See *id.* at 564 (noting that while "[t]he State's interest in preventing underage tobacco use is substantial, and even compelling . . . tobacco retailers and manufacturers have an interest in conveying truthful information about their products to adults, and adults have



deny access to information at all. The ban would simply require that companies communicate the information in a manner less misleading to the children at whom the commercials are aimed.

Similarly, the Court stated in *Reno v. ACLU* that the “interest [in protecting children] does not justify an unnecessarily broad suppression of speech addressed to adults.”<sup>190</sup> FTC Commissioners have also expressed their desire not to regulate the content of commercials to a level that is suitable for children. As former Commissioner Swindle pointed out, “[N]ot every alcohol or tobacco ad that depicts a cartoon character, cute pet, or something that might appeal to children is necessarily targeted at children.”<sup>191</sup> Recognizing that companies often use cartoon characters or celebrities in commercials aimed at adults, the regulation proposed here would not affect such commercials. Thus, commercials for products designed for adults could still contain cartoon characters or celebrities and would not be subject to any other restrictions placed on advertising that targets children.<sup>192</sup>

## VI. WAYS TO PROTECT CHILDREN FROM ADVERTISING OTHER THAN GOVERNMENT REGULATION

In addition to these suggested changes in governmental regulation of advertising aimed at children, cooperation from other institutions would help reduce the harms that advertising causes children. In order to effectively combat these problems, businesses that produce products aimed at children, the advertising companies that promote these products, and the government must all work together.<sup>193</sup>

Advertisers have already made a significant attempt at self-regulation with the formation of CARU and its guidelines.<sup>194</sup> Companies tend to follow CARU’s guidelines; a 1993 study found that 96% of ads met CARU’s standards.<sup>195</sup> However, the study also found that “many of the guidelines were too vague and general to even be subject to empirical assessment.”<sup>196</sup> Based on business’s tendency to follow CARU guidelines,

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a corresponding interest in receiving truthful information about tobacco products.”).

190. *Reno*, 521 U.S. at 875.

191. Swindle, *supra* note 146.

192. However, if it was demonstrated that an ad for alcohol or tobacco caused minors to purchase the advertised product, the FTC has indicated its willingness to take action. *Id.*

193. *See* Nixon, *supra* note 57, at 22.

194. *See* CARU Guidelines, *supra* note 68.

195. APA TASK FORCE, *supra* note 23, at 19 (citation omitted).

196. *Id.* (citation omitted).

a possible way to reduce the harm caused to children would be for CARU to more clearly define, publicize, and enforce its guidelines.<sup>197</sup>

Businesses can help fight some of the problems caused by advertising to children, particularly child obesity, by modifying the products they produce for children. Subway, which produces many healthful products, runs a “Fresh Step” campaign that attempts to influence children to make good eating and lifestyle decisions. The campaign features Jared Fogle, who has appeared in previous successful Subway ads targeting adults.<sup>198</sup>

Other organizations have also attempted to promote ideals that counteract advertising for unhealthful foods. A campaign run by the Center for Science and the Public Interest that urged children to use skim or 1% milk instead of 2% or whole milk was successful; communities in which the campaign ran showed significant increases in the amount of 1% and skim milk purchased.<sup>199</sup> There are currently other attempts to promote a healthful lifestyle, but these campaigns lack adequate funding to effectively combat the advertising that influences children to make unhealthful diet and lifestyle decisions.<sup>200</sup> A campaign ran by the National Cancer Institute had a \$3.5 million budget, while the annual advertising budget for McDonald’s is \$665 million.<sup>201</sup> Increased government funding of organizations attempting to promote a healthful lifestyle would help these organizations effectively deliver their messages.

## VII. CONCLUSION

Something clearly must be done about America’s obesity problem. The regulation of commercials aimed at children, a practice that researchers have demonstrated leads to obesity, is a reasonable place to start. The regulations on commercial speech aimed at children suggested above conform to the rationales for allowing more extensive regulation of commercial speech that the Court identified in *44 Liquormart*: “When a State regulates commercial messages to protect consumers from misleading, deceptive, or aggressive sales practices, or requires the disclosure of beneficial consumer information, the purpose of its regulation

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197. See BRIAN WILCOX ET AL., AM. PSYCH. ASS’N, REPORT OF THE APA TASK FORCE ON ADVERTISING AND CHILDREN: RECOMMENDATIONS 7 (2004), <http://www.asu.edu/educ/epsl/CERU/Guidelines/CERU-0402-201-RCC.pdf>.

198. *Childhood Obesity; Subway restaurants use familiar figure to fight*, WOMEN’S HEALTH WKLY., Aug. 5, 2004, at 32.

199. KAISER REPORT, *supra* note 16, at 9 (citations omitted).

200. *Id.*

201. *Id.* (citation omitted).

is consistent with the reasons for according constitutional protection to commercial speech and therefore justifies less than strict review.”<sup>202</sup>

One of the Court’s principal concerns with regulation of commercial speech is “aversion towards paternalistic governmental policies that prevent men and women from hearing facts that might not be good for them.”<sup>203</sup> However, as Justice Scalia noted in his concurrence in *44 Liquormart*, “[I]t would also be paternalism for us to prevent the people of the States from enacting laws that we consider paternalistic, unless we have good reason to believe that the Constitution itself forbids them.”<sup>204</sup> The regulations proposed here would not prevent adults from receiving information. Instead, they would require companies to make more complete disclosures regarding the nature of their products and communicate this information in a manner less misleading towards children. Thus, the proposed regulations are constitutional and in accordance with the Court’s view that “[t]he First Amendment . . . does not prohibit the State from insuring that the stream of commercial information flow cleanly as well as freely.”<sup>205</sup>

The proposed restrictions on advertising also take into account the programmers’ need to fund the programming that the FCC has deemed necessary for children’s development.<sup>206</sup> Other countries have restrictions far stricter than those proposed here, and these countries still provide an adequate amount of television programs aimed at children.<sup>207</sup> Indeed, these proposed regulations do not place any limit on the amount of commercial material broadcasters can air, and instead are aimed at reducing the misleading nature of the commercials aimed at children.<sup>208</sup> A fundamental problem with achieving further legislation regulating commercials, especially those for unhealthful foods, is that “[l]egislators tend to be on the side of the food industry.”<sup>209</sup> Thus, the complete ban on advertising aired

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202. *44 Liquormart*, 517 U.S. at 501.

203. *Id.* at 517 (Scalia, J., concurring).

204. *Id.*

205. *Va. Bd. of Pharmacy v. Va. Citizens Consumer Council*, 425 U.S. 748, 771–72 (1976).

206. S. REP. NO. 101-66 (1991) (recognizing the expenses associated with producing educational television shows, including money for conducting research and hiring educators).

207. APA TASK FORCE, *supra* note 23, at 23.

208. Of course, the proposed regulations should not, and are not intended to increase the amount of commercial material aimed at children. The regulations are proposed while recognizing that market forces should prevent broadcasters from significantly increasing the amount of commercials aired during children’s programs. *See supra* Part IV.B.4.

209. David Kiley, *A Food Fight Over Obesity in Kids*, BUS. WK. ONLINE, Sept. 30, 2004, [http://www.businessweek.com/bwdaily/dnflash/sep2004/nf20040930\\_0110\\_db035.htm](http://www.businessweek.com/bwdaily/dnflash/sep2004/nf20040930_0110_db035.htm) (quoting Kelly D. Brownell, director of Yale University’s Center for Eating & Weight

during shows for which children eight and under make up the majority of the audience that the APA recommends<sup>210</sup> is probably not a politically viable option at this time. Also, such a ban would give broadcasters little incentive to air any more programming for children than the three-hour minimum required by the FCC.

The suggestions for modified regulations set forth in this Note would not unduly burden companies, advertisers, or broadcasters. The suggested restrictions on commercial speech are not total bans on commercial speech directed at children. Instead, they leave advertisers free to direct truthful, nonmisleading commercial speech at children.<sup>211</sup> Companies could still produce whatever legal products they choose and promote them to children. But, they would have to increase their disclosure of truthful information about these products and communicate the information in a manner that children can understand. Advertisers would have to modify the methods that they use to promote these products, but inventing new advertising techniques is already a fundamental part of the advertising business. Broadcasters could still air commercials during children's programming in order to earn the revenue necessary to continue producing the programming that the FCC feels benefits children. In fact, the restrictions proposed here would make broadcasters' jobs easier in some respects as they would not have to conform to rigid time restrictions on commercial material or face penalties for inadvertent placements of ads. Also, the concept of host-selling would disappear with the ban on celebrities or cartoon characters in ads aimed at children.<sup>212</sup> In all, these proposed modifications to the CTA should not increase the burden on advertisers or broadcasters, and should decrease the amount of misleading commercial speech directed at children.

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Disorders).

210. APA TASK FORCE, *supra* note 23, at 22–23.

211. The Court has expressed its objection to complete bans on a type of commercial speech, noting that such bans “are particularly dangerous because they all but foreclose alternative means of disseminating certain information.” 44 *Liquormart*, 517 U.S. at 501.

212. Eliminating celebrities and cartoon characters from commercials aimed at children would make it impossible for a commercial to contain a character from a children's show.

## BOOK REVIEW

### A Practitioner's View of Broadcaster Power

*Speak Softly and Carry a Big Stick: How Local TV Broadcasters Exert Political Power*, J. H. Snider, New York: iUniverse, Inc. 2005, 592 pages.

Andrew J. Siegel\*

For the past eighteen years, I have worked for CBS. My current title is Assistant General Counsel, and I represent the CBS-owned television stations. As such, I was fascinated by the title of J. H. Snider's *Speak Softly and Carry a Big Stick: How Local TV Broadcasters Exert Political Power*.<sup>1</sup> Since on a daily basis I represent our local TV stations, I was curious about Dr. Snider's views.

What I learned is that *Speak Softly* is an attack on Congress' award of a second channel to broadcasters for high definition television in the Telecommunications Act of 1996 ("1996 Act"). Dr. Snider makes no secret of his disdain for this spectrum award: "I lamented that broadcast TV—whether in high or standard definition—was a gross misuse of spectrum and that it would be much better used for either mobile higher powered licensed services or lower powered unlicensed services."<sup>2</sup>

According to Dr. Snider, the spectrum award was not in the public interest.<sup>3</sup> Therefore, he concludes that the only reason broadcasters received this additional spectrum must have been because Congress was

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\*Assistant General Counsel, CBS Corporation. The views expressed herein are solely the Author's.

1. J. H. SNIDER, *SPEAK SOFTLY AND CARRY A BIG STICK: HOW LOCAL TV BROADCASTERS EXERT POLITICAL POWER* (2005).

2. *Id.* at xix–xx (citations omitted). Throughout *Speak Softly*, the author has a habit of citing to earlier articles he wrote to support positions that he takes. This brings to mind the adage about a lawyer who is his own client.

3. Dr. Snider even titled Part II of *Speak Softly*, which makes up the majority of the book, "Case Study: The Great Spectrum Giveaway."

afraid of the broadcasters.<sup>4</sup> *Speak Softly* consists of Dr. Snider's attempts to find support for his conclusions.

*Speak Softly* is divided into three parts. In the first part, Dr. Snider examines the relationship between local TV broadcasters, the viewing public, and politicians. He uses a political science model of principal-agent theory. Using this model, Dr. Snider posits that the viewing public is the principal, broadcasters are the agents, and politicians are the targets that broadcasters are supposed to be watching.<sup>5</sup> Dr. Snider contends that agents occasionally have interests that conflict with the interests of their principals. The agents then have to hide their conflicting interests from their principals. *Speak Softly* examines different theoretical interests, types of conflicts, and relationships.

In the second part of *Speak Softly*, Dr. Snider attempts to apply the theories discussed in Part I to explain why broadcasters received additional spectrum for high-definition television. Dr. Snider theorizes that if the principal/public had known that its agents/local broadcasters were trying to get this additional spectrum, the public would have wanted to make a profit off of the deal and would not have just given it away. This becomes Dr. Snider's conflict for purposes of his principal-agent theory. As a result, *Speak Softly* claims local broadcasters hid their desire for the spectrum. The broadcasters went to the party it was supposed to be watching—the politicians—to get the spectrum. For reasons unknown, the politicians were afraid of the broadcasters and gave them the spectrum they wanted behind the public's back.

The final part of *Speak Softly* contains Dr. Snider's proposed resolution to his perceived principal-agent conflict, among other things.

A major problem with Dr. Snider's theory is that *Speak Softly* offers no proof that politicians were afraid of broadcasters. *Speak Softly* calls the politicians' fear of broadcasters "the Allegation—the alleged link between broadcaster control of news and broadcaster political power regarding telecommunications policy."<sup>6</sup> In other words, broadcasters can report negative stories on politicians, so politicians do not want to upset broadcasters.<sup>7</sup>

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4. *Id.* at 203.

5. *Id.* at 5.

6. *Id.* at 234. *See also id.* at 202–03.

7. This fear of negative coverage presupposes that politicians have done something to warrant a negative story since even Dr. Snider does not contend that broadcasters broadcast false news reports. If Dr. Snider believes that all politicians have such skeletons in their closets, his opinion does not reflect well on politicians. Also, it would seem to have to be a very serious skeleton to warrant voters remembering it at election time.

In support of the Allegation, *Speak Softly* offers one anecdote and unsupported assertions that politicians' fear of broadcasters exists. The anecdote involves a letter given to Senator Bob Dole by Nick Evans, a broadcaster in Senator Dole's state, during the debate about awarding additional spectrum to broadcasters as part of the 1996 Act. The letter threatened to tell viewers that Senator Dole's plan to auction the additional spectrum to broadcasters would destroy free over-the-air television. Senator Dole eventually backed down from his plan and the 1996 Act passed. As *Speak Softly* notes, it is not clear what the threat was in the Evans letter,<sup>8</sup> and it may have been an insignificant factor in Senator Dole's decision.<sup>9</sup>

In addition to the anecdote above, *Speak Softly* next tries to find circumstantial evidence that politicians are afraid of broadcasters. Among others, Dr. Snider presents the following unsourced analogies: "Human [sic] don't walk into the cages of lions because they know they would be eaten alive. Similarly, members of Congress may not poke sticks into the eyes of their local TV broadcasters out of fear that they, too, would be eaten alive."<sup>10</sup> Similarly:

During my interviews regarding the Telecom Act of 1996, when I would hear somebody make the Allegation, I would ask: "do you have any hard evidence?" In response, the interviewee would often look at me as though I were an idiot (some even expressed open contempt) because the question revealed to them that I understood nothing about politics or human life. They felt that the threat of broadcaster news bias was obvious but that no broadcaster would be stupid enough to provide me with a verifiable case study.<sup>11</sup>

However, Dr. Snider acknowledges that he has no proof that politicians have any such fear: "The lack of concrete and verifiable evidence to back up the Allegation was also one of the most noteworthy features of my interview feedback."<sup>12</sup>

Another curious postulation in *Speak Softly* is that the public did not know about the broadcasters' desire for additional spectrum. However, this claim is belied by the sheer number of news reports that objected to the broadcasters' spectrum desire, as cited in the book. These included editorials in the *Wall Street Journal* and *New York Times*;<sup>13</sup> articles on the subject in newspapers including the *Washington Post*, the *San Diego*

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8. SNIDER, *supra* note 1, at 471.

9. *Id.* at 472. That does not stop Dr. Snider from saying without support: "It is reasonable to think he took the Evans letter seriously."

10. *Id.* at 114.

11. *Id.* at 251 (emphasis added).

12. *Id.*

13. SNIDER, *supra* note 1, at 99.

*Union-Tribune* and even the *Associated Press*;<sup>14</sup> articles in magazines including *The Nation*, *The New Republic*, and *Wired*;<sup>15</sup> and even reports on CBS<sup>16</sup> and on ABC's *Nightline*.<sup>17</sup> I do not know if all of these articles and reports treated the spectrum proposals with equal depth, but the volume alone indicates that the issue was available for the public to scrutinize.

Another troubling issue in *Speak Softly* is its misuse of quotations. There are two instances of individuals being quoted for a proposition, only to indicate in a footnote that the quotation had nothing to do with the propositions. For example, in discussing the valuation of the spectrum sought by broadcasters, *Speak Softly* offers the following Al Franken quotation: "The sad thing is all the members of Congress who were lied to. . . . For some reason, it doesn't seem to bother them. I don't know. Maybe they want to make sure they can get on TV."<sup>18</sup>

The problem is that the footnote accompanying this citation states the following: "Franken's comment was about the 1995 fight over fin-syn but is equally applicable to the spectrum giveaway, which happened at almost the same time."<sup>19</sup>

So if readers do not read all the way through the footnote, they would not know that Franken was not discussing valuation—the quotation had nothing to do with the issue being discussed. *Speak Softly* similarly uses a quotation from Jim Goodmon of Capitol Broadcasting on one subject to support a premise it did not apply to,<sup>20</sup> but objects to the National Association of Broadcasters putting together two separate events and showing them as one.<sup>21</sup>

Moreover, given the extensive footnoting contained in *Speak Softly*, Dr. Snider adopts a troubling number of positions with limited support or no support whatsoever. Dr. Snider claims neither experience working for local television stations on the management side nor employment in a newsroom.<sup>22</sup> This does not stop him from discussing the dynamic between news departments and management—belittling the firewall separating local

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14. *Id.* at 221–23.

15. *Id.* at 226–29.

16. *Id.* at 99.

17. *Id.* at 230–31.

18. SNIDER, *supra* note 1, at 307.

19. *Id.*

20. *Id.* at 349.

21. *See id.* at 376.

22. Dr. Snider does claim journalism experience by osmosis, as he says: "I have also looked at the press through the eyes of journalists. Over the years, I have been a member of the Society of Professional Journalists, The Radio-Television News Directors Association, the National Press Club and the Authors Guild. I am married to a former journalist." *Id.* at xxv.



television station newsrooms from sales departments—without any support.<sup>23</sup> *Speak Softly* also repeatedly claims that newsrooms hire private detectives to do dishonest things to get stories so that the stations can claim they knew nothing about this practice. There are no examples provided of this behavior—only citations to three 1999 articles written by the same author in the *New York Times*.<sup>24</sup>

*Speak Softly* at times confuses its subject matter. It discusses malfeasance by print journalists to support the proposition that local TV reporters are not committed to “journalistic norms of truth-telling.”<sup>25</sup> Then, it discusses the violation of journalistic ethics of faking events—and uses as an example inserting virtual ads in sporting events.<sup>26</sup> What is the connection between what happens in a stadium and a newsroom? *Speak Softly* does not provide an answer. Additionally, *Speak Softly* purports to be about the power of local broadcasters—but the book focuses on the lobbying prowess of the National Association of Broadcasters, not individual TV stations. *Speak Softly* also uses 20/20 hindsight. It criticizes decisions made in 1996 based on technology that would allow a different result today, but not available then,<sup>27</sup> and complains that cost estimates in 1996 were higher than the costs are today.<sup>28</sup>

In the final part of *Speak Softly*, consistent with Dr. Snider’s views on broadcast television use of the spectrum, *Speak Softly* proposes that broadcasters completely give up their entire spectrum.<sup>29</sup> Broadcasters should do this because Dr. Snider believes that “The future of TV is TV delivered over the Internet.”<sup>30</sup> Among other benefits cited by *Speak Softly*, giving up their spectrum would save millions of neotropical birds killed each year by broadcast towers.<sup>31</sup> *Speak Softly* also wants the FCC to get out of the spectrum management business with anyone allowed to broadcast. Interference would be handled by each consumer’s equipment. Dr. Snider states:

If a consumer buys a TV set that is too dumb to coordinate sharing the broadcast band underlay with other devices within the home, the

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23. For example, “In reality, however, general managers often act like news directors and news directors as general managers, so the precise placement of the ethics firewall, when defined in terms of persons, rather than functions, is ambiguous.” SNIDER, *supra* note 1, at 355. See also *id.* at 359, 361–62.

24. See *id.* at 127, 140, 176, 375.

25. *Id.* at 373–75.

26. *Id.* at 375.

27. See, e.g., SNIDER, *supra* note 1, at 309, 317.

28. *Id.* at 336–37.

29. *Id.* at 514.

30. *Id.* at 515.

31. *Id.* at 516.

conflict is not for the FCC to decide by, as the broadcasters demand, banning anything<sup>32</sup> but a TV set from using the broadcast underlay within the home.

*Speak Softly* also proposes that broadcasters give up their analog channel within eighteen months because that was the schedule used in Berlin, Germany.<sup>33</sup> *Speak Softly* notes that the German government subsidized the purchase of analog converter boxes for low-income consumers, but does not indicate how many people this applied to or what the cost of the subsidy was. Given the comparative size of the German and United States populations, omitting these numbers is somewhat disingenuous. Finally, *Speak Softly* proposes that broadcasters publish their ethics codes on the Web, including, among other things, detailing their agency relationship with the public, having the codes signed by management, acknowledging that conflicts exist, and giving auditing rights to outside parties.

The final chapter of *Speak Softly* contains one other major proposal. Dr. Snider proposes the creation of a “Committee on Candidate Information and Elections.” This “Citizens’ Committee” would be made up of 500 randomly selected voters, under the age of 66, who would have the power “to propose legislation that would go directly to the floors of the House and Senate for a vote.”<sup>34</sup> The Citizens’ Committee would also have the power to approve candidates for governmental agencies nominated by the President, such as the Federal Election Commission, subject to Senate approval, or even nominate candidates itself—although it would have to use search firms to do so.<sup>35</sup> The Citizens’ Committee would also have to turn to outside parties, such as foundations and think tanks, to actually draft legislation.<sup>36</sup>

To this book’s credit, the principals (readers) who read *Speak Softly* will have no doubt where their agent (the book) stands. *Speak Softly* objects to broadcasters receiving additional spectrum. Perhaps there is an academic market for *Speak Softly*, but its claims as to what occurs at local television stations do not match what this Review Author sees on a daily basis. That may not be true at other local television stations, but *Speak Softly* provides no proof to the contrary. From the standpoint of this practicing member of the Communications Bar, *Speak Softly* is of little use.

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32. SNIDER, *supra* note 1, at 512.

33. *Id.* at 513.

34. *Id.* at 505.

35. *Id.* at 506.

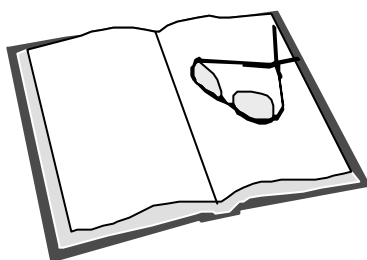
36. *Id.* at 507. Coincidentally, Dr. Snider notes in his preface that he is employed by the New America Foundation, a Washington think tank, as a Senior Research Fellow.

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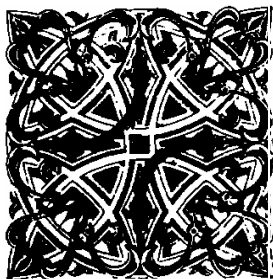


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