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Shovel-ready broadband stimulus
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By Thomas W. Hazlett

Plagued with the sharpest economic downturn in a generation, US policy makers scrolled through a series of emergency deficit-enhancement measures in 2008-09. The third and final such effort was enacted in February. At $800bn, it set a new standard for government red ink: 12 per cent of 2009 GDP - twice the previous post-World War II high.

The theory is that, by sweeping unemployed resources into the marketplace, society not only gets a bargain, it bucks up consumers and investors, instilling confidence. And don't forget this stimulation: emergency spending projects are to Congress what free beer is to a college fraternity party.

Markets are yet to feel the buzz, but what society will be getting is, in some instances, already visible. Consider the $7.2bn subsidy spread across the Broadband Technology Opportunities Act (Department of Commerce) and the American Recovery and Investment Act (Department of Agriculture), monies to fund up to 80 per cent of the cost of building private high-speed data networks in "unserved" and "underserved" areas.

As much as it hurts me to say this about programs with such well-polled names, neither program will achieve what it advertises for the US economy. They do offer real hope, however, that the recession will soon be over for communications lawyers and shareholders of ridiculously inefficient rural telephone companies.

In macro-economic terms, meanwhile, the "broadband stimulus" may be perverse: firms that had been building rural broadband networks have reportedly halted operations, circling back to Washington. In March, industry consultant Joseph Upton noted that rural phone carriers were "paralysed," unsure how to play the subsidy game. "One CEO told me that she had six previous quarters of 25 per cent growth in a company that had been on the skids," wrote Upton, "but the minute the stimulus word came out, all business just stopped."

Former Commerce Department official Larry Irving, an advisor to the Obama Administration, explains that, "If a project was planned but not yet funded, then it would qualify" for federal dollars. If private funds were already committed, it's too late.

Sounds exactly right. The goal here is not to replace private investments, but to leverage and expand them. But God created Washington lawyers for a reason, and this is a perfect reason. A "funded" project can easily become "unfunded," rising again with new plans, technologies, owners and contractors - and eligible for millions of dollars. The emergency now is not to build broadband networks, but to attend meetings and schmooze government officials.

Ultimately, the $7.2bn will be awarded in "beauty contests," where bureaucrats examine competing proposals - say, a plan to distribute satellite broadband receivers to 600 native Americans on a remote reservation in Arizona, versus a fibre optic loop connecting a hospital in rural Arkansas with the University of Arkansas Medical School - and make their picks based on their values, mood, and whim. A group of 71 economists expert in telecommunications policy, including two Nobel Laureates (and this author), have urged a different approach, "reverse auctions." The government would state its performance criteria and then take bids, selecting the lowest price offers.

The proposal has only a remote chance of being adopted because it is both transparent and economical. Having to make goals objective and explicit takes the discretionary political fun away. And assigning rights by competitive bidding is like having that fraternity party without any beer at all.

While sold as an emergency injection of "shovel ready" projects, beauty contests take time. And broadband - which the government has trouble defining, let alone funding - demands planning. So the FCC has launched a proceeding to determine what broadband is, where networks exist, and how we need to boost them. This inquiry hopes to wrap up by February 2010. Quick for a regulatory commission, but that deadline misses the "stimulus" train. So billions will be spent - policy makers hope - before the actual plan ever arrives.

Of course, planning is often over-rated. The US already spends $7bn every year on subsidies for "universal service" in the telephone business. As Robert Crandall of the Brookings Institution writes: "There is no evidence that the existing subsidies reduce traditional voice telephone rates or increase telephone subscriptions." Instead, some 900 small, inefficient rural telephone companies work the "cost-plus" system. I found, in a 2006 study, that carriers were awarded incredibly rich federal pay-outs - as much as $13,345 per line per year, as in the case of a Hawaiian telco operator - many multiples of the cost of competitive, unsubsidized cellular or satellite phone service.

An audit released by the FCC Inspector General late last year found that 23.3 per cent of the subsidy payments made directly to phone companies were "erroneous." That adds up to about $1bn per year in documented waste, fraud, or abuse. And this in a program set-up in 1996, not facing any emergency, and not stimulating anything but the grease industry - now a growing service business in the "stimulus" sector.

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