Netheads are Looking to Take a Byte out of Telephone Callers
by Andrew Brod
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It's an economist's maxim that there's no such thing as a free lunch, that somehow nice things must be paid for by someone. But the allure of a free lunch is a powerful one. Two recent examples come to mind.

The first example is the growing discontent over the way Internet service providers (ISPs) and local phone companies charge for access to the Internet.

Phone companies tend to charge a set monthly fee for local calls, in part because it's quite costly to monitor a large number of short calls. Economic theory predicts that local callers will have no incentive to economize when they call locally, but while true, this hasn't really mattered because, aside from teenagers, most people don't seem to want long local calls.

But then came Internet, giving some local callers a reason to spend significantly more time on the phone. While the average voice phone call takes from two to five minutes, the average call to an ISP takes nearly 20 minutes.

In addition, Internet phone calls are not spread through the day, but tend to cluster in the early evening, a time of heavy phone calling as well. At first, the per-minute charges levied by most ISPs induced economizing behavior: There was good reason to disconnect from the Internet when each additional chunk of time had a price attached. Then a few ISPs changed their pricing, allowing unlimited access at a monthly rate. Soon, in a headline-generating move, ISP giant America Online (AOL) followed suit with its own flat per-month rate.

With monthly fees charged by local phone companies and many ISPs, Internet users now have no economic incentive to restrict Internet usage, and this means no incentive to restrict the length of their local phone calls to ISPs.

As more people call their ISPs, they're taking much longer to get off the line, thereby congesting local phone systems that were designed for brief voice transmissions.

It's local phone congestion that is causing the most worry now because ISPs either already have sufficient capacity to handle the longer calls, or, like AOL, are working on it. The access issue has been thrown by ISPs into the laps of local phone companies.

If ISPs continue to charge by the month, then to ensure good local service and access, local phone companies will need to invest in greater capacity. Who should pay?

One possibility is to have those causing congestion pay for the upgrades. Many cities have express traffic lanes for commuting cars with two or more people in them. This implicitly levies a penalty (in terms of increased travel time) on those single-person cars

causing most of the congestion problems.

A per-minute fee for Internet phone calls would work similarly, and those who use the phone for an average of two minutes wouldn't have to help pay for those long Internet calls.

The fee would also provide an incentive to Internet users to economize on call time: no more hours-long connections maintained to get online stock quotes every 15 minutes or to "save one's place" at the Internet trough.

Many Internet users don't like this idea, of course. But if phone companies finance the improvements with a general rate hike, everyone would be paying.

Nonusers (including little old ladies!) would be partially subsidizing users, a free lunch any heavy Nethead is bound to like.

What about forcing the phone company to finance the upgrades itself?

This is no different, given the regulation to which such companies are subject. If the rate of return to phone company investors falls too low as a result of upgrading expenses, public utility commissions are likely to authorize a rate hike anyway. Either way, the result would be a broad-based subsidy that would leave no incentive to discipline one's use of a public resource.

A second, briefer, example of free lunches in the news involves the recent decision by the city of Greensboro to annex 6,200 acres of land just northwest of the city.

People just outside the city pay lower county taxes and pay private providers for many services, but they benefit from having Greensboro so close by. Many of those people work in the city, see movies in the city, go to restaurants in the city, and so on. Why shouldn't they help pay for upkeep of the roads, parks and other amenities they use?

Of course, they'd prefer to have their share paid by Greensboro residents, just as Internet users would prefer to have some of their Internet access costs paid by little old ladies.

But each group is just looking for that free lunch.