FEDERAL TELECOMMUNICATIONS LAW:

A LEGISLATIVE HISTORY OF

THE TELECOMMUNICATIONS ACT OF 1996

PUB. L. NO. 104-104, 110 STAT. 56 (1996)

INCLUDING

THE COMMUNICATIONS DECENCY ACT

Volume 10
Document Number
174

BY

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INTRODUCTION

AN OVERVIEW OF THE TELECOMMUNICATIONS ACT OF 1996

The "Telecommunications Act of 1996," signed into law on February 8, 1996, opens up competition between local telephone companies, long-distance providers, and cable companies; expands the reach of advanced telecommunications services to schools, libraries, and hospitals; and requires the use of the new V-chip technology to enable families to exercise greater control over the television programming that comes into their homes. This Act lays the foundation for the investment and development that will ultimately create a national information superhighway to serve both the private sector and the public interest.

President Clinton noted that the Act will continue the efforts of his administration in ensuring that the American public has access to many different sources of news and information in their communities. The Act increases, from 25 to 35 percent, the cap on the national audience that television stations owned by one person or entity can reach. This cap will prevent a single broadcast group owner from dominating the national media market.

Rates for cable programming services and equipment used solely to receive such services will, in general, be deregulated in about three years. Cable rates will be deregulated more quickly in communities where a phone company offers programming to a comparable number of households, providing effective competition to the cable operator. In such circumstances, consumers will be protected from price hikes because the cable system faces real competition.

This Act also makes it possible for the regional Bell companies to offer long-distance service, provided that, in the judgment of the Federal Communications Commission (FCC), they have opened up their local networks to competitors such as long-distance companies, cable operators, and others. In order to protect the public, the FCC must evaluate any application for entry into the long-distance business in light of its public interest test, which gives the FCC discretion to consider a broad range of issues, such as the adequacy of interconnection arrangements to permit vigorous competition. Furthermore, in deciding whether to grant the application of a regional Bell company to offer long-distance service, the FCC must accord "substantial

weight" to the views of the Attorney General. This special legal standard ensures that the FCC and the courts will accord full weight to the special competition expertise of the Justice Department's Antitrust Division--especially its expertise in making predictive judgments about the effect that entry by a bell company into long-distance may have on competition in local and long-distance markets.

Title V of the Act is entitled the "Communications Decency Act of 1996." This section is specifically aimed at curtailing the communication of violent and indecent material. The Act requires new televisions to be outfitted with the V-chip, a measure which President Clinton said, "will empower families to choose the kind of programming suitable for their children." The V-chip provision relies on the broadcast networks to produce a rating system and to implement the system in a manner compatible with V-chip technology. By relying on the television industry to establish and implement the ratings, the Act serves the interest of the families without infringing upon the First Amendment rights of the television programmers and producers.

President Clinton signed this Act into law in an effort to strengthen the economy, society, families, and democracy. It promotes competition as the key to opening new markets and new opportunities. This Act will enable us to ride safely into the twenty-first century on the information superhighway.

We wish to acknowledge the contribution of Loris Zeppieri, a third year law student, who helped in gathering these materials.

Bernard D. Reams, Jr.
William H. Manz

St. John's University
School of Law
Jamaica, New York
April 1997

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COMPETITIVE STATUS OF THE BELL OPERATING COMPANIES

HEARING

BEFORE THE

SUBCOMMITTEE ON TELECOMMUNICATIONS, CONSUMER PROTECTION, AND FINANCE

OF THE

COMMITTEE ON ENERGY AND COMMERCE HOUSE OF REPRESENTATIVES

NINETY-NINTH CONGRESS

SECOND SESSION

ON

H.R. 3687 and H.R. 3800

BILLS TO PERMIT THE BELL OPERATING COMPANIES TO PROVIDE INFORMATION SERVICES AND TO MANUFACTURE TELECOMMUNICATIONS EQUIPMENT SO LONG AS SUCH SERVICES AND MANUFACTURING ARE NOT SUBSIDIZED WITH THE PROCEEDS FROM THE PROVISION OF LOCAL EXCHANGE TELEPHONE SERVICE OR OTHER REGULATED TELECOMMUNICATIONS SERVICES AND REGULATION BY THE FEDERAL COMMUNICATIONS COMMISSION

MARCH 13, 1986

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COMPETITIVE STATUS OF THE BELL OPERATING COMPANIES

THURSDAY, MARCH 13, 1986

HOUSE OF REPRESENTATIVES,
COMMITTEE ON ENERGY AND COMMERCE,
SUBCOMMITTEE ON TELECOMMUNICATIONS,
CONSUMER PROTECTION, AND FINANCE,
Washington, DC.

The subcommittee met, pursuant to notice, at 9:40 a.m., in room 2123, Rayburn House Office Building, Hon. Timothy E. Wirth (chairman) presiding.

Mr. WIRTH. The subcommittee will please come to order. Today the subcommittee is holding a hearing on what has become one of the most heavily talked about issues since the breakup of AT&T, and that is the competitive status of the Bell Operating Companies and their efforts to diversify into new markets from which they are presently barred.

The efforts to overturn the restrictions contained in the AT&T antitrust decree, otherwise known as the modified final judgment or the MFJ, which prohibits the local telephone companies from providing information services, manufacturing equipment, or offering long distance service, has already taken on many new dimensions. It has been featured on the covers of several national magazines, and it has certainly generated a great deal of business for those who conduct telecommunications seminars.

Armies of analysts have flooded the financial community with forecasts on the baby Bells and how the MFJ restrictions affect their investment appeal. Today, however, our focus will be a bit different.

Just as our hearings 3 weeks ago on the FCC's regulatory policies focused on how consumers are faring, our primary focus today is how freeing the BOC's from the restrictions imposed by the divestiture agreement would affect consumers. We must focus this morning not only on the general issue of why these restrictions might well be lifted but also on how, in allowing the BOC's to enter new markets, their ratepayers can be protected from having their phone bills subsidize the provision of new services, services that some argue will only benefit large businesses.

In sum, the subcommittee must closely examine how the local telephone companies' expansion into new markets will affect local rates.

This is not a new issue for the subcommittee. This subcommittee has consistently advocated the benefits of competition and the tech-

nological innovation that flows from it. In addition, we have continually sought to protect the financial viability of the local telephone companies upon which most Americans rely for their daily telephone needs.

After the divestiture agreement was announced by AT&T and the Justice Department, the subcommittee held hearings on how the Bell Operating Companies would be affected by divestiture, with a special emphasis on making sure that the local telephone companies would not be unfairly treated or wither away.

The subcommittee went on unanimously to approve legislation which contained several provisions intended to protect the viability of local telephone companies, and thus help to hold down local telephone rates.

The subcommittee has another related tradition in this area, a tradition of promoting competition through encouraging open entry and the removal of legal and regulatory barriers which impede technological innovation and the introduction of new services to the public. We have long been guided by the idea that if a company can invent a better process or product, whether it's a mousetrap or a modem, why should it be forbidden from offering it?

Keeping in mind this long tradition of concern for the financial viability of the BOC's, as well as our support for a policy of open entry and technological innovation, the proper framework for analyzing the MFJ restrictions on the local telephone companies falls quickly into place. I believe our analysis of this question must be guided by placing a heavy burden on those who argue that denying the BOC's entry into new markets is in the public interest.

The question should not be why let them enter these markets, but instead we should ask, why should the BOC's not be allowed to compete and offer new services? Those who want to continue to prohibit the BOC's from offering information services, it seems to me, must demonstrate why such restrictions are justified.

One market where there has been general consensus that AT&T and the BOC's should be barred from entering is the area of electronic publishing. I have long felt that when it comes to the provision of information content, we must protect and promote the first amendment goal of encouraging the widest possible diversity of information sources. Allowing a telephone company to offer electronic publishing services over its own dominant transmission facilities could undermine this principle, given the phone company's incentive and ability to discriminate against competing providers of information services.

The free flow of information to the public is simply too important for us to take that risk.

It has been, and continues to be, my belief that the public interest is best served by allowing companies to compete freely, and by encouraging them to offer new and innovative services that the public might not otherwise receive.

Further, we must not limit our review to the question of whether or not to allow the BOC's into new areas currently placed off-limits. We must take the analysis one important step further.

The AT&T divestiture was reached in a way that was very insensitive to consumers' needs. The agreement struck between AT&T and the Justice Department was guided largely by antitrust con-

cerns and in many ways disregarded the concerns of the average telephone consumer. We cannot allow that mistake to be made again.

Therefore, today we must ask two critical questions. First, will allowing the BOC's to diversify benefit local ratepayers; and, second, if it cannot be demonstrated that ratepayers will directly benefit, will local ratepayers at least not be harmed by the entry of the BOCs into these fields?

Just as the burden is clearly on those who would oppose lifting the MFJ restrictions, the burden of developing clear procedures to protect the ratepayer and competition rests on those who seek to lift these restrictions.

Underlying all of these issues is the basic question of how communications policy is made and who should make it. The Federal courts, through the interpretation of an antitrust agreement, is not the proper forum for making critical decisions that affect the future of our Nation's telecommunications industry.

Congress, through the FCC, is the proper place for the formulation of communications policy, so that our overriding objective, universal telephone service at affordable costs for all Americans, is achieved. The major problem, however, is that many of us have lost faith in the FCC as an agency truly concerned about the average consumer's pocketbook when it comes to the cost of telephone service.

Consequently, as we face the crucial question of how to protect ratepayers, it is not enough to leave all the answers to the FCC.

We have a number of distinguished panels today to help us sort through these complicated issues that we face. We welcome all of them. Before turning to our first panel, I would ask members if they have opening statements they might make.

Mr. Rinaldo.

Mr. RINALDO. Thank you, Mr. Chairman. Mr. Chairman, I want to commend you for scheduling this hearing today which will in effect really examine the competitive status of the Bell Operating Companies.

As someone who has served on this subcommittee throughout the transition period from a monopoly to competition, I think it's helpful for us to look at the Bell Operating Companies to determine how well they are doing in the newly competitive environment. In my own view, the subcommittee should pay particular attention to this aspect of telecommunications policy.

The fact of the matter is that the long range health of the BOC's will have a direct impact on residential rates and local ratepayers. I think all members of the subcommittee agree that local ratepayers should continue to have access to an efficient and affordable telephone system.

If we want such a system, we have to ensure that the BOC's remain healthy, strong and able to participate in technological developments and progress in the telecommunications field. I think it is clear that the BOC's want to participate in this progress, and it is clear that public policy supports that point of view.

Right now, there are numerous requests for waivers before the court. The FCC is looking at the structural separation requirements set down by Computer II and has opened the new Computer

III inquiry. Moreover, the Department of Justice will issue a report next year that will provide us a broad perspective on some of the issues we are examining today.

The fact of the matter is that we are only at the beginning of a new era. I have no doubt we will continue to experience growing pains in the wake of divestiture. But right now, all indications are that the BOC's are healthy.

We are seeing greater competition in the long distance market. The court has granted a number of waivers to BOC's to enter new fields.

It's entirely appropriate, however, at this time for the subcommittee to oversee these developments and to ensure that the transition to competition occurs without any major difficulties. With that perspective in mind, I want to welcome our witnesses and particularly Rodney Joyce who served so well on this side of the table prior to his most recent assignment, and express my appreciation to them for the testimony that they will share with us today.

Thank you, Mr. Chairman.

Mr. WIRTH. Thank you. Mr. Leland.

Mr. LELAND. Thank you, Mr. Chairman. I welcome the opportunity to examine the—to examine and discuss the competitive status of the Bell Operating Companies.

It is becoming increasingly clear that there is growing interest in this issue. I must confess that while I have an open mind on this issue, there are some problems that must be addressed before I could support lifting the business restrictions on the Bell Operating Companies.

There is evidence or the potential for substantial benefits to the consumer if the Bell Operating Companies are allowed into some presently proscribed activities. I recognize, however, that there are some very serious issues that would tend to mitigate against freeing the Bell Seven.

First and foremost, we must consider whether the Bell Operating Companies are fulfilling their commitment to the local ratepayer. We also must consider whether the local residential ratepayer who wants and needs only basic telephone service will benefit from lifting the modified final judgment restrictions.

In other words, Mr. Chairman, we must ensure that the ratepayers, not just the stockholders, share in the benefits.

In hearings held earlier this year, this subcommittee determined that millions of Americans presently are without telephone service. While I have heard a great deal of discussion from the Bell Operating Companies about their desire to lift the MFJ, they have demonstrated comparatively little interest in discussing and, more importantly, in implementing a national life line telephone service program.

As I've stated previously, I believe the new revenues that might be derived from new business activities of the BOC's should be considered as potential sources of funding for a life line service program. I look forward to the response of the BOC's to this issue.

In private discussions with representatives of the Bell Companies, Mr. Chairman, I have raised two other issues I believe we should discuss today. Organized labor has played a predominant

role in building the great communications network we have today. They deserve to share in the future of this industry.

While I recognize that many of the issues in this area are the subject of ongoing private negotiations, I do want to express my concern, and the concern of many of my colleagues, that this issue be dealt with fairly and expeditiously.

Finally, Mr. Chairman, I hope this subcommittee will look closely at the issue of opportunities for socially and economically disadvantaged Americans in the common carrier industry. The level of participation of women and minority Americans in the common carrier industries is shamefully, shamefully, low, particularly in the area of entrepreneurial activities.

If legislation relating to new business opportunities for the BOC's moves, or begins to move, in this subcommittee, I will offer an amendment encouraging the Bell Operating Companies and their affiliates to joint venture with and subcontract to socially and economically disadvantaged companies. This language would refer to both manufacturing and information service activities.

While at this time I do not believe that a numerical set-aside is necessary, it is evident that the industry needs to be encouraged in this area.

Mr. Chairman, I regret that I cannot stay for the entire hearing. I have to chair a Postal Operations Subcommittee hearing. And I also have to attend a joint Energy Subcommittee hearing concerning the oil crisis and oil import fees. Issues that are very important to my constituents in Houston.

Before leaving, however, Mr. Chairman, I want to commend you for holding these very important hearings. I look forward to reviewing the transcript of today's proceedings.

I, too, would like to extend my welcome to the witnesses and particularly Rodney Joyce, who has worked with us so well in the past.

Thank you, Mr. Chairman.

Mr. WIRTH. Thank you. Mr. Tauke.

Mr. TAUKE. Thank you, Mr. Chairman. Mr. Chairman, I, too, thank you for calling these hearings to examine what is obviously a very important set of issues relating to the operation of our telecommunications network in the Nation.

Over the last several years, this subcommittee and Congress, as a whole, has played a role in the formulation of telecommunications policy. But generally that role has been one of providing pressure upon other agencies of government and the court system, and in that way influencing policy.

Part of the question that we face today is not only what should our policy be but who should make the policy. Should we continue to allow the policies that are governing the telecommunications system be established by the courts? Or, is it appropriate for those of us who have a broader array of issues to consider in the development of policy, issues other than antitrust considerations, to make those policies?

Obviously, a large number of the Members of Congress are interested in seeing Congress play a role in developing policy. As of this morning, 105 Members of the House of Representatives are cosponsoring H.R. 3800, the legislation I introduced along with Congress-

man Swift, which does permit the Bell Operating Companies to offer enhanced information services and to provide, or to enter into, the manufacturing of telecommunications equipment.

It seems to me that today during this hearing we have an opportunity to look at the kinds of policies that this subcommittee should recommend to the Congress. In doing so, I am hopeful that we will reach the conclusion that the kinds of policies recommended in H.R. 3800 are indeed policies that will serve the consumers well, that will enhance the trade situation of the United States, and will improve the Nation's telephone network and telephone system.

It seems to me very clear that H.R. 3800 and the policies it embraces are good for consumers and good especially for consumers in rural America. As Mr. Rinaldo, my colleague from New Jersey, indicated in his opening statement, the health of the Bell Operating Companies is critical for the future of communications services at a reasonable cost to consumers. That, in effect, is our goal, to provide the widest possible array of telecommunications services to consumers and to provide those services at the lowest possible prices.

The fact is that in many parts of the country, those services will not be offered if the Bell Operating Companies are unable to provide those services. If we are going to provide the health services, the message services, and the various other enhanced information services that technology now permits to many consumers in America, we must permit the Bell Operating Companies to offer those services.

But it isn't just the provision of services that is important. It's also the future of the telecommunications network and what that will mean for the cost of basic telephone service for individuals. If the Bell Operating Companies are only permitted to offer services in a defined monopoly, a monopoly which is ever shrinking and which is under attack from many other players in the telecommunications field, then the future of the Bell Operating Companies is not very bright. In fact, the future of the consumers who are served by the Bell Operating Companies is also very cloudy, because if the Bell Operating Companies are going to watch their business shrink, the only way that they can hold up their revenues and support the infrastructure of the system is to raise rates.

So, part of the effort to serve consumers is to ensure that the Bell Operating Companies themselves are healthy. But beyond that, obviously if the Bell Operating Companies are offering other services that will share in the joint and common costs, that also is going to lower the cost of basic telephone service for consumers.

This issue of consumer protection obviously is one that needs to be examined carefully during the hearings. We must figure out how we are going to be able to provide these kinds of new services and at the same time ensure that there is no cross-subsidy from the monopoly segment of the business to the competitive segment of the businesses of these companies.

I would like to include in the record, Mr. Chairman, two letters that have been written by Chairman Fowler of the FCC, one to Congressman Swift and myself, and one to the chairman of the full committee, the distinguished gentleman from Michigan, John Dingell. These eight pages of communications from the Chairman of

the FCC speak directly to the issue of how the FCC would attempt to ensure that the competitive services could be conducted in such a way as to ensure that there was no cross-subsidy.

I ask unanimous consent that these be included in the record.

Mr. WIRTH. Without objection, they will be included in the record.

[Testimony resumes on p. 26.]

[The text of H.R. 3687 and H.R. 3800 and the letters referred to by Mr. Tauke follow:]

I

99TH CONGRESS
1ST SESSION

H. R. 3687

To permit the Bell operating companies to provide information services and to manufacture telecommunications equipment so long as such services and manufacturing are not subsidized with the proceeds from the provision of local exchange telephone service or other regulated telecommunications services.

IN THE HOUSE OF REPRESENTATIVES

NOVEMBER 5, 1985

Mr. WYDEN introduced the following bill; which was referred to the Committee on Energy and Commerce

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A BILL

To permit the Bell operating companies to provide information services and to manufacture telecommunications equipment so long as such services and manufacturing are not subsidized with the proceeds from the provision of local exchange telephone service or other regulated telecommunications services.

Be it enacted by the Senate and House of Representatives of the United States of America in Congress assembled,

SECTION 1. SHORT TITLE.

This Act may be cited as the "Telephone Ratepayer Protection and Technology Promotion Act of 1985".

SEC. 2. AUTHORITY TO PROVIDE INFORMATION SERVICES SUBJECT TO STATE REGULATION TO PREVENT CROSS—SUBSIDIZATION.

Notwithstanding any other provision of law, a Bell operating company may engage in the provision of information services or in the manufacture in the United States of telecommunications equipment, or both, to the extent permitted by regulations that—

(1) are prescribed by the State commission in each State in which such operating company, or any entity controlling such operating company, provides local exchange telephone service or any other telecommunications service;

(2) prevent such operating company from using the revenues it derives from the offering of local exchange telephone service or any other regulated telecommunications service or product to defray any costs associated with engaging in the provision of information services or the manufacture of telecommunications equipment, or both; and

(3) ensure that a reasonable portion of the joint and common costs of plant, equipment, and other resources is allocated to the provision of information services or the manufacture of telecommunications equipment, or both.

SEC. 3. DEFINITIONS.

For purposes of this Act—

(1) the term "Bell operating companies" has the same meaning as such term has in the Modification of Final Judgment entered August 24, 1982, in *U.S.* v. *Western Electric,* Civil Action No. 82–0192 (United States District Court, District of Columbia), except that such term does not include any centralized organization for the provision of engineering, research, and administrative services, the costs of which are shared by such operating companies or their affiliates;

(2) the term "information services" has the same meaning as such term has in such Modification;

(3) the term "telecommunications equipment" has the same meaning as such term has in such Modification, except that such term includes customer premises equipment (as defined in such Modification); and

(4) the term 'regulated communications service or product' means a telecommunications service or product for which the rates are subject to review and approval or disapproval by a State commission.

SEC. 4. EFFECTIVE DATE.

This Act shall take effect on September 1, 1986.

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I

99TH CONGRESS
2D SESSION

H. R. 3800

To permit the Bell operating companies to provide information services and to manufacture telecommunications equipment, subject to regulation by the Federal Communications Commission.

IN THE HOUSE OF REPRESENTATIVES

NOVEMBER 20, 1985

Mr. TAUKE (for himself, Mr. SWIFT, Mr. LOTT, Mr. SLATTERY, Mr. NIELSON of Utah, and Mr. MATSUI) introduced the following bill; which was referred to the Committee on Energy and Commerce

APRIL 3, 1986

Additional sponsors: Mr. WHITTAKER, Mr. GINGRICH, Mr. MADIGAN, Mr. SKEEN, Mr. SUNDQUIST, Mr. WORTLEY, Mr. SILJANDER, Mrs. BENTLEY, Mr. FORD of Tennessee, Mr. BUSTAMANTE, Mr. FUQUA, Mr. MONSON, Mr. DOWDY of Mississippi, Mr. SHAW, Mr. QUILLEN, Mr. BILIRAKIS, Mr. DUNCAN, Mr. PEPPER, Mr. TALLON, Mr. HEFNER, Mr. GLICKMAN, Mrs. LLOYD, Mr. WHITLEY, Mr. SMITH of Florida, Mr. ROBERTS, Mr. ORTIZ, Mr. FASCELL, Mr. HATCHER, Mr. CHAPPELL, Mr. BARNARD, Mr. BONER of Tennessee, Mrs. MEYERS of Kansas, Mr. FRANKLIN, Mr. SPENCE, Mrs. VUCANOVICH, Mr. WILSON, Mr. STENHOLM, Mr. SCHUETTE, Mr. DYMALLY, Mr. ARMEY, Mr. BOULTER, Mr. LEATH of Texas, Mr. ROBINSON, Mr. BARTON of Texas, Mr. YOUNG of Missouri, Mr. SKELTON, Mr. COLEMAN of Missouri, Mr. DELAY, Mr. HENRY, Mr. CROCKETT, Mr. EDWARDS of Oklahoma, Mr. SENSENBRENNER, Mr. DAVIS, Mr. DERRICK, Mr. EMERSON, Mr. BADHAM, Mr. JACOBS, Mr. CHAPPIE, Mr. ANDREWS, Mr. PARRIS, Mr. FAZIO, Mr. SPRATT, Mr. CARR, Mr. MCEWEN, Mr. BONIOR of Michigan, Mr. TRAXLER, Mr. PURSELL, Mr. CAMPBELL, Mr. OXLEY, Mr. APPLEGATE, Mr. STALLINGS, Mr. HYDE, Mr. FORD of Michigan, Mr. FAUNTROY, Mr. O'BRIEN, Mr. HERTEL of Michigan, Mr. PORTER, Mr. HUNTER, Mr. FLIPPO, Mr. ROTH, Mr. BEVILL, Mr. CHANDLER, Mr. FEIGHAN, Mr. HAWKINS, Mr. CHENEY, Mr. EVANS of Iowa, Mr. KLECZKA, Mr. BROWN of California, Mrs. JOHNSON, Mr. MCCANDLESS, Mr. HANSEN, Mr. FIELDS, Mr. LEWIS of California, Mrs. MARTIN of Illinois, Mr. FOGLIETTA, Mr. DANNEMEYER, Mr. ROYBAL, Mr. BOSCO, Mr. LIGHTFOOT, Mr. MCCLOSKEY, Mr. WYLIE, Mr. SMITH of Iowa, Mr. ZSCHAU, Mr. DIXON, Mr. KOLBE, Mr. STUMP, Mr. MILLER of Ohio, Mr. TORRICELLI, and Mr. BEREUTER

Deleted sponsor: Mr. BATES (added March 12, 1986; deleted March 20, 1986)

A BILL

To permit the Bell operating companies to provide information services and to manufacture telecommunications equipment, subject to regulation by the Federal Communications Commission.

Be it enacted by the Senate and House of Representatives of the United States of America in Congress assembled,

SECTION 1. SHORT TITLE.

This Act may be cited as the "Telecommunications Equipment and Information Services Act of 1985".

SEC. 2. FINDINGS.

The Congress finds that—

(1) the Federal Communications Commission is the appropriate Federal entity for overseeing and regulating the telecommunications industry;

(2) the Bell operating companies currently comprise one-half of the asset base of that industry;

(3) continued economic growth of the domestic telecommunications industry requires that the Bell operating companies be viable businesses in both the short- and long-term;

(4) such continued economic growth is adversely affected by the restrictions that prohibit the Bell oper-

ating companies from meeting the demands of the competitive marketplace;

(5) such continued economic growth and the international competitiveness of the United States telecommunications industry are important and vital to—

(A) the long-term research and development projects and programs of the United States telecommunications industry,

(B) the rapid development and introduction into the marketplace of new and innovative telecommunications equipment and services for American residential and business telecommunications users,

(C) the development of efficient, reliable, and state-of-the-art telecommunications networks to serve the needs of American telecommunications consumers, and

(D) the maximizing of employment opportunities for United States workers in the telecommunications industry; and

(6) the provision of universal telephone service at reasonable rates for all Americans is closely linked to the continued economic growth of the domestic telecommunications industry.

SEC. 3. AUTHORITY TO PROVIDE INFORMATION SERVICES AND TO MANUFACTURE TELECOMMUNICATIONS EQUIPMENT.

Notwithstanding any other provision of law, a Bell operating company may engage in the provision of information services or in the manufacture in the United States of telecommunications equipment, or both, subject to the limitations and conditions contained in this Act.

SEC. 4. LIMITATIONS AND CONDITIONS ON PROVISION OF INFORMATION SERVICES.

(a) SUBJECT TO FCC REGULATION.—The authority granted by section 3 to a Bell operating company to engage in the provision of information services shall be subject to such charges, practices, classifications, and regulations as the Commission may establish in the public interest.

(b) INAPPLICABILITY TO ELECTRONIC PUBLISHING.—The authority granted by section 3 to a Bell operating company to engage in the provision of information services shall not apply to electronic publishing.

(c) LACK OF IMPEDIMENT TO COMPETITION REQUIRED.—The authority granted by section 3 to a Bell operating company to engage in the provision of information services shall be available only if the Commission determines, in its discretion, after consultation with the Secretary of Commerce and the Attorney General, that there is no substantial

possibility that any Bell operating company could impede competition in the information services business.

SEC. 5. LIMITATIONS AND CONDITIONS ON MANUFACTURE OF TELECOMMUNICATIONS EQUIPMENT.

(a) SUBJECT TO FCC REGULATION.—The authority granted by section 3 to a Bell operating company to engage in the manufacture of telecommunications equipment shall be subject to such charges, practices, classifications, and regulations as the Commission may establish in the public interest.

(b) LACK OF IMPEDIMENT TO COMPETITION REQUIRED.—The authority granted by section 3 to a Bell operating company to engage in the manufacture of telecommunications equipment shall be available only if the Commission determines, in its discretion, after consultation with the Secretary of Commerce and the Attorney General, that there is no substantial possibility that any Bell operating company could impede competition in the telecommunications equipment manufacturing business.

SEC. 6. REPORT ON EMPLOYMENT IMPACT.

(a) CONTENTS OF REPORT.—The Commission shall annually assess the impact of this Act on employment in the telecommunications equipment manufacturing and information services industries. The Commission shall include in its annual report to Congress under section 5(g) of the Commu-

nications Act of 1934 a summary of the results of the assessment which shall contain—

(1) a description of negotiations and other actions taken by the Bell operating companies (A) to increase employment in the United States within the telecommunications industry as a consequence of this Act, and (B) to reduce direct and indirect adverse effects on employment in the telecommunications industry that may result from engaging in new business operations as a consequence of this Act; and

(2) an estimate, developed in consultation with the Department of Labor, of net changes in employment as a consequence of this Act, together with a breakdown of the data used in developing such estimate.

(b) PROCEDURES FOR ASSESSING EMPLOYMENT IMPACT.—The Commission shall, in conducting the assessment required by subsection (a), provide interested persons the opportunity to present written and oral comment on matters to be included in the report required by such subsection.

SEC. 7. DEFINITIONS.

For purposes of this Act—

(1) the term "Bell operating companies" has the same meaning as such term has in the Modification of Final Judgment entered August 24, 1982, in *U.S.* v. *Western Electric,* Civil Action No. 82–0192 (United

States District Court, District of Columbia), except that such term does not include any centralized organization for the provision of engineering, research, and administrative services, the costs of which are shared by such operating companies or their affiliates;

(2) the term "information services" has the same meaning as such term has in such Modification;

(3) the term "electronic publishing" has the same meaning as such term has in such Modification;

(4) the term "telecommunications equipment" has the same meaning as such term has in such Modification, except that such term includes customer premises equipment (as defined in such Modification); and

(5) the term "Commission" means the Federal Communications Commission.

SEC. 8. EFFECTIVE DATE.

(a) IN GENERAL.—Except as provided in subsections (b) and (c), this Act shall take effect on September 1, 1986.

(b) AUTHORITY TO ESTABLISH REGULATIONS.—The authority of the Commission to establish charges, practices, classifications, and regulations and to institute proceedings under this Act shall take effect upon the enactment of this Act.

(c) EFFECTIVE DATE OF AUTHORITY.—The authority to manufacture telecommunications equipment under section

3 shall be effective on September 1, 1986, or such later date as the Commission may establish in its determination under section 5(a).

FEDERAL COMMUNICATIONS COMMISSION
WASHINGTON

OFFICE OF
THE CHAIRMAN

March 12, 1986

Honorable Al Swift
U.S. House of Representatives
Washington, D.C. 20515

Honorable Thomas J. Tauke
U.S. House of Representatives
Washington, D.C. 20515

Dear Congressman Tauke:

As you know, I support your effort in H.R. 3800 and would like to take this opportunity to address a number of concerns that have been raised with regard to the entry of the Bell Operating Companies (BOCs) into competitive enterprises.

This Commission is committed to assuring American consumers the widest variety of telecommunications services at least possible cost. We have watched competitive forces gain strength in markets in which the regional Bell companies currently compete. We have witnessed evolving technologies challenge the established public switched network. Our response to the new, competitive telecommunications environment will determine not only the prices, but also the availability of new services to the general body of consumers.

It will of course be necessary to examine carefully the question of appropriate terms and conditions under which the BOCs should be permitted to enter new fields so as to protect ratepayers from subsidizing unregulated businesses; however, the importance of allowing the BOCs to compete in the market for nonexchange services should not be underestimated at a time when competition is challenging the Bell system exchange services.

A number of states already have approved intra-LATA toll competition, threatening the continued subsidy of residential rates by BOC toll charges. Satellites, cable and fiber optics provide a potent source of competition in the market for basic transmission services. In addition, many large users are now building information services into their in-house telephone systems. Yet, it may be that unless the BOCs are permitted, under appropriate safeguards, to offer competitive services over their own network, the average consumer will not be afforded the same options available to the large business user. Today, the average consumer's chief link to the new information age is through the local loop. And, unless the cost is low enough, the average consumer will be unable to take advantage of the new telecommunications technologies.

Moreover, it appears that there may be true cost efficiencies to be gained from interconnecting or integrating equipment in the local exchange switch for purposes of providing competitive services (as well as cost savings to be gained from integrating Bell company operations in the provision of both regulated and unregulated activities). The general public should be permitted to receive the benefits of such integration efficiencies.

The Commission has engaged in a number of proceedings which address the appropriate safeguards that should accompany any foray by a BOC into the competitive arena. Our experience to date suggests that in many instances, regulatory techniques short of an outright ban on competitive activities can successfully protect ratepayers from subsidizing competitive activities and competitors from potentially anticompetitive practices. As I have noted in a letter to Chairman Dingell (copy enclosed), the Commission has gained considerable experience in devising accounting mechanisms to ensure the proper allocation of costs incurred in the provision of both regulated and unregulated activities. In addition, we are set to begin a proceeding aimed at taking a hard look at the methods of separating the costs of regulated telephone services from the cost of the unregulated activities of telephone companies. The ultimate goal of this proceeding will be to ensure that ratepayers do not end up subsidizing failed diversifications with higher telephone rates.

We also are currently engaged in reviewing our "Computer II" rules which require the BOCs to offer any "enhanced" services through fully separated subsidiaries. Market changes referred to above have called into question the continuing validity of these requirements. Our goal in the "Computer III" proceeding is to eliminate the shortcomings of the Computer II scheme which denies the public the ability to realize efficiencies that can result if enhanced services are integrated with a carrier's basic services. This may make economical services that today are currently uneconomical, and in other cases, may make existing services available at a lower price than is possible under Computer II.

This Commission obviously would not alter its Computer II rules in the absence of a substitute mechanism for ensuring that a carrier cannot abuse its market position to the disadvantage of consumers or competitors. Accounting procedures are vital in this respect. An open architecture network can be another invaluable competitive tool. One of the Commission's proposed alternatives to the costly structural separation requirement of Computer II is an open architecture network, coupled with accounting safeguards, in which potential service providers would be afforded vital access to the local network, comparable to the access given to the local

telephone company itself. The open architecture network would provide a basis for full and fair competition in the provision of enhanced and information services. It has the potential for increasing the number of competitive service vendors, who will be able to gain access to the local loop, and for driving down the prices for competitive services.

There would appear to be little incentive for the BOCs to undertake development of such a network if they were not permitted to compete on equal footing in the provision of competitive services. They would have no vested interest in providing the means to achieve a low priced, competitive marketplace for nonexchange services if they were not in the position to profit from such an environment.

The Commission does not intend, through its Computer III proceeding or its planned revision of accounting procedures for regulated/unregulated activities, to oust the states from their proper and necessary role in regulating the state rate base. The accounting mechanism contemplated by the Commission for realizing an appropriate split of joint and common costs between regulated and unregulated telephone company activities would preserve intact the established separations process whereby costs in the companies' regulated accounts are allocated to the state and interstate jurisdictions, with the state commissions having full authority over the recovery of the state revenue requirement, including making disallowances as permitted by state law. We do consider it necessary, however, to formulate a nationwide policy on the propriety of, and conditions under which, the BOCs should be permitted to provide competitive services. Our current assessment is that leaving this determination to the state commissions has a significant potential for disrupting the competitive provision of telecommunications services. The regional Bell companies operate on an integrated multistate, regional basis. A patchwork of state approaches could confuse BOC business procedures and compound state problems in controlling improper cost shifting. Additionally, as this Commission has stated on previous occasions, we have an interest in preventing regional Bell company cross-subsidies since cross-subsidization could hinder the goal of cost-based access charges for interexchange carrier interconnection with local exchange facilities.

I firmly believe that the FCC's expertise should be brought to bear on the issue of under what conditions the BOCs should be permitted to enter new areas of enterprise. As I have indicated above, we have already begun to face, out of necessity, the many and multi-faceted issues involved in regulating or deregulating the activities of monopoly service providers whose service areas are no longer sancrosanct from the forces of competition.

I trust that this letter will be of some assistance in your continuing effort to assess the proper direction of our national telecommunications policy.

Sincerely,

Mark S. Fowler,
Chairman

FEDERAL COMMUNICATIONS COMMISSION
WASHINGTON

OFFICE OF
THE CHAIRMAN

March 12, 1986

Honorable John D. Dingell
Chairman, Committee on Energy and Commerce
United States House of Representatives
2125 Rayburn House Office Building
Washington, D.C. 20515

Dear Chairman Dingell:

I appreciated the opportunity to discuss telecommunications issues and the role of the FCC with the committee in February. The following explanation of the evolution of FCC cost allocation techniques will, I hope, respond to your question about the types of ratepayer protection from cross-subsidy of deregulated services that the Commission is considering.

Regardless of the tremendous organizational and structural changes we have witnessed in the last few years in the telecommunications industry, and the rapidly multiplying choices that a telecommunications consumer faces today, the fundamental role of the federal regulator has not changed. Each change and each new service which involves the nation's telecommunications network must be scrutinized and tested for conformance with the principles underlying national telecommunications policy: preservation of universal service, efficient and economical use of the nation's resources, promotion of competition, and assurance of nondiscriminatory access. These tests of principle require specific procedures and ground rules which can be applied by the staff and followed by the regulated industry to demonstrate factually and concretely that compliance with Commission policy will be achieved in any new venture proposed.

As technology and new markets evolve in a dynamic competitive marketplace, technically sophisticated knowledge is required of regulators and new monitoring and assessment techniques must be deployed. The FCC has recognized this need as can be seen from the coupling of deregulatory actions with detailed implementation, investigation and monitoring guidelines. The Commission's broad Computer II decisions to deregulate the provision of enhanced services and customer premises equipment (CPE) in 1980 were implemented over the next few years in Common Carrier Docket 81-893 and other related proceedings. These dockets outlined specifically how accounting and reporting would be performed to facilitate regulatory review and monitoring of common carrier new service ventures and provided for the separation of deregulated from regulated activities through a separate subsidiary.

The separate subsidiary concept is a regulatory tool designed to put the exchange carrier's offerings of these services on a more even footing with competitors. This approach is accomplished by artifically "handicapping" exchange carriers' access to the local network to, in effect, mirror the access of competitors. Several years' experience with the separate subsidiary approach and the emergence of new lines of business for exchange carriers have highlighted some basic flaws with the rigid Computer II separate subsidiary concept. In its Computer III proceeding the Commission is addressing the important questions that have arisen regarding whether the proper regulatory approach should be not to handicap exchange carrier access to the local network but rather to promote an "open network" environment wherein all providers could be allowed to make equal use of the economies and advantages inherent in the existing local network, thereby fostering fuller use of this vast national resource. Thus, the knowledge and experience gained from the Computer II proceedings is being applied in an evolutionary fashion in the current policy deliberations in the Computer III docket.

The increased movement of regulated carriers into more diverse lines of business and the questions being considered in the Computer III docket underscore the need to refine the regulatory tools available to assure that costs of providing regulated and unregulated services are properly allocated. The Commission's experience with the Computer II framework can again be drawn upon as we design practical, workable accounting rules to address the separation of joint and common costs between regulated and deregulated services.

The deregulation of portions of previously regulated business, such as customer premises equipment, and the introduction of new services have been relatively straightforward to date from a cost allocation standpoint. That is, customer premises equipment could be clearly severed from other components of the network. The adverse impact CPE deregulation could have had on local rates if precipitous action had been taken was recognized and ameliorated by the Commission's orders on deregulation without impeding the competitive provision of such equipment. The Commission did this by phasing in the effect of its decision over a five year period. During the phase-in period, the Commission staff continued an oversight role of the CPE account (transitional removal of frozen investment levels over five years) and ordered a midcourse correction in the industry's calculations which led to closer conformance with the Commission intent. The whole process will be completed by the end of this year, with no financial dislocations. In the meantime, during the five-year phase-in period, there can be little doubt that consumers have had the benefits of a competitive CPE marketplace and can maximize their own self-interest in purchasing terminal equipment.

A new service or business activity, whether judged to be a regulated or nonregulated activity, could be subjected to similar cost allocation techniques if it were as clearly severable as CPE. For example, a local exchange carrier might wish to use a building more productively by renting otherwise empty space to another business, such as a barber shop on the lobby floor. That rent revenue and any associated expenses can be captured by current accounting rules. The reviewing regulator can be satisfied that the common carrier business has not been improperly used to subsidize a venture into real estate activity. Even if it were to involve a separate subsidiary which is not even dealing in telephone company buildings, the accounting principles and rules set out by the Commission can be applied to separate regulated from nonregulated business and to prevent cross-subsidization.

Local exchange carriers' desire to provide such state-of-the-art new services as protocol conversion and packet switching led to a series of requests for waiver of Computer II rules and a decision by the Commission to entertain tariff filings under waiver for such services on a collocated and nonseparated subsidiary basis. Again, the policy was applied in a defined review process of the specific portions of the network and the specific investments and expenses involved for the service proposed. Specific reporting requirements are also imposed as a condition of any waiver to permit the FCC staff to monitor actual performance and cost characteristics of the service for evaluation of the accuracy of cost and demand estimates. On the basis of that regular evaluation, corrective action can be ordered where needed.

Protocol conversion and packet switching are only vanguards of the many new services or features which will be emerging. The benefits and economies of innovation can ultimately be spread ubiquitously and be available to all customers who desire them. A more efficient network broadly supported by both business and residence customers is in the nation's interest as a whole and should benefit individual customers as well. For this reason, forcing innovative services and most of the network modernization out of the regulated network by imposing broader regulatory restraints than needed to prevent potential subsidy of deregulated activities may not be the best and is certainly not the only answer available to regulators.

The regulatory process described earlier becomes admittedly more complex when a new service is not as distinctly defined as CPE or even as separable as protocol conversion service as it is presently configured. Many new services will involve a new use of jointly used investments, such as customer loop or trunk plant or common central office equipment -- the plant used jointly for local and toll calling, and in certain configurations to transmit data. Existing methods to allocate such joint costs, which economic theory tells us are strictly allocable, are to be found in the jurisdictional separations process, Part 67 of the Commission's rules. These rules, however, were never intended to perform service by service cost

allocations. They are designed to produce a division of a common carrier's total regulated business into state and interstate segments. Since those rules do not directly apply to the need to allocate joint and common costs between regulated and deregulated services, and since the trend in new services is in the direction of more rather than less sharing of joint plant, new standards and processes are required to avoid a piecemeal and contradictory approach.

The FCC staff is presently drafting a proposal for such guidelines for Commission review and public comment. We are seeking to devise rules which will permit a rational, auditable and universally applicable approach to such cost allocations and for transactions with affiliates. Common overhead costs must also be assigned to prevent subsidy by regulated business. Common cost loadings are routinely developed in cost accounting systems in this and other industries and, again, while there is not one right answer, there are several reasonable standards or models to consider, in addition to the fully distributed cost approach accepted today. The bottom line of the effort is to assure that an appropriate and reasonable assignment of joint and common costs is removed from the regulated segment and assigned to the deregulated uses of that plant or other resource.

The costs allocated under such rules must stand an initial fairness test and the assignment levels will be tracked against actual demand to meet a reasonable performance test. For example, no configuration of joint plant bundled into a deregulated service could be assigned a cost level any less than that attributed to the same configuration of joint plant offered under tariff. How that deregulated service is priced in total to recover such an assignment would not be at issue. The purpose of tracking these cost allocations is not to gauge the success or failure of the deregulated venture, but to evaluate how to assign any growth in cost of joint plant between the regulated and deregulated services.

The Commission expects to release expanded guidelines for allocation of joint and common costs for public comment in the near future and is targeting implementation for 1987 to coincide with a major deregulatory action concerning local exchange carriers' billing and collection services.

If you have further questions on these matters, please do not hesitate to contact either me or my staff.

Sincerely,

Mark S. Fowler
Chairman

Mr. TAUKE. Mr. Chairman, I think today that we will have an opportunity to demonstrate that the effort that we are making that is embraced in H.R. 3800 is good public policy.

I again thank you for calling these hearings and permitting us an opportunity to explore with the many expert witnesses how we can proceed down this road to providing more services at lower costs to the telecommunications consumers of our Nation.

Mr. WIRTH. Thank you, Mr. Tauke.

If the people standing in the back would also like to come stand over here on the side. If there are other people outside who are trying to get in, and if people standing along the back—are there other people outside still? Let's see if we can have people sort of move together in the back there, if we could, so that the people standing on the outside could get in.

Mr. Luken.

Mr. LUKEN. Thank you, Mr. Chairman. I congratulate the chairman for calling this hearing. I think we have an age-old question, a basic question, which must be under the constant scrutiny and review of the Congress in these tumultuous times for our local companies.

Not only have the BOC's suffered the loss of Ma Bell's protective umbrella, but they've had to learn to live with a new regulatory environment that is controlled by the FCC, the Department of Justice, and the Federal courts as well. It's understandable in this situation that they would want to get into some of the exotic new ventures that are on the horizon such as voice mail, home banking, and remote teaching.

These companies, understandably also, want the opportunity to get into manufacturing of telecommunications equipment.

As we address this question, I think we are going to have to approach it from the standpoint of hardheaded realism and recognize that there are catch 22's involved. We shouldn't approach it on the basis of starry-eyed wish lists for any particular group, any legislative solution must be balanced. I submit that, as far as I'm concerned, it must be balanced with four criteria involved.

First, and foremost, will the ratepayer benefit? Second, will necessary and valuable services be more broadly available? That's an argument for legislation. Third, will the regulated entity be jeopardized by risky ventures that it may be getting into? Fourth, will the BOC's use their local telephone monopolies to impede competition in unregulated markets?

I must bring up these caveats, that we have to address as we look into the question of unharnessing our local phone companies from the restraints imposed by the FCC and the courts. They will be getting into unchartered waters, just as some of our financial institutions—and this committee has learned about that, have gotten into unchartered waters to the detriment of the depositors and to the detriment of the taxpayers, in my own State of Ohio. We are reading about this every day in Maryland.

I think we have to distinguish between the high flyer kind of risks, which we might permit if we are simply to advance the cause of deregulation for the sake of deregulation, and of freeing the BOC's from any restrictions.

I think we have to distinguish, as Judge Greene has distinguished, and some of the guidelines that he imposed such as restrictions on the percentage or the amount of investment in unregulated industries and unregulated ventures, are considerations that I think have to go into the whole cafe that we will be considering.

Therefore, Mr. Chairman, I have advanced the criteria that I think will be important. There are other concerns that we may have. For example, again in my own State of Ohio, in another utility area, the legislation that is being considered is restrictive on the utilities and their ability to invest in other industries, and they look at the Florida situation where an electric utility there recently invested in an insurance company with what may be disastrous results.

Obviously, the suggestion here isn't for the BOC's to get into those kinds of unrelated ventures. But I think we have to maintain our balance and maintain our perspective as we continue to review these critical questions which will have an impact on communications in this country for many years to come.

Thank you, Mr. Chairman.

Mr. WIRTH. Thank you, Mr. Luken. Mr. Bliley.

Mr. BLILEY. Thank you, Mr. Chairman. We now have pending before our subcommittee two bills, H.R. 3687 and H.R. 3800, which cause me particular concern. I would like first to address the major provisions which would lift the restrictions in the modified final judgment to permit the regional Bell Operating Companies to manufacture telecommunications equipment.

As you will undoubtedly recall, this proposal was reviewed in considerable detail during the MFJ public interest proceedings. At that time, the court concluded that due to the local exchange market structure if the operating companies were allowed to manufacture telecommunications equipment, new entrants in the industry would be disadvantaged and the development of a competitive market would be frustrated.

The operating companies could purchase their own equipment even though it might be more expensive and possibly of lesser quality and absorb these prices through increased local rates. They would also have the incentive to subsidize the prices of their equipment with the revenues from their monopoly services.

The conditions which led to these conclusions are virtually unchanged today. This was confirmed on January 13, 1986, when Judge Greene ruled on request for clarification of the MFJ, which had been requested by the three RBOC's. The general theme of the order was that the RBOC's continue to exert monopoly power within their regions and, therefore, should not be allowed to use that power to inhibit competition.

There are other adverse consequences which must also be considered. Manufacturing relief would not improve this newly opened market. There are an abundance of American manufacturers. The problem is foreign manufacturers who are subsidized by their governments, while our companies suffer regulatory restraints by our government.

In any event, since the RBOC's tend to diversify through acquisition rather than through new enterprises, no new productive ca-

pacity would be created and the U.S. trade balance would not be changed.

Furthermore, by authorizing the lifting of this restriction, the diversion of management and financial resources to the new venture could well lead to the deterioration of the local exchange service. In light of these considerations, I am deeply concerned that the main benefits that could accrue to the RBOC's if the manufacturing restrictions were removed would be more than offset by the harms that could occur in the newly established market as well as those to the local exchange subscriber.

Mr. Chairman, my concern is not as great as regards proposals to allow the RBOC's to expand into the area of enhanced services. I believe that this may well be an area into which the RBOC's should be allowed to expand.

However, this must be done under careful scrutiny by the FCC. Full, equal access by competitors to the network must be a cornerstone of any decision to lift these restrictions.

We must commit ourselves to ensuring that no company is allowed to use its monopoly power to thwart or eliminate competition in the area of enhanced services. If we are able to guard against anticompetitive abuses, then I believe the public will stand to benefit from these expanded capabilities becoming a part of the telephone network.

Mr. Chairman, I look forward with great interest to the testimony we will hear today and thank you for calling this hearing.

I, too, would like to welcome Rodney Joyce who served so well this subcommittee for so many years to our hearing today.

Thank you, Mr. Chairman.

Mr. WIRTH. Thank you, Mr. Bliley. Mr. Swift.

Mr. SWIFT. Thank you very much, Mr. Chairman. I think there are two potential benefits that can be derived from this legislation. One is obviously to the RBOC's in permitting them to vigorously compete and, therefore, help their economic situation. The second is to the local ratepayers.

A provision that does not provide for both of those is probably not viable. I hope that today we will be able to explore more fully what the benefits are for ratepayers. I think we are helped in that regard by what I perceive as a developing general consensus of what the policy ought be.

At least, I hear both the industry and consumer groups, in general, agreeing to this concept: There should be no subsidies flowing in either direction, either from the regulated monopoly into the competitive services, nor subsidy flowing from the competitive services back into the monopoly portion of the business.

But I have been involved in the telecommunications business long enough to know that, while we may have consensus on that, when we start trying to put specifics to the generalities there may be some substantial disagreements. And it is in that area that I would hope today we could begin to try and add some detail, get some idea of how best we might do this and find out what it is that everybody is talking about when they agree to the concept of no subsidies going in either direction.

In other words, I would like to flush out people's views and flush out the concept today so that we have a better idea of how we are going to go about it.

One last point, Mr. Chairman. We have had in testimony a couple of weeks ago—both from the Chairman of the FCC, and from a witness that was representing the State Regulatory Commissions—that there are accounting systems that will permit us to follow these things with some accuracy. And in the letter that Congressman Tauke referred to from Chairman Fowler, he again reiterates the fact that they believe that they are putting together the kind of system that will be successful in being able to track all of these funds and know that they are going to the right place.

It does seem to me that the legislation Mr. Tauke and I have introduced assumes there is going to be an effective system for doing that. Without it, we are not going to be able to, in reality, achieve even the concept that we've agreed to. And so I am looking forward with particular interest, not so much today, but I hope in the very near future to see what it is that the FCC is coming up with. Because once some such mechanism is in place then I think the rest of this can follow along well, at least as quickly as we can come to some agreement on the details of that concept we agree on with regard to cross-subsidization.

I yield back the balance of my time.

Mr. COATS. The consent decree raised serious considerations for a number of reasons. I hope that we will shed some light on past decisions governing this aspect of the telecommunications industry and provide some answers to assist us in guiding our policies in the future.

Personally, I want to explore a variety of questions ranging from whether we should at this time be tampering with the modified final judgment that has only been in effect for 2 years. Whether the Bell operating companies have been effective in carrying out their mandate to convert the local exchange facilities to permit equal access to the competing long distance companies. Whether the lifting of restrictions lends itself to anticompetitive activities, and whether there are sufficient ratepayer protections.

Along with these concerns, I think it is also appropriate to add that all of us in Congress are concerned about the growing trade deficit, and agree that action must be taken to address this.

Last year, this committee adopted H.R. 3131, the Telecommunications Trade Act of 1985, because the majority of us felt that we must keep American companies competitive in world markets. For this reason, the hearing today is relevant because the legislation we have before us presents another possible option in the telecommunications trade sector that could help improve this imbalance. Namely, the provision of information services and the manufacturing of telecommunications equipment by the Bell operating companies. The divestiture of AT&T has major implications for trade in domestic telecommunications markets. The consent decree agreement opened up U.S. equipment markets to foreign suppliers, but has prevented a sizable portion of our domestic industry resource base from competing in foreign markets.

The predictable result has been a flood of equipment imported into this country, and since the U.S. constitutes nearly half the

world market for telecommunications equipment and services, we must closely analyze the consent decree that calls for a continuation of the policy that might inhibit competition and limit consumer choice.

In carefully analyzing this policy, we must ask ourselves also whether we should let the modified final judgment stand pending a Department of Justice study and report that will be submitted to this committee by July 1, 1987, or whether we are shortchanging ourselves in the development of technology if we don't return these policy decisions to Congress and to the Federal Communications Commission.

I look forward to hearing from our witnesses today on these often competing concerns and questions, and sorting out where we have to go in this field.

Mr. WIRTH. Mr. Oxley.

Mr. OXLEY. Thank you, Mr. Chairman. Today marks the third and final hearing of this subcommittee's examination of common carrier issues in the wake of the AT&T divestiture. I want to welcome all of our witnesses here today to examine the role of the Bell operating companies and the possible consequences of allowing them to engage in manufacturing and information services.

I particularly want to welcome Rodney Joyce, the gentleman from Kansas, who is returning to this subcommittee after several months' absence, albeit in an entirely different capacity. As associate minority counsel for this subcommittee, Rodney was a tireless worker, and a valuable source of information to both members and staff. His excellent work performance carried over to NTIA, where he has done a commendable job during his tenure as acting director. So again, Rodney, welcome back. We look forward to your insights today.

Mr. Chairman, the issue we are today considering is not a new one. There have been legislative proposals to modify the consent decree floating around the Hill for some time, and I am pleased to be a cosponsor of one of them, H.R. 3800, sponsored by our good friends Mr. Tauke and Mr. Swift.

I cosponsored this bill because I believe we must begin to act to help reduce this Nation's burgeoning trade deficit. Allowing seven new competitors into this marketplace will go a long way toward making the United States more competitive overall in the provision of telecommunications equipment and information services.

This subcommittee has heard reams of testimony as to how far U.S. companies lag behind in the telecommunications area, largely due to barriers from abroad, and it simply makes no sense in my mind to keep in existence domestic barriers that have essentially the same effect as those constructed by other nations.

I understand that there is some concern about the various legislative proposals, or about whether there should be even legislation at all, and I look forward to addressing those concerns today so that we can get the facts on the table and proceed to the next step in the legislative process. I thank the Chair and yield back the balance of my time.

Mr. WIRTH. Thank you. Mr. Ritter.

Mr. RITTER. Thank you, Mr. Chairman, and I would also like to welcome my good friend, Rodney Joyce, and I would like to associ-

ate myself with the remarks of my colleagues. Rodney was a tireless performer for this committee, and introduced many of us who came to the committee to the telecommunications issues.

Mr. Chairman, as the subcommittee continues its review of competition in the telephone industry, I just hope we focus on how the American consumer is to ultimately benefit from the breakup of the old Bell System, and the new era of competition. For better or for worse, the breakup has taken place and we are moving away from the subsequent initial shock and confusion.

The question before the Congress, the FCC, the Justice Department, the Court, and other key decisionmakers is where we go next, and how do we get there. I want to make certain that in our desire to get there we don't forget to take the consumer with us. I would suggest that the guidepost throughout the debate should be how public policy in the telecommunications industry can best serve the users of our telecommunications system. By "users," I mean the residential customers primarily, but I am also referring to the other users, the business users from the mom and pop store to today's largest corporations. Residential and business users have a lot in common. They each want to see good universal service maintained, affordable prices, and the best in technology. They also want less confusion and less uncertainty when it comes to phone service and the varied options.

Options may be the key as we seek to define telecommunications policy for the future. Give the customers options, and I believe they will choose wisely once they understand the new terrain. If the residential customer and the business customer are to have a full range of options, then I think we have to seriously consider the wisdom of maintaining the current regulatory environment, which not only surrounds the Bell operating companies which we will discuss in detail today, but also others. AT&T, for example. Such regulations, as we discussed in our last hearing, required AT&T to use large trucks to deliver the paperwork for filing to the Federal Communications Commission.

What I believe we need is a policy that allows the BOC's, AT&T, and the many other creative competitors making their nitch in the telecommunications market to use their resources and expertise to make their respective best contributions to the economy of this Nation.

I believe it is especially important in the face of growing international competition. We are very much concerned about the level of the playing field vis-a-vis our foreign competitors. We also need to be concerned with that same level domestically. This is a much bigger issue than simply AT&T versus the BOC's, and that is what we in Congress, the FCC, the Justice Department, and the courts have got to grapple with.

Thank you, Mr. Chairman.

Mr. WIRTH. Thank you very much. Mr. Bryant.

Mr. BRYANT. Thank you, Mr. Chairman. I appreciate very much the chairman calling this hearing today. This is an important series of hearings, because it is well past time for this subcommittee to examine carefully the provisions of the modified final judgment, and carefully form policy decisions rather than continuing to

leave them exclusively to the Justice Department, the Federal Communications Commission, and the courts.

In doing so, however, I want to urge my colleagues to continue to keep the average ratepayer's interest forefront of our discussions. The seven regional holding companies are seeking very extensive modifications of the modified final judgment. I am sure that we will hear a great deal today about the very serious dangers of further residential telephone rate increases unless those modifications that they advocate are adopted.

We have heard these claims before. When the original AT&T Justice Department divestiture agreement was announced in 1982, the members of the subcommittee were deeply concerned about its impact on the financial health of the local operating companies. I know that executives of many of the Bell Operating Companies expressed the concern that the local companies would suffer serious financial deterioration under the original agreement. On the strength of those representations, the subcommittee pressed for a series of modifications. Judge Greene modified the agreement in accord with many of those concerns.

For a number of reasons, including the subcommittee's work, the dire predictions heard in 1982 by the Bell operating companies that they were going to go to rack and ruin never came true. The regional Bell operating companies financial performance since divestiture have been outstanding, and Mr. Chairman, I would direct your attention and that of the members of the subcommittee, to the chart before them at the present time, and also to the handouts they just received, which indicate that all seven regional holding companies had profits of nearly $1 billion or more in 1985. [See p. 40.]

The regional holding companies outperformed all other utilities last year. Overall utility profits fell 5 percent last year, while regional holding company profits grew an average of 10 percent, according to the Business Week-Standard & Poor's annual survey released this week. I would point out that this chart came directly from Business Week figures.

Even more impressive, the seven regional holding companies significantly outperformed the top 900 U.S. corporations in 1985. Average profits in all industries fell 11 percent.

Finally, investors do not appear to fear for the future of the regional holding companies, even under the existing restrictions of the modified final judgment. The regional Bell Operating Company stocks have out performed the Dow even in the record bull market of the past two years. Since divestiture, the Dow Jones Industrial Average has risen by 35 percent, and the Dow Jones Utility Average about 39 percent. By contrast, however, the stock values of four of the regional Bell Operating Companies have risen by over 70 percent, and the other three chalked up increases of 48 percent or more.

I would also draw the attention of the committee to the Xeroxed copy you have, which is a reduced version of this full page advertisement which appeared yesterday in the Wall Street Journal, run by Bell South, which says: "Bell South, two years old, and growing stronger every day."

This does not appear to be a company in need of major changes in the modified final judgment in order to prevent it from going to rack and ruin, and the other dire consequences that we have heard in the past.

I would point out, Mr. Chairman, that the regional holding companies are seeking entry into competitive manufacturing and information processing markets, but I have seen no evidence that the revenues from these activities, conducted largely on an unregulated basis, would contribute one dime to the rate base or do anything to ease the burden on the average ratepayers. We have been offered no assurances that these activities would do anything more than contribute to greater holding company profits. Much has changed in this industry since divestiture, but there remains one constant: Local telephone service remains a monopoly in every city in the country.

We have no local service competition, except in very narrow areas, in very few markets in very few cities. When you move to a new city or start a new business, there is still only one company from which to obtain local telephone service. While that is the case, I believe the subcommittee should be very cautious about allowing firms which hold such monopoly power to enter competitive fields.

It was, after all, AT&T's control of access to the customer through the local loop which ultimately gave the company the power to stifle competition for nearly two decades.

I believe strongly in free enterprise. I believe that our entire economy benefits by allowing every business to try to bring new technologies and services to the public, and I have supported competition in this industry as vigorously as anyone in the Congress for a very long time. But before making enormous changes in the existing rules, I believe we must have very strong assurances that the ratepayers will not bear the burden of financing new ventures through their phone bills, and that competition will not be diminished.

The local operating companies and their parent holding companies are in very sound financial health. They are not facing a financial or business crisis, and I urge my colleagues to take the time to examine the issues involved here carefully and thoughtfully, rather than rushing to a precipitous judgment on issues that will have a profound impact on the structure of the industry.

I thank you for allowing me to make this opening statement.

[Mr. Bryant's opening statement follows:]

STATEMENT OF THE HONORABLE JOHN BRYANT: COMPETITIVE STATUS OF THE BELL OPERATING COMPANIES

March 13, 1986

Mr. Chairman, throughout the major communications policy changes of the past several years, the members of this Subcommittee have held the interests of the average consumer to be our first priority. Unfortunately, many of the principal policy changes have been made elsewhere -- at the Justice Department, where anti-trust theory alone has ruled, and at the FCC, where deregulation, rather than the consumer's interest in healthy competition has become an end in itself.

For that reason, this is a very important series of hearings. It is well past time for this Subcommittee to examine carefully the provisions of the Modified Final Judgment, and to make careful, informed policy decisions, rather than continuing to leave them exclusively to the Justice Department, the Commission and the courts.

In doing so, however, I want to urge my colleagues to continue to keep the average ratepayer's interest paramount in our discussions.

The seven regional holding companies are seeking very extensive modifications of the MFJ. I'm sure that we will hear a great deal today about very serious dangers of further

residential telephone rate increases unless those modifications are adopted.

We have heard such claims before.

When the original AT&T-Justice Department divestiture agreement was announced in 1982, the members of the Subcommittee were deeply concerned about its impact on the financial health of the local operating companies. Although I was not a member of the House at the time, I know that privately, executives of many of the BOC's expressed the concern that the local companies would suffer serious financial deterioration under the original agreement. On the strength of those representations, the Subcommittee pressed for a series of modifications. Judge Greene modified the agreement in accord with many of those concerns.

For a number of reasons, including the Subcommittee's work, the dire predictions heard in 1982 never came true. The RBOC's financial performance since divestiture has been outstanding:

o All seven regional holding companies had profits of nearly $1 billion or more in 1985;

o The regional holding companies outperformed all other

utilities last year. Overall utility profits fell five percent last year, while regional holding company profits grew an average of 10 percent, according to the Business Week-Standard and Poor's annual survey released this week;

o Even more impressive, the seven regional holding companies significantly outperformed the top 900 U.S. corporations in 1985 -- average profits in all industries fell 11 percent;

o Finally, investors do not appear to fear for the future of the regional holding companies even under the existing restrictions of the MFJ. RBOC stocks have outperformed the Dow even in the record bull market of the past two years. Since divestiture, the Dow Jones Industrial Average has risen by 35 percent and the Dow Jones Utility Average by 39 percent. By contrast, the stock values of four of the RBOC's have risen by over 70 percent, and the other three chalked up increases of 48 percent or more.

Despite this outstanding performance and the clear judgment of the financial community that the outlook is rosy, we continue to hear that there are major competitive threats which the RBOC's cannot currently meet -- threats which might undercut the local ratebase and necessitate more residential telephone rate

increases.

The primary threat, we are told, is that competitors are offering new services which will allow major business customers to bypass the local network, leaving greater costs to be borne by residential ratepayers.

The Subcommittee has heard this before, as well. As far back as 1959, when the FCC permitted construction of the first private microwave networks over the Bell System's objections, AT&T raised the specter of bypass and higher local rates. But by 1976, 190,000 miles of private microwave networks had been built with no impact on local telephone company revenues or local rates. Similarly, the many private line services offered in the years since have had no serious impact.

The only serious bypass threat today has been created by the FCC. A major change in AT&T's long distance strategy, ignored by the FCC in many cases and encouraged by the Commission in others (such as approval of AT&T's MEGACOM tariff) could make it attractive for large numbers of business users to access AT&T long distance services directly rather than through the local loop. The AT&T bypass threat to the ratebase differs from past bypass services because of the sheer size of the company's

customer base -- AT&T continues to hold an 85 percent share of the long distance market.

But the remedy for that threat lies at the Commission, in correcting dangerous and ill-advised decisions, not in altering the MFJ. The regional holding companies are seeking entry into competitive manufacturing and information processing markets. But I have seen no evidence that the revenues from these activities, conducted largely on an unregulated basis, would contribute one dime to the ratebase or do anything to ease the burden on average ratepayers. We have been offered no assurances that these new activities would do anything more than contribute to greater holding company profits.

Much has changed in this industry since divestiture, but there remains one constant: local telephone service remains a monopoly in every city in the country. We have no local service competition except in very narrow areas, in very few markets, in very few cities. When you move to a new city or start a new business, there is still only one company from which to order local telephone service. While that is the case, I believe the Subcommittee should be very cautious about allowing firms which hold such monopoly power to enter competitive fields. It was, after all, AT&T's control of access to the customer through the local loop which ultimately gave the company the

power to stifle competition for nearly two decades.

I believe strongly in free enterprise. I believe that our entire economy benefits by allowing every business, large and small, to try to bring new technologies and services to the public. And I have supported competition in this industry for a very long time.

But before making enormous changes in the existing rules, I believe we must have very strong assurances that ratepayers will not bear the burden of financing new ventures in their bills and that competition will not be diminished.

The local operating companies and their parent holding companies are in very sound financial health. They are not facing a financial or business crisis. I urge my colleagues to take the time to examine the issues involved here carefully and thoughtfully, rather than rushing to a precipitous judgment on issues that will have a profound impact on the structure of the industry.

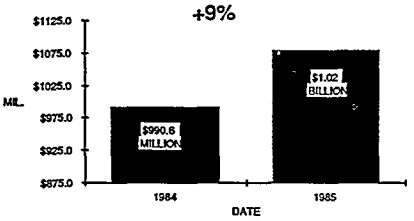
REGIONAL HOLDING COMPANY PROFITS 1984 -1985

BUSINESS WEEK UTILITY COMPOSITE 1985 PROFITS -5%

BUSINESS WEEK ALL INDUSTRY COMPOSITE 1985 PROFITS -11%

RHC AVERAGE 1985 PROFITS +10%

AMERITECH: +9%



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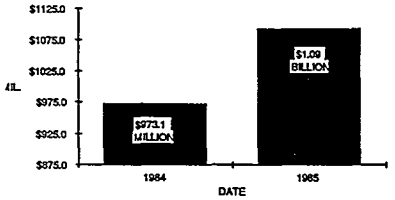

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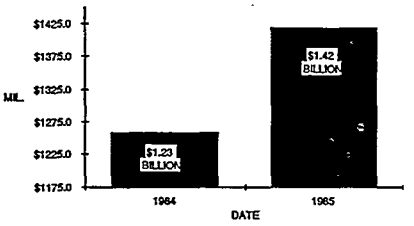

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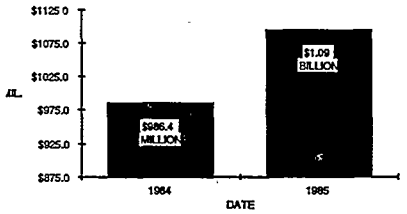

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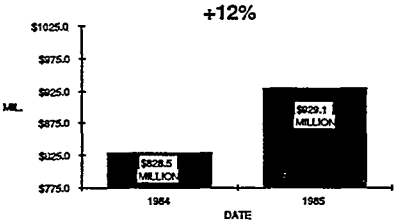

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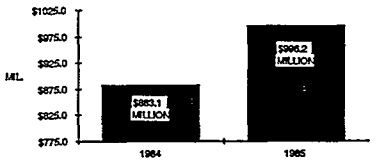

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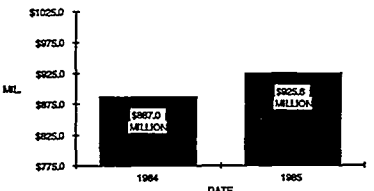


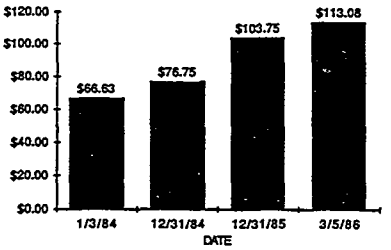
Source: Value Line January, 24, 1986, Business Week March 17, 1986.

REGIONAL HOLDING COMPANY STOCK PRICES 1984-1985

Dow Jones Utilities Average: +39%
(1/3/84 - 3/5/86)

Dow Jones Industrial Average: +35%
(1/3/84 - 3/5/86)

AMERITECH: +70%



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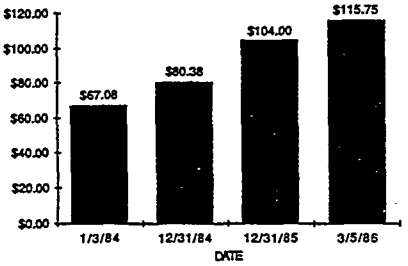

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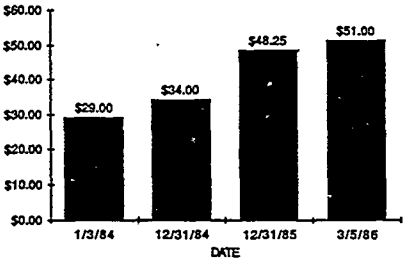

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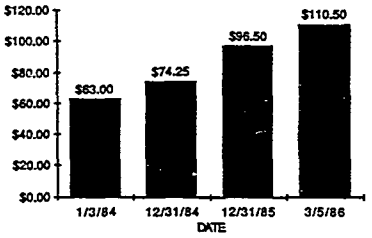

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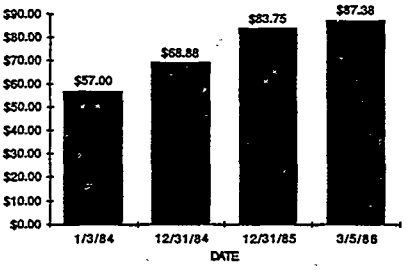

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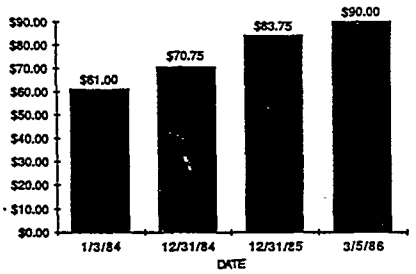

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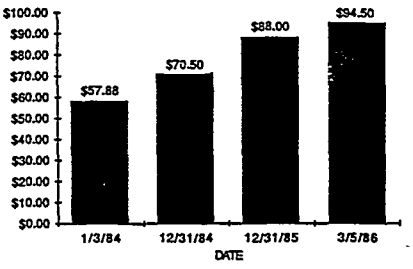

Mr. WIRTH. Thank you, Mr. Bryant. Mr. Nielson.

Mr. NIELSON. Thank you, Mr. Chairman. I also would like to welcome Rodney Joyce back. He performed yeoman service for this committee, and we hope to continue to work with you on issues of this type.

Mr. Chairman, I would like to thank you for holding this hearing. I feel the issues need to be examined. In recent committee actions, we have recognized the importance of maintaining a strong telecommunications and manufacturing capacity in this country. I feel allowing the Bell Operating Companies to engage in telecommunications equipment manufacturing and expand information services is a positive step.

The objective of the AT&T consent decree was to increase competition in the telecommunications service and products. With the decree's restrictions on the Bell companies, however, competition has not and is not likely to be extended to those small town and rural areas of the country. There is a large portion of my district that is rural, and I am naturally concerned that my constituents have access to the benefits of competition in the long distance service.

The philosophy of the consent decree sought to prevent the Bell companies from using their control of the local network to impede competition. If that control was indeed a reality at the beginning, it is certainly rendered impossible by the accomplishment of equal access as of September of this year. At that time, equal access will be available under the same conditions and cost by tariff to all carriers. Local Bell companies are not in a position to exercise any control over the process after equal access is available.

Non-Bell companies, such as MCI and United Telecom, are already able to offer long distance service, both inside and outside franchised local service areas. However, for the most part these services do not extend to rural areas, therefore, denying the benefits of long distance competition to rural areas.

In small towns and rural areas of the country, AT&T will still be the sole long distance carrier, since other common carriers either choose not to, or refuse to serve these areas because they don't think they will be as profitable.

Therefore, if these small towns and rural areas are to receive the benefit of competition in long distance service, that service must be either required by the other common carriers, such as U.S. Telecom, MCI, GTE, or it must be offered by the local Bell companies. Otherwise, these areas will not receive the benefits in the form of lower long distance rates to be derived from the divestiture of AT&T.

Put our best foot forward for the benefit of customers. The telephone network technology, international trade, and American free enterprise, the local Bell company should be allowed to offer long distance services as well as manufacture of telecommunications equipment.

I am happy to be a cosponsor of H.R. 3800 which handles the telecommunications equipment, and I also supported H.R. 3431 for trade, to allow us to enter the Japanese market, and I would like to see it extended further into competition in the other areas.

I look forward to the hearings today, and I again thank the chairman.

Mr. WIRTH. Thank you, Mr. Nielson. Mr. Slattery.

Mr. SLATTERY. Thank you, Mr. Chairman. I, too, would like to commend you for scheduling hearings to review the impact of the restrictions contained in the modified final judgment, which divested the Bell Operating Companies from AT&T and I would also like to welcome my fellow Kansan back to the committee, back to the old battleground, and wish you well in your new endeavors.

I have been particularly concerned about the restrictions which prevent the BOC's from providing information services and for manufacturing telecommunications equipment. For too long, policymaking in this area has been spearheaded by the judiciary and driven solely by that branch of Government's antitrust focus.

While antitrust considerations deserve careful attention, sound public policy in this area would also consider issues such as technological development, universal service, local rates, and the balance of trade.

The telecommunications industry is evolving at a rapid pace which far exceeds the legislative or judicial decisionmaking processes capacity to respond. This makes it increasingly difficult to justify many of the existing line of business restrictions imposed on the BOC's as part of the AT&T consent decree.

Instead of being allowed to enter lines of business dictated by consumer demand, the BOC's are only allowed to compete in those dictated by the Federal judiciary. For this reason, I am an original cosponsor of H.R. 3800. The Telecommunications Equipment and Service Act, which was authored by my subcommittee colleagues, Mr. Swift and Mr. Tauke. These two gentlemen truly deserve a lot of credit for their leadership in this important field.

This bill directs the FCC and the Commerce Department to determine if the BOC's should be allowed to engage in new lines of business, such as manufacturing telecommunications equipment and provision of information services. Allowing the BOC's to enter these lines of business would offer several benefits to American consumers. When the basic telephone network is put to greater use, all consumers benefit because the fixed costs are spread over more users, and with new services sharing the costs, pressure on local rates decreases.

There are many services that could be made more affordable to more consumers if we allowed more efficient use of the existing network. In addition, because the BOC's make up half of the domestic telecommunications industry, this legislation will help the U.S. remain competitive in world markets by introducing new competitors into the economy.

In closing, I would like to emphasize my strong belief that this legislation should be amended to include provisions which would prevent the BOC's from using any of the revenues derived from the provision of basic local phone service, or other regulated services to help pay the cost of these new services.

The goals of universal service and technological innovation are not necessarily incompatible. We should promote competition in those sectors where the market will bear it, but provide basic protection in those areas where it will not.

Representative Wyden has introduced similar legislation, including this provision.

I look forward to working with him in order to include his proposal in H.R. 3800, and I commend the gentleman from Oregon for his long history of commitment to the provision of basic, affordable telephone service to all Americans.

This legislation clearly provides us with the opportunity to do something that is good for the telephone users of this country, while at the same time making good business sense.

I am hopeful, Mr. Chairman, that we can make this bill a committee priority, and I am hopeful that we can move it quickly.

I yield back any time that I might have remaining.

Mr. WIRTH. Thank you, Mr. Slattery. We have also been joined by the gentleman from Oregon, who has been engaged in this issue on behalf of seniors, small business, and others.

Mr. Wyden.

Mr. WYDEN. Thank you very much, Mr. Chairman. I do appreciate your leadership in this area, and I think my colleagues have said it very well, and I will just make a couple of points, and I want to thank my colleague from Kansas for his kind words as well.

I think it is pretty clear that this committee feels strongly about healthy local phone companies. We understand that that is in the ratepayers interest, and I think we understand also that the changes that we are contemplating help this country deal with its burgeoning trade deficit.

But I think our concern, and a number of our colleagues have pointed it out correctly, is the prospect that a low-income senior citizen, or a handicapped person, or a small business person on a tight financial string, would be forced to subsidize the new ventures of local Bell companies unless there are explicit consumer protections. To make sure that that doesn't happen, I have introduced the Telephone Ratepayer Protection and Technology Promotion Act. What my legislation says is that the State public utility commissions must first set up regulations which ensure that none of the revenues derived from the provision of basic local phone service or other regulated services are used to pay the cost of the new competitive ventures.

One thing that I would be receptive to hearing about today, Mr. Chairman, what might be an offshoot of my resolution, where the Federal-State board would set up uniform criteria for the regional companies to get into the new competitive fields. After those uniform criteria were set up, the State public utility commissions would administer the criteria. That would be something that I would be very interested in hearing testimony on today.

The last point that I will mention, Mr. Chairman, is that I think there is a great danger if Congress surrenders this issue to the Federal Communications Commission.

The Federal Communications Commission has a track record of putting the fixed costs onto the backs of the local ratepayers. I think Congress has to make sure that in return for allowing the local Bell companies to enter into the new fields, the new fields would have to contribute to the upkeep of local phone facilities and resources they use.

If there is not some kind of provision for that we are back into the world of subsidies, and I think that is an issue that we have to deal with.

Again, I want to thank Chairman Wirth for his leadership, and the opportunity he has given me to participate.

Mr. WIRTH. Thank you very much, Mr. Wyden.

[The prepared statements of Hon. Edward J. Markey and Hon. John D. Dingell with attachment follow:]

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7TH DISTRICT, MASSACHUSETTS

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INTERIOR AND INSULAR AFFAIRS
ENERGY AND COMMERCE
CHAIRMAN
SUBCOMMITTEE ON ENERGY CONSERVATION AND POWER
COMMISSION ON SECURITY AND COOPERATION IN EUROPE

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OPENING STATEMENT OF
EDWARD J. MARKEY
AT A HEARING ON
ALLOWING THE BELL OPERATING COMPANIES TO DIVERSIFY
March 13, 1986

Today's hearing will review proposals to remove restrictions on the Regional Bell Operating Companies which prevent them from engaging in certain businesses outside of their basic regulated activity of providing local telephone service to the American public. These proposals are controversial for a number of reasons.

First, ratepayers fear that local rates might rise and local service might suffer if their telephone company is engaged in a tough, competitive fight for market share in unregulated markets such as information services or equipment manufacturing.

Second, existing competitors fear that the RBOCs will use their special access to monopoly revenues, billing histories, and other information derived from their monopoly status to subsidize or otherwise unfairly advantage their competitive subsidiaries.

Third, many observers believe that any relief from the MFJ restrictions should await the outcome of the ongoing investigation by the Department of Justice concerning the status of competition in the industry. The Department expects to complete its investigation and report by next January.

Against these criticisms, the RBOCs argue that they are no longer in any position to engage in anticompetitive behavior because they no longer control a "bottleneck". Moreover, they maintain that rules of cost allocation can be worked out to ensure that basic telephone service does not subsidize their competitive activities. In addition, they maintain that Congress should move ahead without waiting for the Justice Department's report so that the public can enjoy the benefits of their proposal as soon as possible.

The benefits claimed for allowing the RBOCs into the new lines of business are quite broad, ranging from reducing the trade deficit to developing new services unavailable from existing competitors. Frankly, I find most of the claimed benefits to be overstated. Fierce competition already characterizes many of the markets which the RBOCs want to enter. Nevertheless, one of those claimed benefits may turn out to be important enough--the benefit of allowing the RBOCs to provide services sufficient to keep major users from bypassing the local exchange.

Theoretically, at least, the danger to ratepayers from large users leaving their system could outweigh all the other risks posed by these proposals. A steadily declining customer base can only mean higher and higher rates for typical residential customers who have nowhere else to go. I have taken a special interest in the dangers of bypass and its impact on the local ratepayer, and I am sympathetic to the argument of some of the RBOCs on this issue. However, I believe this Subcommittee needs to base its decisions on something more than theory. I look forward to the testimony of the witnesses on this question, as well as responses to a series of questions on the status of bypass which I have already submitted to the FCC.

STATEMENT OF THE HONORABLE JOHN D. DINGELL
TO THE SUBCOMMITTEE ON TELECOMMUNICATIONS,

CONSUMER PROTECTION AND FINANCE

MARCH 13, 1986

I would like to thank the Honorable Timothy Wirth, Chairman of the Subcommittee on Telecommunications, Consumer Protection and Finance for holding today's hearing on the Modified Final Judgment.

The Modified Final Judgment (MFJ) signed by AT&T and the Department of Justice, and approved by U.S. District Judge Harold H. Greene, has been widely and correctly criticized for causing higher local telephone rates and enormous customer confusion and inconvenience.

This corporate restructuring -- the largest in U.S. history -- is now an accomplished fact. Reintegration of the Bell System is neither possible nor, at this stage, desirable.

However, the MFJ's restrictions on the spun-off Bell companies can and should be eliminated. Section II (D) of the MFJ prohibits the BOCs from manufacturing telecommunications services, equipment, and providing interexchange telecommunications services, information services, or "any other product or service, except exchange telecommunications and exchange access service, that is not a natural monopoly service

actually regulated by tariff."

The average citizen looks with considerable skepticism on the changes in the communications industry that have taken place over the last several years. To respond to this skepticism, the benefits of "information age" communications technology should be dispersed as broadly as possible throughout society. However, the MFJ restrictions on information services and equipment manufacturing hamstring the local companies in their efforts to upgrade local networks, and hurt small business and residential customers who are denied new services.

Local public telecommunications networks must not be allowed to become stagnant technological backwaters, while all the new service enhancements are placed in customer premises equipment or in private systems at prices that only the rich and big businesses can afford. This development would privatize the communications revolution, creating a two-tier information society. Private telecommunications enclaves would be available for the privileged, while the general public would be shackled to an increasingly outdated and deteriorating public network.

A democratic society cannot allow only an elite few to reap the benefits of the information revolution. Local companies should be encouraged to put new service enhancements in the local public networks at prices that are generally affordable to residential customers and small businesses.

Allowing the Bell operating companies into information services and equipment manufacturing is the single most important step in bringing these new services to the public. This step

also would allow the Bell Companies to compete more effectively in a fierce global market. The United States had a $560 million trade surplus in telecommunications equipment in 1982 before the AT&T breakup, but is projected to have a $1.1 billion trade deficit in 1985. The cost of this trade deficit is estimated at between 25,000 and 45,000 U.S. jobs.

The restrictions on information services and equipment manufacturing encourage large customers to place technological enhancements outside the local public network. In this way, the restrictions provide an unnecessary and unfair market advantage to software and hardware suppliers -- many of whom are foreign -- thereby adversely affecting our balance of trade in telecommunications equipment.

I am not blind to the potential for monopoly abuse, but in this case the greater danger is preventing the operating companies from upgrading local public networks.

Relaxation of the restrictions must be accompanied by effective safeguards to protect ratepayers and to reduce the possibility of cross-subsidization. A fair share of the costs of jointly used facilities must be assigned to advanced services. Local telephone companies also must provide equal access to their basic transmission services for all competitive suppliers of advanced communications services.

In its Computer Three Inquiry, the Federal Communications Commission (FCC) appears to be moving in the right direction by allowing local companies to put enhancements in the local network subject to strict cost accounting rules. However, it does no

good for the FCC to authorize the Bell companies to provide new services inside the public networks if the Justice Department and Judge Greene prevent them from providing these services at all.

The Bell Companies are also prohibited by the MFJ from providing most types of long distance service. It would be unwise to allow the Bell Companies unfettered entry into the long distance market at this time. Ultimately, however, this restriction, too, should be lifted. A complete ban on entry is not imposed on other local telephone companies, and such a ban makes no sense for the Bell companies. The real questions will be what terms and conditions are necessary to prevent anti-competitive and discriminatory practices.

Despite historical animosities, local telephone companies and competitive long distance carriers now have a clear mutuality of interest. Local companies need strong, healthy alternatives to AT&T. Long distance carriers are the local companies' largest customers. If AT&T continues to dominate the market, the local companies would be at the mercy of a single large customer.

Competitive long distance companies need local companies to provide high-quality access to customers. Their interests may well be advanced by joint ventures with local companies that enable them to provide the sophisticated end-to-end services demanded by large customers.

The process for removal of the restrictions is set out in Section VIII (C) of the MFJ: "the restrictions ...shall be removed upon a showing...that there is no substanial possibility that [a BOC] could use its monopoly power to impede competition

in the market it seeks to enter."

Unfortunately, in his rulings and in his speeches, such as the one before as the Brookings Institution, Judge Greene has interpreted this section to mean that the Bell companies may not enter the information services and interexchange markets until "they have lost their monopoly status in the local markets in which they operate."

The judge has not applied this stringent standard to attempts by the Bell companies to enter non-telecommunications markets. As a result, he has approved requests by the Bell companies to enter unrelated markets such as real estate, financial services and car rentals while delaying or denying Bell company attempts to bring their technical expertise in communications to the public.

The judge's standard for removing the restrictions also ignores marketplace realities. Bypass technology has already destroyed the unified local exchange market. Local telephone companies now serve distinct local customer groups whose needs differ. Increasingly they lack the power to limit options and dictate prices for the large-volume users who generate the bulk of their revenue. However, the local companies are likely to remain the only alternative for residential and small business customers for the forseeable future.

Telcommunications policymakers share Judge Greene's concern about the quality of local service. But the way to promote high quality, state-of-the-art local service is to allow the local companies to take steps to upgrade their networks to make them

more attractive to both large and small users. The public should not have to wait for new network services until the Bell companies have lost every last degree of monopoly power in all local market segments.

The Justice Department is conducting a review of the MFJ restrictions and intends to file a report with Judge Greene by January of 1987. There are indications that the Department may become more flexible on this critical issue. However, Judge Greene may continue to be an obstacle. Even if the Justice Department favors lifting the restrictions, the judge may continue to bar entry or may allow it only under extremely onerous conditions.

An antitrust court should not preside in an unaccountable fashion over the fate of half this Nation's telecommunications resources. In the 1934 Communications Act, Congress created the FCC to regulate interstate communications "so as to make available, so far as possible, to all the people of the United States a rapid, efficient, Nation-wide, and world-wide wire and radio communication service with adequate facilities at reasonable charges...." This Act also reserved to state agencies the authority to regulate intrastate communications.

These agencies are supposed to ensure that all parties are able to monitor and participate in regulatory proceedings that affect their interests. Full and open records are kept and ample opportunity afforded for appeal. Few such vital protections are available before the Justice Department or Judge Greene's court.

Congress did not authorizing these antitrust officials to set

themselves up as a third regulatory layer on top of the state commissions and the FCC. Indeed, the movement has already begun in Congress to move regulatory authority back to the regulators. Representative Wyden has introduced a bill (H.R. 3687) that would authorize state commissions to permit the Bell companies to enter the equipment manufacturing and information services markets. Representatives Tauke and Swift have introduced a bill (H.R. 3800) authorizing the FCC to deal with the matter.

This hearing on the MFJ will display once again the bipartisan Congressional consensus in favor of releasing telecommunications policy from the ideological stranglehold of antitrust policy, unshackling the Bell Companies, and letting the public reap the benefits of the electronic revolution.

March 3, 1986

The Honorable Timothy E. Wirth
Chairman
Subcommittee on Telecommunications
Consumer Protection and Finance
Committee on Energy and Commerce
U.S. House of Representatives
Washington, D.C. 20015

Re: H.R. 3687 and H.R. 3800, Legislation to Permit the Bell Operating Companies to Provide Enhanced Services and Manufacture Telecommunications Equipment

Dear Chairman Wirth:

The National Association of Regulatory Utility Commissioners ("NARUC"), whose membership includes the commissions of the fifty States engaged in the regulation of utility companies and common carriers, respectfully wishes to inform the Subcommittee that the Association is carefully examining the above-referenced legislation and the broader issue of permitting the Bell Operating Companies (BOCs) to diversify into other areas of business other than those currently allowed by the terms of the AT&T consent decree.

As you may know, the NARUC Committee on Communications met during the NARUC Winter Meeting of its Executive Committee, February 24-27, 1986, in Washington D.C.. During these meetings, extensive consideration was given to the issues of BOC diversification in general, and the Tauke and Wyden Bills, H.R. 3800 and H.R. 3687, respectively, in particular. The members of the Communications Committee concluded that further examination of the impact of BOC diversification upon universal telephone service and industry growth is required before taking a position on either of these legislative proposals. Nevertheless, we wish to emphasize to the Congress that we generally support the concept of BOC diversification and we will continue to carefully examine each measure. Indeed, we have established a Subcommittee to examine these issues and report back to the full Committee by April 11, 1986. We also wish to communicate to you the principal concern raised during

Although our members concluded that there is probable consensus favoring BOC entry into other, functionally related, areas of business and manufacturing of telecommunications equipment, our discussions were dominated by concern over State authority to regulate the Regional Holding Companies' (RHCs') operations of new business ventures entered into by the regulated operating companies. For example, although the operating companies are authorized under the MFJ to publish yellow pages, operation of the yellow pages business has, in many States, been transferred to the RHCs who in turn have established subsidiaries to provide these services. These subsidiaries are not subject to regulation by State public service commissions. Our members are sympathetic to the need of the BOCs to diversify. However, we are extremely concerned about the authority of State commissions, which is unclear at best, over the operations of the RHCs. Indeed, if the trend with respect to yellow pages continues to develop, serious questions as to oversight of the diversified activities of the RHCs must be addressed.

We will continue to examine the Tauke and Wyden bills, as well as future legislative proposals, and look forward to elaborating on the thoughts expressed herein during the March 13, 1986 hearings on MFJ issues.

Should you require additional information, please feel free to contact me.

Sincerely,

E. Bruce Hagen
Chairman
NAPUC Committee on Communications

cc: The Honorable John Dingell
The Honorable Al Swift
The Honorable Ron Wyden
The Honorable Thomas J. Tauke

Mr. WIRTH. We have a long hearing this morning, and the Chair is, as usual, going to operate under the 5-minute rule, recognizing members in the order of their appearance. We will also ask all of our witnesses if they would summarize their testimony in 5 minutes, and we will, of course, include their statements in full in the record.

Our first panel this morning includes two representatives of the administration. The Honorable Douglas Ginsburg, Assistant Attorney General for Antitrust at the Department of Justice. Secretary Ginsburg and I have been on a number of panels together, and while we haven't always agreed, he certainly presents a point of view in a very engaging and thoughtful fashion. Mr. Ginsburg we are delighted to have you with us this morning.

Our second panelist is the Honorable Rodney Joyce, Acting Assistant Secretary for Communications and Information at the Commerce Department, who continues in the long tradition of this subcommittee of opening our hearings with testimony from previous staff people who have gone from here to do very well on the outside.

I also notice we have another one in the back who has a good sun tan. Obviously, his practice is going very well.

Mr. Ginsburg, we are delighted to have you here, and thank you very much for joining us.

STATEMENTS OF DOUGLAS H. GINSBURG, ASSISTANT ATTORNEY GENERAL, ANTITRUST DIVISION, DEPARTMENT OF JUSTICE; AND RODNEY L. JOYCE, ACTING ASSISTANT SECRETARY, COMMUNICATIONS AND INFORMATION, NATIONAL TELECOMMUNICATIONS INFORMATION ADMINISTRATION, DEPARTMENT OF COMMERCE

Mr. GINSBURG. Thank you, Mr. Chairman. It is a great pleasure to be here in the company of Rodney Joyce, and my comments today will address several of the issues identified by the subcommittee in its letter of invitation.

I should add, however, that the Department is studying H.R. 3687 and H.R. 3800, which are pending before the subcommittee. The administration has not formulated any views on that legislation, so I will not be addressing that directly.

Our economic success in the decades ahead in the international marketplace depends vitally on our ability to foster technological growth through research and development. Our telecommunications system has to accommodate a growing demand for ever more sophisticated and specialized services that satisfy diverse user needs, and at the same time provides high quality, low cost basic information services to residential users.

As the Federal agency responsible for enforcement of the modified final judgment in the AT&T case, we at the Department are committed to a competition-based policy that fully achieves the decree's purposes. At the same time, we are very much aware of the rapid changes that are occurring in the telecommunications industry, and of the necessity to avoid falling into the trap of enforcing fixed rules and regulations beyond their useful life.

The decree was designed to foster competition in long distance service, by requiring the BOC's to provide access to central office switches for all long-distance companies that is equal to the access they provide to AT&T, and this process of conversion to equal access is scheduled for completion in the next 6 months.

The restrictions in the decree on BOC activity are based on historical and analytical factors indicating two competitive dangers that can arise when rate-regulated monopolies such as the BOCs participate in adjacent competitive markets.

Each of them have been alluded to by various members of the subcommittee this morning. Briefly, they are first and most significant, the danger that arises when in order to compete in adjacent markets, rivals require access to the rate-regulated natural monopoly facilities, here a BOC's local exchange network. The rate-regulated monopolist has the incentive to exclude or to discriminate against rivals in the otherwise competitive market in order to earn supracompetitive profits that rate regulation prohibits it from earning in the monopoly market.

The second concern involves the potential for anticompetitive cross-subsidization. The rate-regulated monopolist has an incentive to include in its rate base for the regulated activity investments, and even current expenses, that are actually attributable to its competitive businesses.

In such circumstances, the monopolist can reduce the price it charges to consumers in the competitive market, and then recoup its loss of income from customers of its monopoly services. Ultimately, the monopolist may then be able to drive its more efficient rivals out of the competitive market, and may obtain power to raise prices in that market as well.

During the 2 years since the AT&T divestiture, the BOC's have very frequently taken advantage of the decree's section VIII (C) waiver provision in order to enter into competitive businesses. The waiver provision in the decree itself represents a mechanism in order to balance the competitive dangers that I have just identified with the very real possibility that diversification by the BOC's may result in significant competitive benefits.

At the Department, we have conditionally supported all waiver requests that have not involved entry into traditional long distance services, information services, or the manufacture of equipment, each of which is specifically restricted by the decree.

We are also keenly interested in improving the efficiency of the waiver process. We want to avoid policies that would require a BOC to return to the court each time there is a change in its business strategy, and for that reason we have sought to broaden many of the waiver requests that the BOC's have presented to us.

Moreover, last fall we filed a petition with the court, joined by five of the BOC's, to make the process of obtaining waivers less time consuming in those several situations where a BOC is seeking a waiver that is substantially similar to one that was already recommended by the Department, or even approved by the court.

Now, our administration of the waiver process has been designed in part to prevent BOC's from misallocating costs to the rate base. And while this process has the beneficial effect of protecting ratepayers, protecting them from burying the costs of the BOC's com-

petitive ventures, its purpose is really to protect competition in the market that the BOC's seek to enter.

The FCC and the State public utility commissions, not the Department of Justice and not the decree court, have primary responsibility for the protection of ratepayers. Some policymakers argue that allowing the BOC's to offer new competitive services will provide revenues that can be used to reduce local rates. If competition in the market being entered is not impeded, however, by the BOCs entry into that market, there will be no excess revenues to subsidize local telephone rates because competition will prevent the BOCs from earning supracompetitive profits in their new markets.

But that is not to say that entry by the BOC's into other businesses will never benefit local ratepayers. To the contrary, the BOC's development of new products and new services, and the facilitation of the provision of such services by others, should stimulate usage of the phone system and as a consequence, individual usage should cost less than it otherwise would.

Mr. WIRTH. Mr. Ginsburg, may I ask you to summarize so we can stay on that 5 minute schedule?

Mr. GINSBURG. Certainly, Mr. Chairman. You are familiar with the process of conversion to equal access, and the companies' progress toward that goal of equal access. It is detailed in my prepared statement, and I will just skip that if I may.

I would like to add, though, that equal access is a concept that we think has further application to the provision of information services as well, and in the context of the FCC's *Computer III* inquiry, which is now giving serious consideration to implementing equal access for information service providers, we have been very supportive of the concept that the BOCs should be allowed to get into information services under those conditions.

[Testimony resumes on p. 72.]

[The prepared statement of Mr. Ginsburg follows:]

STATEMENT

OF

DOUGLAS H. GINSBURG
ASSISTANT ATTORNEY GENERAL
ANTITRUST DIVISION

Mr. Chairman and Members of the Subcommittee:

I am pleased to be here today to discuss the Department's enforcement efforts with respect to the modified final judgment in the AT&T case (hereinafter "MFJ"). My comments today will address several of the issues identified by the Subcommittee: the competitive status of the seven regional holding companies ("BOCs"); whether the MFJ line of business restrictions should be modified or removed; whether there are mechanisms that are necessary to protect ratepayers; and the current Federal Communications Commission's Computer III Inquiry. The Department is studying H.R. 3687 and H.R. 3800, which are pending before the Subcommittee. The Administration has not, however, formulated any views on this legislation, and so I do not address it.

Our economic success in the next two decades in an international marketplace will depend largely on our ability to foster technological growth through research and development. The growth of the telecommunications industry is central to that development. Thus, it is important that this country continue to maintain the best telecommunications system in the world. Our telecommunications system must accommodate a growing demand for more sophisticated and specialized services that satisfy diverse user needs and at the same time provide high-quality, low cost basic communications services.

As the federal agency responsible for enforcement of the MFJ, we at the Department are committed to a competition-based policy that fully achieves the decree's purposes. At the same time, we are very much aware of the rapid changes that are occurring in the telecommunications industry. We will not fall into the trap of enforcing fixed rules and regulations beyond their useful life.

I. Historical Framework of the MFJ

The MFJ has brought about one of the most significant industrial restructurings in our country's history. By requiring AT&T to divest its regulated local operating companies, the decree caused the creation of the BOCs. The decree left to AT&T the potentially competitive manufacturing and long-distance businesses, as well as a significant portion of Bell Labs. The local plant and facilities, as well as sufficient assets to establish a joint research and development organization, now known as Bellcore, were assigned to the BOCs.

The decree is designed to foster competition in long-distance service by requiring the BOCs to provide access to central office switches for all long-distance companies that is equal to the access provided to AT&T. This process was begun in 1984 and, with some exceptions, is scheduled for completion

by September of 1986. Additionally, the BOCs are enjoined from otherwise discriminating between AT&T and the other long-distance providers. The BOCs were also limited generally to providing local-exchange telecommunications and exchange-access services unless a waiver is obtained from the decree Court.

The restrictions in the decree on BOC activity are based on historical and analytic factors indicating that two competitive dangers may arise when rate regulated monopolies, such as the BOCs, participate in adjacent competitive markets. The first and most significant danger arises when, in order to compete in the adjacent markets, rivals require access to the rate regulated, natural monopoly facilities (here a BOC's local-exchange network). Under such circumstances, the rate-regulated monopolist has the incentive, and may have the ability, to limit its rivals' access to its monopoly facilities, or more likely in the present circumstances, to provide access only on discriminatory terms that disadvantage its rivals in the competitive market. The rate-regulated monopolist has the incentive to exclude or to discriminate against rivals in the otherwise competitive market in order to earn supracompetitive profits that rate regulation prohibits it from earning in the monopoly market. The control of the monopoly may also give the rate-regulated monopolist the ability to impede competition by its rivals in the adjacent

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markets if the rivals must have unimpeded and non discriminatory access to the monopoly in order to compete effectively.

The second concern involves the potential for anticompetitive cross subsidization. Under rate-of-return public utility regulation, a monopolist is entitled to earn up to a set return on its investment in facilities used to provide the regulated service. The monopolist has an incentive to include in its rate base for the regulated activity investments and current expenses that are actually attributable to its competitive activities. In such circumstances, the monopolist can reduce the price it charges consumers in the competitive market and recoup the loss of income from customers of its monopoly services. The monopolist may ultimately drive more efficient rivals out of the competitive market and may obtain the power to raise prices in that market. Moreover, as a result of cross-subsidization, consumers of the regulated monopoly service are charged more than the true cost of providing those services.

It was because of these competitive concerns that the decree, as originally drafted, envisioned an absolute ban on BOC diversification. As entered by the Court, however, section VIII(C) of the decree permits the BOCs to obtain waivers from the decree restrictions if they can show that there is no substantial possibility that they can use their monopoly power

over regulated service to impede competition in the market they seek to enter. Section VIII(C) thus represents a mechanism to balance the competitive dangers identified above with the very real possibility that diversification by BOCs may result in significant competitive benefits.

II. Operation of the Line of Business Restriction Waiver Process

During the two years since divestiture, the BOCs have frequently taken advantage of the VIII(C) waiver process. As of March 7, the Department has received 89 waiver requests (more than 3 per month). The Department has forwarded favorable recommendations to the Court respecting approval of 62 requests, and has objected to only 2 requests. The Court has approved 54 requests and has 8 pending before it.

The Department has conditionally supported all waiver requests that have not involved traditional landline long-distance services, information services, or the manufacture of telecommunications equipment or customer premises equipment -- each of which is specifically restricted by the decree. We have recommended that the Court include in all granted waivers conditions designed to prevent opportunities for cross-subsidization and discrimination and to ensure that the firms are not authorized indirectly to offer services that they would not be able to offer directly.

The Department is keenly interested in improving the efficiency of the waiver process. We seek to avoid policies that would require a BOC to return to the Court each approved business strategy. The Department has therefore sought to broaden many waiver requests. We have also carefully avoided conditions that would require our ongoing monitoring of the competitive ventures' activities or of any transactions between the venture and the affiliated BOCs. We are very much aware that we are a law enforcement agency, not a regulatory agency; therefore, we have attempted to minimize and if possible, avoid altogether--any conditions that require ongoing supervision by the Department.

Moreover, last fall we filed a motion, joined by five of the BOCs, to make the waiver process less time-consuming in those situations where a BOC is seeking a waiver substantially similar to a waiver already recommended by the Department or entered by the Court. We hope and expect that the motion will be granted by the Court and will further expedite the current waiver process.

The Department's administration of the waiver process has in part been designed to prevent BOCs from misallocating costs to the rate base. While this process has the beneficial effect of protecting ratepayers from bearing the costs of the BOCs' competitive ventures, its purpose is to protect competition in

the market the BOC seeks to enter. The FCC and the state public utilities commissions, not the Department or the decree Court, have primary responsibility for the protection of ratepayers. It appears that since divestiture, those regulators are more actively and successfully identifying improper cost allocations. They are using separations requirements and new cost accounting rules to ensure that BOC diversification costs are not borne by local ratepayers.

Some policymakers argue that allowing the BOCs to offer new competitive services will provide revenues that can be used to reduce local rates. If competition in the market being entered is not impeded, however, there will be no excess revenue to subsidize local telephone rates because competition will prevent the BOCs from earning supracompetitive profits. That is not to say that entry by the BOCs into other businesses will never benefit local ratepayers. To the contrary, the BOCs' development of new products and services and their facilitation of the provision of such services by others should stimulate usage of the phone system and, as a consequence, individual usage should cost less than it would otherwise.

III. Equal Access

The Department's primary decree enforcement effort has been to ensure that equal access is implemented effectively. Last year, following an investigation of the manner in which AT&T discharged its obligations to achieve equal access for

long-distance carriers, we required AT&T to make certain changes to its order processing systems. We have also supported the FCC's efforts to foster equal access by recommending the adoption of ballot and allocation procedures by which local telephone subscribers choose or are assigned to a long-distance carrier.

Recently, we completed an extensive investigation of the BOCs' implementation of equal access. I am pleased to report that, after some initial difficulties, the BOCs are making substantial progress in implementing equal access. Many of them have now moved past the half-way mark in converting end offices to provide equal access to their customers' phone lines. Our role has been to ensure that the BOCs provide to customers and to long-distance carriers accurate and timely information acknowledging the receipt of orders and notifying carriers of any conflicts. In addition, we are seeking to ensure that orders are processed and activated in a timely fashion. To that end, a number of BOCs have implemented new order processing systems that are more accurate, understandable, and timely.

While the process seems to be working better today than it was six months or a year ago, the size and complexity of the entire undertaking would indicate that some other problems may arise before the conversion to equal access is complete. We will, of course, continue to devote the resources necessary to ensure that the equal access requirements of the MFJ are satisfied in 1986.

In addition, the FCC has supplemented the decree's equal access requirements for AT&T and the BOCs by imposing equal access obligations on independent local-exchange carriers. It is clear that we and the Commission have a common goal -- to foster competition to the maximum degree possible.

IV. Computer III

Equal access is not, however, a concept that is limited to long-distance service; it applies to the provision of information services as well. The Commission, in the context of its Computer III Inquiry, is giving serious consideration to implementing equal access for all information service providers. If technically feasible, equal access may make it possible to permit dominant carriers, such as the BOCs, to enter newly-developing information services markets without impeding competition. The Department believes that the Commission generally should condition the authority of the BOCs to engage in information services on the BOCs' providing to others the same interconnection to its bottleneck facilities that it provides to itself or its affiliates.

Equal access for information service providers has three essential components. First, the technical quality of the connection must be equal. Second, all users, including the BOC's affiliates, must be provided unbundled access at the same

fee under tariff. Third, the location of the information service provided by a BOC affiliate should not disadvantage a competitor. This may mean that if a BOC or its affiliate provides the service at its central office site, then other providers must be allowed to colocate there, as well. We believe that the feasibility of equal interconnection is perhaps the most important issue in the Commission's Computer III Inquiry, and it will be a important aspect of our January 1987 report to the Court.

The Department has also supported, in principle, replacing the separate subsidiary requirements currently imposed under the Commission's Computer II rules with accounting rules that can effectively prevent cross-subsidization. In an "open architecture environment," accounting and information disclosure rules may be adequate to minimize any competition risks that otherwise might result from allowing a bottleneck monopolist to engage in both regulated service and competitive ancillary services. While it may be difficult to develop and enforce such rules, the potential benefit of encouraging the development of our telecommunications system makes such proposals worthy of serious consideration.

V. 1987 Report

At the time the MFJ was entered, the Department, conscious of the rapid rate of technological change in the industry, committed itself to investigating changes in the

telecommunications industry three years after the divestiture of AT&T and to reporting our findings to the decree Court. We are moving with dispatch to fulfill that commitment. Our expert, Mr. Peter Huber, working in cooperation with the Division's Communications and Finance Section, has begun gathering the economic, technical, and marketing data necessary to make a considered evaluation that will provide the basis for the Department's Report to the Court. That Report will carefully examine all competitive factors in the telecommunications industry that bear on the future of the decree. The Report will also address broadly the issue of BOC diversification.

Mr. Huber has already contacted representatives from all interested sectors. The Annenberg School, in cooperation with the Department, recently conducted an informational seminar for the specific purpose of identifying and focusing the issues for the Report. Representatives from all interested governmental organizations attended, and participants representing the BOCs, long-distance carriers, information services providers, equipment manufacturers, user groups, consumer groups, and state regulatory agencies discussed the issues that Mr. Huber will evaluate. Moreover, the Department, on behalf of Mr. Huber, has sent out a letter seeking comments and data on a variety of issues. Thus, the factual inquiries necessary for the Report are well underway. I am confident that the

Department will be able to meet its deadline and file its Report with the Court in January 1987.

One hears a great deal today about "bypass," that is, the alleged ability of large businesses to connect directly to a long-distance carrier without going through the local exchange. Some BOC's have argued that the phenomenon now is so pervasive that it has eliminated the bottleneck monopoly characteristic of the local-exchange network. Of course, if the practical ability to bypass the local exchange did exist for most long-distance callers, competition would reign supreme in exchange-access service, and the concerns that motivated the AT&T case and the decree would disappear. While we will carefully study the issue of bypass in our 1987 Report, we currently have no reason to believe that bypass has eliminated the local exchange bottleneck. Surely households and, in terms of absolute numbers, all but a small minority of businesses continue to face a monopoly provider of local-exchange service and of access to long-distance and information carriers.

Regardless of the state of bypass, however, technological changes in the form of open architecture -- that is, equal interconnection and colocation -- may so reduce the ability of the rate-regulated, bottleneck monopolist to provide discriminatory access to its facilities that an absolute ban on entry into adjacent competitive markets -- at least information services markets -- may no longer be necessary. As a result,

open architecture may provide an environment in which it is possible for regulators and courts to control any residual competitive or regulatory problems with considerably less onerous and costly conditions. If technology can be developed that makes interconnection to the local switch for all information services providers truly transparent and equal, then the benefits of keeping the BOCs out of information service may no longer outweigh the costs.

The telecommunications industry has undergone massive changes in the last five years. The AT&T divestiture has only accelerated the underlying and broader changes resulting from the merging of technologies in the computer and communications fields. Thus, it is imperative that the Department keep abreast of these changes and continue to understand current market conditions in the telecommunications industry insofar as they affect the BOCs and competition in markets adjacent to local telephone services. We fully intend to do so.

Mr. Chairman, that concludes my prepared remarks. I would be happy to respond to any questions that you or other members of the Subcommittee may have.

Mr. WIRTH. Thank you very much, Mr. Ginsburg. Mr. Joyce.

STATEMENT OF RODNEY L. JOYCE

Mr. JOYCE. Thank you, Mr. Chairman. Members of the subcommittee. I appreciate this opportunity to discuss this morning the competitive changes that have taken place in the American telecommunications industry, and to suggest some of the steps which the Government should consider in light of these developments.

For more than a decade, Government communications policies have aimed at reducing both the level and the intensity of Government regulation of the telecommunications industry. The basic objective has been to foster innovation, to expand customer choices, and generally to substitute greater reliance on the marketplace forces for Government decisionmaking. The procompetitive and deregulatory policies which have been pursued by the past four administrations have had strong bipartisan congressional support, and they have produced substantial public dividends. American consumers and businesses today enjoy a broader array of communications equipment and service choices than anywhere in the world.

And very importantly, the increased competition and the resultant customer gains have had virtually no adverse impact on other important national goals, such as ensuring the continued universal availability of basic telephone services for all Americans at reasonable and affordable prices.

Telephone subscribership levels in this country today are as high as they have ever been.

Competition is furthest along in two industry segments, long distance service and terminal equipment provision, and we expect competition in these sectors will continue and will grow stronger as the years go by.

Another part of the communications business that seems likely to become more competitive in the future is the provision of local transmission services. This is the part of the business in which the Bell companies now make their living.

Six years ago, NTIA studied competitive trends in this industry segment, and we concluded that at that time it probably would be the next frontier for competition development, and today we are beginning to see competition emerge on this frontier as local transmission alternatives appear around the country.

Competitive developments in local service undercut Government regulations premised on the notion that local transmission constitutes a "natural monopoly." These new competitive developments also indicate a need to reexamine our existing policies towards local communication services.

Last year, NTIA released a report entitled, "Competition Benefits," It assessed public gains and losses due to competition and deregulation in 14 communication sectors.

That report shows that this country's procompetitive policies have, on balance, provided substantial public benefits. Prices have fallen in many cases, choices for consumers have expanded, innovation has been encouraged, and new business and employment opportunities have been provided.

Last year our agency also published a general review of U.S. domestic communications policies, and we examined the areas where we believe significant reforms are still warranted. Our Domestic Policy Report looked at existing approaches not only in terms of their impact on the communications industry, but we also assessed those policies in terms of their consequences for continued American technological leadership, foreign trade, and making sure that ordinary telephone subscribers have a chance to benefit from the advances which have taken place in this field.

We at NTIA are now in the process of building upon these two 1985 reports as well as our earlier report on the next frontier, and we plan to release a detailed assessment of actual and potential competitive conditions in local telecommunications markets later in the year.

It is important that we have the most accurate and up to date information that is available regarding increased local service competition. This is because so many government policies today are based on the premise that there continues to be a natural monopoly bottleneck, an assumption that some experts now maintain is becoming increasingly obsolete.

In conclusion, when Secretary Baldrige last testified before the subcommittee, he stated that today more than ever telecommunications policy has important social, political, and economic implications. Our national leadership, he noted, is being challenged more than ever before. Unnecessary regulation will needlessly hobble the industry, and thus will have an adverse effect on American enterprise.

Needless regulation will also burden consumers. He said we must be willing to ask ourselves whether existing government procedures and regulations are helping or hindering our communications industry as it seeks to compete more effectively both in this country and abroad. At NTIA, we are doing what we can do to fulfill the Secretary's commitment, and to ensure communications policies which will contribute to the overall competitiveness of this key sector of the economy.

That concludes my prepared statement, Mr. Chairman.

Mr. WIRTH. Thank you very much, Mr. Joyce.

The record will be left open for 30 days for other questions and comments that you may want to add.

Mr. Joyce, the BOC's have stated that lifting the MFJ restrictions will benefit the average consumer by making more services available. I'm sure that we all agree that consumers deserve the advantages associated with new technologies and new services, and that the average local telephone customer would benefit directly from being able to access such services through their local telephone company.

Could you tell us, in your opinion, what types of new services would you anticipate that consumers might be able to receive if local telephone companies were not prohibited from providing information services to consumers?

Mr. JOYCE. Well, of course, it's difficult to say specifically what the marketplace will end up providing. That would depend, to a significant extent, on what services consumers want.

We can look, to some extent, to what services are being provided by the local phone companies in other countries of the world which don't have restrictions of the sort that exist in this country. I'm told that even, for example, in Bombay, India, the telephone company provides its telephone customers with a morning wake-up service. That's a service that, at least theoretically, there might be a market for in this country.

Mr. WIRTH. So, you are saying if we go through all of this, American consumers will get wake-up services?

Mr. JOYCE. What I'm saying is that is theoretically one market possibility.

Mr. WIRTH. I mean, is there a list or a catalog of these? If we open this up for information services, how are consumers going to benefit from this?

Mr. JOYCE. Well, as I say, it depends. The precise nature of the services for which there might be market opportunities can't be predicted in advance.

Mr. WIRTH. Mr. Ginsburg, what in your opinion would occur and what's the position of the Justice Department of having consumers have access to these services?

Mr. GINSBURG. If the proposition, as I understood it, was that prohibition on entry into information services were simply deleted wholesale, just removed from the environment, my prediction is that the consumers would receive some additional information services from their telephone companies, but fewer services at higher prices and a lower quality than would otherwise be the case.

The otherwise is a case-by-case selective examination of proposals that the telephone companies bring forward to provide information services and to do so under terms that enable competitors, where practical, to compete with them in the provision of those same services.

Mr. WIRTH. So, you are suggesting that there are new services from which consumers would benefit from.

Mr. GINSBURG. I think the consumer is going to benefit from new information services provided through the telephone system.

Under the current situation with the decree restriction in place, the consumer will benefit even more if a means can be devised to allow the telephone companies to participate in providing those services. I think the least desirable outcome for consumers would be one in which the restrictions are simply deleted without protections put in place to prevent the telephone companies from monopolizing the information services in question.

Mr. WIRTH. Let me put it the other way. Let me put it negatively. Are there services that consumers won't get if the restrictions stay in place?

Mr. GINSBURG. Well, I think there is actually one experience where a service has, in fact, not been offered because of the current restrictive environments. This was a call-forwarding service that would not have been provided but for special relief.

But I think the basic point is that these new information services need to be accommodated in the most competitive possible fashion. That means either by keeping the telephone company out of the business or by letting it into the business subject to safeguards.

Mr. WIRTH. Let me jump to another issue, Mr. Ginsburg, on my time to an issue that people are familiar with, yellow pages, which it seemed to us were a natural function and extension of local telephone companies.

Telephone ratepayers help finance these profitable enterprises and in most cases the revenues derived from yellow pages provided a significant contribution to local telephone companies' regulated activities. In Colorado, I believe about $1.50 goes to the local ratepayer from yellow page revenues.

In 1982, this subcommittee unanimously approved legislation that would have left the lucrative yellow pages with the local telephone companies rather than with AT&T, and that was included in the MFJ.

However, we now understand that some regional BOC's have shifted their yellow page operations out of their regulated operations and into unregulated subsidiaries. This arrangement, at least in part, would appear to abandon the intent of both the Congress and the court, that the revenues derived from yellow pages continue to support local ratepayers.

In some cases, the regulated BOC's now receive only a fixed publishing fee from the regional holding company.

Can you tell us what the Justice Department is doing to ensure the yellow page revenues are used to hold down local rates?

Mr. GINSBURG. Mr. Chairman, the yellow page business is, in fact, becoming competitive. I would rather predict that instead of finding the yellow page revenues being used to hold down local rates, we will find yellow page revenues declining in the face of competition.

One of the regional holding companies is now entering—at least one—the business of publishing competitive yellow pages in areas served by other telephone companies, not within the holding company. Now, under the decree it was contemplated, as you said, that the yellow page revenues would be a source of income to support local service.

In fact, however, there is nothing in the decree that enables us to control the structural change that you described, or to prevent it for that purpose. We have no control under the decree over what the BOC's do in this area.

Mr. WIRTH. What should we do, then? It was the intent of the Congress and of the court, it was my understanding, to ensure that yellow page revenue would continue to go to local rates. Should we abandon that goal?

Mr. GINSBURG. I think it's fair to say, Mr. Chairman, that that was the court's contemplation, and that it expected that through the measures provided in the decree, by leaving the yellow page business with the local telephone companies, it would be providing a source of additional revenue to hold down local telephone rates.

That contemplation is perhaps frustrated or disappointed to the extent that the companies are able lawfully to rearrange the yellow page function within the holding company. But I think we should be pleased to see that business moving toward a competitive status.

There is nothing inherently monopolistic about the publication of a yellow page directory. If an entrepreneurship under either the re-

gional holding companies or others provides consumers with the benefit of competitive yellow pages——

Mr. WIRTH. Again, let me go back to the question. Should that money go back to support the local ratepayers?

Mr. Joyce, what's the Commerce Department or the administration's position on that?

Mr. JOYCE. Well, we don't have a specific position on that narrow issue.

Mr. WIRTH. It's a pretty big issue. I mean, the rates in Colorado are $8 a month approximately, and $1.50 comes—that's 20 percent of the rates. That's not a narrow issue.

That's a pretty big issue.

Mr. JOYCE. Negative things could happen if government regulators force a business enterprise engaged in a competitive activity to use the profits from that competitive activity to subsidize some other line of business. There is a risk that if that occurs—if that kind of government action occurs—that the company engaged in that business would simply discontinue providing or engaging in that particular line of business.

I don't think that there is anything in the decree that explicitly says that the profits from the Bell Companies provision of yellow pages directory should be used to subsidize local telephone rates. The decree simply says that particular line of business would go to the Bell telephone companies rather that AT&T.

It leaves it up to State regulators, as I recall it, to make a decision on how the profits would be handled in each individual state. If some States which previously required profits from yellow pages' operations to be used to subsidize local telephone rates have discontinued that regulatory practice, I suspect in part it's because they have recognized that, as the yellow pages publishing business becomes increasingly competitive, they simply can't continue that practice, else the Bell companies would leave the business.

Mr. WIRTH. Let me say just two comments and then go to the next question.

First, it seems to me from what we have heard this morning is that the administration does not have a position. Your job is policy position, not enforcing the consent decree; the administration does not have, therefore, a policy on yellow page revenue being used to hold down local rates.

Second, that the only concerns that we have heard from the administration this morning is a concern that the only goal that we are looking at is a goal of encouraging competition. That's fine. I think that is shared here. The goal of competition is shared.

But we also have a goal of trying to figure out what kinds of revenues are going to go to hold down local rates to assure universal telephone service at a price everybody can afford, which I think you touched on in your opening statement, Mr. Ginsburg. We share that goal as well.

The question is: How does yellow pages feed into that? I haven't heard either of you saying that there is a policy of the administration that something that is as major as this and symptomatic of other competitive offerings ought to be used to help local ratepayers.

You heard the local ratepayer concern all morning long up here. But let me go on. We can come back to this, I'm sure.

So, Mr. Coats.

Mr. COATS. I have nothing of this panel, Mr. Chairman.

Mr. WIRTH. Mr. Oxley.

Mr. OXLEY. No.

Mr. WIRTH. Mr. Nielson.

Mr. NIELSON. No.

Mr. WIRTH. Mr. Moorhead.

Mr. MOORHEAD. We have always been concerned that if the monopoly used their money that they made on monopoly to finance a competitive business, you are going to run into some real problems and some unfair practices.

But in the inverse, some kinds of businesses might make money one year and lose it the next. If you were using the profits off of a side business that was not regulated to finance the monopoly operation, you could well find the situation where there was a loss in one particular year, and you would be violating the principle that we've tried to develop through the years here, that you don't mix the profits of one with the profits of the other.

I would like your comment on that.

Mr. GINSBURG. Mr. Moorhead, I think that's just one of the reasons one has to be cautious about searching for sources of revenue to support—essentially to cross-subsidize—low local rates.

The idea of creating adjacent monopolies, like a yellow pages monopoly, or relying upon competitive businesses which may have their good years and their bad to supply revenues that can then be dedicated to the subsidization of local telephone rates, seems to me to be a policy that is not only mistaken but almost certain in the long run to fail in bringing out an efficient telephone system.

Mr. NIELSON. Mr. Chairman, may I ask a couple of questions of Mr. Joyce?

Mr. WIRTH. Yes.

Mr. NIELSON. What are the chances of rural customers ever receiving information service if the Bell Operating Companies are not allowed to offer them?

What realistic chance do they have of receiving information services?

Mr. JOYCE. Well, the Bell telephone companies are, in all likelihood, better equipped to efficiently and economically provide information services——

Mr. NIELSON. So, you would recommend they be allowed to do that?

Mr. JOYCE [continuing]. So it probably means that if the Bell Companies were allowed to engage in that business with appropriate safeguards, chances are that the rural telephone customers would have those services available to them more expeditiously.

Mr. NIELSON. And you would look favorably on that possibility?

Mr. JOYCE. Yes.

Mr. NIELSON. What kind of trends has the NTIA observed with respect to the exportation of research and development?

Will these trends be affected by allowing the Bell Operating Companies to manufacture, provide information services?

Do you believe that the exportation of the research and development will be enhanced or lessened if they are allowed to manufacture and provide information services?

Mr. JOYCE. Well, again no one can be certain what will occur. But one of the phenomenons that occurs generally in a competitive open environment is a promotion of innovation, a promotion and an increase in technological research and development. To permit fair and open competition in new market segments in the telecommunications industry, by companies which are well equipped to become active competitors, might well have those same stimulative effects, to increase productivity, increase innovation and increase research and development throughout the industry.

Mr. NIELSON. Do you think lifting the restrictions will affect the trade balance significantly?

Some say it will. Some say it won't. How do you feel?

Mr. JOYCE. Again, no one can be certain. But what some would say is that the restrictions imposed on the Bell telephone companies today are, in effect, a trade barrier erected by our country, our own Government.

There is a lot of talk in this country about unfair trade barriers erected by foreign governments, and indeed there are a number of foreign governments who make it difficult, unnecessarily difficult, for American companies to compete. We have in this country, arguably, a trade barrier of our own, by prohibiting potentially very significant and very important competitors from competing in very significant lines of business.

Mr. NIELSON. So you think that H.R. 3800 is possibly something we should examine very carefully and take a good look at?

Mr. JOYCE. The idea of opening up the telecommunications marketplace to fair competition is one that is worthy and ought to be explored. Yes.

Mr. NIELSON. I read in the paper that the administration is opposed to H.R. 3431, as passed by this committee, and is seeking to have it killed in the Ways and Means Committee.

Is that correct?

Mr. JOYCE. Frankly, I don't know what position, if any, the administration has taken on that particular——

Mr. NIELSON. Congressman Matsui was able to get such a statement from the trade representative in the Ways and Means Committee, and that was not stated in this committee when we passed that bill by a similar representative.

Mr. JOYCE. As I say, I don't know what, if any, position the administration has taken on that particular bill.

Of course, that bill does not deal with the—nor does it have any provision included within it that deals with the AT&T consent decree.

Mr. NIELSON. Thank you, Mr. Chairman.

Mr. COATS. Mr. Chairman, may I ask one question of Mr. Ginsburg?

Mr. WIRTH. Yes.

Mr. COATS. Mr. Ginsburg, if Congress decides not to address this issue in this session and we wait for the Justice Department report due in January 1987, how long do you anticipate that it might be before the court, the FCC, might take action based on your report?

Mr. GINSBURG. Mr. Coats, let me say, first of all, that the FCC may well take action even before then. The current matter pending there of greatest relevance is the Computer III Inquiry, and that may well be resolved even before the end of this year.

As for the court's consideration of our findings and any recommendations that accompany them in January 1987, it's not possible to predict when the court would resolve the issues that we raise. I think it is fair to anticipate, however, that any changes that we may recommend in the decree would be the subject of adversarial proceedings and that it would take at least a matter of several months before the court were able to complete them.

Mr. COATS. So we are probably at least 18 months away?

Mr. GINSBURG. We are more than a year away from changes based on our report, and I would hope not more than—if any changes are recommended, not more than 18 months.

Mr. COATS. Thank you.

Mr. BRYANT [presiding]. The Justice Department is preparing a comprehensive review for the court on the competitive status of the BOC's. Many of us believe that antitrust concerns alone cannot guide the development of the telecommunications industry.

I believe that communications policy goals such as universal service at affordable rates must be fully taken into account. I think it's fair to say that you are guided principally by antitrust concerns, whereas Mr. Joyce, your mandate is to advise the President about communications policy.

I think there are many of us on the committee who are concerned that the communications policy goal of providing universal service at affordable rates is adequately considered in whatever recommendations are ultimately submitted to the court.

Mr. Joyce, what procedures for making recommendations to the court would you suggest so that the court is fully apprised of the communications policy objectives, particularly the goal of assuring that local ratepayers benefit, or at least are protected, in the event the restrictions are lifted?

Mr. JOYCE. Well, I have two responses. First, the Commerce Department staff is working closely with the Antitrust Division staff in an attempt to assist them in the preparation of the materials which they are, at present, undertaking to compile.

And, second, since the Commerce Department has its own jurisdiction and its own peculiar interests that are not strictly antitrust related, we are doing our own research. We are compiling materials and updating previous studies that we have undertaken. Ultimately, what we envision happening is sometimes toward the end of the year the administration as a whole—based upon materials submitted and made available by the Antitrust Division of the Justice Department and materials on the telecommunications and trade policy matters that have been provided by the Commerce Department, and perhaps other materials provided by other agencies of the Government—the administration, perhaps the Cabinet or the President will make the final decision on what, if any, recommendations to make to the court in the way of revising the consent decree.

The administration's ultimate recommendation undoubtedly will be based upon a full analysis of the communications policy issues, the antitrust issues, and all the other issues that are raised.

Mr. BRYANT. Mr. Ginsburg, do you have any objections to having NTIA's input in conducting the Justice Department's review with respect to the steps that should be taken to ensure that ratepayers benefit, or are at least protected, in the event that there is a modification to the decree?

Mr. GINSBURG. In doing the report to the court, Mr. Chairman, we are seeking input from as wide an array of sources as possible, beginning with other Government agencies, NTIA, the FCC, and so on, but also extending to every affected element in the relevant industries.

To this end, you may know that recently the Annenburg Foundation here in Washington held a meeting at which perhaps 30 or 40 representatives of all of those different interests, including the staff of this subcommittee, participated in order to help inform the debate and advise the Department and its expert about the issues that should be addressed.

So, we are anxious to have that sort of input from every possible source.

Mr. BRYANT. The Chair would recognize the gentleman from Ohio, Mr. Luken.

Mr. LUKEN. Mr. Ginsburg and Mr. Joyce, there are a couple of new buzzwords that have emerged during the debate over whether to relax these MFJ and FCC restrictions. One is "comparably efficient interconnection" or CEI, and the "open network architecture" or ONA.

There appears to be no clear consensus about what these terms mean. I would like to go into that. The FCC states in Computer III that the BOC should be allowed to offer enhanced services through their local networks as long as they provide competitors with interconnection that is comparable to their own interconnection in terms of price and function.

Open network architecture is not defined at all, and the BOC's along with the rest of the industry seem to disagree on what it might mean.

Now, Mr. Ginsburg, the development of healthy competition in the information service and long distance markets will depend on the ability of the competitors to obtain access to BOC facilities, a point that I think you made, under the same terms and conditions that the BOC's provide to themselves. The Justice Department has told the FCC that it believes that open network architecture, rather than regulation, could allow the BOC's into unregulated markets as long as the FCC specifies interconnection standards.

You have made these points. Does that state your position conceptually at least?

Mr. GINSBURG. Yes, it does. And I think it is also fair to say that there is not precise content yet to the terms that you used.

Mr. LUKEN. Well, that's what I wanted to ask. Do you believe that these concepts then should be more specifically defined and more fully implemented before the BOC's are allowed into the new markets?

Mr. GINSBURG. Yes. I think we have advised the FCC that that would be necessary and have encouraged the FCC, whose role it really would be, to undertake just that task.

Mr. LUKEN. Well, do you think it's realistic to develop such a system?

Mr. GINSBURG. Well, based on what we have seen thus far, which is admittedly preliminary coming from some of the BOC's, we are hopeful and optimistic that it is practical to do so.

Mr. LUKEN. Can you amplify on that? What are the problems?

Mr. GINSBURG. Well, some of the problems are still a matter of some dispute, even at this preliminary stage, among various observers in this field.

For instance, the significance of colocation is not yet clear. It has been our view that the location of an information—the equipment associated with providing an information service should not be—should not put the independent company at an avoidable disadvantage compared to the BOC.

Mr. LUKEN. At what time in the future could such a system be developed for the colocation problem to be worked out?

Mr. GINSBURG. Well, I think that if the FCC takes up this mandate, it could resolve most of these questions in fairly short order. I would hope this year or early next year.

It would need to get information from the BOC and from other members of the industry in order to be able to resolve the matters on the basis of a full understanding, though.

There is no——

Mr. LUKEN. They could get information as to whether it's feasible.

Mr. GINSBURG. As to whether it's feasible or——

Mr. LUKEN. We don't know whether it's feasible.

Mr. GINSBURG. Well, we don't know whether it's feasible to—we don't know exactly what is feasible in this area, but what we want to identify is really the—a system that is feasible and that minimizes the disadvantage under which the non-BOC providers would labor.

Mr. JOYCE. Mr. Luken, just as a point of information on that, on that issue, as I'm sure you know, the FCC has begun a formal process and has requested public comments from all interested parties on how to go about defining "comparably efficient interconnection." They have received literally reams of paper from scores of parties within the last couple of months I think.

A new round of submissions are being prepared and being sent in about now. So there is a process underway at the FCC now to define——

Mr. LUKEN. To define, but then actually arriving at putting it in place, that seems to be pretty far into the future.

Mr. GINSBURG. Well, not necessarily, Mr. Luken. Let me say that just a few years ago, the concept of equal access for interexchange carriers was also just that, a concept that had never been proven, let alone implemented. And, yet here we are——

Mr. LUKEN. You think these are comparable?

Mr. GINSBURG. I think we are at a similar stage to where we were in 1982 with respect to equal access, providing for its implementation before anybody knew exactly what it looked like.

And I think it's a great tribute to the BOC's that they, in working with the interexchange characters (sic)—carriers—have given a definition. Now, there are still going to be problems with it. Even with equal access, there are issues that have not been resolved that have not even yet been confronted.

Nobody knows yet what constitutes a bona fide request with respect to end offices that won't be converted in 1986. But we will get to those when we have to.

Mr. LUKEN. Mr. Joyce, incidentally, I don't think I am more influenced to visit Bombay because of the central wake-up service than I was before. But NTIA has repeatedly advocated the removal of the MFJ restrictions and the relaxation of Computer II, the separate subsidiary requirements. However, NTIA has emphasized the complexity of the CEI, which we've just been talking about, and has stated these complexities deserve serious intention.

Now, even if the open network architecture and CEI are eventually defined and become feasible objectives, as we've been discussing, to ensure the development of competitive markets, are you suggesting that the restrictions on the BOC's be relaxed before these concepts become a reality?

Mr. JOYCE. No, I think that——

Mr. LUKEN. What time do you think the relaxation should occur?

Mr. JOYCE. We have suggested that equal access should be provided, and we believe that it can be provided—defined and then provided—fairly expeditiously, and simultaneously the prohibition on information services should be removed, simultaneously.

Mr. LUKEN. Simultaneously? But not one independent of the other?

Are there other safeguards such as accounting and cost allocation that are also necessary to protect the ratepayers? Would that still be necessary before the BOC's get into competitive ventures?

Mr. JOYCE. Yes. I think that no one would disagree but that there ought to be in place a whole series of procedures to ensure that there is no predatory conduct.

And one important——

Mr. LUKEN. Well, that's a——

Mr. JOYCE [continuing]. Feature is the accounting separations.

Mr. LUKEN. Does that insulate? Is that what the accounting separation does? Do we have a catch-22 here?

If we insulate the disadvantages from possible losses, don't we also take away from the advantages that we are seeking of getting into the unregulated ventures and, therefore, providing a broader property base, and also profit base upon which the ratepayer would benefit?

Mr. GINSBURG. Mr. Luken, I think if the safeguard procedures are unduly burdensome, the result is to diminish the incentive to diversify into those other businesses and to deprive the consumers as well as the companies of the benefits of that diversification.

Now, currently the FCC has a separations requirement that it's reconsidering in the light of the possibility of relying instead on accounting techniques which are considerably less burdensome and costly.

And we have encouraged it to pursue that, that line of reasoning, and to see whether it can't, by relying on the new uniform system

of accounts, which should be final next month I think, at that point drop the separation requirements and rely on the accounting techniques. That would be a great advance.

Mr. LUKEN. Well, the accounting techniques are a form of insulation, right? We are insulating against cross-subsidization. We are separating the entities or the operations.

Mr. GINSBURG. It's purely an accounting separation, however. It does not require physical separation, separate corporations, separate subsidiaries, all of the trappings that are now required.

Through the accounting approach, one simply uses the uniform system of accounts to allocate and track expenditures.

Mr. LUKEN. Well, it doesn't insulate the ratepayer from possible losses which the unregulated venture might incur, does it?

Mr. GINSBURG. I believe it's intended to do just that.

Mr. LUKEN. Then, it insulates. It isolates.

Mr. GINSBURG. I will accept that wording.

Mr. LUKEN. So, if it isolates the ratepayer and insulates the ratepayer against loss, isn't it also going to insulate the ratepayer from this corresponding benefits of that unregulated business?

Mr. GINSBURG. I see your point. The benefits that I contemplate would come from the BOC's entry into an information service and not in the cross-subsidy of local rates. They are in the provision of that information service on a more efficient basis than would otherwise be possible.

If the telephone company has the natural advantage in providing the information service, if it has an advantage that no one can really compete with, it should be allowed to provide that service to those who take it. But there should be a mechanism to make sure that only those who use the service pay for it.

And the accounting system will direct itself to concerns like that. It will not result in cross-subsidization.

This notion that somehow the entry into competitive businesses is going to generate revenues with which to hold down local rates is a misleading and dangerous one, Mr. Luken. Competitive businesses do not generate rents from which to cross-subsidize other businesses. They generate a competitive return on capital, and no more.

Mr. LUKEN. And you've advanced the position that unless the regulated monopoly utilizes its monopoly power, it's not likely to make money. That's what you said in your statement.

If it gets into a competitive business without some anticompetitive advantage, it's not likely to make money.

Mr. GINSBURG. It will make just a competitive return on its investment.

Mr. LUKEN. What types of cost allocations plans would you recommend?

Mr. GINSBURG. I'm sorry. I didn't——

Mr. LUKEN. What kind of cost allocation plans would you recommend, cost allocation?

Mr. GINSBURG. Well, I think that's addressed by the uniform system of accounts that the FCC is developing, under which common equipment used in both the monopoly and competitive service would be compelled——

Mr. LUKEN. Would the competitive services contribute to the joint or the common costs?

Mr. GINSBURG. To the extent that they used common equipment, certainly.

Mr. LUKEN. They should pick up a fair proportion, then?

Mr. GINSBURG. Yes.

Mr. LUKEN. Thank you, Mr. Chairman. You've been very tolerant.

Mr. SWIFT [presiding]. The Chair will recognize the gentleman from Iowa.

Mr. TAUKE. Thank you, Mr. Chairman. Mr. Ginsburg, following up on what Mr. Luken just asked you, is it not true then that if the competitive services share the common costs that that would be of help to the ratepayer for basic telephone service?

Mr. GINSBURG. If the common cost is no greater than it otherwise would be.

Mr. TAUKE. Right.

Mr. GINSBURG. But let me take a simple example. The General Counsel's function within the holding company may require the addition of more lawyers than otherwise would be the case. And surely the competitive services should be held accountable for the incremental costs incurred by that office because of the entry into the competitive business.

In the case of a joint case that can't be broken up that way, one has to make some sort of fair allocation, as Mr. Luken suggested. And that would be a gain if the alternative is that the ratepayers are left covering the entire costs themselves.

Mr. TAUKE. So, if you have all additional costs covered by the competitive operation, and you have shared—you have all common costs shared, then the ratepayers do receive some benefit even though there is not a direct subsidy from the competitive arena to the monopoly?

Mr. GINSBURG. Yes. Now, that, of course, presupposes that there is existing excess capacity in the rate base which can be used to support the competitive service.

Mr. TAUKE. Right.

Mr. GINSBURG. That should be——

Mr. TAUKE. And if there is no excess capacity, the ratepayers wouldn't lose because any excess would have to be picked up by the competitive side?

Mr. GINSBURG. That's correct. And, of course, the State public utility commissions do try to assure that there is no unreasonable—such excess capacity by prohibiting companies from stockpiling large parcels of real estate and all of that sort of thing unless they are going to be used in the provision of the regulated service in the very immediate future.

Mr. TAUKE. Mr. Joyce, you indicated in the answer to an earlier question that one of the competitive services was wake-up calls which alarmed some of our members.

I wonder if we could run through some other services that might be offered and see if you agree with me that these are possibilities. I have observed in the past that voice message storage services could be available, computer protocol conversion that would allow incompatible computers to talk to one another might be available,

utility monitoring services, health monitoring services to allow elderly citizens especially, for example, to have heart monitors or other kinds of monitors that would alert senders for emergency care needs, various indirected data bases could be offered in conjunction with third party vendors, such as airline schedules or library services. You could have at-home shopping. Are all of these kinds of services things that are within the realm of possibility if we have the restrictions on information services lifted?

Mr. JOYCE. I think absolutely. The possible array of new services is quite exciting. And new innovations undoubtedly would be developed—could be developed almost daily to provide new opportunities for telephone customers that simply can't and don't exist today, in part because of the restrictions.

Mr. TAUKE. Mr. Ginsburg, taking——

Mr. JOYCE. If I may just follow up with one—to try to make the point perhaps a little more clearly, to use one specific example in addition to the call wake-up service.

Today, telephone companies, of course, don't offer a voice storage service which is one of those that you mentioned. But telephone customers can provide for themselves that kind of service by purchasing what is oftentimes a very expensive recorder-phone device that they hook on to their own telephone.

The purchase of that device, of course, is beyond the means of some—of a great number of telephone customers, perhaps costing $200 to $150.

If the telephone companies were allowed to provide that kind of service, by in effect putting a very large recorder phone device in their telephone company offices, and then allowing telephone customers to subscribe to that service for a monthly fee, perhaps that convenience of a recorder-phone kind of service could be made available to the far broader array of customers than can afford it today.

We don't know whether that could occur and would occur, but it is certainly a conceivable possibility.

Mr. TAUKE. Mr. Ginsburg, in the course of your testimony, you have indicated that you are seeking to find information from a variety of sources within the administration to prepare your study which you will be submitting to the court in January 1987.

I wonder if you can tell me if the statement that will be submitted to the court will be representative of the Justice Department's position, or will it be representative of the administration's position, and if that statement is going to take into account only antitrust considerations, or if it will take into account a variety of other policy considerations that might be considered when we make policy in this area.

Mr. GINSBURG. Our undertaking to the court was to report on the competitive conditions within the telecommunications industry and in that regard, we are talking about essentially a factual report.

That factual report will be the outcome of the process now underway, that process is a factual inquiry being conducted by an expert engaged by the Department for that purpose.

When the facts are in, I think it will be appropriate for the administration to make such recommendations to the court through the Department, as it deems appropriate. But there has to be some

rather clear distinction between the factual basis from which we are operating, which is being assembled in discharge of our obligation to the court, and on the other hand, the recommendations that we may make on the basis of those facts.

Mr. TAUKE. I understand that. But could you clarify for me if you have to rely primarily on antitrust considerations as you compile facts? Is it in that arena, the competitive arena, or do you when making policy recommendations, do you go beyond antitrust considerations and policies and look beyond to other broader telecommunications policies?

Mr. GINSBURG. Well, within the framework of the decree in which the report is based, I think it would be somewhat limited and considerations—to take an example as far afield as possible—such as employment effects, would not likely be deemed relevant to the antitrust court, although I think they would be relevant to the Congress and should be directed to the Congress rather than to the court.

Mr. TAUKE. So, those things really couldn't be considered by the court, but obviously could be by us in making policy judgments.

Mr. GINSBURG. Yes, sir.

Mr. TAUKE. One last question. Mr. Ginsburg, we had quite a bit of discussion about the obvious problems with cross-subsidization and other things relating to the Bell Operating Companies, especially as we look at these new services and new arenas of business, but as I look at the makeup of the telecommunications industry, I note that the fifth largest of the companies that offered local service in 1984 revenues for operations in this country is GTE, which obviously is involved in local telephone service, where it has monopoly in the long-distance arena. It provides enhanced services through GTE tele net. It produces telecommunications equipment, and does a few other things besides.

How does the regulatory process that has to operate to protect GTE consumers, how does that differ from what would have to be in place in order to protect the BOC consumers?

Mr. GINSBURG. Well, the principal difference between the consumer subscriber to GTE's telephone services, and the AT&T consumer is as follows, and we face this in the context of the consent degree entered into when GTE sought to acquire Sprint, the long distance arm.

The GTE telephone subscribers are not only many fewer in number than those of any of the RBOC's, but they are scattered geographically around the country. One finds them in Los Angeles, in Little Rock, and in Tampa, and a few other population centers, and the affiliation of their local telephone company with a long distance company does not pose a significant threat to competition in the same way we think is true in the rest of the country, because telephone calls originating in—let us say the Tampa market—unless they are going to another area also served by GTE, would not be able to travel entirely along GTE's facilities.

Mr. TAUKE. Mr. Ginsburg, I hesitate to interrupt, but I think we are two trains passing in the night here. My customers, or my constituents in Dyersville, IA, are served by GTE, and they have excellent service, a fine company.

But when the Iowa Commerce Commission sets rates for the customers of local telephone service in Dyersville, how do they know that those rates aren't being jacked up in order to support GTE's manufacturing sector. And if they can figure that out for the folks in Dyersville, IA, who are served by GTE, why couldn't they figure it out for the folks in Dubuque, IA, who are served by Northwestern Bell?

Mr. GINSBURG. Well, it is the burden of the State public service commission to determine that the charges being passed along to ratepayers are only the appropriately incurred charges. That task is somewhat more haunting if the company is affiliated with activities in a lot of different markets, to be sure.

That task remains to the extent that any local regulated monopoly has unregulated activities affiliated with it. Now, I think it is perhaps—there is some benefit, perhaps, to being able to compare, for the local public service commission, the presentations made by one company as compared with another in the same State, so that significant discrepancies in their cost claims can be identified, and in fact that is happening at the federal level too, now that we have multiple regional companies.

Mr. TAUKE. Thank you, Mr. Ginsburg. I guess the point is that in some instances it is being done.

Thank you, Mr. Chairman.

Mr. SWIFT. Let me ask of the chairman of the full committee, would you like to go now, or would you like to go and answer the vote. We are going to try and keep the committee rolling, and we will defer to your desires.

Mr. DINGELL. I do not ask for my desires. I will be glad to sit there in the chair and ask the questions while the members of the subcommittee go vote.

Mr. SWIFT. Mr. Wirth is going to be back in time for us to go anyway, so why don't you do whatever is most convenient.

Mr. DINGELL. I want to do what pleases the Chair.

Mr. SWIFT. I will sit here and look important, while you sit down there and be important.

Mr. DINGELL. You are very kind. Thank you, Mr. Chairman. With those understandings then, Mr. Chairman, I have two unanimous-consent requests. First, that I be permitted to insert into the record an opening statement, together with a letter from the communications committee of the National Association of Regulatory Utility Commissioners, at an appropriate place. [See p. 47.]

Mr. SWIFT. Without objection.

Mr. DINGELL. I would like to begin with a simple statement that I take no sides with regard to who should achieve what benefits, or prosper in what way with regard to the breakup of AT&T, and I am neither a pleader for the Bell Operating Companies, nor for AT&T, nor against any of them or any other person.

I am very much distressed at the process which I see I would like to direct this question to Mr. Ginsburg with regard to the process followed by the Department of Justice and Judge Greene with regard to matters before the judge.

Let us take specifically the question of waivers. I believe that the process has two steps; first, a Bell Operating Company files with the Department of Justice. Then the Department of Justice recommends for or against to the court. There is opportunity for comment at both stages. I am not certain that the comment reaches the judge, however, and the comment is particularly a process in which opponents participate. There are a number of meetings between the Department of Justice staff and industry. No public record is kept, or is available. I am told that the judge does not meet privately with either the Department of Justice staff or industry. Is that a fair description, Mr. Ginsburg, of the way the waiver process works?

Mr. GINSBURG. I can't speak for the judge's practices, except with respect to the Department, and we do not meet privately with him.

Mr. DINGELL. OK.

Mr. GINSBURG. Otherwise, I think that is a fair description.

Mr. DINGELL. That varies rather startlingly from a rule making process before, or other process before the Federal Communications Commission, does it not? It also varies rather startlingly from the requirements as imposed by the Administrative Procedures Act, with regard to the rights of the interested parties either AT&T, a complainant, or a Bell Operating Company, if they were before the FCC.

Mr. GINSBURG. It is a different procedure than contemplated by the APA for formal rulemaking.

Mr. DINGELL. Is there any notice given with regard to any waiver request, or any other matter that might come before Judge Greene? Is there any printing in the Federal Register? I believe the answer is, no.

Mr. GINSBURG. When we receive a waiver request, we make that information publicly available. It does not appear in the Federal Register. It appears in our regular releases.

Mr. DINGELL. You might say that that notice is sufficient. That anybody who is lucky enough to find out about it will know it, and those who are not blessed with good fortune will not. Is that a fair statement?

Mr. GINSBURG. Well, it seems to me since scores I think in excess of a hundred people have participated in various waiver proceedings, that there is wide publicity about each of these petitions.

Mr. DINGELL. Well, can you oppose my description of the matter. For example——

Mr. GINSBURG. I just don't know whether there is anyone who is unaware, given the trade press coverage of these issues, Mr. Dingell.

Mr. DINGELL. That simply means you are unaware of those who are unaware. It doesn't mean that you know that there are people unaware. Or that you know that anyone who would like to know is unaware.

Mr. GINSBURG. And that would be equally true if we published in the Federal Register, I must say.

Mr. DINGELL. Of course, everybody is aware of the fact that the Federal Register is the mechanism which is utilized to inform people of rulemaking and similar matters before Federal regulatory bodies, an action in which Judge Greene is diligently engaged.

Mr. GINSBURG. That is true, Mr. Dingell. Let me say that in the 2 years of experience that we have had here, I don't believe we have yet heard from someone who claimed not to have been aware at the appropriate time of the pendency of a waiver petition, and to have been prejudiced thereby.

Mr. DINGELL. Now, does the department solicit the views of the Department of Commerce?

Mr. GINSBURG. Well, we don't solicit views in each of these petitions unless there is some special reason to. As I say, we notify the public of them, and we receive comments while the matter is under review in the department, and then, of course, the court receives comments again while the matter is pending there.

Mr. DINGELL. Have you ever received views from the Department of Commerce?

Mr. GINSBURG. Yes, we have.

Mr. DINGELL. I believe that the Department of Commerce cannot file views independently with Judge Greene, can they?

Mr. GINSBURG. No. It is not a party to the case, sir.

Mr. DINGELL. OK. Nor can the FCC?

Mr. GINSBURG. Well, non-parties—let me say that non-parties are free to submit matters to the court. The court—although not as a matter of right—but the court has had a practice of considering whatever has been submitted to it.

Mr. DINGELL. What does that mean? 'The practice of considering.' I find that an interesting word. Did they consider matters in the same fashion that the FCC would?

Mr. GINSBURG. It means that when, for instance, the court issued its most recent opinion concerning Pacific Telex's acquisition of Communications Industry, it made repeated references to the views of various other firms that had submitted comments, and dealt with their comments in the course of its opinion.

If I may correct myself for the record, the FCC can and does submit comments in these proceedings.

Mr. DINGELL. Do they submit them to the Department of Justice, or directly to the judge?

Mr. GINSBURG. To the court.

Mr. DINGELL. To the court directly. Tell me what are the resources available to the court to review the comments and other information which is made available to it in connection with its review of the breakup? The judge has two law clerks?

Mr. GINSBURG. I am not aware of what resources the court has beyond those normally available to any Federal district court judge.

Mr. DINGELL. So, they would be the same as any Federal district judge, two law clerks?

Mr. GINSBURG. Whatever that would be.

Mr. DINGELL. And the Department of Justice essentially provides them the staff for the judge in dealing with these matters?

Mr. GINSBURG. Well, in that we sift through, analyze, and make a recommendation along with our analysis for the judge——

Mr. DINGELL. So, the answer to that is, yes.

Mr. GINSBURG. That can be seen as performing a staff-like function, but we are not accountable in the same way as a staff would be to the judge to come to a particular conclusion.

We make a recommendation.

Mr. DINGELL. You have uttered one of my concerns. Now, in dealing with a waiver request, does the Department of Justice have the obligation to keep a public record of all meetings with interested parties?

Mr. GINSBURG. I don't believe we do, no.

Mr. DINGELL. Is such a record kept?

Mr. GINSBURG. No, it is not.

Mr. DINGELL. Are parties able to reply to statements and allegations of other parties in the suit? For example, are they able to reply to opponents with regard to off-record contacts?

Mr. GINSBURG. Well, we receive written comments from one party, for instance, and other parties may then comment on those comments.

Mr. DINGELL. You also receive oral comments, do you not?

Mr. GINSBURG. If we have a meeting with an interested person, then there are oral comments.

Mr. DINGELL. Is any other person informed of oral comments received from one party, or from one source?

Mr. GINSBURG. Only insofar as we may relate them in the course of our recommendation to the court.

Mr. DINGELL. Now, in my days as a law clerk to a Federal judge, if one of the parties to the suit wanted to come before him, he insisted that all parties come before him. He also relied on the public record, and not upon one of the parties to the lawsuit as being essentially staff. Is there anything that has changed in the Federal rules of civil procedure that has caused this remarkable change in the way matters are processed before the court?

Mr. GINSBURG. I don't think there is anything particularly novel or modern about the procedure that the court has set up.

The consent decree was agreed to by AT&T and the United States, and the waiver provision, instead of providing that matters be submitted originally to the court, provides that they be submitted originally to the United States for a recommendation.

Mr. DINGELL. Who has the right to appeal decisions by the judge. For example, if the judge ruled that one of the Bell Operating Companies could get into businesses that are prohibited, such as the long-distance market, could MCI appeal?

Mr. GINSBURG. Well, first let me say in answer to your first question, a party may pursue an appeal to the court of appeals, and a nonparty, an interested person, may also appeal by seeking leave of the court to intervene for the purpose of appeal.

That has not happened, by the way, Chairman Dingell. No nonparty has sought to appeal a line of business order.

Mr. DINGELL. Now, the Huber investigation referred to in your testimony is going to be the Department's report to the judge, is that correct?

Mr. GINSBURG. That is correct.

Mr. DINGELL. Will it be a factual basis for the Department's report to the judge?

Mr. GINSBURG. Well, Mr. Huber is compiling a factual record that is meant to describe the state of competition in the telecommunications industry. If those facts suggest to the Department or the administration that we should recommend changes in the modified final judgment, then we will clearly separate it from the facts themselves, and also make such recommendations.

Mr. DINGELL. Who is being consulted in connection with this study and who has the opportunity to present comments on this matter to the judge? What is the process for a person making comments with regard to the factual statements, or with regard to the recommendations?

Mr. GINSBURG. With regard to the facts being assembled by Mr. Huber, we have sought to get comments from as wide an array of interests as possible. Indeed, he is ready to speak with anyone that is interested in the subject, and has met with scores of interested parties already.

When the report is submitted to the court, if there are recommendations associated with the report, the court may decide to have a hearing on those recommendations. That is beyond our ability to predict.

Mr. DINGELL. Will the public have any opportunity to comment on the Department's recommendations before they are sent to the judge? And when I say public, I mean BOCs', ordinary citizens, industrial consumers of telecommunication services, or any other person who might have an interest.

Mr. GINSBURG. I would anticipate that the appropriate time for comments on our recommendations will be after—if we make any—will be after we make them.

Mr. DINGELL. After May?

Mr. GINSBURG. Yes. We are gathering the facts, and if those facts suggest to us that we should recommend changes in the decree, we will make our recommendation and any changes will necessarily, of course, require the consent of the court, and undoubtedly a full process within the court.

Mr. DINGELL. Mr. Ginsburg, I note that my time is rapidly coming to a conclusion, and I want to thank the chairman for having been so patient with me, and I want you to understand that my comments here are not hostile to any party to the proceeding or anybody else in the telecommunications business, nor in any way are they in any fashion to indicate a lack of confidence or respect for you.

I am one who is very concerned that the processes and procedures of our Government be fair to all persons, and that everybody have an opportunity to appear, have appropriate notice, and that the decisionmakers shall function on a record which shall, in fact, be reviewable. I note enormous amounts of these sorts of require-

ments are absent in the process which is going forward before the judge in spite of your best efforts, and I am satisfied in spite of the best efforts of Judge Greene, for whom I also have the highest respect.

Let me just ask again how are parties able to reply to the statements and allegations their opponents make in off-the-record comments?

Does the Department act as a messenger, essentially asking each party to comment on others' allegations?

Mr. GINSBURG. In evaluating a waiver petition, we receive—assuming we receive comments from other interested persons—we would explore all of the issues raised by those comments by going back to the petitioning company and demanding satisfaction on any of the things that have been raised and brought to our attention.

Mr. DINGELL. This is a process which, however, is dependent upon both the skill, the good fortune, the careful review of the record, and the integrity of the Department. Is that not so? There are no built-in requirements in the process which would give anyone confidence that we may rely on anything other than the good character and the skills of the Department?

Mr. GINSBURG. Any party, and particularly any petitioner that believes that the Department hasn't discharged itself properly with respect to a petition, may go to the court notwithstanding our objection to the petition.

Mr. DINGELL. I just would observe that no scandal has yet occurred, but I believe you have before you a process which invites scandal. If such does occur it will be, I believe, hair curling. I would urge you to address the process defects which I observed, and also to be apprehensive of the fear which I have, and I hope you share, that this process does invite scandal by denying full participation in sunlight. As has been observed by one of the Justices of the Supreme Court, the best prophylaxis is sunlight as opposed to functioning in dark places.

Mr. GINSBURG. Mr. Dingell, I think the process suffers from several defects, but I really didn't think that the potential for that sort of scandal was one of them. I think the important defects are that it is time consuming, resource intensive, and intrudes the Department to an unwarranted degree in the plans of the various companies.

Mr. DINGELL. I will not quarrel with the defects you find, but I do observe the others. Can you tell us how this process is implementing the requirements of the 1927 or the 1934 statute, which set out a number of congressional policy directions with regard to the assurance of adequate and appropriate telecommunications services at fair and appropriate prices?

Mr. GINSBURG. The decree itself derives not from the Federal Radio Act of 1927, nor the Communications Act of 1934, but rather from the antitrust laws.

There is no conflict, I think, between those two different sources of law, however, insofar as the courts have always held that the Communications Act is to be interpreted in such a way as to give correct sway to competitive considerations.

Mr. DINGELL. I have no problems with the idea that there should be competition, especially under the 1934 act and the antitrust laws, but the 1934 act sets forth a number of other national goals, including universal service and a number of other matters including fairness in pricing and access to the citizenry. How is that being implemented under the process now going forward before the judge?

Mr. GINSBURG. The process going forward before the judge does not have any direct effect on pricing, and pricing decisions still have to be made pursuant to tariff procedures at the FCC.

Mr. DINGELL. You will concede, however, that pricing decisions which are based on some structural decisions may be quite different than pricing decisions which would be founded upon a different set of structural determinations by the judge, is that not so?

Mr. GINSBURG. I am sorry, I just don't understand that question, Mr. Dingell.

Mr. DINGELL. The judge may make one of two determinations with regard to the structure of the industry. That decision under conventional ratemaking law, could imply quite possibly two different pricing structures? Is that not so.

Mr. GINSBURG. That is possible.

Mr. DINGELL. What attention is being given under the antitrust laws by the judge to the pricing consequences, the questions relative to universal service, or other matters included in the 1934 statute.

Mr. GINSBURG. Well, the judge concerned himself with the consequences of each step in this process for the maintenance of low-cost, basic service for local ratepayers, and indeed his warrant for doing so under the antitrust laws is not as clear as when he is concerning himself only with competition.

Mr. DINGELL. There is no requirement under the antitrust laws that that should be available at all, is there?

Mr. GINSBURG. Yet, he has been very concerned that he not pursue a single goal under the antitrust laws compromising an obvious national policy with respect to universal, low-cost service.

Mr. DINGELL. But those good citizens who are troubled—and just one last question, Mr. Chairman, and I will be content to yield—but those requirements of the 1934 act are set forth in the 1934 act. There is a standard procedure for their being considered in bringing a requirement for notice, and hearing, and an opportunity for all persons to be heard. That is absent in the proceedings now going forward under the Judge, is that not so?

Mr. GINSBURG. Those and other differences. Differences both in the procedure and the substance of what the court is doing. I don't think that there is an anomaly there, sir.

Mr. DINGELL. But is it so that they are absent.

Mr. GINSBURG. They are absent.

Mr. DINGELL. Mr. Ginsburg, again I want you to understand my questions are perhaps not as fine as they might be, but any lack of kindness is not founded on lack of respect for you, or for the Judge, or for any of the parties before this proceeding.

Mr. GINSBURG. I appreciate that, Mr. Chairman.

Mr. DINGELL. Thank you, Mr. Chairman.

Mr. WIRTH. Mr. Swift.

Mr. SWIFT. Thank you, Mr. Chairman. I didn't understand a phrase in your testimony. Economics is not my strong suit, I guess. Could you tell me how you define a "supracompetitive" profit? What is that, Mr. Ginsburg.

Mr. GINSBURG. Yes; that is a profit higher than would be possible in a competitive environment for activity of a particular risk level. If you are to buy corporate bonds, Mr. Swift, you expect to get a return which considers the risk involved and a competitive rate of return, because there is a good market out there pricing those bonds competitively.

If you are able to realize supracompetitive returns, it is because competition is not driving the return down to that level.

Mr. SWIFT. Well, as you know from my opening statement, some of my concerns are how we work out the details of the pricing mechanism on this. Do I understand from your paragraph on page 7, then, that if there were supracompetitive profits, which you don't believe there will be, but is the inference that you would think it would be all right to send some of the supracompetitive profits over as a direct subsidy to the monopoly area if they existed, or am I reading something into your paragraph that you didn't mean?

Mr. GINSBURG. Well, since I didn't contemplate that they would be there, I really didn't address that further question, what to do if they are there.

The subsidization of local service may be a goal that the Congress or the FCC wishes to pursue because of various important policies like the maintenance of universal service.

I would caution, however, that in seeking revenues for the—to make it possible to achieve that policy, it is unwise to look to diversification as a source of such revenues.

Mr. SWIFT. I don't happen to disagree with that, nor do I think those kinds of profits are going to be there. But I think it is important to understand what you are saying, because I am beginning to hear this consensus that I talked about, that there shouldn't be overt subsidy going either way.

What we want to talk about is what, in fact, are we going to put on each side of that line. And that becomes kind of critical, because what will happen, I am afraid, is that one person is going to draw the line, and somebody else is going to say "this is a subsidy." So if you are not contemplating an overt subsidy, that is within the framework of what I see as a developing consensus.

But let's explore a little bit further. Would you, in your concept of this, think that a competitive business should pay its fair share of fixed costs on a for-use basis? If they use fixed costs, they would pay for that and you would not call that a subsidy? I don't mean to put words in your mouth.

Mr. GINSBURG. Well, that is correct. If the same plant and equipment serves both the regulated business and the competitive business, then some allocation of the fixed cost of that plant and equipment must be made between the two. It would be inappropriate for the ratepayers of the monopoly service to cover the entire cost of the plant and equipment when some of it is being used to participate in the competitive market.

By parity of reasoning, and I think this is where you are going, the competitive pricing—the competitive business conducted by the telephone company should be expected to make a contribution to the overhead of the telephone company for its use of those common facilities.

Mr. SWIFT. The monopoly ratepayer benefits.

Mr. GINSBURG. Where that is possible, sir, it is because there are economies of scale or of scope that have not been fully realized purely by the telephone business, or the regulated business, and if diversification makes it possible to realize those economies, then everyone is better off, although one does want to make sure they are allocated properly.

Mr. SWIFT. But this is an area in which the jargon sometimes makes it very hard to understand exactly what we are saying. I keep waiting for the day when the telephone industry will change over to English.

When I am talking about fixed costs, which you said yes, they should pay their share on some reasonable basis, probably of use or something like that, I am including poles and wires. Is that your understanding of fixed costs? A share of that?

Mr. GINSBURG. Let us draw it out a little bit more and suggest that we are talking about an information service provided over the poles and wires from the central office to the subscriber.

Mr. SWIFT. That is what I am talking about.

Mr. GINSBURG. Now, ideally, that service would be provided by the telephone company and by independent competitors, all of them using the same poles and wires to go from the central office to the subscriber.

Mr. SWIFT. Right.

Mr. GINSBURG. And each of them should be charged an equal amount, and each of them, therefore, should be making a contribution to the cost of having the poles and wires there in the first place.

Now, that may not always be possible. It may be that the service is one that cannot, as a practical matter, be provided on a competitive basis, and that only the affiliate of the telephone company is in a position economically to use the poles and wires to provide the service to the subscriber in question.

Where that is the case, it is difficult—very important, but also more difficult—to devise an appropriate allocation of costs. It is also, of course, because it is a monopoly, a less desirable situation in and of itself. We don't have the discipline of competition to hold the price of that information service down.

Our concern is in minimizing the situations in which the information service is monopolized by the telephone company, and in finding the maximum sway for structural solutions that allow competition in the provision of those services.

Mr. SWIFT. Let me just repeat that back to be sure I understand precisely what you have said. Now, you are saying that information services—both those that the RBOC is providing, and the competitors—if they utilized the fixed costs, if they utilized the poles and wires, should pay a reasonable proportion of—they should pay for their use, in effect, of those fixed costs.

You are further saying that in a situation in which the RBOC is providing a service for which there is no competition and perhaps technically can't be any competition, they should pay something, although you are telling me it is a little harder to figure out what that should be. Is that an accurate summary of what you said, sir?

Mr. GINSBURG. That is correct.

Mr. SWIFT. Let me go back in and grab one of those phrases that gets kicked around in the industry. Is relative use a way that you would suggest going about trying to determine what that cost is?

Mr. GINSBURG. There are various ways in which to allocate the responsibility for a lump sum cost like that. I would really have to defer to the FCC and the State regulators for expertise in how best to do it.

Even in the very narrow example of access charges for interexchange carriers, we have had more than one system in use in the last couple of years.

Mr. SWIFT. It is always too bad when we have to defer to the FCC. I yield back the balance of my time.

Mr. TAUKE. Mr. Ginsburg, let me just clarify what it was that I think you said earlier. You indicated that as we moved through the process, that various parts of the administration would be formulating a policy relating to the issues that are before us today, but that that policy would be the basis for, perhaps, legislative recommendations or other regulatory decisions by the administration, it wouldn't necessarily be the guiding light, if I understood you correctly, behind the Justice Department's recommendations accompanying the report that will be filed next January.

So, therefore, it would be conceivable, if I understood you correctly, that the Justice Department recommendations accompanying that report might be in some ways inconsistent with it, or perhaps even contradictory to the administration's policy.

Did I understand you correctly?

Mr. GINSBURG. I don't think so, Mr. Tauke. I apologize.

Mr. TAUKE. There is no necessity to apologize.

Mr. GINSBURG. I should be clearer. The process that we contemplate is as follows: We will continue the project already begun of assembling as full a factual picture as possible regarding the state of competition in the telecommunications industry. That will, when done, constitute a comprehensive report that will be made to the court in January.

When we see what those facts look like, they may suggest to us as a matter of policy that there should be modifications in the current decree. Perhaps in the nature of the subjects under discussion today, realization of some of the restrictions, perhaps, and other types of modifications.

And we will make recommendations to the court insofar as they suggest themselves on the basis of the facts that we gather. The court, however, is not an appropriate forum for recommendations that run beyond considerations of altering the decree on the basis of competition policy. The proposition that the decree should be altered, or that the law should be changed, I should say, for reasons unrelated to the purposes of the decree, should not really be addressed to the court, and probably would not be entertained by the court. But they would have relevance in the Congress and in the

public debate, and I should think that same factual basis, if it provides us with basis for more broadsweeping recommendations, would lead us to make those recommendations to the Congress.

Mr. TAUKE. Suppose that the administration in the development of its policy concludes that for economic reasons, and perhaps trade reasons, maybe even some consumer interest reasons, that it is desirable that the decree be modified, but that it doesn't really have antitrust reasons for making those recommendations.

Do I understand, then, that the administration policy would still be reflected in recommendations to the court even though the basis for those recommendations might not be antitrust policy considerations?

Mr. GINSBURG. I would not think so. I think if the basis for the recommendations are things apart from antitrust policy, we should direct them to the Congress.

Mr. TAUKE. So, then, I guess that gets back to my question: Is it not possible then that the administration would recommend no change in the MFJ on the basis of antitrust policy, but then turn around and come to the Congress and say: Our view is that it is in the national interest to change the modified final judgment?

Mr. GINSBURG. That is, at least, a logical possibility.

Mr. TAUKE. I wonder if it wouldn't be more appropriate, and maybe you should tell me, would it not seem more logical if not more appropriate for the administration to develop a policy that is based on the whole host of policy considerations that are out there, and then have the Justice Department base its recommendation on that broader policy?

Mr. GINSBURG. Since we are willy-nilly committed to this large scale report to the court, and are committed to doing a thorough job in that regard, I think it is most sensible for us to see what the facts that we are so busily gathering look like before we engage in the exercise you described regardless of how broad ranging it might be.

Mr. TAUKE. Mr. Chairman, I believe this points up the need for Congress to continue to take a very careful look at this issue, and Mr. Chairman, I have other questions, and I know the time is escaping. Could we submit questions——

Mr. WIRTH. The record, as noted earlier, will be left open for 30 days for questions and answers from members of the subcommittee.

Gentlemen, we thank you very much for being with us today. We greatly appreciate your time and patience, and you have been here for a long chunk of time, but I think it has been very productive for the record, for the members, and so on, and we thank you very much, and look forward to working with you both.

Thank you.

[Testimony resumed on p. 174.]

[The following information was submitted for the record:]

U.S. House of Representatives
Committee on Energy and Commerce
Room 2125, Rayburn House Office Building
Washington, DC 20515

April 21, 1986

Honorable Douglas H. Ginsburg
Assistant Attorney General for
the Antitrust Division
Department of Justice
10th Street and Constitution Avenue, N. W.
Washington, D. C.20530

Dear Mr. Ginsburg:

Thank you for your testimony before the Subcommittee on Telecommunications, Consumer Protection, and Finance on March 13, 1986 with respect to the restrictions in the Modified Final Judgment that prohibit the Bell Operating Companies (BOCs) from entering lines of business related to the communications services they currently provide.

For the record of the hearing I ask that you respond to the following questions by May 19, 1986.

In approving and modifying the Consent Decree signed by the Department of Justice and AT&T, Judge Harold Greene applied "public interest" standards identical to those required under the Tunney Act. In his August 1982 opinion he stated:

> Although the statute (that is, the Tunney Act) is explicit as to the Court's obligation to make a public interest determination, it provides relatively little guidance as to the meaning of 'public interest' in this context. What is clear is that, whatever other factors a court may take into account, it must begin by defining the public interest in accordance with the antitrust laws.

In this opinion, Judge Greene also stated:

> ...the Court will attempt to harmonize competitive values with other legitimate public interest factors. If the decree meets the requirements for an antitrust remedy -- that is, if it effectively opens the relevant

markets to competition and prevents the recurrence of anticompetitive activity, all without imposing undue and unnecessary burdens upon other aspects of the public interest -- it will be approved.

Question 1. Do you agree that under this standard the Department of Justice and Judge Greene are required first to satisfy the antitrust objectives of opening markets to competition and preventing anticompetitive activity, and to take into account other aspects of the broad public interest only in so far as doing so does not interfere with the attainment of antitrust objectives?

In approving the restrictions on the BOCs, Judge Greene appears to have been guided by this priority of antitrust objectives over other public interest objectives. In his August 1982 opinion he stated:

> In addition, the Court must assess the effect of the restrictions upon other important public policies. Many persons, including particularly the States, claim that these restrictions would have adverse consequences in that they would either undermine the financial viability of the divested operating Companies, or produce substantial increases in the rates for local telephone service, thus eroding the statutory goal of universal telephone service for all Americans. This factor, to be sure, cannot preclude the imposition of a restriction necessary to preclude the anticompetitive activity; but to the extent that a restriction does not have a pro-competitive effect, it may not be imposed if it infringes upon other important public policies. (Emphasis added.)

In the same opinion, the Judge also stated:

> Similarly, there is no need for a hearing concerning the effect of the restrictions upon local rates. Any testimony on that issue could only be speculative and would be unlikely to assist the Court in its public interest determination. In addition, the effect of the restrictions upon local rates does not represent the crux of the Court's decision on these questions. (Emphasis added.)

Question 2. Doesn't this standard imply that the restrictions would have been imposed on the BOCs so long as they were deemed to be necessary to achieve the antitrust objective of preventing anticompetitive conduct -- even if the imposition of these restrictions would have increased local telephone rates?

Question 3. Under this standard for approving the restrictions, aren't the goals of maintaining the financial health of the divested Operating Companies, ensuring affordable local rates, and even the statutory goal of universal service, all declared to be secondary to the single goal of protecting competition?

In his August, 1982 opinion Judge Greene incorporated into Section VIII(C) of the MFJ the standard for removing the restrictions. He stated:

> "...the removal of the restrictions should be governed by the same standard which the Court has applied in determining whether they are required in the first instance. Thus, a restriction will be removed upon a showing that there is no substantial possibility that an Operating Company could use its monopoly power to impede competition in the relevant market."

Question 4. Doesn't this standard state clearly that any restriction will be eliminated if it is shown that it is not needed to prevent anticompetitive abuses in the markets the BOCs are seeking to enter?

In his July 1984 opinion, Judge Greene asked:

> ...whether, in addition to the specific standard set forth in section VIII(C), the Court could and appropriately should take into account broader considerations, specifically those articulated in other parts of the decree (e.g., the requirement of equal access) and those which are among the decree's dominant purposes (e.g., the efficient, economical provision of local telephone service).

He answered that he may take such larger considerations into account, saying, "Accordingly, in passing upon such (waiver) motions, the Court will take into account, inter alia, the decree's fundamental principles and purposes."

In his January 13, 1986 opinion he stated:

> These companies (that is, the BOCs) inherited billions of dollars in tangible and intangible assets at the time of divestiture because the Court and others concluded that these assets would be used in the public interest, that is, in the provision of excellent yet low-cost telephone service to American consumers, and that this objective would be accomplished without the re-creation of the dangers to fair competition that existed before. This Court firmly intends to enforce the decree in light of that purpose.

Question 5. In these later opinions, has the provision of efficient low-cost telephone service been elevated from a secondary consideration -- which should be taken into account, if at all, only if it does not "negate" the antitrust goal of promoting competition and about which there is "no need for a hearing" since it is not the "crux" of the Court's decision -- to a "dominant purpose" of the Decree?

Question 6. Is it within the Department of Justice's authority or expertise to report to the Court that the entry of a BOC into a new line of business would have no substantial possibility of impeding competition in the new market, but that nevertheless the BOC should continue to be prevented from entering this market because such entry might increase local telephone rates?

The market reality is that local telephone companies cannot compete fully or effectively in the local exchange business for large institutional customers unless they can offer an array of sophisticated information services and interexchange services (such as least cost routing). If these large customers leave the local public network, or substantially reduce their reliance on it, the local network could stagnate and local telephone rates could rise above what they would otherwise be. This argument is clearly relevant to the question of whether the restrictions impede or advance the statutory goal of universal telephone service.

In his January 13, 1986 opinion, Judge Greene stated:

> The decree simply does not contemplate that the Regional Companies may use claims of inability to compete with respect to the services they are permitted to provide as levers for prying open markets that are prohibited to them.

Question 7. Hasn't Judge Greene stated in this opinion that the antitrust decree he administers does not permit him to consider some arguments that show that continued imposition of restrictions on the BOCs are themselves a threat to universal service?

Question 8. Is it within the Department's authority and expertise to report to the Court that the entry of a BOC into a new line of business poses some risk of impeding competition in the new market, but that this risk is outweighed by the benefits of upgrading the local public network and keeping local telephone rates lower than they would otherwise be and therefore to recommend such entry?

In his August 1982 opinion, Judge Greene incorporated the standard for removing the BOC restrictions into Section VIII(C) of the MFJ and also rejected the "unforseen conditions" standard, stating:

> The test usually applied to a contested modification of a consent decree was ... whether there were 'unforseen conditions' that indicated the modification was appropriate. Some parties contend that a different standard may not be applied to the removal of the restrictions. However, there appears to be no reason why the decree itself cannot contain provisions governing the expiration of some of its restrictions.

On July 24, 1984, Judge Greene issued an opinion in which he articulated a monopoly power test instead of a competitive harm test for removing the modifications on information services, long distance and equipment manufacturing until certain conditions were fulfilled. He stated:

> The Court will not even consider the substantive merits of a waiver request seeking permission to provide interexchange services until such time as the Regional Holding companies lose their bottleneck monopolies and there is substantial competition in local telecommunications service. That is not now.... Similar considerations govern the appropriateness of entry of the Regional Holding Companies into the information services and equipment manufacturing markets. No significant technological or structural changes have occurred in these markets to justify a relaxation of these line of business restrictions and no requests for waivers in these markets will be considered unless and until such changes have taken place. (Emphasis added.)

In his speech before the Brookings Institution Judge Greene repeated this view:

> ...the decree as it presently stands allows the regional holding companies to enter the long distance and information services markets only when they have lost their monopoly status in the local markets in which they operate. (Emphasis added.)

In his January 13, 1968 opinion he restated this standard:

> The Regional Companies also suggest as a justification for being permitted to enter the markets at issue here that they are or soon will be beset by competition for the local telecommunicatons markets, in

the form of bypass or otherwise. Section VIII(C) of the decree provides for this eventuality by stating that an Operating Company may enter a prohibited market when there is "no substantial possibility that it could use its monopoly power to impede competition in the market it seeks to enter." With respect to inter-exchange and information services, that means that an Operating Company may enter these fields when its local monopoly has ended and there is substantial competition in the particular local telecommunications market. (Emphasis added.)

Question 9. By now interpreting the VIII(C) standard to mean that no waiver of the information services, equipment manufacturing and interexchange services restrictions will even be considered until the BOCs have lost local monopoly power, hasn't Judge Greene re-imposed the "unforseen conditions" standard that he apparently rejected back in 1982?

Question 10. Doesn't this interpretation of Section VIII(C) effectively mean that the BOCs cannot bring their communications expertise to bear on related lines of business for the forseeable future? Doesn't this force them to seek out unrelated non-communications markets to enter -- where consumers may receive less benefit and the companies face greater risk?

Question 11. Has the Department ever made a favorable recommendation on a waiver request from a BOC to enter into the information services, interexchange or manufacturing markets?

Question 12. What conditions are sufficient to persuade the Department to make such a favorable recommendation to the Judge? For information services, interexchange service, and equipment manufacturing, is a sufficient condition a showing that BOC entry will not impede competition in markets to be entered or is a sufficient condition a showing that the BOC has lost every last vestige of monopoly power in each segment of the local telecommunications market?

The reality of the local telecommunications marketplace is that local telephone companies now serve distinct local customer groups whose needs and options differ. Increasingly they lack the power to limit options and dictate prices for the large-volume users who generate the bulk of their revenue. However, the local companies are likely to remain the only alternative for residential and small business customers for the forseeably future.

Question 13. In order to recommend a waiver of the information services, equipment manufacturing or interexchange restrictions, does the Department have to make a finding that the BOCs are subject to substantial competition for residential and small

business customers or is it sufficient to find that the large customers who generate most of their revenue can obtain local telecommunications services from other sources?

Question 14. Who has the burden of proof in a waiver request? Do the BOCs have to show that there is no substantial possibility of competitive harm, or do opponents have to show that there is a definite, specific threat to competition? If the burden of proof is now on the BOCs, under what circumstances would you recommend that this burden of proof be shifted?

Question 15. Shouldn't the standard for BOC entry into new markets be whether the advantages to the public -- including greater convenience, increased diversity of suppliers, reduction of prices caused by economies of scale and scope, and trade benefits -- outweigh the risks of competitive harm? How would such a standard differ from the VIII(C) competitive harm standard and Judge Greene's monopoly power test for information services, interexchange and equipment manufacturing?

Question 16. Is the standard for eliminating a restriction from the decree -- so that henceforth no waivers would be needed -- different from the VIII(C) standard that has been applied to requests for a waiver of a restriction? If so, what is this different standard?

In a number of the Judge's opinions he addressed the question of whether a BOC has shown that its entry into a prohibited market is needed to promote competition in that market. For instance, in his January 13, 1986 opinion he stated:

> The information services market is hardly a monopoly market: a number of corporations engage in this business, both large and small, and the entry of the Regional Companies is not needed to make it a competitive one.

Question 17. Is this a valid standard? Does the Department have to find that BOC entry into a new market will transform that market from a non-competitive one into a competitive one in order to recommend a waiver to Judge Greene?

Question 18. If a market a BOC is seeking to enter is a monopoly or an oligopoly -- such as the domestic manufacture of network equipment -- doesn't BOC entry automatically increase competition, rather than pose a substantial possibility of impeding it?

Question 19. If the market a BOC is seeking to enter is already fiercely competitive, isn't BOC entry unlikely to impede competition?

You stated in your testimony that reductions in local rates should not be anticipated from BOC entry into new communications markets since "there will be no excess revenue to subsidize local telephone rates because competition will prevent the BOCs from earning supra-competitive profits."

Question 20. Did you mean to imply that the BOCs will not be allowed into a new market unless there is already substantial competition? Would the Department prevent BOCs from providing such services as "Custom Calling II" voice storage which other providers have not even attempted to offer and, which is most efficiently provided by locating voice storage equipment in a local central office. Does the Department take the position that that since no one else is able to provide this service economically the BOCs should not be able to provide it either?

Question 21. Suppose that the BOCs are allowed into a related communications service only on the condition that a fair and equitable portion of the joint and common costs of the local network are assigned to the new service -- a goal that Chairman Mark Fowler of the FCC endorses in his letter to me of March 12, 1986 (copy enclosed). Wouldn't such a cost allocation effectively shift some costs currently being recovered through local rates to the new services, thereby reducing the burden on ratepayers and keeping local rates below what they would otherwise be?

Question 22. Suppose that the BOCs were losing the large customers who are a major source of local revenue. In the absence of a waiver enabling the BOC to compete for these large customers, lost revenue would have to recovered from the remaining ratepayers. In such a circumstance, wouldn't the grant of a waiver keep local rates lower than they otherwise would be?

Because of the MFJ restrictions that prevent the BOCs from providing advanced communications services, large institutional telephone customers have an incentive to purchase increasing amounts of customer premises equipment that provide these services. A recent domestic policy study by the Department of Commerce found that while AT&T, GTE, ITT, Rolm, and other U.S suppliers have slightly more than half of the market for customer premises switching equipment, Canadian, European, and Japanese suppliers have increased their market shares rapidly. In effect, the information services restriction has provided an unnecessary market advantage to foreign suppliers.

Question 23. Does the Department have the authority or expertise to take these trade considerations into account in recommending a waiver to Judge Greene? If yes, under what standard do you consider trade matters? Do you give antitrust and trade considerations roughly equal weight or are you required

under the antitrust laws you enforce to give priority to antitrust considerations?

Judge Greene appears to think that even regulatory obligations and separate subsidiary requirements are insufficient to prevent anticompetitive abuse and that prohibitions continue to be necessary. In his January 13, 1986 opinion, he stated:

> The Bell System was under an interconnection obligation with respect to the services it provided, yet there was evidence that it did not consistently abide by its responsibilities in that regard...This lawsuit accordingly became necessary, and so did the decree in this case. The Court therefore will not rely on injunctive remedies alone...Likewise, the separate subsidiary requirement, while helpful, is obviously not adequate by itself to override the prohibitions in the decree and the dangers that gave rise to their formulation and adoption.

Question 24. Does the Department of Justice have the authority or expertise to fashion remedies solely to ensure compliance with regulations established by the Federal Communications Commission pursuant to its authority under the 1934 Communications Act? Does Judge Greene have the authority to enforce such remedies?

Question 25. Isn't it more productive now to shift the debate from questions of whether the BOCs should be allowed to compete to questions of what the ground rules ought to be for allowing them to compete fairly? If now is not the time for such a shift, under what circumstances does the Department think such a change is appropriate?

In your March 13, 1986 testimony, you supported removal of separate subsidiary requirement, stating:

> The Department has also supported, in principle, replacing the separate subsidiary requirements currently imposed under the Commission's Computer II rules with accounting rules that can effectively prevent cross-subsidization.

Question 26. In Justice Department recommendations to Judge Greene, does it make any sense to impose a separate subsidiary requirement as a condition for allowing the BOCs to provide communications services when these services could be more efficiently provided through the public network?

Question 27. If the Department is in substantial agreement with the regulatory framework developed by the FCC in the Computer III Inquiry, would the Department recommend a similar

framework to Judge Greene as soon as the FCC takes final action on Computer III or would the Department insist on undertaking a separate study before making a recommendation to Judge Greene?

In your March 13 testimony to the Subcommittee, you stated:

> The FCC and the state public utilities commissions, not the Department or the decree court have primary responsibility for the protection of the ratepayers.

Question 28. Shouldn't accounting and ratepayer protection safeguards be developed and administered by a regulatory agency, not a law enforcement agency?

As I indicated at the March 13 hearing I am disturbed by the process followed by the Department of Justice and the Court in regard to lifting the restrictions on the BOCs. To my knowledge, no signficant abuses have resulted from the procedural defects I find, but the process could allow problems to occur. Informal protections for interested parties are not commensurate with the importance of the issues involved one-half the telecommunications resources of the country are tied up and prevented from competing in a fierce global market. Moreover, if the Department and the Court are intent upon considering telecommunications policy matters, then the procedural protections available to interested parties before the FCC are preferable to the informal protections you described in your testimony.

Question 29. Please describe the process followed by the Justice Department and Judge Greene in considering a request by a BOC for a waiver of an MFJ restriction on its business opportunities. Are there any time limits within which the Department or the Judge must act on such a request?

Question 30. Who is entitled to comment on a waiver request before the Department? Who is entitled to comment before the Court? Must there be opportunity for comment before the Department on the Department's recommendation to the Judge or is it sufficient to allow public comment before the Judge?

Question 31. Describe any steps the Department and the Court take to ensure that interested parties find out about the request.

Question 32. Does the Department seek out those individuals and businesses who would favor or benefit from the waiver or does it hear only from those opposed? How many non-BOC comments have you received in favor of a waiver request? From whom were they received?

Question 33. Does the Department solicit the views of the Secretary of Commerce or the head of the National Telecommunications and Information Administration (NTIA) -- who is responsible for formulating and presenting Administration policy on telecommunications?

Question 34. Does the Secretary of Commerce or the head of NTIA submit comments to the Justice Department on particular waiver requests? How often have they done so?

Question 35. Is the Secretary of Commerce or the head of NTIA entitled to file views independently with Judge Greene? Have they done so? Are these views submitted as part of the opinion of the United States in the case? If not, why not?

Question 36. Does the Department intend to work with the Secretary of Commerce or the head of NTIA to develop a common Administration position on the continued need for BOC restrictions?

Question 37. Has the Department sought out the views of the FCC before it has submitted a recommendation Judge Greene on a waiver request? Has the FCC submitted its views to the Department? How often? On what issues?

Question 38. Has the FCC ever submitted its views to Judge Greene on a waiver request? How often? On what issues?

Question 39. In considering a waiver request, does the Department have a legal obligation to keep a public record of all meetings with interested parties? Does the Department have a practice of keeping such a public record?

Question 40. Describe the process whereby interested parties are able to reply to the claims and allegations their opponents make in (1) the written statements they file with the Department and (2) any off-the-record contacts with Department staff.

Question 41. You referred in your March 13 testimony to a motion to make the waiver process less time-consuming in those situations in which a BOC is seeking a waiver substantially similar to a waiver already recommended by DOJ and granted by the Court. This approach is in line with recommendations contained in last year's domestic policy report by NTIA and also suggested in my letter to you last August. What progress has been made in obtaining Judge Greene's approval for these "generic" waivers requests? How does the Judge's decision on this request differ from the Department's original request?

Question 42. Judge Greene's January 13, 1986 opinion suggested to many that he would not grant certain kinds of

waivers for the forseeable future. Has this chilled any efforts of the Justice Department to move forward with motions to grant waivers that they would otherwise have filed with Judge Greene?

Question 43. Provide a list of all parties who can appeal a decision by Judge Greene. If he ruled that the BOCs could enter the prohibited long distance market, could MCI appeal? If an interested party is not on this list, how could he get on it?

Question 44. What are the differences between the waiver process and the process for modifying the MFJ so as to eliminate a restriction entirely?

Question 45. Will the Huber investigation you refer to in your March 13 testimony be the Department's report to the Judge, in January 1987, or will it be the factual basis for the Department's report?

Question 46. Will the Department's report simply be a factual analysis or will it contain recommendations for or against lifting the restrictions?

Question 47. Will the public have an opportunity to comment on the Department's factual findings and policy recommendations before they are sent to Judge Greene?

Question 48. Is Judge Greene under any legal obligation to review the appropriateness of the continued imposition of the restrictions in light of the report you intend to file in January 1987? Is he under any constraint to act within a specified time?

Question 49. Can a BOC independently file a motion for modification of the MFJ, or must it wait for the DOJ to file its motion? If a BOC does file such a motion, what is the procedure whereby it will be considered? Is there any requirement for the Department of Justice or Judge Greene to act on such a motion within a specific period of time?

Your prompt response to these questions is greatly appreciated.

Sincerely,

JOHN D. DINGELL
CHAIRMAN

U.S. Department of Justice

Antitrust Division

Office of the Assistant Attorney General *Washington, D.C. 20530*

OCT 2 1986

Honorable John D. Dingell
Chairman, Committee on Energy
and Commerce
House of Representatives
Washington, D.C. 20515

Dear Mr. Chairman:

This letter responds to your April 21, 1986 letter, which requests responses to certain questions concerning the restrictions in the Modification of Final Judgment (MFJ) entered in the AT&T case. 1/ In particular, your questions involve the restrictions that prohibit the Regional Bell Operating Companies (RBOCs) from entering certain lines of business. Your questions and our responses are set out below. Before responding to your questions, however, I will briefly discuss an important development that has occurred since you wrote your letter and that promises to ensure the continued development of our telecommunications industry. On June 19, 1986, Senate Majority Leader Bob Dole introduced S. 2565, the "Federal Telecommunications Policy Act of 1986," a bill that would consolidate federal regulatory authority over the telecommunications industry in the Federal Communications Commission (FCC). The proposed bill would (a) require the FCC to promulgate a detailed set of regulations identical in substance to the consent decrees entered in the AT&T and GTE 2/ cases, (b) empower the FCC to remedy violations of the regulations, (c) empower the FCC to modify or rescind, and to grant exemptions and waivers from, the regulations at a later date, and (d) provide that violations of the regulations shall not be deemed to constitute violations of any existing antitrust decree. After the bill is enacted, I would expect

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1/ United States v. AT&T, 552 F. Supp. 131 (D.D.C. 1982), aff'd sub nom. Maryland v. United States, 460 U.S. 1001 (1983).

2/ See United States v. GTE Corp., 603 F. Supp. 730 (D.D.C. 1984).

motions to be filed with the court to vacate the AT&T and GTE decrees, on the ground that the continued existence of the decrees would be inconsistent with the regulatory authority given to the FCC by the bill; and I expect that the court would decide to vacate the decrees for that reason.

For the reasons stated in my speech to the Computer and Communications Industry Association on July 17, 1986 (a copy of which is enclosed), I strongly support the Dole bill. In fact, if the bill is passed by Congress in the form outlined above, the Antitrust Division would be prepared to move in the district court for vacation of the decrees. In responding to your questions, I have attempted to explain how the Dole bill would address some of the issues raised by your questions.

Question 1: Do you agree that under [the Tunney Act's public interest] standard the Department of Justice and Judge Greene are required first to satisfy the antitrust objectives of opening markets to competition and preventing anticompetitive activity, and to take into account other aspects of the broad public interest only in so far as doing so does not interfere with the attainment of antitrust objectives?

Answer: In general, the answer to this question is "yes." This question concerns the appropriate meaning of the public interest standard under the Tunney Act, 15 U.S.C. § 16(e). The Department has discussed this matter on several occasions both in the context of the AT&T case and in connection with other antitrust consent decrees. 3/ With specific reference to the AT&T case, the Department's position at the time the decree was entered was that under the applicable public interest standard:

3/ The Department argued that the Tunney Act did not apply in terms to the entry of the AT&T decree, but we agreed that Tunney Act procedures (and standards) should apply. See 552 F. Supp. at 145.

> "The Court must determine whether the remedies contained in the decree constitute a reasonable vindication of the competitive principles embodied in the Antitrust laws. The Court should not rely upon noncompetition policies as a basis for rejecting the relief proposed here unless the Court concludes that the proposed decree unnecessarily contravenes another clear public policy." 4/

On the other hand, the Department believed that it was essential to consider the views of federal and state regulatory agencies in determining whether the proposed relief in the MFJ was in the public interest. And during the implementation phase of the AT&T decree, the Department has placed great weight upon the views of state regulatory agencies and the FCC in considering various aspects of the decree. At bottom, however, because the decrees were entered to settle antitrust suits and because the antitrust laws have the sole purpose of protecting competition, the Department in enforcing the decrees has necessarily focused on competitive concerns. The Court's own authority to construe the decrees is similarly limited.

Your question thus raises one of the concerns that has led the Department to support the Dole bill: the bill possesses the great virtue of allowing other important factors to be taken into account in carrying out the decrees' regulatory scheme that cannot now be addressed by the decree court itself, such as the interests of local telephone users and the significant role of telecommunications in international trade.

4/ Brief of the United States in response to the Court's memorandum of May 25, 1982 (filed June 14, 1982) at 22. See Competitive Impact Statement filed in connection with the proposed MFJ, 47 Fed. Reg. 7170, 7180 n.32 (Feb. 17, 1982).

In sharp contrast to the limited mandate of the Department and the Court under the decrees, if the Commission were given jurisdiction over a regulatory regime substantively identical to the decrees, that agency could apply the provisions of the existing decrees under a "public interest" standard that is much broader than that available under the decrees. That broader public interest standard would also permit the Commission to consider a different mix of criteria in determining whether the particular restrictions now found in the decrees should be retained, rescinded, or modified.

Question 2: Doesn't [the] standard [applied by the decree Court in approving the MFJ in August 1982] imply that the restrictions would have been imposed on the BOCs so long as they were deemed to be necessary to achieve the antitrust objective of preventing anticompetitive conduct--even if the imposition of these restrictions would have increased local telephone rates?

Answer: In entering the MFJ, the Court focused its inquiry primarily on whether the line of business restrictions were necessary to prevent unlawful discrimination or anticompetitive cross-subsidy by regulated natural monopoly providers of exchange telecommunications services. The decree restrictions are intended, in part, to prevent local operating companies from misallocating the costs of a competitive venture to the local ratebase where such prevention is necessary to prevent an anticompetitive effect in the market to be entered. To that extent, the restrictions limit the ability of local operating companies to increase ratepayers' costs. State regulators are also concerned about local operating companies adding costs to the ratebase to support competitive ventures; generally, however, their interest has been limited to

protecting rate payers rather than attempting to protect competition in the line of business subject to the restriction. Thus, while the decree and regulatory agencies approach the issue of cross-subsidy from different perspectives, each generally achieves the same result--not imposing undue costs on rate payers.

Question 3: Under this standard for approving the restrictions, aren't the goals of maintaining the financial health of the divested Operating Companies, ensuring affordable local rates, and even the statutory goal of universal service, all declared to be secondary to the single goal of protecting competition?

Answer: No. While, as discussed above, the Department's and the Court's enforcement of MFJ necessarily has focused on competitive concerns, the goals of maintaining the financial health of the Operating Companies, ensuring affordable local rates and universal services are all important public policy goals that are not adversely affected by the MFJ. The Department and the Court spent considerable time both during the consideration of the proposed decree and during consideration of the Plan of Reorganization ensuring that the divested RBOCs had sufficient assets to ensure their financial health. These efforts were apparently quite successful, since the RBOCs have reported substantial profits in each year following divestiture. Combined profits for the RBOCs last year were over $9 billion,

and AT&T and all seven RBOCs are ranked in the top 25 corporations in the United States in terms of dollar amount of profits.

Moreover, the post-divestiture competitive environment has brought dramatic price reductions for telecommunications equipment and long-distance service. And, contrary to some predictions, the divestiture itself has not led to higher local rates; rather, regulatory changes, such as changes in the depreciation schedules adopted prior to divestiture, have largely been attributable for the increases in local rates. Finally, I note that recent actions by the RBOCs indicate strongly that local rates may be stabilizing; for example, Pacific, NYNEX, and Bell South have all initiated proposals to place a moratorium on local rate increases in connection with more flexible pricing opportunities. On balance, then, both residential customers and business customers are paying less for their telephone service than they were prior to divestiture.

Question 4: Doesn't this standard state clearly that any restriction will be eliminated if it is shown that it is not needed to prevent anticompetitive abuses in the markets the BOCs are seeking to enter?

Answer: Yes.

Question 5: In [the decree Court's opinions of July 26, 1984, and January 13, 1986] has the provision of

efficient low-cost telephone service been elevated from a secondary consideration--which should be taken into account, if at all, only if it does not "negate" the antitrust goal of promoting competition and about which there is "no need for a hearing" since it is not the "crux" of the Court's decision--to a "dominant purpose" of the Decree?

Answer: No. The Section VIII(C) standard is clearly a competition-based one. The Court must determine whether there is a substantial possibility that the RBOC will use its monopoly power over exchange telecommunications services to impede competition in the market it seeks to enter.

Question 6: Is it within the Department of Justice's authority or expertise to report to the Court that the entry of a RBOC into a new line of business would have no substantial possibility of impeding competition in the new market, but that nevertheless the BOC should continue to be prevented from entering this market because such entry might increase local telephone rates?

Answer: No. The Department has not sought, and will not seek, to usurp the authority of federal and state regulators concerning whether RBOC diversification will increase or decrease local rates. As discussed above, the Department's role and its expertise in this area are largely limited to the issue whether anticompetitive effects are likely to flow from RBOC diversification. Under the Dole bill, of course, the FCC's powers would not be so limited.

Question 7: Hasn't Judge Greene stated in [his January 13, 1986] opinion that the antitrust decree he administers does not permit him to consider some arguments that show that continued imposition of restrictions on the BOCs are themselves a threat to universal service?

Answer: No. The opinion to which you refer (the January 13, 1986 opinion) does not address the question whether universal service is threatened by the line of business restrictions. The portion of the opinion referred to in your letter addresses issues relating to the competitive customer premises equipment market, not regulated exchange services. The Court simply rejected an RBOC argument that they may ignore the decree's restrictions on the provision of interexchange service if it is necessary to be more successful in selling customer premises equipment (CPE). The Court held instead that the line-of-business restrictions could be removed only upon obtaining a waiver processed under the Section VIII(C) standard.

Question 8: Is it within the Department's authority and expertise to report to the Court that the entry of a BOC into a new line of business poses some risk of impeding competition in the new market, but that this risk is outweighed by the benefits of upgrading the local public network and keeping local telephone rates lower than they would otherwise be and therefore to recommend such entry?

Answer: If the proposed service, on balance, will increase the network's efficiency, it would be appropriate to recommend a waiver to allow the RBOC to provide such a

service, even if there is some risk to competition in the market for the proposed service. Our recommendation would be based on a balancing of the competitive costs and benefits of entry, although, as a practical matter, such balancing on a case-by-case basis is very difficult. (The burden is on the BOCs to establish those competitive benefits. See Answer to Question 14.) If, however, the RBOC's entry would harm competition without any countervailing competitive (i.e., efficiency) benefits for the network, we could not recommend a waiver simply because the RBOC promised to use some of its monopoly profits to subsidize local rates.

Question 9: By now interpreting the VIII(C) standard to mean that no waiver of the information services, equipment manufacturing and interexchange services restrictions will even be considered until the BOCs have lost local monopoly power, hasn't Judge Greene re-imposed the "unforeseen conditions" standard that he apparently rejected back in 1982?

Answer: No. The decree has always recognized that the line of business restrictions are justified only because of the monopoly power of the RBOCs in the provision of local exchange services. Thus, it has been understood that if the RBOCs lost that monopoly power or if other technological changes occurred, then the restrictions would no longer be necessary. The Court added Section VIII(C) to the decree because it foresaw that the RBOCs might some day lose their monopoly power

over local exchange services or otherwise demonstrate that they could not use such monopoly power to impede competition in a related line of business, because of the nature of the business or because of changes in technology. See United States v. AT&T, supra, 552 F. Supp. at 194-195.

Question 10: Doesn't this interpretation of Section VIII(C) effectively mean that the BOCs cannot bring their communications expertise to bear on related lines of business for the foreseeable future? Doesn't this force them to seek out unrelated non-communications markets to enter--where consumers may receive less benefit and the companies face greater risk?

Answer: This question has two parts. With reference to the first part of the question, it is not entirely true that the decree disables the RBOCs from bringing their communications expertise to bear in related markets. For example, by providing equal access for interexchange carriers, the decree contemplates that the RBOCs will play an integral role in the provision of long distance service through high quality exchange access services. Moreover, by requiring the RBOCs to provide exchange access for all information services providers, the decree requires the RBOCs to use their expertise to foster more efficient and advanced utilization of the network that necessarily causes the RBOCs to be at the forefront of technological development. On the other hand, to the extent that the line-of-business restrictions prevent RBOC entry

into related lines of business (in particular, information services) in order to protect competition in those markets, economies of scale and/or scope may be lost.

With respect to the second part of this question, nothing in the VIII(C) standard "forces" the RBOCs to go into any market. RBOCs may choose to diversify if they can show that such diversification is not likely to impede competition in the market they seek to enter. The Department believes that, assuming no competitive problem exists, entry into diverse lines of business is a matter best left to the business judgment of the RBOCs. As your question implies, however, it is difficult to determine whether the RBOCs would have made the same judgments had they been able to enter businesses that the MFJ has foreclosed.

Question 11: Has the Department ever made a favorable recommendation on a waiver request from a BOC to enter into the information services, interexchange or manufacturing markets?

Answer: Yes. On a number of occasions the Department has recommended waivers to allow RBOCs to enter interexchange and information services markets. For example, the Department favorably recommended that the RBOCs be permitted to provide E-911 emergency services, a type of information service. The Department also has recommended a number of waivers to

permit RBOCs to provide interexchange paging services and voice storage information services in connection with their paging ventures. In addition, the Department recently recommended a waiver to permit Ameritech to manufacture telecommunications equipment and customer premises equipment abroad, for sale or use outside of the United States. The decree Court has permitted the RBOCs to offer all these services subject to certain conditions.

Question 12: What conditions are sufficient to persuade the Department to make such a favorable recommendation to the Judge? For information services, interexchange service, and equipment manufacturing, is a sufficient condition a showing that BOC entry will not impede competition in markets to be entered or is a sufficient condition a showing that the BOC has lost every last vestige of monopoly power in each segment of the local telecommunications market?

Answer: The Department makes its recommendations on waiver applications on the basis whether an RBOC can use its monopoly power over exchange telecommunications services and exchange access to impede competition in the market it seeks to enter. The fact that the RBOCs now have bottleneck control over local exchange service is an important factor in the analysis of the potential for competitive harm. This is because, for information services, interexchange services and manufacturing of telecommunications equipment and CPE, access to the local network is essential for competitive providers of such services and for

manufacturers. Thus the RBOCs' market power is relevant. As the RBOCs' control over local exchange services lessens over time, the need for the restrictions also lessens. The status of technological development is also relevant. In connection with the FCC's Computer III inquiry, the Department stated that if an open network architecture could be developed to allow non-discriminatory access for information services providers, then it would be possible to consider a removal of the information services restrictions in the MFJ as well as the separate subsidiary requirements of Computer II--even though the local exchange remains a bottleneck. See Comments of the Department of Justice (filed Nov. 13, 1985) at 27-28.

Question 13: In order to recommend a waiver of the information services, equipment manufacturing or interexchange restrictions, does the Department have to make a finding that the BOCs are subject to substantial competition for residential and small business customers or is it sufficient to find that the large customers who generate most of their revenue can obtain local telecommunications services from other sources?

Answer: The issue whether changing market conditions for large business customers lessens the need for the line of business restrictions for interexchange services, information services and manufacturing is one of the important questions now being studied in connection with the Department's report on the line of business

restrictions to be submitted to the Court (or to the FCC, depending on the status of the Dole bill) in January 1987. That report should aid the decisionmakers' evaluation of the effect of possible competition for different segments of the local service marketplace. Moreover, the 1987 Report process should provide objective market data on the extent to which there are different user groups and whether there is now competition for large business customers or whether competition is likely to develop in the near future.

Question 14: Who has the burden of proof in a waiver request? Do the BOCs have to show that there is no substantial possibility of competitive harm, or do opponents have to show that there is a definite, specific threat to competition? If the burden of proof is now on the BOCs, under what circumstances would you recommend that this burden of proof be shifted?

Answer: The burden of proof in the waiver process is on the RBOCs. The question whether this burden should be shifted will be addressed by the 1987 Report to the Court.

Question 15: Shouldn't the standard for BOC entry into new markets be whether the advantages to the public --including greater convenience, increased diversity of suppliers, reduction of prices caused by economies of scale and scope, and trade benefits--outweigh the risks of competitive harm? How would such a standard differ from the VIII(C) competitive harm standard and Judge Greene's monopoly power test for information services, interexchange and equipment manufacturing?

Answer: The Section VIII(C) standard for RBOC entry into new markets was carefully considered during the Tunney Act proceeding concerning the proposed decree. See United States v. AT&T, supra, 552 F. Supp. at 194-195. To the extent that competitive factors are relevant to the waiver process, the Department and the decree Court, which has jurisdiction to address antitrust issues only, can make appropriate determinations whether a waiver is appropriate.

As discussed above, however, neither the Department nor the Court possess the authority to consider whether other "advantages to the public" might outweigh the risk of competitive harm posed by a waiver request. In contrast, although the Dole bill would transfer the section VIII(c) waiver authority to the FCC in its present form, the Commission could subsequently decide to apply a broad public interest standard that would permit consideration of the factors mentioned in your question.

Question 16: Is the standard for eliminating a restriction from the decree--so that henceforth no waivers would be needed--different from the VIII(C) standard that has been applied to requests for a waiver of a restriction? If so, what is this different standard?

Answer: No. So long as the restrictions remain part of the MFJ, administered by the Court, the standard for eliminating a restriction from the decree ought to be

the same as waiving a restriction. In either case, it is a competition-based evaluation of the potential for competitive harm should an RBOC enter a new line of business. Moreover, in either case, conditions could be attached to prevent or minimize residual concerns of discrimination or cross-subsidy if such concerns are deemed relevant.

Question 17: Is [the question whether "a BOC has shown that its entry into a prohibited market is needed to promote competition in that market"] a valid standard? Does the Department have to find that BOC entry into a new market will transform that market from a non-competitive one into a competitive one in order to recommend a waiver to Judge Greene?

Answer: The status of competition in a market that an RBOC seeks to enter is relevant to the Section VIII(C) test only in so far as it indicates an ability by the RBOC to impede competition in that market. Thus, in some respects RBOC entry into highly competitive markets where access to the networks is not essential is less likely to result in competitive harm than a situation where an RBOC enters a market that is not highly concentrated but is highly dependent upon exchange access.

Question 18: If a market a BOC is seeking to enter is a monopoly or an oligopoly--such as the domestic manufacture of network equipment--doesn't BOC entry automatically increase competition, rather than pose a substantial possibility of impeding it?

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Answer: Not necessarily. As indicated in the answer to the preceding question, it may be easier for an RBOC to impede competition in exchange access dependent markets such as manufacturing if they are highly concentrated than in situations where the market is very competitive. But the evaluation must be undertaken with specific reference to a particular market. Crucial to any evaluation is whether the RBOC controls access to a rate-regulated essential facility, and whether the RBOC could engage in cross-subsidy by shifting costs from the market to be entered to the regulated ratebase.

Question 19: If the market a BOC is seeking to enter is already fiercely competitive, isn't BOC entry unlikely to impede competition?

Answer: As noted above, generally it will be more difficult for RBOCs adversely to effect competition in highly competitive markets than in concentrated markets. The competitive harm inquiry focuses, however, not on the current situation in the market to be entered, but on the potential for abuse by the RBOC of its control over access to the local exchange monopoly and its ability to cross-subsidize its entry into the market.

Question 20: [In your testimony before the Subcommittee on Telecommunications, Consumer Protection, and Finance of the House Committee on Energy and Commerce on March 13, 1986,] [d]id you mean to imply that the BOCs will not be allowed into a new market unless there is already substantial competition? Would the Department prevent BOCs from providing such services as "Custom Calling

II" voice storage which other providers have not even attempted to offer and, which is most efficiently provided by locating voice storage equipment in a local central office? Does the Department take the position that since no one else is able to provide this service economically the BOCs should not be able to provide it either?

Answer: This question has a number of separate parts that I will answer separately. First, with respect to my testimony concerning the RBOCs' ability to subsidize local rates through diversification, I did not mean to imply that RBOCs could not enter new markets unless there is substantial competition in the market. Rather, my testimony refers to the simple economic fact that RBOCs earning a competitive return in a newly entered market are unlikely to have, over a long period, available excess revenues to support lower local phone services.

Second, the portion of your question relating to Customer Calling II voice storage type services raises a difficult issue. Your question implies a belief that such services are natural monopoly services that can be provided efficiently only by the local exchange carriers. If this assumption is true, then the MFJ, which permits the RBOCs to offer "natural monopoly" services regulated by tariff, would not prevent the RBOCs from providing this service. See Section II(D)(3) of the decree. Moreover, the Department, in

its comments on the FCC's Computer III inquiry, recognized that there may be some ancillary or enhanced services that are natural monopoly services. See Comments of the Department of Justice (filed Nov. 13, 1985) at 16-21. We were skeptical, however, of the ability of the FCC to predict in advance whether particular services are natural monopolies.

Third, with respect to voice storage services, it may be as efficient to locate voice storage equipment at PBX facilities as it is to locate such equipment at a central office switch. It is clear that voice storage services may be provided by a variety of equipment in addition to Custom Calling II type equipment. These issues will undoubtedly be addressed in the FCC's Computer III docket and in the Department's 1987 Report.

Question 21: Suppose that the BOCs are allowed into a related communications service only on the condition that a fair and equitable portion of the joint and common costs of the local network are assigned to the new service--a goal that Chairman Mark Fowler of the FCC endorses in his letter to me of March 12, 1986 (copy enclosed). Wouldn't such a cost allocation effectively shift some costs currently being recovered through local rates to the new services, thereby reducing the burden on ratepayers and keeping local rates below what they would otherwise be?

Answer: To the extent that the local network is enhanced to allow for new communications services or information services, and an equitable portion of the joint and

common costs are assigned to the new services, then it is likely that the burden on local ratepayers will be reduced. In our view, whether RBOCs should enter these new markets is a function both of establishing equitable means properly to allocate costs, and establishing open network architecture standards to prevent discrimination in access to the local network. If these two issues are resolved satisfactorily, the Department is prepared to recommend waivers of the restrictions in the decree to permit RBOC provision of such new services.

Question 22: Suppose that the BOCs were losing the large customers who are a major source of local revenue. In the absence of a waiver enabling the BOC to compete for these large customers, lost revenue would have to be recovered from the remaining ratepayers. In such a circumstance, wouldn't the grant of a waiver keep local rates lower than they otherwise would be?

Answer: This hypothetical question assumes that certain large customers constitute a separate relevant market, and that the RBOCs have no monopoly power over access to such large customers. If the assumptions are true, then the basis for the decree restrictions as to these customers is no longer valid, and the restrictions should be removed for this hypothetical market. This, of course, is one of the issues we are studying in connection with the 1987 Report.

Question 23: Does the Department have the authority or expertise to take . . . trade considerations into account in recommending a waiver to Judge

Greene? If yes, under what standard do you consider trade matters? Do you give antitrust and trade considerations roughly equal weight or are you required under the antitrust laws you enforce to give priority to antitrust considerations?

Answer: This question follows a summary of market conditions suggesting that the RBOCs may be unable to provide advance communications services, and that these restrictions impair this Nation's foreign trade. In the Department's view, this concern has not yet been substantiated. In fact, the RBOCs have been permitted and encouraged to improve their local network capabilities to facilitate "advanced communications services." See Answer to Question 10, supra. With respect to the specific question, moreover, the Department does not have the authority or expertise to factor foreign trade considerations into its waiver recommendations, and the decree Court has jurisdiction to address only antitrust issues in the context of supervising an antitrust decree.

Under the Dole bill, of course, the FCC could take foreign trade concerns into account in deciding whether to grant waivers or modify or eliminate the line-of-business restrictions. See Answers to Questions 1 and 5, supra.

Question 24: Does the Department of Justice have the authority or expertise to fashion remedies solely to ensure compliance with regulations established by the

Federal Communications Commission pursuant to its authority under the 1934 Communications Act? Does Judge Greene have the authority to enforce such remedies?

Answer: As discussed above, in the context of the AT&T case, the Department has authority and expertise, and the decree Court has jurisdiction, only with respect to the antitrust issues underlying that case. Thus, the Department does not seek to fashion decree related remedies "solely to ensure compliance with regulations established by the Federal Communications Commission." The Department, and the decree court, rely where appropriate on the FCC and state and local regulatory bodies in making decree related recommendations and decisions.

Question 25: Isn't it more productive now to shift the debate from questions of whether the BOCs should be allowed to compete to questions of what the ground rules ought to be for allowing them to compete fairly? If now is not the time for such a shift, under what circumstances does the Department think such a change is appropriate?

Answer: In many respects the two formulations of the "debate" contained in your question are simply different ways of addressing the same issue. The issue is whether the RBOCs should be permitted to enter competitive markets. Focusing on that question necessarily requires consideration whether there are circumstances, such as accounting rules, separation requirements, and open network architecture interconnection standards that will allow the RBOCs to

expand their service offerings but not unduly impede competition in the process. The decree contemplated that an evaluation of these circumstances was appropriate on a continuing basis as requests for waivers arose. In entering the MFJ, the Court also contemplated that a comprehensive review of this issue should be conducted every three years following divestiture, since it was assumed that market and technological conditions in telecommunications were subject to rapid change that might make the restrictions unnecessary. As indicated above, our review is well underway.

Question 26: In Justice Department recommendations to Judge Greene, does it make any sense to impose a separate subsidiary requirement as a condition for allowing the BOCs to provide communications services when these services could be more efficiently provided through the public network?

Answer: This question raises important issues concerning the efficacy of separate subsidiary requirements for enhanced or information services. Separate subsidiaries may be a useful tool to minimize the potential for cross-subsidy when an RBOC enters a market that does not require access to the local exchange facilities. In such a situation, few, if any, economies are lost due to the imposition of the separate subsidiary requirement since the businesses are sufficiently unrelated that separate management would be as efficient as combined management.

With respect to information services, however, use of separate subsidiaries can cause significant efficiency losses and consumer welfare losses. At the same time, the competitive dangers of RBOC entry into such services is greater because access to the network is so important for competing suppliers of the service. In our Computer III filing at the FCC, the Department took the position that it is appropriate to give serious consideration to replacing separate subsidiary requirements if accounting rules can be substituted effectively, and if open network architecture standards can be implemented. In an open network architecture environment, accounting and information disclosure rules may be adequate to minimize any competition risks that otherwise might result from allowing a bottleneck monopolist to engage in both regulated service and competitive ancillary/information services. While it obviously will be difficult to develop and enforce such rules, the potential benefit of encouraging the development of our telecommunications system makes such proposals worthy of serious consideration.

Question 27: If the Department is in substantial agreement with the regulatory framework developed by the FCC in the Computer III Inquiry, would the Department recommend a similar framework to Judge Greene as soon as the FCC takes final action on Computer III or would the Department insist on undertaking a separate study before making a recommendation to Judge Greene?

Answer: The Department expects to place heavy reliance on the work of the FCC, especially in areas relating to accounting rules, interconnection standards, pricing and unbundling of services. As indicated previously, if the RBOCs can achieve the open network architecture standard at issue in Computer III, then it is appropriate to consider waiving the MFJ restrictions on information services. As noted above, the Department is studying the information services marketplace in connection with its 1987 Report.

Question 28: Shouldn't accounting and ratepayer protection safeguards be developed and administered by a regulatory agency, not a law enforcement agency?

Answer: Yes.

Question 29: Please describe the process followed by the Justice Department and Judge Greene in considering a request by a BOC for a waiver of an MFJ restriction on its business opportunities. Are there any time limits within which the Department or the Judge must act on such a request?

Answer: The process followed by the Department and the decree Court in considering a request by an RBOC for a waiver of the MFJ is set forth in the Court's July 26, 1984 Opinion, 592 F. Supp. 864, 873-874, and in the Court's September 14, 1984 and March 13, 1985 Memorandum Orders; copies of the latter, unpublished orders are enclosed.

Under the procedures established by the Court, an RBOC seeking a waiver of the decree's line of business restrictions submits its request to the Department, together with a detailed proposal describing the products or services to be offered, the means by which they are to be offered, and the conditions proposed to assure that the RBOC will not use its monopoly power to impede competition in the market it seeks to enter. Under existing procedures, line of business waiver requests are referred initially to the Department "to encourage informal negotiation and resolution, to avoid inundation of the Court with requests, and to make use of the expertise of the Department of Justice."

In order to facilitate the Department's review of these requests, we have asked the General Counsel of each RBOC to identify the "other interested parties," i.e., nonparties who will be affected by their company's entry into the new line of business, and to serve copies of their request on those parties at the time the request is formally submitted to the Department.

We have also asked the RBOC to transmit a letter with each request informing the interested party of their

ability to participate "formally or informally" in the Department's review of the waiver request. Upon receipt of the waiver request and any comments received, the Department reviews the request in light of the standard set forth in Section VIII(C) of the decree and the Court's rulings. If the Department concludes that the RBOC has satisfied the Section VIII(C) standard, we submit to the Court a proposal for an appropriate order. This proposal is served on all interested persons recognized by the Court's June 28, 1985 order, as well as on all parties that participate in the Department's review. Similarly, if the Department opposes a request, its opposition will be served on all parties and interested persons and filed with the Court.

In an effort to avoid unnecessary delay in our consideration of waiver requests, while permitting interested persons the opportunity to consider and submit informed comments, the Department has requested that comments be submitted within 21 days of the RBOC's application to the Department. However, it is our practice to consider comments submitted at any time up to the time we file our recommendation with the Court. The Department also submits all comments to the Court for its consideration along with the Department's recommendation.

Once the Department files its recommendation and proposed order with the Court, parties and interested persons have a second opportunity to submit comments on the proposed waiver request by filing such comments directly with the Court, and they may also file replies to the comments submitted to the Court by others. The Court then rules on the waiver request.

Question 30: Who is entitled to comment on a waiver request before the Department? Who is entitled to comment before the Court? Must there be opportunity for comment before the Department on the Department's recommendation to the Judge or is it sufficient to allow public comment before the Judge?

Answer: Everyone, including parties to the decree and "other interested parties" (i.e., any non-party), who desires to comment on a waiver request, is entitled to submit comments to the Department and to the Court.

Comments are submitted to the Department before we formulate our recommendation to the Court. Based on our experience to date, comments submitted to the Department by the parties to the decree (AT&T and the RBOCs) and other interested parties are extremely useful in assisting the Department in its analysis of the competitive effects of the proposed waiver. Thus, the opportunity for comment before the Department is a necessary part of the process by which the Department formulates its recommendations to the District Court.

Question 31: Describe any steps the Department and the Court take to ensure that interested parties find out about the request.

Answer: As a prerequisite to considering a waiver request, the Department requires the RBOCs to identify the "interested parties" who will be affected by the proposed RBOC entry into the new line of business. The RBOC seeking the waiver must serve copies of the request on those parties at the time the request is formally submitted to the Department. In order fully to inform the "interested parties" of their ability to participate in both the Department's and the Court's consideration of the request, we also require that the service of the waiver request on "interested parties" be accompanied by a transmittal letter that informs the party that the Department invites comments concerning the waiver request. The transmittal letter also asks that such comments be directed to the Department within 21 days. As part of its consideration of each waiver request, the Department reviews the adequacy of the scope of the RBOC's service of the request.

In addition to requiring service of waiver requests on "interested parties," the Department maintains a list of all waiver requests that are pending before both the Department and the Court, and makes this list

available to the public at no charge. The availability of this list, which is updated every Friday, has been publicized in the telecommunications trade press, and is widely distributed to the trade press, the parties to the decree, and interested parties every week.

Finally, service of the waiver request along with the Department's recommendation become a matter of public record at the Court upon service and filing by the Department. The Department will also informally solicit comments from specific parties and non-parties in those instances when it believes that such comments will assist in its analysis of a pending waiver request.

Question 32: Does the Department seek out those individuals and businesses who would favor or benefit from the waiver or does it hear only from those opposed? How many non-BOC comments have you received in favor of a waiver request? From whom were they received?

Answer: The Department seeks to identify and notify all those individuals and businesses who would "be affected" by RBOC entry into the proposed line of business, as well as all persons who may have an interest in any waiver request. In many instances, the Department cannot determine whether a non-party will favor or oppose a waiver until it receives its comments.

The Department does receive comments from non-parties that support waiver requests, as well as from non-parties who oppose waiver requests. For example, the Institute for Professional Education and Dale Carnegie Training Institute recently submitted comments supporting BellSouth Corporation's request for a waiver to provide certain training and educational courses and related services. The Department also receives comments that do not object to a particular waiver request, but instead seek to highlight ambiguities or raise issues that are not addressed directly by the request. For example, Datapro Research Corporation submitted comments on the BellSouth training and educational courses waiver request that stated no general objection to the requested waiver, but urged that "BellSouth should not be permitted to mail advertising materials concerning its training courses . . . to prospective customers throughout its service area as part of its regular mailing of monthly telephone bills" (an advantage not available to BellSouth's non-monopoly competitors). Datapro's comments also argued against the inclusion of salaries of BellSouth instructors in BellSouth's ratebase.

Question 33: Does the Department solicit the views of the Secretary of Commerce or the head of the National Telecommunications and Information Administration (NTIA)--who is responsible for formulating and

presenting Administration policy on telecommunications?

Answer: The Department has not expressly solicited the views of the Secretary of Commerce or the Assistant Secretary in charge of the NTIA with regard to waiver proposals. The Department has informed them, however, that their views will be considered whenever they are relevant to the Department's analysis of the competitive effects of a specific waiver request. Moreover, the Department has met with officials of the Department of Commerce and other federal and state agencies to receive their comments on proposed waivers.

Question 34: Does the Secretary of Commerce or the head of NTIA submit comments to the Justice Department on particular waiver requests? How often have they done so?

Answer: Neither the Secretary of Commerce nor the head of NTIA has submitted comments to the Justice Department on any particular waiver request.

Question 35: Is the Secretary of Commerce or the head of NTIA entitled to file views independently with Judge Greene? Have they done so? Are these views submitted as part of the opinion of the United States in the case? If not, why not?

Answer: Congress, in enacting 28 U.S.C. § 516, has reserved the conduct of litigation in which the United States, an agency, or officer thereof is a party, to officers of the Department of Justice. See United States v. AT&T, 524 F. Supp. 1331, 1335 n.14 (D.D.C. 1981). Thus, as officials of an executive branch agency, the

Secretary of Commerce and the head of NTIA are not entitled to file views independently with the decree Court. The Department, however, has transmitted their views to the decree Court whenever the Department of Commerce has so requested.

Question 36: Does the Department intend to work with the Secretary of Commerce or the head of NTIA to develop a common Administration position on the continued need for BOC restrictions?

Answer: As discussed above, we have already begun work on our 1987 Report on the restrictions. Once our expert, Mr. Peter W. Huber, completes his investigation of the changes that have occurred in the industry since the AT&T divestiture and submits a draft report of his factual findings, it will be necessary for the Administration to formulate appropriate legal and policy proposals that address those findings. At that time, the Administration also will need to consider NTIA's forthcoming update of its 1985 report on the state of the telecommunications industry.

Question 37: Has the Department sought out the views of the FCC before it has submitted a recommendation Judge Greene on a waiver request? Has the FCC submitted its views to the Department? How often? On what issues?

Answer: Yes. The Department has sought the views of the FCC before submitting its recommendation to the District Court in those instances where the FCC's input was expected to be helpful to the Department's analysis of the waiver request. The FCC, as an independent

federal agency, has participated directly in the decree Court proceedings by filing comments with the Court, and has participated informally in the Department's consideration of various requests (and various decree enforcement-related issues) through staff level discussions. See Answer to Question 38.

Question 38: Has the FCC ever submitted its views to Judge Greene on a waiver request? How often? On what issues?

Answer: The FCC submitted its views to the District Court on December 15, 1982, concerning the RBOCs' request for a waiver pursuant to Section VIII(C) of the MFJ to expand their cellular radio serving areas.

Question 39: In considering a waiver request, does the Department have a legal obligation to keep a public record of all meetings with interested parties? Does the Department have a practice of keeping such a public record?

Answer: The Department must consider waiver requests "formally or informally with the requesting Regional Holding Company and all other interested parties." United States v. Western Electric Co., 592 F. Supp. 846, 873 (D.D.C. 1984), appeal dismissed, 777 F.2d 23 (D.C. Cir. 1985). The Department does not keep a public record of all meetings with interested parties and is not legally obligated to do so. Our experience suggests that some interested parties who are potential or actual suppliers to the RBOCs, or who depend upon the RBOCs for access services, are more

forthcoming in providing their candid views to the Department on an informal basis and when the Department can assure them of anonymity. This is consistent with the Department's traditional enforcement responsibilities, which often require that information received from complainants and putative defendants be kept confidential. See, e.g., 15 U.S.C. § 1314(g) (exemption from Freedom of Information Act for materials produced pursuant to Civil Investigative Demand Request).

Formal comments from interested parties, however, are included on the list that the Department maintains of all waiver requests that are pending before both the Department and the Court. This list is made available to the public at no charge, and is widely distributed to the trade press, the parties to the decree, and interested non-parties. In addition, the Department sets forth in significant detail, the basis for any recommendation concerning a waiver request. Should any party or interested person disagree with the Department's recommendation, they have an opportunity to file comments directly with the decree Court.

Question 40: Describe the process whereby interested parties are able to reply to the claims and allegations their opponents make in (1) the written statements they file with the Department and (2) any off-the-record contacts with Department staff.

Answer: In addition to the procedure discussed in response to previous questions, the following supplemental comments are appropriate. Interested parties may reply to the claims and allegations made by others in responsive comments to the Department at any time prior to the Department's filing of its recommendation to the Court. Interested parties may also file comments and replies directly with the Court.

The Department invites replies to issues raised in informal comments when it believes such replies would be useful in its analysis of the pending waiver request by inviting the appropriate party (or non-party) to submit its comments on the issues raised informally by others.

Moreover, the Department's basis for any recommendation concerning a waiver is a matter of public record when the Department files with the decree Court. The Court's procedures allow for interested parties to file comments on all proposed waivers.

Question 41: You referred in your March 13 testimony to a motion to make the waiver process less time-consuming in those situations in which a BOC is seeking a waiver substantially similar to a waiver already recommended by DOJ and granted by the Court. This approach is in line with recommendations contained in last year's domestic policy report by NTIA and also suggested in my

letter to you last August. What progress has been made in obtaining Judge Greene's approval for these "generic" waiver requests? How does the Judge's decision on this request differ from the Department's original request?

Answer: On March 13, 1986, the District Court issued a Memorandum Order setting forth the procedures for reviewing waiver requests that exactly duplicate a previous request. In such instances, the waiver shall be deemed approved by the Court 14 days after the Department has submitted the request to the Court, unless comments are filed with the Court or the Court sua sponte stays approval.

The Department had sought a procedure whereby identical waiver requests would be submitted directly to the decree Court for review. However, the decree Court's March 13 order requires that waiver requests that exactly duplicate a previous request first must be submitted to the Department for preliminary review.

Question 42: Judge Greene's January 13, 1986 opinion suggested to many that he would not grant certain kinds of waivers for the foreseeable future. Has this chilled any efforts of the Justice Department to move forward with motions to grant waivers that they would otherwise have filed with Judge Greene?

Answer: No; however, we cannot say whether the opinion has chilled the willingness of the RBOCs to apply for such waivers.

Question 43: Provide a list of all parties who can appeal a decision by Judge Greene. If he ruled that the BOCs could enter the prohibited long distance market, could MCI appeal? If an interested party is not on this list, how could he get on it?

Answer: The parties to the MFJ (the United States, AT&T, and the RBOCs) can appeal, as of right, a decision by the decree Court. Non-parties (any interested person) may also appeal by seeking leave to intervene from the District Court for purposes of appeal. See United States v. AT&T, supra, 552 F. Supp. at 217-220.

Question 44: What are the differences between the waiver process and the process for modifying the MFJ so as to eliminate a restriction entirely?

Answer: The decree Court has provided guidance concerning the differences between the waiver process and process for modifying the MFJ so as to eliminate a restriction entirely. In its January 13, 1986 Opinion concerning Ameritech's proposal to provide voice storage services, the Court observed that "voice storage is an information service, and since the Regional Companies are clearly prohibited from providing any information service, there is no basis for a clarification motion . . ." 627 F. Supp. at 1110. The Court then stated that what Ameritech was seeking was an order to remove the information service restriction, which "can be achieved only by a request for modification which might require compliance with the standard established by such decisions as United States v. Armour & Co.,

402 U.S. 673 (1971), or by a motion for a waiver which makes the showing required by Section VIII(C)." Ibid.

The Court thus seems to contemplate that the line of business restrictions could be removed pursuant either to a motion for a waiver under Section VIII(C) or to a request for modification in accordance with the standards for modifying antitrust decrees set forth in the applicable Supreme Court decisions. In addition, at the time the decree was entered, the Department undertook to report to the Court concerning the line of business restrictions generally, every third year after divestiture. See United States v. AT&T, supra, 552 F. Supp. at 195. Pursuant to that undertaking, the Department will file a report on the line-of-business restrictions in January 1987.

Question 45: Will the Huber investigation you refer to in your March 13 testimony be the Department's report to the Judge, in January 1987, or will it be the factual basis for the Department's report?

Answer: As noted above, Mr. Huber will prepare a factual report that should form the basis for the Department's recommendations concerning the appropriateness of retaining, modifying, or eliminating some or all of the line-of-business restrictions.

Question 46: Will the Department's report simply be a factual analysis or will it contain recommendations for or against lifting the restrictions?

Answer: No final decision about the substantive content of the Department's report can be made until Mr. Huber has completed his factual report. However, we anticipate making recommendations concerning whether there is a continued need for the various line of business restrictions.

Question 47: Will the public have an opportunity to comment on the Department's factual findings and policy recommendations before they are sent to Judge Greene?

Answer: The Department has solicited comments for the 1987 Report from every segment of the public. In addition to meeting with representatives of many industry and consumer groups, the Department has also met with representatives of various Executive Branch Departments, Federal agencies, Congressional committees, and state regulatory agency representatives. Moreover, the Department has issued a letter requesting specific comments, documents, and data from any interested party. We believe, therefore, that the public will have had an ample opportunity to comment on the relevant issues prior to the time the Department's recommendations are sent to the decree Court, the FCC, or both, depending on the nature of the recommendations and the status of the Dole bill.

Question 48: Is Judge Greene under any legal obligations to review the appropriateness of the continued imposition of the restrictions in light of the report you intend to file in January 1987? Is he under any constraint to act within a specified time?

Answer: No, the Court is under no legal constraint to review the appropriateness of the continued imposition of the line of business restrictions in light of the 1987 Report, or to act on our recommendations in any specific time. However, since the Department undertook to provide the report in connection with the entry of the decree, we have every expectation that the Court will consider our recommendations as well as the comments of interested parties. Moreover, since the report will involve an issue of major national significance, we expect the Court to act expeditiously.

Question 49: Can a BOC independently file a motion for modification of the MFJ, or must it wait for the DOJ to file its motion? If a BOC does file such a motion, what is the procedure whereby it will be considered? Is there any requirement for the Department of Justice or Judge Greene to act on such a motion within a specific period of time?

Answer: An RBOC has the right to file a motion for a modification of the decree directly with the Court. Based on prior experience, we would expect the Court to seek the views of the Department and any other interested party before ruling on such a motion. The Court is under no obligation to act within a set time period on a motion for modification of the decree.

I hope that this letter has been responsive to your questions and helpful to you and the Committee. We look forward to working with you on these extremely important issues.

Sincerely,

Douglas H. Ginsburg
Assistant Attorney General

UNITED STATES DISTRICT COURT
FOR THE DISTRICT OF COLUMBIA

UNITED STATES OF AMERICA, Plaintiff, v. WESTERN ELECTRIC COMPANY, et al., Defendants.	Civil Action No. 82-0192

FILED

MAR 3 1983

JAMES F. DAVEY, Clerk

MEMORANDUM ORDER

The Department of Justice, joined by the seven Regional Holding Companies, has asked the Court to modify its procedures for reviewing line of business waivers submitted by the Regional Companies under section VIII(C) of the decree. Aside from a brief filing by AT&T indicating that it does not oppose the motion, no comments have been received by the Court.

Under this Court's September 14, 1984 order, every request for a line of business waiver is first screened by the Department of Justice. If the Department approves the request, it files a motion with the Court. Comments are due fourteen days later, and replies are due ten days after the filing of comments.

The motion now before the Court would modify this procedure for requests that exactly duplicate a previous request. If that

previous request has already been approved by the Court, duplicate requests that are filed with an undertaking binding the requesting party to all terms and conditions of the approved waiver will be deemed approved ten days after filing if neither the Department nor any other interested party objects. If objections are filed, the procedures of the September 14, 1984 order govern. If a request and undertaking are filed that exactly duplicate a waiver request already pending before the Court, the duplicate request would be deemed approved as soon as the Court approves the pending request.

The suggested modification is admirable insofar as it would conserve the resources of the Court and the parties. However, it also carries with it certain hazards. Line of business waivers are to be granted only "upon a showing by the petitioning [Operating Company] that there is no substantial possibility that it could use its monopoly power to impede competition in the market it seeks to enter." United States v. Western Electric Co., 604 F. Supp. 256, 258 (D.D.C. 1984) (quoting section VIII(C) of the decree). The burden of proof is on the petitioning company. Id. While it seems plausible that particular line of business waivers that are granted to one regional company will generally be granted to the other regional companies as well, this will not always be the case.

In reviewing any waiver request, the Court must consider, inter alia, the petitioning company's market power, its previous success at insulating its monopoly exchange business from its other, competitive enterprises, and its record of public service in providing exchange communications. The Court must also review the amount and quality of competition existing at the time the waiver is sought in the market which the regional company seeks to enter. A system of automatic approval is obviously ill-suited to meet these concerns.

This Court finds that the competing goals of judicial economy and careful review of waiver requests can best be accommodated by a procedure that expedites the treatment of duplicate requests, yet also creates a mechanism for identifying duplicate requests that raise concerns not encountered in the originally approved request.

Accordingly, it is hereby

ORDERED that the following expedited procedures for line of business waivers be and they hereby are adopted by the Court:

1. Every waiver request shall be submitted to the Department of Justice for preliminary review.
2. When a request is identical to one previously approved by the Court, the Department may apply whatever expedited review procedure it deems warranted. It shall then take one of three actions.

(A) First, it may decline to approve the waiver.[1/]

(B) Second, it may approve the waiver and file a statement with the Court certifying that (i) the Department has reviewed the request; (ii) the request is identical in all respects to a waiver previously granted by the Court; (iii) the requesting company has bound itself to all terms and conditions imposed upon the previously approved waiver; and (iv) the Department believes that the requested waiver raises no factual or legal issues that are significantly different from those raised by the previously approved waiver. If this statement is filed, the waiver request shall be deemed approved by the Court at the expiration of a fourteen-day period, unless comments are filed with the Court or the Court sua sponte stays approval. If comments are filed or a stay entered before expiration of the fourteen-day period, the procedures established in the September 14, 1984 order will apply.[2/]

1/ In that event, the procedures established by the September 14, 1984 order will apply.

2/ The fourteen-day period for comments will in either event run from the date of filing of the Department's motion.

(C) Third, it may approve the waiver and file a motion that declines to make the certifications described in subparagraph (B), supra. In that event, the procedures established in the September 14, 1984 order will apply.

3. When a request is identical to one already approved by the Department and pending before the Court, the Department may likewise apply whatever expedited review procedure it deems warranted. It shall then (A) decline to approve the waiver; (B) approve the waiver and file a motion that makes the certification described in subparagraph 2(B), supra; or (C) approve the waiver without making that certification. If Justice Department approval is granted with the proper certification, the waiver shall be deemed approved by the Court when the Court approves the previously pending waiver, fourteen days have elapsed since the filing with the Court of the request for which deemed approval is sought, and no comments have been received with respect to the request for which deemed approval is sought. In all other cases, the September 14, 1984 order shall govern.

4. The September 14, 1984 Order shall continue to govern all requests for a line of business waiver that are not described in this Order.

March 13, 1986

HAROLD H. GREENE
United States District Judge

UNITED STATES DISTRICT COURT
FOR THE DISTRICT OF COLUMBIA

UNITED STATES OF AMERICA, Plaintiff, v. WESTERN ELECTRIC COMPANY, INC., AND AMERICAN TELEPHONE AND TELEGRAPH COMPANY, Defendants.	Civil Action No. 82-0192
UNITED STATES OF AMERICA, Plaintiff, v. AMERICAN TELEPHONE AND TELEGRAPH COMPANY, et al., Defendants.	Misc. No. 82-0025 (PI)

FILED
SEP 14 1984
JAMES E. DAVEY, Clerk

MEMORANDUM ORDER

On August 27, 1984, the Department of Justice filed its response to requests from the Regional Holding Companies for waivers of the line of business restrictions of Section II(D) of the decree. In its response, the Department recommended that the following requests be granted subject to the parties' agreed-upon conditions:

Bell Atlantic Leasing Subsidiary

NewVector Cellular Enterprise (US West)

Real Estate Subsidiary (BetaWest and PacTel)

Retail Stores (Nynex and PacTel)

Foreign Business Ventures (Ameritech and PacTel)

The Department also suggested that all objections to these motions and the proposed orders be filed within fourteen days of the Department's filing.

Because there is some doubt over the deadline for submitting objections to or comments on the specific waiver requests listed above, the Court will extend the time for the filing of responses. In order to avoid similar confusion concerning the time for filing responses to future requests for waivers of the line of business restrictions that are supported by the Department of Justice, a more general briefing schedule is likewise established. Accordingly, it is this 14th day of September, 1984,

ORDERED That any responses to the Department of Justice's motions and proposed orders of August 27, 1984 concerning the following waiver requests:

Bell Atlantic Leasing Subsidiary

NewVector Cellular Enterprise (US West)

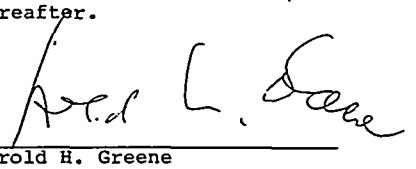
Real Estate Subsidiary (BetaWest and PacTel)

Retail Stores (Nynex and PacTel)

Foreign Business Ventures (Ameritech and PacTel)

shall be filed not later than October 1, 1984, and that any replies to the responses may be filed not later than October 10, 1984, and it is further

ORDERED That hereafter responses to any motion and proposed order filed by the Department of Justice recommending that a waiver of the line of business restrictions be granted shall be filed not later than fourteen days from the date of the Department's filing, and that replies to such responses, if any, shall be filed not later than ten days thereafter.



Harold H. Greene
United States District Judge

Department of Justice

"THE FEDERAL TELECOMMUNICATIONS POLICY ACT OF 1986"

REMARKS OF

DOUGLAS H. GINSBURG
ASSISTANT ATTORNEY GENERAL
ANTITRUST DIVISION

BEFORE THE

COMPUTER AND COMMUNICATIONS INDUSTRY ASSOCIATION

ON

JULY 17, 1986

GOOD MORNING. I AM PLEASED TO BE HERE TODAY TO DISCUSS AN IMPORTANT EFFORT TO ENSURE THE CONTINUED COMPETITIVE DEVELOPMENT OF THIS NATION'S TELECOMMUNICATIONS INDUSTRY. ON JUNE 19, SENATE MAJORITY LEADER BOB DOLE INTRODUCED S. 2565, THE "FEDERAL TELECOMMUNICATIONS POLICY ACT OF 1986," A BILL THAT WOULD CONSOLIDATE FEDERAL REGULATORY AUTHORITY OVER THE TELECOMMUNICATIONS INDUSTRY IN THE FEDERAL COMMUNICATIONS COMMISSION. THE PROPOSED BILL WOULD (A) REQUIRE THE COMMISSION TO PROMULGATE A DETAILED SET OF REGULATIONS IDENTICAL IN SUBSTANCE TO THE CONSENT DECREES ENTERED IN THE AT&T AND GTE CASES 1/, (B) EMPOWER THE COMMISSION TO REMEDY VIOLATIONS OF THE REGULATIONS, (C) EMPOWER THE COMMISSION TO MODIFY OR RESCIND, AND TO GRANT EXEMPTIONS AND WAIVERS FROM, THE REGULATIONS AT A LATER DATE, AND (D) PROVIDE THAT VIOLATIONS OF THE REGULATIONS SHALL NOT BE DEEMED TO CONSTITUTE VIOLATIONS OF ANY EXISTING ANTITRUST DECREE. AFTER THE BILL IS ENACTED, I WOULD EXPECT MOTIONS TO BE FILED WITH THE COURT TO VACATE THE AT&T AND GTE DECREES. THE BASIS OF THOSE MOTIONS WOULD BE THAT THE CONTINUED EXISTENCE OF THE DECREES WOULD BE INCONSISTENT WITH THE REGULATORY AUTHORITY GIVEN TO THE COMMISSION BY THE BILL. AND I EXPECT THAT THE COURT SHOULD DECIDE TO VACATE THE DECREE FOR PRECISELY THAT REASON.

1/ UNITED STATES V. AT&T, 552 F. SUPP. 131 (D.D.C. 1982), AFF'D SUB NOM. MARYLAND V. UNITED STATES, 460 U.S. 1001 (1983); SEE UNITED STATES V. GTE CORP., 603 F. SUPP. 730 (D.D.C. 1984).

I STRONGLY SUPPORT THE PROPOSED LEGISLATION. IN FACT, IF IT IS PASSED BY CONGRESS IN THE FORM OUTLINED ABOVE, THE ANTITRUST DIVISION WOULD BE PREPARED TO MOVE IN THE DISTRICT COURT FOR VACATION OF THE DECREES.

A. THE IMPACT OF THE DECREES IN THEORY AND PRACTICE

THE AT&T DECREE, WHICH WAS SIGNED OVER FOUR AND ONE-HALF YEARS AGO, HAS BROUGHT ABOUT ONE OF THE MOST SIGNIFICANT INDUSTRIAL RESTRUCTURINGS IN OUR COUNTRY'S HISTORY. THE DECREE REQUIRED AT&T TO DIVEST ITS REGULATED LOCAL OPERATING COMPANIES BY JANUARY 1, 1984. AT&T DID SO BY DIVIDING ITS 22 BELL OPERATING COMPANIES (BOCS) INTO THE SEVEN REGIONAL HOLDING COMPANIES (RBOCS) WITH WHICH WE ARE ALL NOW FAMILIAR. THE DECREE LEFT THE POTENTIALLY COMPETITIVE MANUFACTURING AND LONG DISTANCE BUSINESSES, AS WELL AS MOST OF BELL LABS, TO AT&T. IN CONTRAST, THE DECREE GAVE THE RBOCS THE LOCAL PLANT AND FACILITIES, AS WELL AS SUFFICIENT ASSETS TO ESTABLISH A JOINT RESEARCH AND DEVELOPMENT ORGANIZATION NOW KNOWN AS BELLCORE. THE DECREE WAS DESIGNED TO FOSTER COMPETITION IN LONG DISTANCE BY REQUIRING THE RBOCS' LOCAL OPERATING COMPANIES TO PROVIDE, FOR ALL LONG DISTANCE COMPANIES, ACCESS TO THE BOCS' LOCAL EXCHANGE NETWORKS THAT IS EQUAL TO THE ACCESS PROVIDED TO AT&T. THIS PROCESS WAS BEGUN IN 1984 AND, WITH MINOR EXCEPTIONS, IS SCHEDULED FOR COMPLETION BY SEPTEMBER OF THIS YEAR.

THE DECREE ALSO LIMITS THE BOCS GENERALLY TO PROVIDING LOCAL EXCHANGE TELECOMMUNICATIONS AND EXCHANGE ACCESS SERVICES

UNLESS A WAIVER IS OBTAINED FROM THE DECREE COURT. THE LINE-OF-BUSINESS RESTRICTIONS IN THE AT&T DECREE AND THE RELATED WAIVER PROCESS BASICALLY REQUIRE THE DECREE COURT--WITH OUR HELP--TO REGULATE THE RBOCS' ENTRY INTO NEW BUSINESSES. TO DATE, WAIVERS SUBJECT TO CONDITIONS HAVE BEEN GRANTED TO ALLOW THE RBOCS INTO PRACTICALLY EVERY BUSINESS THAT THEY HAVE SOUGHT TO ENTER, OTHER THAN INFORMATION SERVICE, INTEREXCHANGE (I.E., LONG-DISTANCE) SERVICE, AND TELECOMMUNICATIONS EQUIPMENT MANUFACTURING.

THE DECREE'S LINE-OF-BUSINESS RESTRICTIONS WERE BASED ON HISTORICAL AND ANALYTIC FACTORS INDICATING THAT TWO COMPETITIVE DANGERS MAY ARISE WHEN FIRMS THAT CONTROL NATURAL MONOPOLIES AND THAT ARE RATE-REGULATED, SUCH AS THE BOCS, PARTICIPATE IN ADJACENT COMPETITIVE MARKETS. THE FIRST AND MOST SIGNIFICANT DANGER ARISES WHEN, IN ORDER TO COMPETE IN ADJACENT MARKETS, RIVALS REQUIRE ACCESS TO THE RATE-REGULATED, NATURAL MONOPOLY FACILITIES. (HERE, A BOC'S LOCAL EXCHANGE NETWORK). UNDER SUCH CIRCUMSTANCES, THE RATE-REGULATED MONOPOLIST HAS THE INCENTIVE (BECAUSE THE PROFIT IT CAN EARN FROM ITS OWNERSHIP OF THE MONOPOLY FACILITY IS CONSTRAINED BY REGULATION), AND MAY HAVE THE ABILITY (BECAUSE IT OWNS THE NATURAL MONOPOLY), TO LIMIT ACCESS TO ITS MONOPOLY FACILITIES OR--MORE LIKELY IN THE PRESENT CIRCUMSTANCES--TO PROVIDE ACCESS ONLY ON DISCRIMINATORY TERMS THAT DISADVANTAGE ITS RIVALS IN THE COMPETITIVE MARKET.

THE SECOND CONCERN INVOLVES THE POTENTIAL FOR ANTICOMPETITIVE CROSS-SUBSIDIZATION. UNDER RATE-OF-RETURN

REGULATION, A MONOPOLIST MAY EARN UP TO A SET RETURN ON ITS INVESTMENT IN FACILITIES USED TO PROVIDE THE REGULATED SERVICE. THE MONOPOLIST HAS AN INCENTIVE, HOWEVER, TO INCLUDE IN ITS RATE BASE ANY INVESTMENTS OR CURRENT EXPENSES IT MAY MAKE IN ORDER TO PARTICIPATE IN A COMPETITIVE MARKET. IN SUCH CIRCUMSTANCES, THE MONOPOLIST CAN REDUCE THE PRICE IT CHARGES CONSUMERS IN THE COMPETITIVE MARKET AND RECOUP THE LOSS OF INCOME FROM CUSTOMERS OF ITS MONOPOLY SERVICES. WHERE THIS OCCURS, CONSUMER WELFARE IS HARMED IN TWO WAYS: (1) THE MONOPOLIST DRIVES MORE EFFICIENT RIVALS OUT OF THE COMPETITIVE MARKET AND MAY ULTIMATELY OBTAIN THE POWER TO RAISE PRICES IN THAT MARKET; AND (2) CONSUMERS OF THE REGULATED MONOPOLY SERVICE ARE CHARGED MORE THAN THE COST OF THOSE SERVICES.

THE AT&T DECREE WAS INTENDED TO FOSTER COMPETITION IN THE INTEREXCHANGE AND INFORMATION SERVICES MARKETS AMONG COMPANIES OTHER THAN THE RBOCS BY REQUIRING AFFIRMATIVE TECHNOLOGICAL CHANGES THROUGH THE EQUAL ACCESS PROCESS. AT THE SAME TIME, BY IMPOSING LIMITATIONS ON THE RBOCS' ENTRY INTO NON-TELEPHONE MARKETS, THE DECREE WAS INTENDED TO REMOVE THE RBOCS' INCENTIVE TO RETARD COMPETITION IN NONREGULATED MARKETS.

UNLIKE THE AT&T DECREE, WHICH WAS DESIGNED, IN PART, TO KEEP LOCAL TELEPHONE COMPANIES OUT OF LONG-DISTANCE, THE 3-YEAR-OLD GTE DECREE WAS DESIGNED TO STRUCTURE AND REGULATE THE ENTRY OF THE GTOCS INTO LONG DISTANCE AS A RESULT OF GTE'S ACQUISITION OF SPRINT. DESPITE ITS DIFFERENT APPROACH--RATHER THAN EXCLUDING GTE FROM NONREGULATED BUSINESSES, IT REGULATES

GTE'S PARTICIPATION IN CERTAIN MARKETS--THE GTE DECREE ADDRESSED COMPETITIVE CONCERNS SIMILAR IN KIND TO THOSE PRESENT IN AT&T. THE GTE DECREE ALSO FOSTERS COMPETITION IN THE INTEREXCHANGE AND INFORMATION SERVICES MARKETS, IN PART THROUGH EQUAL ACCESS REQUIREMENTS, ALTHOUGH IT IS LIMITED TO A SIGNIFICANTLY SMALLER PORTION OF THE NATION'S TELECOMMUNICATIONS MARKETS, THAN THE RBOCS POSSESS.

THE COMPETITION-BASED POLICIES ON WHICH THE AT&T AND GTE DECREES WERE FOUNDED HAVE CONFERRED SIGNIFICANT BENEFITS ON AMERICAN CONSUMERS. SINCE DIVESTITURE, THE MAJOR ASPECTS OF THE TELECOMMUNICATIONS INDUSTRY HAVE BECOME MORE COMPETITIVE AND THUS HAVE BEEN CHARACTERIZED BY THE INTRODUCTION, AT AN UNPRECEDENTED PACE, OF INNOVATIVE NEW PRODUCTS AND SERVICES COUPLED WITH DRAMATIC PRICE REDUCTIONS. FOR EXAMPLE, IN THE MARKET FOR CUSTOMER PREMISES EQUIPMENT, DEREGULATION ALLOWS CONSUMERS THE OPPORTUNITY TO PURCHASE THEIR CPE FROM A WIDE VARIETY OF VENDORS. A NOVEMBER 1985 REPORT BY THE NATIONAL TELECOMMUNICATIONS AND INFORMATION ADMINISTRATION (NTIA) ESTIMATED THAT THE PER-LINE PRICE OF KEY TELEPHONE SYSTEMS WOULD DECREASE BY 25 PERCENT IN 1985 ALONE, AT THE SAME TIME AS TECHNOLOGICAL ADVANCES MADE SUCH SYSTEMS MORE VERSATILE THAN EVER BEFORE. SIMILARLY, IN THE MARKET FOR TELECOMMUNICATIONS EQUIPMENT, INDUSTRY SOURCES REPORT THAT THE PER-LINE PRICE OF CERTAIN CENTRAL OFFICE SWITCHING EQUIPMENT HAS BEEN CUT IN HALF, AS NUMEROUS AMERICAN AND FOREIGN FIRMS COMPETE WITH EACH OTHER TO SUPPLY CENTRAL OFFICE EQUIPMENT TO THE BOCS. THIS

COMPETITION HAS GIVEN THE BOCS ADDITIONAL INCENTIVES TO ACCELERATE THEIR PLANT REPLACEMENT AND MODERNIZATION PROGRAMS, TO THE BENEFIT OF RESIDENTIAL TELEPHONE SUBSCRIBERS AS WELL AS MAJOR BUSINESS CUSTOMERS. AND IN THE MARKET FOR LONG DISTANCE SERVICES, AT&T HAS REDUCED ITS RATES TIME AND AGAIN, MAKING THE PRICE OF DIRECT-DIALED CALLS 25 PERCENT LOWER THAN IT WAS AT DIVESTITURE; INDEED, FOR CERTAIN LARGE CUSTOMERS, AT&T'S LONG DISTANCE CHARGES ARE ONLY ONE-HALF OF WHAT THEY WERE AT THAT TIME.

FINALLY, WHILE THE PRICE OF FLAT RATE LOCAL EXCHANGE SERVICE HAS INCREASED BY APPROXIMATELY 35 PERCENT IN THE FIRST TWO YEARS AFTER DIVESTITURE, THIS INCREASE IS FAR SHORT OF THE ESTIMATES MADE BY SOME OBSERVERS IN 1982. MOREOVER, THAT INCREASE IN RATES IS BETTER EXPLAINED BY OTHER FACTORS, SUCH AS INFLATION AND REGULATORY CHANGES, THAT HAVE NOTHING TO DO WITH THE DIVESTITURE. ON BALANCE, BOTH RESIDENTIAL CUSTOMERS AND BUSINESS CUSTOMERS ARE PAYING LESS FOR THEIR TELEPHONE SERVICE THAN THEY WERE PRIOR TO DIVESTITURE, BY TAKING ADVANTAGE OF THE NEW COMPETITIVE ENVIRONMENT.

B. THE DEPARTMENT'S REASONS FOR SUPPORTING THE PROPOSED LEGISLATION

AS YOU KNOW, THE DEPARTMENT AND ITS CONSULTANT, MR. PETER W. HUBER, CURRENTLY ARE ENGAGED IN A COMPREHENSIVE STUDY OF THE CHANGES THAT HAVE OCCURRED IN THE INDUSTRY DURING THE YEARS SINCE THE AT&T DIVESTITURE. WE WILL REPORT OUR FINDINGS IN JANUARY 1987, EITHER TO THE FCC OR TO THE DECREE COURT, OR TO BOTH, DEPENDING ON WHETHER THE DOLE BILL HAS BEEN

PASSED, AND ON WHETHER THE DECREES HAVE BEEN VACATED. OBVIOUSLY, I AM NOT NOW IN A POSITION TO CONCLUDE WHETHER THE RESTRICTIONS THAT THE DECREES PLACE ON AT&T, THE BOCS, AND GTE AND ITS SUBSIDIARIES ARE STILL NECESSARY OR HAVE BECOME OUTMODED. BUT I DO WANT TO STRESS THAT IT IS NOT BECAUSE WE DISAGREE WITH THE POLICIES UNDERLYING THE DECREES, OR THE COURT'S DECISIONS ENFORCING THEM, THAT WE SUPPORT THE DOLE BILL.

BEFORE DIVESTITURE AND IN THE EARLY POST-DIVESTITURE PERIOD, THE DEPARTMENT HAD IMPORTANT RESPONSIBILITIES FOR MONITORING, ON BEHALF OF THE COURT, THE STEPS THAT AT&T AND THE BOCS TOOK TO MAKE DIVESTITURE WORK. WE STILL MUST OVERSEE THE PROCESS OF CONVERSION TO EQUAL ACCESS, WHICH IS SCHEDULED TO BE COMPLETED IN SEPTEMBER. BUT IT HAS BECOME INCREASINGLY CLEAR TO US IN THE YEARS SINCE DIVESTITURE THAT DAY-TO-DAY ADMINISTRATION OF THE DECREES SHOULD ULTIMATELY BECOME THE RESPONSIBILITY OF THE FCC.

THE CURRENT DECREE REGIME HAS CREATED AN INEFFICIENT PARALLEL SYSTEM OF FEDERAL REGULATION FOR THE TELECOMMUNICATIONS INDUSTRY, WITH THE COMMISSION ON ONE TRACK, AND THE DEPARTMENT AND THE DECREE COURT ON THE OTHER. SINCE JANUARY 1984 WE HAVE RECEIVED OVER 110 BOC REQUESTS FOR WAIVERS OF THE AT&T DECREE'S LINE-OF-BUSINESS RESTRICTIONS. ANALYZING MANY OF THESE REQUESTS REQUIRES A MAJOR COMMITMENT OF THE DEPARTMENT'S STAFF AND SUPERVISORY RESOURCES, AND ALMOST ALL OF THEM REQUIRE LENGTHY PERIODS FOR THIRD-PARTY COMMENTS, DEPARTMENT DECISIONS ON WHETHER TO SUPPORT THE REQUEST AND ON WHAT CONDITIONS, AND COURT ACTION ON THE WAIVER REQUEST.

THE DEPARTMENT--AND I BELIEVE THE COURT--NEITHER EXPECTED NOR DESIRED SUCH A RESULT WHEN THE DECREE WAS ENTERED. UNFORTUNATELY, HOWEVER, THE COMPLEXITIES OF THE DECREE AND THE CONFLICTING INTERESTS OF AT&T, THE BOCS, AND OTHER TELECOMMUNICATIONS FIRMS HAVE BROUGHT US TO THE POINT WHERE WE ARE ACTING NOT AS THE PROSECUTORS WE ARE, BUT AS THE REGULATORS THAT ARE NEEDED TO ADMINISTER THE DECREE. AND THE FACT IS THAT, UNLIKE THE DEPARTMENT, THE COMMISSION IS A REGULATORY AGENCY, POSSESSED OF A BROAD REGULATORY MANDATE FROM CONGRESS, AN ADMINISTRATIVE EXPERTISE, A PROCEDURAL AND REMEDIAL FLEXIBILITY, AND A STAFF CAPACITY DEVOTED TO TELECOMMUNICATIONS REGULATION THAT IS NECESSARILY GREATER THAN OUR OWN.

MOREOVER, EXPERIENCE HAS SHOWN THAT IT IS VERY DIFFICULT TO COORDINATE THE COMMISSION'S ENFORCEMENT OF ITS STATUTORY RESPONSIBILITIES WITH THE DEPARTMENT'S AND THE COURT'S ENFORCEMENT OF THE DECREES. IF OUR TELECOMMUNICATIONS INDUSTRY IS TO GROW AND TO COMPETE SUCCESSFULLY IN THE WORLD ECONOMY, IT IS IMPERATIVE THAT THE PRESENT DUAL REGULATORY SYSTEM BE RESTORED TO A UNITARY SYSTEM BASED ON THE EXPERT AGENCY--THE COMMISSION--THAT CAN BEST ENSURE THAT THE REGULATORY REGIME EMBODIED IN THE DECREES IS IMPLEMENTED IN A MANNER CONSISTENT WITH OTHER TELECOMMUNICATIONS-RELATED REGULATIONS.

INDEED, THE BILL ALSO POSSESSES THE GREAT VIRTUE OF ALLOWING IMPORTANT FACTORS TO BE TAKEN INTO ACCOUNT IN CARRYING OUT THE DECREES' REGULATORY SCHEME THAT CANNOT NOW BE ADDRESSED BY THE DECREE COURT ITSELF, SUCH AS NATIONAL SECURITY

INTERESTS, THE INTERESTS OF LOCAL TELEPHONE USERS, AND THE SIGNIFICANT ROLE OF TELECOMMUNICATIONS IN INTERNATIONAL TRADE. BECAUSE THE DECREES WERE ENTERED IN ORDER TO SETTLE ANTITRUST LAWSUITS, WHICH HAVE THE SOLE PURPOSE OF PROTECTING COMPETITION, THE COURT IN DRAFTING THE WAIVER STANDARD AND THE DEPARTMENT IN ENFORCING THE DECREES HAVE OF NECESSITY FOCUSED ON COMPETITIVE CONCERNS. THE DECREE COURT'S OWN POWER TO APPLY AND TO MODIFY THE DECREES IS SIMILARLY LIMITED.

IF, ON THE OTHER HAND, THE COMMISSION WERE GIVEN JURISDICTION OVER A REGULATORY REGIME SUBSTANTIVELY IDENTICAL TO THE DECREES, THAT AGENCY COULD APPLY THE PROVISIONS OF THE EXISTING DECREES UNDER THE BROADER "PUBLIC INTEREST" STANDARD. AS NOTED ABOVE, SUCH A STANDARD WOULD PERMIT THE COMMISSION TO CONSIDER IMPORTANT FACTORS THAT CANNOT BE TAKEN INTO ACCOUNT IN THE DECREE COURT. THE PUBLIC INTEREST STANDARD WOULD ALSO PERMIT THE COMMISSION TO CONSIDER A DIFFERENT MIX OF CRITERIA IN DETERMINING WHETHER THE PARTICULAR RESTRICTIONS NOW FOUND IN THE DECREES SHOULD BE RETAINED, RESCINDED, OR MODIFIED. IN MY VIEW, SUCH REGULATORY FLEXIBILITY REPRESENTS SOUND PUBLIC POLICY.

THOSE ARE THE POLICY REASONS WHY THE DEPARTMENT SUPPORTS THE PROPOSED LEGISLATION. NOW I WISH TO TOUCH BRIEFLY ON THE LEGAL REASONS FOR OUR SUPPORT. FIRST, IN OUR VIEW THE PROPOSED LEGISLATION IS PLAINLY CONSTITUTIONAL AND DOES NOT IMPROPERLY INTRUDE ON THE PROVINCE OF THE COURTS TO ADMINISTER JUDICIAL DECREES. THIS IS NOT A "COURT-STRIPPING" BILL. RATHER,

CONGRESS PLAINLY HAS THE POWER UNDER THE COMMERCE CLAUSE TO IMPOSE REGULATIONS SUCH AS THOSE CONTAINED IN THE DECREES, AND A COURT, THROUGH AN INJUNCTION OR CONSENT DECREE, CANNOT OUST CONGRESS FROM THE EXERCISE OF POWERS THAT THE CONSTITUTION DELEGATES TO THE LEGISLATURE. INDEED, THE LAW IS CLEAR THAT IF CONGRESS CHANGES THE SUBSTANTIVE LAW WHILE A COURT ORDER EITHER IS ON APPEAL OR HAS BECOME FINAL BUT REMAINS EXECUTORY--AS THESE DECREES ARE--THEN THE COURTS MUST ENFORCE THE NEW SUBSTANTIVE LAW AS CONGRESS HAS DECLARED IT. CONGRESS COULD NOT, WITHOUT RAISING SEPARATION OF POWERS QUESTIONS, ENACT LEGISLATION THAT OPERATES DIRECTLY ON THE AT&T AND GTE DECREES BY VACATING OR MODIFYING THEM STATUTORILY, OR THAT EXPLICITLY DIRECTS THE OUTCOME OF FUTURE PROCEEDINGS UNDER THE DECREES. UNDER THE PROPOSED LEGISLATION, HOWEVER, CONGRESS WOULD DO NO SUCH THING. THE COURTS WILL HAVE AN OPPORTUNITY TO DECIDE WHETHER THE DECREES MUST BE VACATED IN WHOLE OR IN PART IN ORDER TO REFLECT THE CHANGED LEGAL CIRCUMSTANCES AND TO AVOID FRUSTRATING THE COMPREHENSIVE NEW REGULATORY SCHEME ESTABLISHED BY CONGRESS.

SECOND, I SUPPORT THE PROPOSED LEGISLATION BECAUSE IT WOULD NOT CHANGE ANY OPERATIVE PROVISION OF EITHER DECREE. AS I HAVE ALREADY STATED, AT THIS TIME THE DEPARTMENT IS NOT PREPARED TO CONCLUDE THAT ANY PARTICULAR CHANGES IN THE DECREES ARE JUSTIFIED. NOR DO I BELIEVE THAT ANY OTHER OBSERVER OF THIS INDUSTRY CURRENTLY HAS THE REQUISITE OVERVIEW OF COMPETITION IN THE PRESENT AND FUTURE MARKETPLACE TO KNOW WHAT WOULD

CONSTITUTE SOUND POLICY. WE WILL ALL HAVE THE BENEFIT OF THE HUBER REPORT SOON ENOUGH; WHEN WE HAVE THE FACTS IT WILL BE TIME TO BASE POLICY RECOMMENDATIONS ON THOSE FACTS. THE POINT IS THAT, ONCE THAT REPORT IS IN AND THE RANGE OF REASONABLE PROPOSALS FOR CHANGE HAS BEEN IDENTIFIED, THE RESPONSIBILITY FOR SORTING THROUGH AND IMPLEMENTING THOSE PROPOSALS SHOULD BE ASSIGNED TO THE SINGLE MOST COMPETENT AND EXPERT AGENCY AVAILABLE TO DO THE JOB--THE FCC.

IN MY VIEW, ANY EFFORTS TO ALTER THE DECREES DURING THE LEGISLATIVE PROCESS WOULD INEVITABLY CREATE COMPLEXITIES THAT WOULD SERVE ONLY TO DIMINISH THE CHANCES OF PASSAGE AND CREATE ADDITIONAL UNCERTAINTY IN THE INDUSTRY. MOREOVER, SIGNIFICANT DISPARITIES BETWEEN THE LEGISLATION AND THE DECREES MIGHT CAUSE UNCERTAINTY IN THE COURTS ABOUT THE LEGAL IMPACT OF THE LEGISLATION ON THE DECREES, AND THUS ABOUT THE EXTENT TO WHICH THE DECREES SHOULD BE VACATED.

FINALLY, WHEN THE LEGISLATION IS PASSED AND THE COURT VACATES THE DECREES, THE COMMISSION WILL HAVE THE POWER AND AN APPROPRIATE PROCESS--RULEMAKING BY THE EXPERT AGENCY WITH FULL PUBLIC COMMENT--THROUGH WHICH TO MAKE APPROPRIATE CHANGES IN THE REGULATORY SCHEME NOW EMBODIED IN THE DECREES.

* * *

I BELIEVE THAT IT IS EXTREMELY IMPORTANT THAT CONGRESS ACT QUICKLY TO CONSOLIDATE REGULATORY RESPONSIBILITY FOR THE TELECOMMUNICATIONS INDUSTRY IN THE FCC. OTHERWISE, THE CURRENT FRACTURED STATE OF FEDERAL TELECOMMUNICATION REGULATION WILL

CONTINUE TO CAUSE CONFUSION, DELAY, AND UNCERTAINTY IN THE TELECOMMUNICATIONS INDUSTRY. MOREOVER, IF CONGRESS HAS NOT TRANSFERRED AUTHORITY OVER THE DECREES' REGULATORY REGIME PRIOR TO NEXT YEAR, CONSIDERATION AND IMPLEMENTATION OF RECOMMENDATIONS FOR REGULATORY CHANGE ARISING OUT OF MR. HUBER'S REPORT AND NTIA'S FORTHCOMING UPDATE OF ITS 1985 REPORT MAY BE MIRED IN A MORASS OF JURISDICTIONAL CONFLICTS AND OVERLAPS. REQUIRING THAT THIS NECESSARILY COMPLEX PROCESS BE CARRIED OUT UNDER THE CURRENT SCHEME OF DIVIDED FEDERAL AGENCY AND COURT REGULATION WILL NEEDLESSLY COMPOUND THE DIFFICULTIES.

BEFORE CONCLUDING, I WOULD LIKE TO CLARIFY ONE POINT. WHILE THE DEPARTMENT IS CONVINCED OF THE MERITS OF THE DOLE BILL AND THE NECESSITY OF LEGISLATIVELY TRANSFERRING THE DECREES' REGULATORY REGIME TO THE FCC BEFORE THIS CONGRESS ADJOURNS, OUR ENTHUSIASTIC SUPPORT SHOULD NOT BE MISTAKEN FOR AN ABANDONMENT OF OUR ENFORCEMENT OF THE DECREES. AS LONG AS THE DECREES REMAIN UNDISTURBED, AT&T, THE RBOCS, AND GTE MUST COMPLY WITH THEM. A FAILURE TO COMPLY, MOREOVER, IS A SERIOUS MATTER THAT CAN RESULT IN CIVIL AND/OR CRIMINAL PENALTIES. WE EXPECT FIRMS TO RESPECT AND OBEY THE LAW, INCLUDING THE DECREES, AND, IF THAT EXPECTATION IS NOT MET, THE DEPARTMENT WILL TAKE EVERY STEP NECESSARY TO ELIMINATE AND PUNISH VIOLATORS. WE HAVE MADE THIS CLEAR TO THE COMPANIES, AND WE MEAN IT.

IN SUM, THE DEPARTMENT STRONGLY SUPPORTS THE DOLE BILL AS THE APPROPRIATE SOLUTION TO OUR CURRENT, UNSATISFACTORY SYSTEM

OF DUAL REGULATION OF THE TELECOMMUNICATIONS INDUSTRY. WE WILL, IN ANY EVENT, GO FORWARD WITH PREPARING OUR JANUARY 1987 REPORT ON THE AT&T DECREE RESTRICTIONS FOR SUBMISSION TO THE COURT OR THE FCC. AND, I STRESS, THE DEPARTMENT WILL CONTINUE FULLY TO DISCHARGE ITS ENFORCEMENT RESPONSIBILITIES UNDER THE AT&T AND GTE DECREES UNLESS AND UNTIL THEY ARE VACATED BY THE COURTS.

THANK YOU.

Mr. WIRTH. On our second panel, is Mr. Larry DeMuth, executive vice president and general counsel of U.S. West in Englewood, CO; second, Mr. Gary McBee, vice president of Federal Regulations for Pacific Telesis; third, the Honorable Paul Levy, chairman of the Massachusetts Department of Public Utilities; fourth, Mr. Phillip Onstad, a member of the Domestic Communications Committee and chairman of the International Communications Committee of ADAPSO; fifth, Mr. Uzal Martz from the American Newspaper Publisher Association; sixth, no stranger to the committee, Mr. Henry Geller, former Assistant Secretary of Commerce and presently with the Washington Center for Public Policy Research; seventh, another veteran of the subcommittee, Mr. Gene Kimmelman, legislative director of the Consumer Federation of America; and, finally, Mr. Robert Coackley, department manager for HP Laboratories, Hewlett-Packard in Palo Alto, CA.

Gentlemen, we greatly appreciate your being here; this has been a long morning, and we would hope that you all would be able as well to recognize the subcommittee's rules in which we would ask you all to summarize your testimony in 5 minutes.

Your testimony will be included in full in the record, and as pointed out earlier the record will be left open for 30 days for questions and answers.

As I look across this room, I think all of you have testified before the subcommittee at earlier dates, and we are very pleased to have you all here.

Thank you very much. Why don't we just start with you, Mr. DeMuth and perhaps move right down the table.

Thank you all.

STATEMENTS OF LAURENCE W. DeMUTH, EXECUTIVE VICE PRESIDENT AND GENERAL COUNSEL, U S WEST; GARY W. McBEE, VICE PRESIDENT OF FEDERAL REGULATIONS, PACIFIC TELESIS GROUP; PAUL F. LEVY, CHAIRMAN, MASSACHUSETTS DEPARTMENT OF PUBLIC UTILITIES; PHILLIP C. ONSTAD, MEMBER, DOMESTIC COMMUNICATIONS COMMITTEE, CHAIRMAN, INTERNATIONAL COMMUNICATIONS COMMITTEE, ASSOCIATION OF DATA PROCESSING SERVICE ORGANIZATIONS; UZAL H. MARTZ, JR., CHAIRMAN, TELECOMMUNICATIONS COMMITTEE, AMERICAN NEWSPAPER PUBLISHER ASSOCIATION; HENRY GELLER, WASHINGTON CENTER FOR PUBLIC POLICY RESEARCH; GENE KIMMELMAN, LEGISLATIVE DIRECTOR, CONSUMER FEDERATION OF AMERICA; AND ROBERT COACKLEY, DEPARTMENT MANAGER, HP LABORATORIES, HEWLETT-PACKARD CO.

Mr. DEMUTH. Thank you, Mr. Chairman. I appreciate the opportunity to appear to present U S West's views on the restrictions contained in the modified final judgment which brought about the breakup of the Bell System.

I'm sure that you are aware that a continuation in—we believe that a continuation of these restrictions is inappropriate and unnecessary in today's environment. All three of the main restrictions of that decree are based upon an era that is now past and one

in which AT&T assumed end-to-end responsibility for the one technology which provided telephone service.

As that technology advanced, and as communications and computer technology merged, that one end-to-end market for telephone service became many markets. The Bell System resisted that reality and sought to maintain its control in order to preserve its monopoly and the pricing structures which were implicit in that monopoly.

The antitrust suit and the modified final judgment which resulted from that suit were designed to terminate that resistance and to restructure the industry. The thinking behind the MFJ was thus based upon a backward look at what had existed in an era of monopoly. That approach was designed to address behaviors that were a part of a system which ended with the spinoff of the operating telephone companies.

The decree failed to comprehend both the effects of the decree itself and the response of the companies which were created as a result of divestiture. The MFJ requires equal access and interconnection of long-distance carriers into local exchange network. The Bell System had prohibited that type of free interconnection.

But U.S. West has welcomed the opportunity and the challenge to provide equal access. Fair and equal interconnection is part of the economic life blood of the divested companies.

The consent decree, or the MFJ, contemplates and requires the unrestricted interconnection of all types of terminal equipment at the end of the network and on the customer's premise. In the Bell System, that type of free interconnection was not permitted.

Today, in the 14 States which U S West serves, freedom of interconnection of customer premise equipment is as matter of fact as is the reliability of dial tone.

The consent decree was designed to prevent any one manufacturer from being the dominant supplier for the Bell Operating Telephone Co. Again, the result has been as desired. And today, Western Electric can no longer count on the operating companies as captive clientele.

In addition to these changes which were mandated by the modified final judgment, we have initiated other activities that have accelerated movement into a new and entirely different environment. For example, U.S. West has declared publicly and is now pursuing implementation of a philosophy of open network architecture.

The old Bell System reality was closed network architecture. End-to-end responsibility and the prohibition against so-called foreign attachments sought to exclude all but the customer from using the network. Open network architecture makes the network available to customers and competitors alike on equal terms and conditions.

It contemplates the widest possible use of the facilities which are essential to all who desire access to every home and place of business in America. And it eliminates the ability to use those essential facilities in ways that disadvantage any user or any potential competitor.

In short, the situation which was addressed in the drafting of the decree has completely ceased to exist. The new environment is dra-

matically different as a result of the decree and the response of companies like U S West.

The restrictions designed to create that dramatic difference are simply no longer necessary. Our operating telephone companies separated from their previous owner and set adrift in a technological revolution and a competitive marketplace have found that competitive behavior is essential for economic survival.

There is no longer a viable opportunity nor a long term incentive to utilize essential facilities in an anticompetitive manner. History will probably teach that the MFJ was a correct and appropriate response to developing technology and the need to promote a free marketplace in the telecommunications and information industry. But the continued march of technology and the response of the divested companies have now rendered obsolete the restrictions of that decree which were designed to ensure the very environment which now exists.

[The prepared statement of Mr. DeMuth, follows:]

TESTIMONY on Behalf of U S WEST
March 13, 1986

My name is Laurence W. DeMuth, Jr. I am Executive Vice President and General Counsel of U S West. Prior to assuming this position I was Vice President and General Counsel of the Mountain States Telephone and Telegraph Company for 16 years. Prior to becoming General Counsel, I practiced law in Denver for 15 years.

U S West is a Colorado corporation headquartered in Denver. It was formed in 1983 and on January 1, 1984, acquired ownership of the stock of three telephone companies previously owned by the American Telephone and Telegraph Company, The Mountain States Telephone and Telegraph Company, Northwestern Bell Telephone Company and Pacific Northwest Bell Telephone Company. It also provides cellular communications services through its NewVector subsidiary. U S West also has several other subsidiary businesses engaged in the provision and maintenance of telephone equipment and systems, financial, real estate, publishing and international business activities.

The telephone companies owned by U S West provide local exchange and intraLATA services in 14 states from Iowa and Minnesota west to Washington and Oregon, and from New Mexico and Arizona north to the Canadian border. These states contain both large metropolitan areas such as Minneapolis, Phoenix, Seattle and Denver as well as very sparsely populated areas such as rural portions of Arizona, Montana, Utah, New Mexico, Wyoming and the Dakotas.

We believe the uniqueness of our serving territory, which includes almost half of the continental United States, gives us a perspective on the needs of large population centers as well as of rural America. In the two years since divestiture, we have invested almost $4 billion in new facilities to serve our customers' needs.

Within the territory we serve are major business users such as IBM, Boeing, Honeywell, Control Data and 3M. These businesses, as well as many others, are both large users of our services and large providers of telecommunication services to themselves and other companies. These customers have highly advanced and sophisticated needs that require us to make use of the newest advances in telecommunications.

Our companies also provide service to major Federal locations including the Los Alamos facilities of the Department of Energy, the headquarters of the Strategic Air Command, the

headquarters of the military's space command and the headquarters of the North American Air Defense Command, as well as large Navy installations in the Puget Sound area. We are thus extremely mindful of the need to maintain an efficient and responsive communications capability in times of national emergencies.

The greatest obstacle we face in the operation of our business is the Modified Final Judgment ("MFJ"). The MFJ has turned the Department of Justice and the presiding divestiture Court into regulators of the divested Bell telephone companies. Because of the MFJ, the shareholders, directors, and employees of the telephone companies are restricted in their ability to make normal business decisions in the day-to-day operation of their companies. Customers are likewise unable to purchase services that they desire. The MFJ not only restricts us and our customers in the provision of telephone services, but also restricts our ability to enter other lines of business. The artificial definitions of our basic business contained in the MFJ, prevent us from making use of new technology in the provision of information services. The MFJ's definitions and assumptions are unrealistic in today's environment.

Emphasis should be placed on the fact that we do not seek to turn back the clock and recreate the Bell System. Divestiture has occurred and should not be undone. Nor, we believe, should anyone want to undo divestiture and recreate the past, for in the past this industry was driven by the policies established by AT&T. Today, our industry is driven by one concept: technology. No company, regulator, legislature or, indeed, the Congress, can dictate the development of the communications industry because of the explosion that is taking place in communications technology.

Twenty years ago, a call from New York to California had to travel over AT&T's transcontinental copper cables. Today that call can travel over AT&T's copper cables, or over AT&T's or another carrier's microwave radio network, or it might be carried over fiber optic cables, or it might travel from one earth station to another by way of a satellite. It was the advent of new technology that allowed intercity carriers to enter the marketplace. It is doubtful that anyone would have attempted to duplicate the long distance network if the only technology available to do so was to bury huge copper cables from coast-to-coast.

It is often said that the good old days probably weren't. That concept applies to the telephone industry. Those who want to bring back the days of one-stop shopping for telephone service ignore the impact of technology. Western Electric simply could not produce the variety of equipment available today. Customers demand and have tremendous choice in even simple

telephone sets. Some people, for example, want a clock-radio telephone. Others want automatic dialing phones, or phones that have large buttons, or cordless phones, or phones in their cars or briefcases. To suggest that one company can anticipate customer demand and supply that demand nationwide is to ignore reality.

Technology, by allowing new companies to invent, design, manufacture and market phones, has also allowed the price of telephone sets to drop dramatically. Customers are no longer required to pay monthly charges forever, for telephone sets. Phones can be purchased in the same manner that any household or office appliance is purchased. Customers, not the phone company, can decide how much they want to pay for a set, what color and shape it should be, what features it should have and from whom they should buy it.

Customers are no longer required to have their premises wired by the telephone company. A new home today can be wired for telephone service in the same manner it can be wired for electricity, cable television, intercom or computer services.

In today's environment, computers communicate and telephones compute. Businesses can purchase information systems that involve computer technology and communications technology that are indistinguishable. It is no surprise that AT&T builds and markets computers, while IBM, through its wholly-owned ROLM subsidiary, builds and markets telephones, or that IBM has taken a substantial ownership interest in MCI, the nation's second largest long distance carrier. The breakup of the Bell System created a marketplace that is driven by the demands and decisions of customers, rather than by the decisions of AT&T's leaders. Traditional American traits of innovation, invention and marketing are now free to operate in the communications industry in a way that was impossible when that industry was controlled by AT&T.

When owned by AT&T, the telephone companies had little flexibility in the operation of their business. Practices and procedures were written at AT&T and distributed nationwide. Innovative thinking was discouraged. Employees functioned as lockstep bureaucrats and administrators, not market-driven respondents to customer needs. AT&T owned the Western Electric Company and with Western Electric, AT&T owned Bell Telephone Laboratories. Prior to divestiture, more than 90 percent of Western Electric's sales were to the telephone companies owned by AT&T.

AT&T established the policies that denied interconnection to the local exchange network of customer premise equipment if not provided by the Bell System. AT&T established the policies that denied the use of the local exchange facilities to MCI and

other long distance companies. AT&T actively argued those policies before the Federal Communications Commission, the Courts and the Congress.

U S West has established corporate policies that are dramatically different from Bell System policies prior to divestiture. Today, an entirely different spirit exists in the companies owned by U S West. Employees are encouraged and rewarded in demonstrating innovative thinking. Customer satisfaction is paramount in how we operate the business. No longer do employees function as if they are working for a monopolistic public utility. Indeed, U S West's name is reflective of the Company's philosophy. It contains neither the word "Bell" or "telephone".

We believe competition is to be welcomed rather than hindered. We believe an active and open marketplace can provide the widest variety of services at the lowest price far better than can cumbersome regulatory mechanisms. We thus have supported deregulatory efforts of the Federal Communications Commission and our state commissions even though deregulation allows easy entry of other providers into what has traditionally been "our" business. We believe that customers should decide what services and products they want to purchase rather than having only the availability of products and services that the "telephone company" decides should be offered.

Unfortunately, the MFJ's restrictions fail to recognize the tremendous technological and policy changes that have taken place as the result of and since divestiture. It must be recognized that Judge Greene has heard no evidence in the case since over four years ago and even that evidence dealt primarily with the policies AT&T used more than ten years ago. Obviously, the telecommunications industry of today is not the industry that was described to Judge Greene. The fundamental error of the MFJ is that it assumes that absent the restrictions, the pre-divestiture conduct of AT&T will be repeated even though AT&T no longer owns the telephone companies. Nothing could be further from the truth.

Since divestiture, AT&T's public pronouncements regarding the MFJ restrictions indicate that AT&T believes the restrictions ought to be maintained. This is understandable since the restrictions protect AT&T from competition from the divested telephone companies. But AT&T is not correct when it states that the restrictions are necessary to avoid unfair use of the local exchange facilities. AT&T's argument is built on the assumption that even though the facilities are no longer owned by AT&T the facilities would be used in an anticompetitive manner, or, in other words, in the same manner as when AT&T owned the facilities. In AT&T's words, if we do not learn from

history, we are bound to repeat history. But AT&T is wrong in assuming that no one has learned from history and that the divested children will commit the sins of their parent.

What is the lesson history teaches regarding local exchange facilities? Simple. The American people no longer want a monopolistic single source end-to-end supplier of communications equipment and services.

AT&T did not act clandestinely. It openly advocated that it believed it should refuse interconnection of CPE and of other long distance companies. Its top officials, such as former Chairman John DeButts, at every opportunity, actively espoused AT&T's belief that a monopoly was in the best interests of the American people. AT&T vigorously fought the antitrust case on every front, both in the Courtroom and in the Congress.

U S West understands the lesson of history. Our telephone companies welcome competition. We do not urge regulators to bar entry to new providers of communications services. We settled the MCI litigation totally apart from AT&T in order to remove that litigation as a hindrance to a good working relationship with MCI. We established a plan for allocating long distance customers to all carriers rather than automatically defaulting customers to AT&T. That plan was later adopted by the FCC, and is now required nationwide. We have recently filed with the FCC in its Computer Inquiry III proceeding, our Corporate policy regarding the complete open-architecture offering of our facilities, whereby our facilities will be made available to any provider of communications services that wants them. Thus, a company such as General Motors that may own its switches may desire to purchase local distribution. Or, a cable television company that owns a distribution network may wish to purchase switching services.

Even a cursory look at the CPE market makes it clear that the restrictions are unnecessary. No one would seriously contend that problems exist in attaching CPE to the local exchange network. The FCC's rules establish technical standards for telephone sets and if a set meets those standards it is simply plugged in by a customer.

The original agreement between AT&T and the Department of Justice provided that AT&T would receive all existing CPE and further, that the divested Bell companies would be prohibited from providing any CPE. However, Judge Greene refused to approve the agreement unless AT&T agreed the divested companies would be allowed to market new CPE. Today AT&T and the divested companies, together with thousands of other companies, offer CPE in a highly competitive marketplace without problems in interconnecting with the local exchange facilities. Under AT&T's argument that the divested companies should be barred

from operating in competitive markets because they would hinder others by denying connection with the local exchange facilities, it would be expected that the divested companies would disadvantage AT&T and other CPE providers to the benefit of their own CPE sales activities. This does not occur. It is apparent that an open and fair marketplace can exist in which the divested companies actively participate, without the requirement of onerous restrictions such as are contained in the MFJ.

The interconnection of long distance carriers is also proceeding in an orderly fashion. Proponents of the restrictions argue that this is the case only because the MFJ prohibits the provision of long distance services by the divested companies. Yet, as noted, CPE is provided by both the divested companies and others without allegations of anticompetitive conduct. It is clear that long distance prohibition is unnecessary.

A similar situation exists regarding the MFJ prohibition barring the divested companies from providing information services. This prohibition is also based on the fear that if the divested companies provide such services, other providers of information services will not be allowed to interconnect with the local exchange networks. However, as is true for CPE and long distance services, no one can contend today that the telephone companies owned by U S West deny interconnection to any information provider. Our NewVector cellular subsidiary provides store and forward information services to its cellular customers, in conjunction with third parties by allowing co-location in NewVector's switching equipment. To suggest that we would begin to deny the use of local exchange facilities to information providers, if we were allowed to provide such services, is simply not reasonable.

The third prohibition contained in the MFJ, the bar against manufacturing telecommunications equipment, likewise makes no sense unless viewed from the perspective of AT&T or other existing manufacturers. All the prohibition does is protect existing manufacturers from competition. The telephone companies are limited to purchasing whatever equipment manufacturers want to make available to them. An analogous situation would be if the Ford Motor Company could sell cars but could not manufacture them. Obviously, Ford would have a product line that would be at the mercy of General Motors, or Chrysler, or the foreign auto makers who could directly limit the ability of Ford to be a meaningful participant in the marketplace, by refusing to sell to Ford cars with advanced features, or by selling to Ford at a high price that would make it difficult for Ford to compete. In such a situation, Ford might have a better idea, but it would not be reflected in a Ford automobile.

It is not surprising that since divestiture, America has become a huge importer of telecommunications equipment. In 1985, this nation imported $800 million more such equipment than it exported. It is more than likely that if one turns over a telephone set in any store in America and looks at the bottom, it will have been manufactured in a foreign nation. The two major suppliers of central office equipment in America are AT&T and Northern Telecom, and the latter is more than 50% owned by Canadian interests.

AT&T and other manufacturers have urged the Department of Justice to prevent the divested companies from being able to even design, or have built for them, equipment that could be used to provide better telephone service. The manufacturing prohibition means the divested companies must purchase only what others are willing to provide to them and, in ever more frequent situations, the suppliers are from foreign nations. At a time when, in many of our 14 states, the people in our agricultural and logging industries are without jobs, it is ironic that because of the MFJ, we are unable to help the economies in our territory by creating manufacturing jobs but must instead purchase only what is available on the open market where much of the equipment is supplied by foreign businesses. Today, technical standards for how the nationwide network operates are being developed by industry groups comprised of communications companies, including local and long distance carriers, manufacturers, trade associations of computer and other information service providers, and of course users. No longer can one company, such as could AT&T, establish technical standards for interconnection to the network.

In summary, we believe the MFJ restrictions not only do not benefit the public interest but directly harm our companies, employees, customers and the nation by contributing to massive trade imbalances. We thus welcome the opportunity to place before the Congress our concerns as to the need to terminate the restrictions contained in the MFJ. We ask for nothing other than the right to compete in a competitive marketplace based on the abilities of our employees.

Mr. WIRTH. Thank you very much, Mr. DeMuth. Mr. McBee.

STATEMENT OF GARY W. McBEE

Mr. MCBEE. Thank you, Mr. Chairman, and members of the subcommittee.

I appreciate the opportunity to address the committee today on one of the most critical issues in telecommunications policy, and that is the impact of the modified final judgment on the Bell Operating Companies.

Pacific believes that the modified final judgment is a major barrier to competition and, more importantly, to the provision of a variety of new services to the American people. In my statement today, I would like to highlight some key points contained in the prepared statement that I have submitted previously.

The benefits of new and exciting information services can be brought to average consumers, not only to those businesses and individuals who can afford sophisticated equipment. Expansion and strengthening of the network through the addition of information services will keep our service quality second to none at rates lower than we could otherwise charge.

The basis for the decree's ban on information services—it was announced over 4 years ago—is rapidly eroding. The effect of the decree also drives intelligence out of the core network to be replaced by customer premises' equipment, a substantial portion of which is produced offshore. The result is a declining balance of trade and reduced U.S. jobs.

The modified final judgment's narrow antitrust perspective has produced a draconian remedy. Concerns about cross-subsidies and other anticompetitive behavior can be resolved without losing the benefits of Pacific's participation in these markets.

Mr. Chairman, the promises of the decree: increased competition and new services in technologies, have not been fully realized. While competition is developing in the market for interexchange services, albeit slowly, the MFJ's constraints have in large part stifled the growth of information services.

These are predominantly local exchange-based services and technologies, the very ones which consumers and small businesses would like to see. Some of the services that we would like to offer have been discussed before. There are a number of them included in my testimony, and I will just mention three.

Videotex based electronic services for those who currently have a PC or plan to have one. The network could become a gateway to these services, providing all customers with access to home shopping and banking, financial and market data, airline and bus schedules, and other types of products and information. We would provide the gateway.

Home and office management services: Voice mail could enable subscribers to create, send and receive recorded messages through any telephone set at home or at the office.

Audiotex services. An example would be a ticket agency's, computer, with synthesized voice provided in the network which could speed the purchase of tickets for sporting events or concerts. Cus-

tomers could automatically select date, price and location through their phone and choose the language they chose to communicate in.

Now, some of these services are available currently in California, if you happen to be a medium- or large-size business and can afford the equipment. You can also get it from some telephone companies in California, but not Pacific. Since pacific serves 80 percent of California, therefore, a majority of Californians are not able to use these services.

I would like to stress that these are just a few examples: many more will emerge. As technology continues to develop, new methods, new applications will come forward. The revolution in telecommunications technology, which has driven public policy and the system's position for over the last 25 years, will continue.

And the only thing that I can say at this point is that we don't know what the future truly holds. Congress should ensure that the public policy framework provides enough flexibility so that these technologies can be implemented. One of the most insidious aspects of the decree is that it kills off new services before they have an opportunity to be tried in the marketplace. Pacific is holding discussions with regulators and others to develop safeguards so that competition is open and fair. The safeguards that may be imposed by the FCC in its third computer inquiry, including accounting controls and some form of comparably efficient interconnection for other service providers, are likely to be the best vehicle for ensuring these public interest goals.

In contrast, the modified final judgment's prohibitions are regulatory overkill. Not only do they deny services, but they also hamper Pacific in meeting its commitment to high quality universal service at reasonable rates.

There is another way that customers benefit: Pacific has proposed that any profits from such services be used to offset the price of local exchange service.

Thank you very much.

[Testimony resumes on p. 214.]

[The prepared statement of Mr. McBee follows:]