DEPARTMENT OF JUSTICE

WRITTEN STATEMENT

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Concerning

THE 1996 TELECOMMUNICATIONS ACT: AN ANTITRUST PERSPECTIVE

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Good afternoon, Mr. Chairman and Members of the Subcommittee. I appreciate this opportunity to share my thoughts on the outlook for competition in the telecommunications industry, and the Justice Department's crucial role in promoting and protecting competition in this industry in the wake of the Telecommunications Act of 1996.

I want to begin by commending the leadership and Members of this Subcommittee, as well as the leadership and Members of the Judiciary Committee as a whole, for their leadership on this important subject, for their support of this landmark legislation, and for sharing the vision that competition can and should replace regulation as the main engine for economic oversight and growth in this industry.

We know from lengthy experience across a variety of industries that competition serves America's consumers well, leading to lower prices, increased product quality and variety as well as more innovation. Competition also serves American businesses, by encouraging them to be more efficient and enabling them better to compete in increasingly global markets. We know from the growth of competition in the long distance market, which was facilitated by the break-up of AT&T, that these precepts apply to the telecommunications industry, just as they do to others. Moreover, in the telecommunications industry, increased competition also promises the added benefit of limiting the need for costly and inevitably imperfect regulation.

In enacting the 1996 Telecom Act, Congress recognized that changes in technology and a number of marketplace factors made a transition to competition possible in the local exchange segment of this industry. Though that transition is possible, and indeed is underway, we must remember that competition will not blossom overnight. Fundamental transitions like the one

called for by the Act are difficult and take time, as they require the development of new, extraordinarily complex legal, technical and economic arrangements so that competition can take root where regulated monopoly had reigned for decades before. Getting these arrangements in place will take not only the incumbents and entrants working together in good faith, but also the persistence and vigilance of regulators at the state and federal levels. In the end, it may even take new technological innovations to overcome the technical problems as well as the resistance of incumbents in bringing competition to a single wire system.

In reviewing the extent of local competition about one year and a half after the Act's passage, it seems that many industry participants underestimated the full extent of the challenge of bringing competition to the local telephone market. In the excitement surrounding the Act's passage, many in the industry predicted that the Act's goal of opening up local markets would be realized quickly. Some of the long distance companies as well as many of the cable companies initially claimed that they could easily bring competition to the local telephone market. Subsequent events have shown, however, that such predictions misjudged the degree of difficulty in developing and instituting the necessary operating systems and technology, as well as just how much time, money, and work was necessary to enter the local telephone market.

In assessing the Act's effectiveness, I think it's critical that we not expect more progress than is realistic. At the same time, it's important to understand that the Act takes us in the right direction, and that any effort to make significant adjustments risks adding to the regulatory uncertainty and further complicating the already complex process of facilitating competition in a market that has long been treated as a natural monopoly. In short, the Act did a remarkably good

job of identifying the necessary market opening steps and any efforts to alter its basic approach would be misplaced.

Simplifying things a bit, I think that consumers will benefit most significantly from two possibilities encouraged by the Act: (1) the development of technological alternatives to wireline service that will provide new ways to deliver telecommunications services; and (2) the offering of new products and services, as well as the bundling of existing services, through a more creative use of the existing facilities.

The development of technologies in the cable and wireless industries that would challenge the single wire monopoly of the local telephone companies began before enactment of the Telecom Act, of course. And many in the industry foresaw the efficiencies and consumer benefits inherent in offering attractive bundles of services that could include local, long distance, Internet access, and paging services, for example. But the enactment of the Telecom Act was a critical step in accelerating these developments and in achieving these goals because it sent the clear signal that the regulatory landscape would welcome and reward competition. Specifically, the Act created new possibilities for local entry through its interconnection, unbundling, and resale requirements as well as a regulatory framework that will ultimately lead to the bundling of different telecommunications services, including local and long distance. In sum, the Act not only allows for and encourages new alternate networks, it also envisions better uses of the existing network by eventually allowing incumbents to employ such facilities more flexibly and requiring them to share such facilities with new entrants who will also be able to use them to develop new types and combinations of services.

In examining the progress thus far, it is essential to understand that the full potential of the Telecom Act will not be realized until alternative technologies -- such as cable and wireless telephony -- can be developed and deployed and other important innovations have a chance to take place. At present, we are seeing a lot of posturing and litigation that is a logical consequence of the fact that, in nearly all markets, the one wire into homes and businesses is the only practical way to deliver voice telephony. Understandably, in this environment, this resource is an essential input to both the incumbent local exchange carriers and their competitors. Accordingly, the price that regulators set for this scarce resource is probably the single most important factor in determining how much and what kind of entry is possible.

In time, we expect to see new forms of delivering local telephone service and the "single wire problem" alleviated. In the meantime, consumers can still benefit from the resale, unbundling, and interconnection requirements of the Act, particularly as companies begin offering new products and bundles of services that heretofore were not available. Doing our part to facilitate these forms of competition, and to help consumers attain these benefits as soon as realistically possible, has been a central priority of the Division since the enactment of the Act. And despite the ongoing battles between the incumbents and entrants, there has been real -- though modest -- progress on this front.

In discussing the implementation of the Telecom Act, I think it is important to step back and examine each of the basic steps in this pro-competition, de-regulatory process that we, along with the FCC and the states, are now embarked upon. Again, to simplify things a bit, I think we can divide the process into three essential steps: (1) developing the necessary legal rules to move

the system from one based on regulated monopoly to one based on competition; (2) ensuring that the various players in the industry -- most notably the incumbent providers -- comply with the rules that govern this transition; and (3) ensuring that the competitive process works effectively, without the illegal creation or exercise of market power.

The Antitrust Division has an important role to play in each of these three steps. In this respect, we appreciate the attention devoted by this Subcommittee, and by others in Congress, to ensuring that our expertise in maximizing competition in general and in the telecommunications industry in particular could be brought to bear upon this process. The Act's vision for antitrust enforcement and the role provided for the Antitrust Division was no accident; the Justice Department's role in evaluating Bell Company applications for in-region long distance entry, the antitrust savings clause, and the repeal of the provision that immunized FCC-approved telephone company mergers from antitrust review, all reflect Congress's appreciation for the value of antitrust and the good work of the Antitrust Division in this industry over the years.

(1) DEVELOPING THE RULES FOR LOCAL COMPETITION

Thanks to the remarkable efforts of the FCC, the state PUCs, and all involved, we have made substantial progress in the first basic step I mentioned -- that is, in developing the necessary new legal rules to make competition for local service possible -- while still respecting our historic commitment to universal service. Under the Act, all incumbent local telephone companies must "unbundle" the elements of their network and lease them to new entrants at cost-based rates as well as make available resold services at a wholesale rate. To facilitate this process, the FCC set forth a pricing methodology, called TELRIC, and undertook what

Chairman Hundt has termed a "trilogy" of rulemakings -- setting out the basic rules for local competition, reforming the interstate access charge rules, and developing an explicit, competitively-neutral universal service system, including new initiatives to bring Internet access to schools and libraries as well as to rural health care clinics.

To assist the FCC in carrying out its mandate within the time lines set out by the Act, we filed comments in both the Local Competition and Access Charge proceedings. As you know, these rules are now in litigation and the Eighth Circuit Court of Appeals has invalidated part of the Local Competition Order. While the Eighth Circuit's ruling was the bad news in this process, the good news is that many of the States have proceeded to follow the basic approach outlined by the FCC, including its commitment to a sound pricing methodology for the necessary access to the incumbent's telephone network.

In retrospect, the battles thus far over the development of the rules of the road for local competition are not surprising. For example, with regard to the setting of the prices of the elements of the incumbents' network, there is a basic tension: if the prices are set too high, that will impede efficient entry; if they are set too low, that will effectively subsidize entry at the expense of the incumbents. With the stakes as high as they are here, getting the necessary rules in place has been no easy task. There has been real progress on this front, but the important point is that the setting of these prices, though critical to efficient entry, will not itself directly benefit consumers. Rather, the consumer benefits will come when entrants get up and running, offering new packages of services, better prices for existing services, and, better yet, using new technologies to improve upon the efficiencies of the present network.

(2) ENSURING COMPLIANCE WITH THE ACT'S MARKET OPENING STEPS

Even with all the litigation and regulatory effort that has gone into the first step (and is still ongoing), it has become clear that the second step I referred to a minute ago -- ensuring that the incumbent providers comply with the Act's market opening measures -- is the most challenging aspect of this process. And, as we at the Antitrust Division see it, the Act contemplates a two-part strategy for encouraging Bell Company compliance with its market opening measures -- the incentive of in-region long distance entry on one hand, and the threat of regulatory and antitrust action to respond to intentional non-compliance or obstructionist acts on the other. Of course, as regards long distance entry, Section 271 of the Act looms large, as it sets out a series of requirements to open the local market and safeguard against anticompetitive practices, all of which must be met before the Bells can offer in-region long distance services.

The Antitrust Division focused on the Section 271 process long before the first application by a Bell for long distance entry because our role under the statute is to assess all such applications under a competition-based standard that we were charged with developing. To best effectuate this role, one of my first acts as Acting Assistant Attorney General was to commence a lengthy internal study, including an analysis of input from interested parties, of the options available to the Department for assessing when Bell entry would be appropriate.

The Department's approach for evaluating when a Bell Company should be allowed to enter the long distance market has two components. The first component of the Department's standard is an inquiry into whether, at the time the application is filed, the local market is open in practice to all three of the types of competitive entry called for by the Act -- the construction of

new facilities, the use of unbundled elements, and resale. If this inquiry is satisfied, local entry will be constrained only by technological limits and the inherent capabilities, resources, and business strategies of the potential competitors, and not by the artificial barriers Congress sought to eliminate.

The second component of the Department's standard is to require that there be some way to measure and to "benchmark" Bell Company performance in the opening of the local exchange market. By establishing basic performance benchmarks, such as the Bell's ability to switch over a certain number of consumers per week, the Department believes that we can ensure that the market opening is permanent. That is, with performance benchmarks in place and a commitment to maintain those levels of performance, the mechanisms available to prevent "backsliding" by the Bell Company will operate more effectively.

One question that many of the Bell Companies have focused on with regard to our standard is the significance of actual competitive entry. In our evaluations of SBC's Section 271 application in Oklahoma and Ameritech's Michigan application, we endeavored to make clear that evidence of actual competitive entry is obviously useful, but not essential, to making the determinations on both components of our test. On the first component of our standard, actual entry can best demonstrate that the Bell Company has taken the necessary steps to open its local market. On the second, we look to any actual entry to provide the kind of benchmark we think can best ensure that the opening of the market is irreversible. Neither of these components, however, require that the Bell Company must lose a certain market share or that entrants must gain any particular number of customers before we would support a Section 271 application.

Rather, our standard requires that the market conditions be such that anyone with a good product has an opportunity to market it without running up against artificial entry barriers.

In sum, we believe that our approach to Section 271 applications strikes the balance necessary to maximize competition, supporting long distance entry when local markets are fully open, but not requiring the Bell Companies to be held out of long distance on account of their competitors' plans. But, with only two Section 271 applications ruled upon thus far, both of which have been denied, some have complained about the slow pace at which local entry is occurring. Especially with all of the rhetorical crossfire that has been occurring, I am concerned that some may lose sight of the important progress that is already being achieved. Hundreds of final interconnection agreements have been reached between incumbent providers and new entrants, real money is being invested in order to provide alternative local telephone service, and an increasing number of customers are being served by competitive local providers.

Also encouraging is the good work that some incumbent carriers have undertaken, particularly with regard to the development of the complex operations support systems that are needed to switch customers to their competitors. With regard to Ameritech's recent application in Michigan, for example, both the Department and the FCC commended Ameritech for its efforts in this regard, and both of us outlined the few specific areas where Ameritech must improve upon its past efforts to obtain long distance entry. As per our basic approach, our comments viewed the actual commercial entry by competitors in Michigan as reflective of the real progress that has already been made in that state, as well as an indication of what we can anticipate elsewhere as this process continues to move forward.

Significantly, the FCC's decision in the Ameritech matter did much to clarify the basic requirements for Section 271 authority, paying considerable attention to the important details of what it takes to open up the local market, such as the necessary arrangements for the operations support systems that will enable competitors to switch over and serve customers previously served by the incumbent. Highlighting the importance of this issue, LCI and Comptel have recently petitioned the FCC to develop a series of reporting requirements to measure the wholesale performance of the incumbent providers in this regard. As we explained in our filing with the FCC on this petition, these systems have been a central concern of ours because they are essential to support full scale competition. Accordingly, our filing encouraged the FCC to develop appropriate reporting requirements in this area as expeditiously as possible.

With most of the basic ground rules in place, we are getting nearer to the time when it will be up to the companies in the marketplace to make good on the Act's promise of competition in local telephone service, and to turn their focus away from the regulatory arenas. To be sure, it will be important to review the basic ground rules from time to time and ask whether further adjustments and fine tuning are needed in light of what we're learning. But the incumbents' duty to open up their local markets is becoming more and more a question of getting the work done rather than "what to do." The Bell Companies should complete the necessary steps to open their local markets. We stand ready to do what we can to clarify what is required of them. And once they complete those steps, we will do what we can to achieve their rapid entry into the long distance market.

It should also be clearly understood, however, that under the Act, market-opening measures by incumbents are legal requirements, not options. If a company fails to meet these obligations, it will be held accountable.

In executing our role under the Act, we do not seek to serve the interests of any individual competitor, but rather to ensure that the local, long distance and other companies in this market can all have at it in a fair fight. In so doing, we will remain attentive to the possibility that one side or the other will seek to "game" this market opening process to its parochial advantage. Throughout whatever maneuvering that may occur in terms of posturing and finger-pointing, we at the Antitrust Division will keep our focus on the marketplace and seek to work with any Bell Company that takes the steps necessary to facilitate competition.

If some Bell Companies take up our invitation to work with them on addressing the obstacles to full and fair competition, we believe that we may see some Bells that can meet the requirements of the Act and gain our support for long distance entry in the not too distant future. In this regard, it is encouraging that the FCC's decision on Ameritech's recent application provided clear direction as to what conditions Ameritech must meet before it will be able to receive Section 271 approval. We are committed to working with Ameritech, or any other Bell who is serious about gaining Section 271 approval, by developing approaches to meet the Act's requirements in ways that are reasonable and not unnecessarily cumbersome.

As I noted at the outset, the bottom line here is that this process is not a sprint; it is a long distance run that requires persistence without getting winded in the process. Congress charted

the right course in the Act, and we intend to work with all of the players in this process -- Congress, the FCC, the States, the incumbents, the long distance companies, and the new entrants -- to best execute our role in moving this industry from regulated monopoly to competitive markets.

(3) PROTECTING THE COMPETITIVE PROCESS

Once the Act's vision of competition begins to take hold in the marketplace, the most important aspect of this pro-competition, de-regulatory process will be the third step I outlined earlier -- protecting the competitive process itself. As you all recognized in your work on the Act, this dimension is where antitrust enforcement can often be most effective. In terms of rooting out unreasonable restraints of trade, preventing anticompetitive mergers and ending any monopolistic practices, the antitrust laws are sure to play an important role in promoting and preserving competition in markets that are emerging from regulation. So far, the biggest challenge on this front has been to monitor and assess the competitive effects of all of the mergers that have been taking place in this industry. So, before I conclude, let me say a few words about how we approached those mergers that have come before us.

The Department's basic mandate under the Clayton Act is to monitor all mergers carefully, ensuring that prospects for competition are not jeopardized by anticompetitive mergers, while recognizing that in many cases, competition will be promoted through efficiency-enhancing combinations. In the communications area, our resources have been stretched to fulfill this mandate as, in the past year alone, we examined two Bell Company mergers, Bell Atlantic/NYNEX and SBC/PacTel. We also have reviewed hundreds of radio mergers following

Congress' decision to loosen the regulatory caps on radio station ownership. And we examined one telephone/cable merger -- US West/Continental Cable -- as well as British Telecom's acquisition of 100% of MCI. In a number of these cases, we secured consent decrees, and in the case of BT/MCI, we are seeking to modify an earlier decree, to address what we saw as anticompetitive aspects of those arrangements.

One important challenge in the wake of the Telecom Act was to apply Section 7 of the Clayton Act to the radio industry for really the first time, because the prior regulations had prevented almost any significant consolidation of ownership. In so doing, we made considerable efforts to educate the industry about the limits to which they could consolidate or engage in other practices that might lessen competition. In my view, these efforts have paid off. In the 17 months after the enactment of Telecom Act, we took enforcement action against 7 radio mergers, obtaining the divestiture of 12 radio stations in a number of markets around the country. And, as a result of these efforts, the application of antitrust to this industry has become much clearer, enabling those in the industry to structure their affairs accordingly.

As you all understand, it will be a long way before we will reach the Act's vision of competitive telecommunications markets, as the road to local competition is not a smooth and quick journey. Although it is less than we all would like, and often out of view, we are making progress. Moreover, I can assure you that the Department of Justice is doing its part to push this process forward and to ensure that competition takes root and can prosper.

I would be happy to answer any of your questions.