DEPARTMENT OF JUSTICE

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before the House Judiciary Committee
on Telecommunications Reform Legislation

It is a great honor to testify before this committee concerning the role of the Department of Justice in promoting greater telecommunications competition. I am grateful to you, Chairman Hyde, and to Congressman Conyers and this committee for holding this hearing and for exercising leadership in this vital area of our economy and competition policy, and to you and Congressman Conyers for introducing telecommunications reform legislation that provides a decisionmaking role for the Department of Justice in connection with allowing the Bell Operating Companies to enter the long distance and manufacturing markets.

Our fundamental vision for the telecommunications future is simple to state, but breathtaking in its implications: Every company will be permitted to compete in every market for every customer. We want that day to come as soon as possible, because increased competition in telecommunications will benefit consumers, spur economic growth and innovation, promote private sector investment in an advanced telecommunications infrastructure and create jobs. We would be naive, however, if we expected an uncomplicated transition from the regulated monopolies that characterize many segments of the telecommunications industry to fully competitive markets.

Vice-President Gore put it best at the Federal-State-Local Telecommunications Summit held earlier this year: "Competition is always better than monopoly. But monopoly power must never be confused with competition. Two enemies of competition are monopoly power and unwise government regulation. We must remember, after all, that the goal we seek is real competition. Not the illusion of competition; not the distant prospect of competition."

There is today, we believe, a broad, bipartisan consensus in favor of moving

telecommunications policy out of the courts and into the statute books so that Congress, representing the public, can craft the kind of comprehensive framework for competitive telecommunications that the nation deserves. The key test for any telecommunications reform measure is whether it helps the American people. To meet this test, it must be effective in opening all telecommunications markets to competition, including -- first and foremost -- currently monopolized markets. And it must ensure that monopolists cannot harm consumers and competition in the transition to competitive -- and then deregulated -- markets.

If we unleash monopolists rather than achieve real competition, American consumers and businesses will pay higher prices and have less choice. We would have less innovation and lower quality. We could lose our position of international leadership in telecommunications, and American businesses could lose a competitive edge. Real competition enables -- and must precede -- real deregulation.

The Administration shares your belief that an essential element to protecting and promoting competition is conditioning Bell Company entry into long distance and equipment manufacturing on a Department of Justice assessment of actual marketplace facts to ensure that such entry will not unravel a decade of progress in opening the long distance and telecommunications equipment markets to competition. Your new bill, Mr. Chairman, H.R. 1528, represents a valuable and important contribution to the ongoing discussion about telecommunications reform. It endorses the sound policy of requiring DOJ approval of Bell Company entry into long distance and equipment manufacturing. It also places a strict time limit on DOJ review. This approach was a critical aspect of legislation that enjoyed broad bipartisan support last year in this committee as well as the House Commerce Committee and that passed the entire House with more than 420 votes. It also received

strong bipartisan support last year from the Senate Commerce Committee.

I would like to devote the balance of my testimony to discussing why a DOJ decisionmaking role is essential to ensuring that telecommunications reform results in real competition, instead of unregulated monopoly.

The History of the Bell System Decree

It is appropriate to begin with some history, because the competition that we have today in long distance and equipment manufacturing is a relatively recent phenomenon, made possible by DOJ's landmark antitrust case against the Bell System. That case, as you know, was a completely nonpartisan undertaking. It began with an investigation that was initiated in 1969 during the Nixon Administration, accelerated with the filing of the case in 1974 in the Ford Administration and was pursued vigorously through the Carter and Reagan Administrations until it was settled in 1982 by my former law professor, William Baxter, President Reagan's Assistant Attorney General for Antitrust. That historic settlement resulted in the entry of the Modification of Final Judgment (or MFJ), which dismantled the Bell System's vertically integrated telephone monopoly.

The seven Regional Bell Operating Companies (Bell Companies) were created by the MFJ and each has a monopoly over local telephone service in its respective region. The MFJ restricts the Bell Companies from entering the long distance and equipment manufacturing markets. These line-of-business restrictions grew out of the central issue in the case: the ability of the local monopoly to impede competition in those other markets.

Before it was broken up, the Bell System used its control over local telephone service to maintain monopolies in long distance and equipment manufacturing. See United States v. AT&T,

552 F. Supp. 131, 162 (D.D.C. 1982), aff'd sub nom., Maryland v. United States, 486 U.S. 1001 (1983). Long after competition in long distance service and communications equipment became technologically and economically feasible, the Bell System abused its control of the local bottleneck to frustrate consumer choice and actual competition.

As Judge Harold Greene, who presided over the eleven month trial of the case and who continues to administer the terms of the MFJ, has explained, it was control of local exchange service

> that gave the Bell System its power over the competition. That control enabled the System to foreclose or impede interconnection to its network of lines of its long distance competitors and of equipment produced by its manufacturing rivals. It also made possible the subsidization of one activity with the profits achieved in another.

United States v. Western Elec. Co., 673 F. Supp. 525, 536 (D.D.C. 1987), aff'd in relevant part, 900 F.2d 283 (1990). In other words, control of the regulated local monopoly bottleneck gave the Bell System the incentive and the ability to discriminate against competitors in other markets in the terms, price and quality of interconnection with the local network and to shift costs from unregulated markets to the regulated local market, where they were passed on to local ratepayers.

Until the success of the Department's suit, regulation and litigation had not been effective in breaking through that local bottleneck. The Bell System proved itself adept at devising new ways to use the bottleneck to hurt competition in other markets more quickly than the courts and regulatory agencies could order solutions. Among other things, the Bell System used its monopoly profits to hire legions of lawyers to make sure that any proceeding that challenged any aspect of the monopoly was bogged down in endless proceedings. For example, the struggle to allow telephone customers the right to use their own equipment on their own premises, rather than being forced to purchase that equipment from the Bell System, spanned decades -- from the beginning of the Hush-a-Phone litigation in the 1940s to the break-up of the Bell System in 1984, which finally resulted in

open competition in customer premises equipment. See, e.g., United States v. AT&T, 552 F. Supp. at 162-63 (discussing a portion of this struggle -- the Bell System's use of "protective connecting arrangements" to discourage the use of competitors' equipment).

The Benefits of Competition After the MFJ

The MFJ addressed the problem of the local monopoly bottleneck and promoted competition in the long distance and equipment manufacturing markets by strictly separating the local monopoly from those markets. Because the local monopolies were barred from competing in the long distance and equipment manufacturing, they had significantly less incentive to impede competition in those markets. Competition in those two markets subsequently exploded. The result has been dramatically lower prices, better quality and more choice for American businesses and consumers.

MCI, Sprint and hundreds of smaller carriers vie with AT&T to provide long distance service to businesses and residences. The New York Times recently reported that in 1994 more than 25 million residential customers changed long-distance carriers -- spotlighting the MFJ's incredible success in bringing real choice to consumers. Residential long distance rates have fallen more than 50 percent since the break-up of the Bell System. The United States now has four fiber optic networks spanning the country, another by-product of competition. Incidentally, AT&T lagged behind its competitors in building a fiber optic network -- not surprising given that monopolists often are not the most innovative companies. These networks make possible all kinds of new services and enhance others, including the Internet. Similarly, businesses and consumers enjoy lower prices, more choice and better quality in communications equipment, as competition has eroded AT&T's

power in that market and forced it to compete for customers.

Because of lower prices and better quality, Americans are communicating with each other, by phone, fax and computer, more than ever before. We are closer to each other and in better touch with each other, for business and pleasure, because of the MFJ and its benefits.

The challenge facing the Nation today is to move forward by expanding competition without losing the hard-won benefits in the markets in which competition has flourished since the entry of the MFJ.

Allowing the Bell Companies into Long Distance

Section VIII(C) of the MFJ provides that any Bell Company may obtain a waiver of the line-of-business restriction as soon as it can show that there is no substantial possibility that it could use its monopoly power to impede competition in the market it seeks to enter. Judge Greene has granted over 250 such waivers. In fact, just last week, Judge Greene approved a waiver request made by all the Bell Companies and supported by the Department that will allow the Bell Companies to provide long distance services to their wireless customers. The core restrictions on the Bell Companies' entry into long distance for landline customers and into equipment manufacturing remain, however.

Ideally, we would like to remove these restrictions and allow the Bell Companies to be able to enter those markets, in keeping with our goal of a future in which every company is free to compete in every market for every customer. The trick, of course, is to ensure that removing the restrictions does not result in the re-creation of the old Bell System, this time on a regional rather than a national basis, complete with the incentive and the ability to impede competition in the long distance and manufacturing markets. Seven separate monopolies, each controlling one large region

of the United States, would be scant improvement for the cause of competition over a single national monopoly.

And there should be no doubt that the Bell Companies' bottleneck still exists. Customers simply have no choice for local service. In fact, in the vast majority of states, it is illegal for would-be competitors to offer a local dialtone. To be sure, some companies have made in-roads in offering alternative means of access to long distance carriers for certain business customers. And imaginable technological developments may eventually provide a basis for widespread competition in the future. But that competition is not here yet.

As long as this bottleneck exists, it is imperative that a judgment be made -- based on market facts -- whether Bell Company entry presents a substantial possibility of impeding competition in other markets, before such entry occurs. Such a judgment requires expertise in markets and competition.

The Need for a Department of Justice Role

The responsibility for making that judgment should be assigned to the Department of Justice. DOJ is the agency with competition expertise, the agency whose unwavering focus is on the protection and promotion of competition. It has effectively enforced the antitrust laws in the telecommunications industry on a completely nonpartisan basis throughout this century, including, of course, bringing the suit that dismantled the old Bell System.

This focus on competition is fundamentally different than the technical, regulatory focus of the FCC. The two agencies complement each other; they are not substitutes. We believe that it is important that the FCC apply a public interest test to Bell Company applications to enter long

distance and manufacturing. But such a test does not obviate the need for a market-based analysis by the Department of Justice.

In fact, wasteful duplication will arise if DOJ does not have a direct decisionmaking role, because requiring the FCC to filter the Department's antitrust analysis on such a critical issue would lead the FCC to duplicate expertise that DOJ already possesses and analysis already done by DOJ. As long as we agree that competition must be our guide, the most efficient, common-sense approach is to have a direct, decisionmaking role for the competition agency.

DOJ has supplemented its basic expertise in markets and competition with specific experience and expertise in telecommunications. Over the past decade, it has assisted Judge Greene in administering the MFJ -- through Republican and Democratic Administrations alike -- by reviewing over 350 requests for waivers under Section VIII(C), an average of about one every two weeks. Many of the most recent waiver requests have involved complex issues related to the competitive impact of the Bell Companies' provision of long distance services or equipment manufacturing.

In addition to reviewing requests for waivers, the Department has worked diligently with Bell Companies and other industry participants in searching for ways to remove the line-of-business restrictions consistent with protecting competition in markets that the Bell Companies seek to enter. Last month, the Department asked Judge Greene to modify the MFJ to permit a limited trial of interexchange service by Ameritech, one of the Bell Companies, in two LATAs in Ameritech's service area, once Ameritech faces actual local exchange competition and there are substantial opportunities for additional local exchange competition in those cities.

The proposal builds on the idea that one possible basis for lifting the line-of-business

restriction is the existence of local competition. It already has had an effect in promoting competition, as last Wednesday AT&T announced its plans to compete with Ameritech in providing local service in the trial area. The Department's motion was filed along with a stipulation by Ameritech and AT&T that the modification is in the public interest. The proposed modification represents an unprecedented consensus of industry participants, originating from a proposal by a Bell Company and now supported by major long distance competitors, local competitors, state regulators and consumer groups.

The proposed modification is the product of thousands of hours of staff work by the Department over the course of more than a year, including several rounds of public comment, as well as intensive discussions with Ameritech, state regulators, potential competitive local exchange carriers, long distance carriers and consumer groups. During that process, the Department deepened its already extensive expertise in telecommunications competition and its understanding of the competitive implications of Bell Company entry into long distance. Last week, we filed our brief in support of the motion, and we hope that Judge Greene will agree with us that the modification is in the public interest.

In short, the Department's experience in working with the MFJ uniquely positions it to assess what is actually happening in the market and whether there is a danger that entry by the Bell Companies could impede competition in other markets.

The only principled basis for concern about a DOJ role is whether it will inject unnecessary delay into the process of deregulation. This concern is utterly misplaced with regard to telecommunications legislation, as any DOJ review can be required to be completed within a specified period after filing of a Bell Company application -- as it is by your bill, Mr. Chairman, and

by Congressman Conyers' bill. Your bills take precisely the correct approach. DOJ would make its determination by a date certain; it is as simple as that. Congress can require it, and that is what these bills do.

The idea that DOJ review would cause unnecessary delay to Bell Company entry into long distance is a smokescreen that obscures the truth: DOJ review will not slow Bell Company entry into long distance unless such entry would be harmful to competition and thus undesirable for American consumers and businesses. Entry will be permitted as quickly as possible consistent with the appropriate entry test established by Congress.

No consideration of this question is complete, however, unless it also considers the long term savings in time and money of DOJ review. Bell Company entry that occurs without assurances that the entry presents no substantial possibility of impeding competition in long distance likely will result in the proliferation of complex, expensive antitrust and other suits under federal and state law, suits that will consume resources better spent on competing to offer American businesses and consumers better service and higher quality. Having DOJ apply a marketplace test as a condition to entry will avoid this waste.

Finally, a DOJ decisionmaking role has enjoyed overwhelming, bipartisan support in the past. It is an intelligent, effective approach to putting consideration of competitive facts and analysis at the center of our telecommunications reform efforts. It puts the interests of American consumers and businesses first.

Mr. Chairman, it is also critical that the test that DOJ applies be suited to achieving the fundamental purpose of DOJ review: protecting competition in long distance and equipment manufacturing, and we are deeply concerned that the test set forth in H.R. 1528 does not accomplish

that. But we are grateful for your leadership and for introducing this important legislation that constructively addresses a crucial policy issue in the telecommunications reform effort. We very much look forward to working cooperatively with you and this committee on inclusion of an appropriate test for allowing Bell Company entry into those markets as soon as such entry does not threaten competition.

Conclusion

I am proud that our country and this Congress have the courage to take on the tough issue of telecommunications reform. It took a lot of courage to break up the Bell System's vertical monopoly and allow competition into the markets for long distance and equipment manufacturing. But we did and as a result we now lead the world in telecommunications.

The easy thing, of course, would be for us stay where we are today. That, however, is not the American way. We welcome the challenge of striving toward a future of open telecommunications markets. But let us confront that challenge in the wisest way possible, and that is by making real competition our guide. A DOJ role in authorizing Bell Company entry into long distance and equipment manufacturing is essential to assuring the kind of telecommunications competition that can and will lead the Nation to prosperity in the 21st Century.