The AT&T Divestiture: Was it Necessary? Was It a Success?

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Little Empirical Evidence that Section 2 Decrees Have Improved Consumer Welfare

- **In reviews of major monopolization cases, Crandall (2001) and Crandall and Winston (2003) find little evidence of consumer benefit from structural remedies.**

- **Similar lack of benefits found by Crandall and Elzinga (2004) in examination of injunctive relief.**

- **No empirical evidence of increased output or lower prices following imposition of the decrees in 18 of 19 cases studied.**

- Robert W. Crandall (2001), "The Failure of Structural Remedies in Sherman Act Monopolization Cases," *Oregon Law Review*, Vol. 80, Spring, pp. 109-198.
- Robert W. Crandall and Clifford Winston (2003), "Does Antitrust Policy Improve Consumer Welfare? Assessing the Evidence, *Journal of Economic Perspectives,* Vol. 17, Fall, pp. 3-26.
- Robert W. Crandall and Kenneth G. Elzinga (2004), "Injunctive Relief in Sherman Act Monopolization Cases," in John B. Kirkwood (ed.), *Antitrust Law and Economics*, Vol. 21, pp. 277-344.

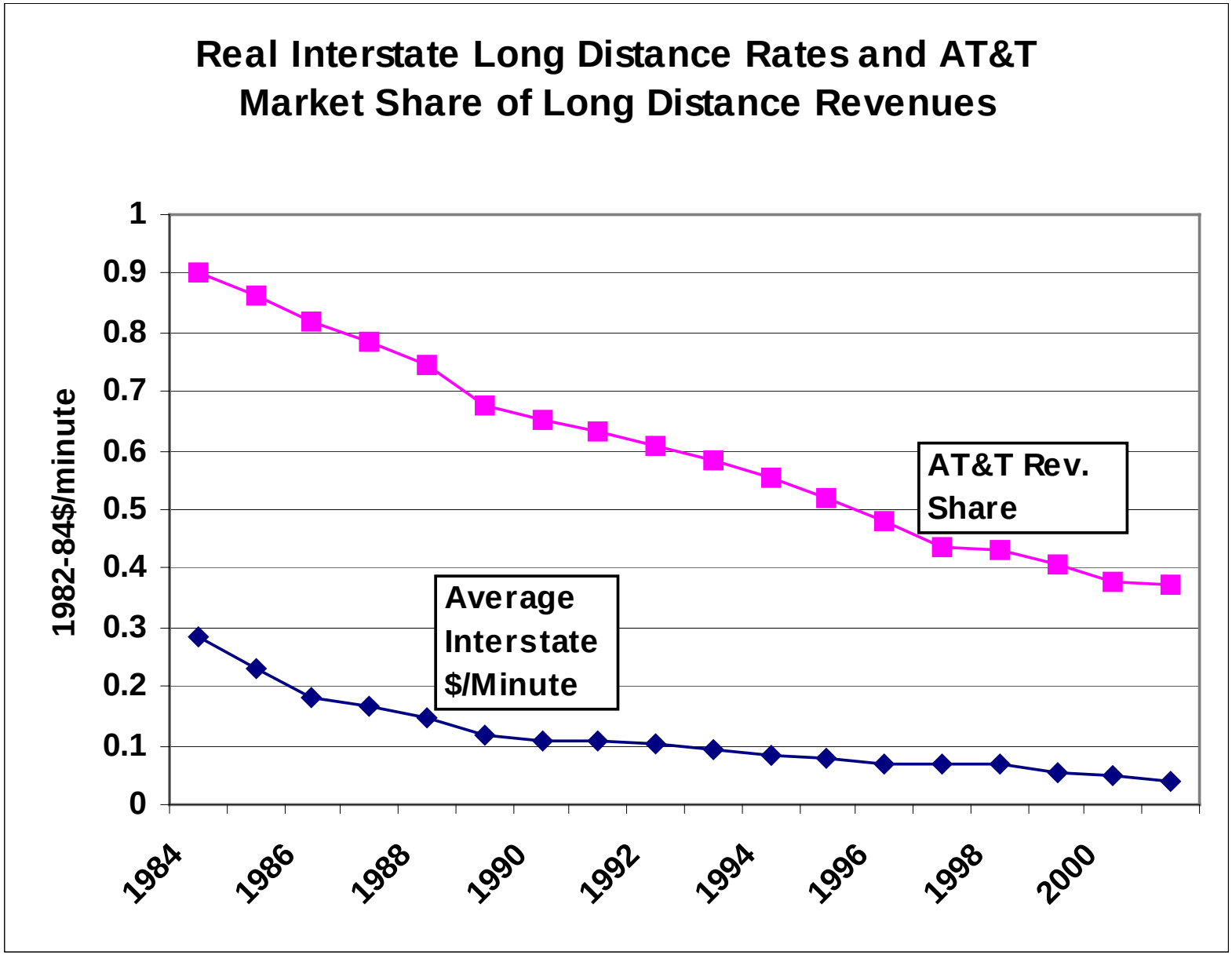
U.S. v. AT&T (1982) Is Generally Viewed as Most Successful of Major Section 2 Cases

- **The 1982 AT&T decree is the major (apparent) exception.**
- **The decree required vertical divestiture of Bell operating companies and equal-access obligations for divested local companies.**
- **Near-term result: long-distance services increased and U.S. long distance rates fell.**
- **But was increased long distance competition due to vertical divestiture?**

The Monopoly Bottleneck in U.S. v. AT&T

- **AT&T's local telephone monopolies accounted for 80-85% of access lines in 1982**
- **Section 2 case focused on use of these monopoly "bottlenecks" to extend monopoly into long-distance and terminal-equipment markets**
- **"Inverse Ramsey" regulatory pricing of local and long distance services created incentives for entry and for AT&T to attempt to block it.**
- **But was vertical divestiture, *i.e.*, *isolation of the network monopoly bottleneck*, necessary to obtain competitive results in long distance and terminal equipment?**

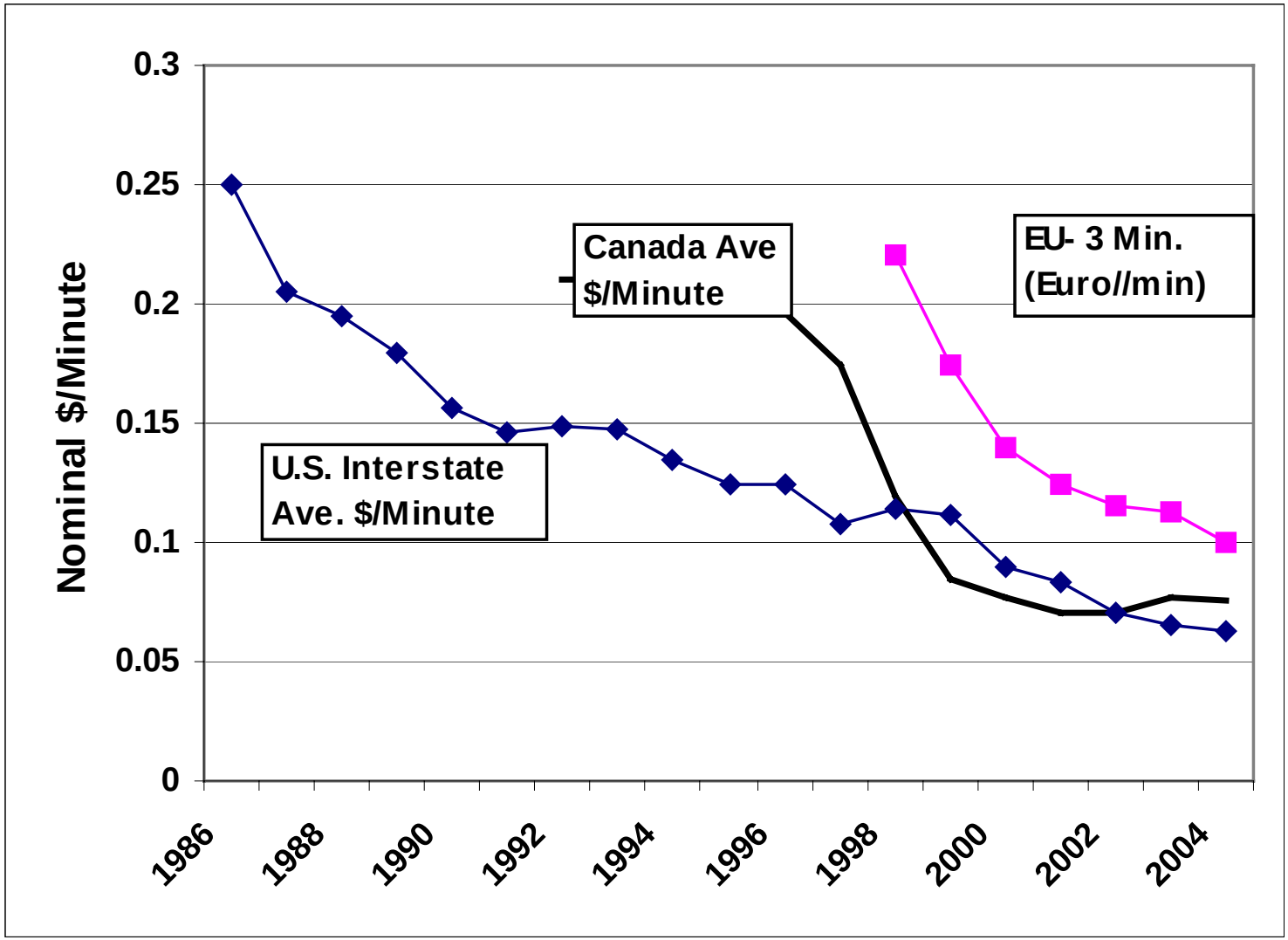
The Decree Appears to Have Worked



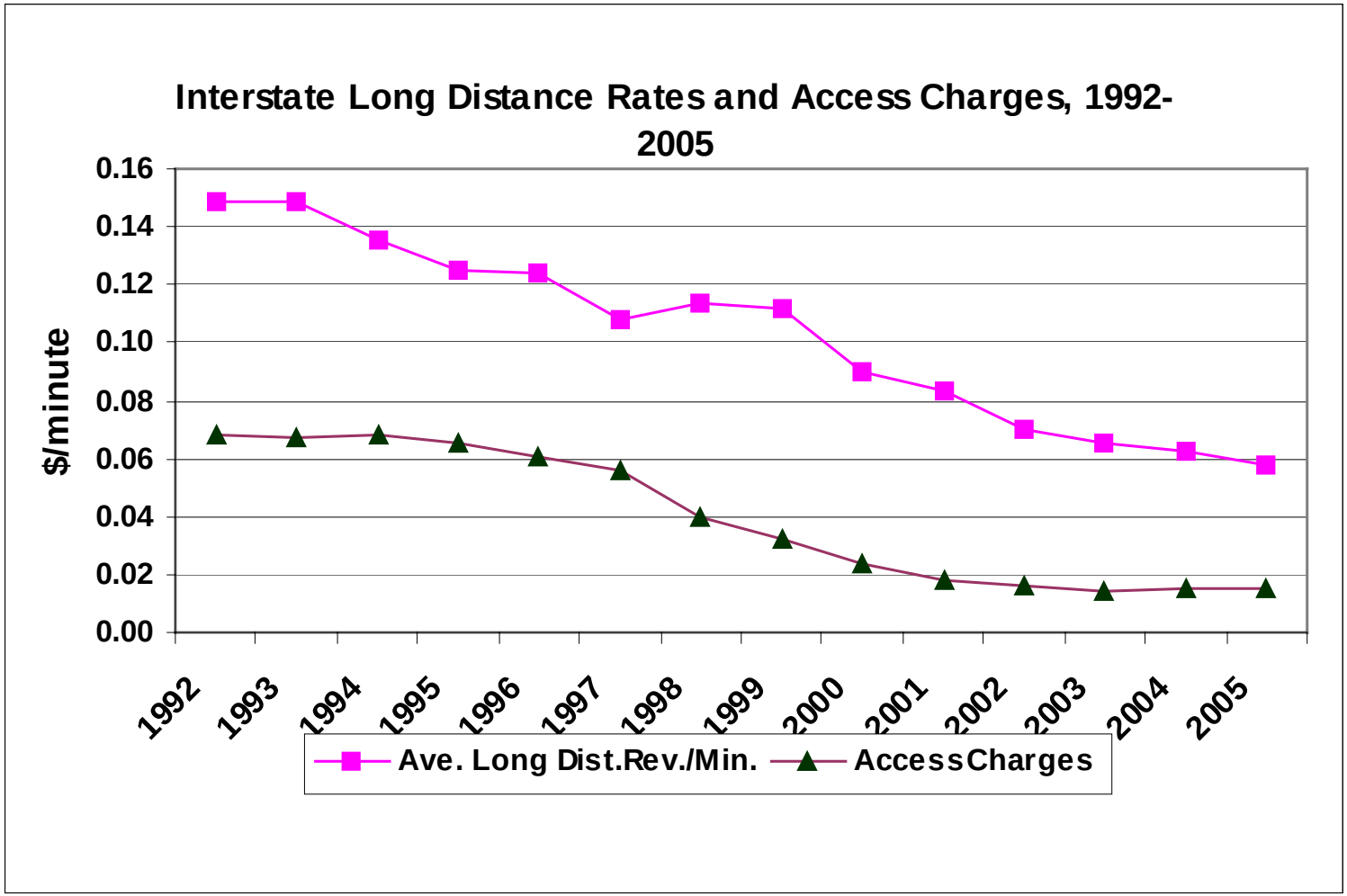
Despite the Apparent Success of AT&T Decree, No Other Country Pursued Vertical Divestiture

- **Following U.S. example, most countries simply required incumbents to originate and terminate entrants' calls ("equal access").**
- **Canada liberalized long distance services in 1992-93**
- **EU liberalized telecom services in 1998.**

Long Distance Rates Fell More Rapidly in EU and Canada without Divestiture



U.S. Long Distance Rates Fell Largely Because FCC Reduced Switched Access Rates



Competition in Long Distance Market Did Not Require "Isolating the Bottleneck" through Vertical Divestiture

- **Simple rule requiring origination and termination of *traffic over incumbents' switches* worked well in U.S. and elsewhere, but did not require isolation of the local bottleneck.**

- **Ironically, but for inefficient regulatory "universal service" pricing, entry into long distance may not have begun occurred in 1970s.**

- **AT&T divestiture exposed the folly of the FCC's pricing policy and forced it to reduce access charges after 1984.**

"Isolating the Bottleneck" Was Costly and Difficult to Administer

- **Econometric analysis of telecom productivity suggests that adjusting to decree cost $5 billion of lost productivity in 1984-85.**

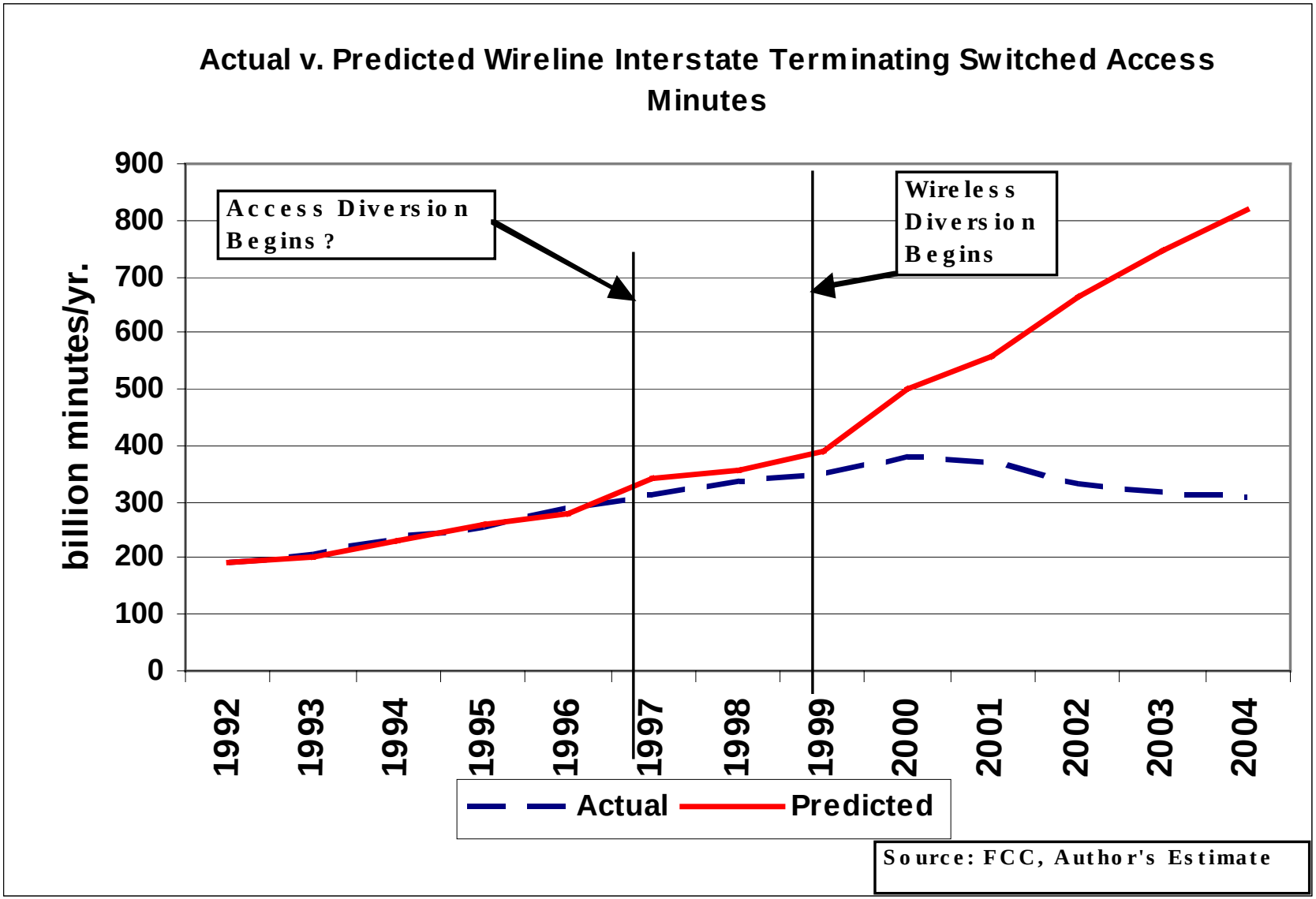
- **Ongoing waiver process for line-of-business restrictions is estimated to have cost another $1.4 billion.**

- **Changes in telecom markets and technology created increasing tensions and problems in enforcing the decree – leading to new legislation in 1996 that created further costs.**

FCC and AT&T Decree Failed to Anticipate the Role of Wireless Competition

- **FCC was allocating spectrum for "cellular" telephony in year DOJ brought the AT&T suit (1974).**
- **Regulatory battles over assigning licenses delayed launch of cellular service until 1983.**
- **FCC assigned only two cellular licenses in each market, but AT&T decree allowed incumbent Bell companies to keep one of them.**
- **Full competition in cellular service did not begin until 1995-6 as a result of Congressional mandate to auction new spectrum in effort to narrow the federal budget deficit.**

Wireless Provided the Greatest Impetus to U.S. Long Distance Competition



The "Price" for Ending the AT&T Decree Was the 1996 Telecommunications Act

- **1996 Act launched network sharing under an "impairment" standard, not the "essential facility" standard in antitrust.**
- **In other countries, sharing is confined to the local loop: acronym is LLU or "local loop unbundling."**
- **But use of LLU by entrants to offer standard, voice services was not profitable; most entrants failed**
- **FCC then expanded sharing criteria to "UNE-Platform"– allowing entrants to lease entire platform**
- **Broadband entrants were allowed to lease only the upper frequencies on local loops at very low prices through "line sharing"**

Eight Years of Network Sharing Under the 1996 Act Did Not Produce Meaningful Competition

- **Most entrants failed and disappeared, stranding at least $50 billion of investment.**
- **"Unbundling" for traditional voice services through UNE-Platform was largely a wealth transfer from incumbents to entrants –MCI and AT&T – and telemarketers.**
- **Broadband entrants did not develop viable businesses through network "line-sharing."**
- **UNE-Platform and line-sharing for broadband have now been abolished due to DC Circuit rulings, and the 1996 Act's experiment in forcing local competition is ending.**

After Twelve Years of the AT&T Decree and Nine Years under the 1996 Act, Telecom Is Vertically Integrated Once Again

- **Verizon bought MCI, and SBC bought AT&T in 2005.**
- **Independent long distance companies could not survive in the new era of wireless and VoIP competition; non-integrated local entrants failed in droves.**
- **Twenty-one years of court- or FCC-enforced vertical separation did not create meaningful local competition.**
- **Technical change, not antitrust, eroded the wireline "bottleneck."**

The Irrelevance of the Bottleneck Today

- **Cellular wireless, cable television and even fixed wireless platforms provide powerful competition to fixed-wire telephone companies today.**

- **Wireless and Internet telephony not only take the "monopoly" out of the "monopoly bottleneck," but threaten to render the network obsolete.**

- **ILECs must now invest enormous sums in their fixed-wire telephone networks if they are to be able to compete with new players and the cable companies.**

- **Lesson for antitrust and telecom policy: changes in markets and technology have eliminated the need to worry about fixed-wire bottlenecks.**

The Lessons Learned

- **AT&T decree may have "worked" at first, but a more limited decree would have worked just as well and at a much lower social cost.**
- **The decree was in force either directly or through its successor – the 1996 Telecom Act –for too long because it created political clients, the entrants and the long distance carriers.**
- **DOJ's target should have been the FCC, not AT&T, because the FCC failed to establish sensible interconnection policies and delayed wireless competition for more than a decade.**