Telecommunications Act of 1996: A Paradigm of Deregulation?

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**Agenda**

- Public Policy Overview
- Pre-Telecommunications Act
- Telecommunications Act of 1996
- Conclusion

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**Public Policy Overview**

- Goals
- Instruments
- Obstacles

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**Public Policy: Instruments**

- Regulation/Social Control
  - Rate of Return Regulation (ROR)
    - Benchmark (Yardstick)
    - Incentive Regulation
    - No Regulation
- Anti-trust/Monopoly Policy

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**Incentive/Price Caps Regulation**

- Competitive Entry Encouraged
- Limit on the Incumbent’s Prices
- Productivity Factor
Role of Competition

- Allocation of Resources
- Incentive for Efficiency
- Threat of Entry Discipline

Role of Competition

- Incentive for Efficiency
  - Prices $\Rightarrow$ costs
  - Pressure to reduce costs
  - Selection of more efficient firms
  - Promote innovation
  - Diminish regulatory imperfections

Additional Motivation for Competition

- Product Differentiation
- Cost Differences
- Benchmark (Yardstick) Competition

Competitive Policy Overview

- Institutional Advantage (Incumbent)
- Technology Advantage (Incumbent)
- Regulatory/Competitive Synergy


Competitive Policy Overview

- Institutional Advantage (Incumbent)
  - Institutionalized cross-subsidies
  - Name recognition
  - Established customer-base

Competitive Policy Overview

- Institutional Advantage
- Technology Advantage (Incumbent)
  - Numbering
  - Metering?
  - High customer switching costs
Competitive Policy Overview

- Institutional Advantage
- Technology Advantage
- Regulatory/Competitive Synergy
  - Competition substitutes for regulation
  - Competition complements regulation
  - Regulation can distort competition

Pre-Telecommunications Act of 1996

- Telephone Companies
  - MFJ: Exchange/Long Distance Separated
  - MFJ: Horizontal Divestiture (Benchmark)
  - MFJ: Manufacturing Restrictions
  - No Telco/Cable Cross-Ownership

- Wireless
  - Preference given to Telco's
  - Two Wireless Providers

- Broadcasting
  - Protection from Cable (Limited)
  - Local Content
  - Ownership restrictions
  - No rate regulation

- Cable
  - Local franchises
  - Limited price control
  - Carriage requirements
Pre-Telecommunications Act of 1996
- Telephone Companies
- Wireless
- Broadcasting
- Cable
- Computer Industry
  - Unregulated

Telecommunications Act: Background
- Amendment to the 1934 Act
- Rural Dominance
- Budget Limitations on Congress

Telecommunications Act of 1996
- Universal Service Maintained
- Cross-Ownership Removed
- Manufacturing Restrictions Removed
- Local/Toll Restrictions Removed
- Broadcast Industry Open
- Computer Industry Status Quo

Competitive Policy Assessment
- Competitive Entry
- Price Discrimination
- Cross-Subsidies
- Universal Service Obligations

Competitive Entry: Positive?
- Cross-Ownership Removed
- Local/Toll Restrictions Removed

Cross-Subsidies
- No Market Test
- Inefficient
- Avoids Competition
- Anti-Competitive
Universal Service

- Inefficient
  - Not Marginal Subscribers
  - Not Targeted
  - Not Desired
- Incidence Not Addressed
- Companies Subsidized

Incidence

- Service Subsidy
- Demand Patterns
- User Subsidy

Public Policy Overview

- "...unleashing monopolies before real competition could mean..."
  - Higher prices for consumers
  - Hinder competition.
- Transitional safeguards needed

Agenda

- Public Policy Overview
- Pre-Telecommunications Act
- Interconnection Pricing
  - Problem
  - Goals
  - Solution?

Intermediate Pricing Problem

- Essential/Bottleneck Facility
- Natural Monopoly
- Input to Competitive Service
- => Interconnection Price Critical

Intermediate Pricing Applicability

- Wireless Competition
- Exchange/Toll Competition
Intermediate Prices Goals

- Encourage Entry
  - Avoid Inefficient Bypass
  - Avoid Network Duplication
  - Incentive to Develop & Maintain Network
- Promote Competitive Market Transition


Interconnection Policy

- Pricing Standard (Sec. 252)
  - Based on Costs
  - Nondiscriminatory
  - Reasonable Profit
- FCC's NPRM 96-98
  - Determines Policy
  - Usurps Cable/IXC/States/LECs

Merger Policy Impact

- Horizontal Mergers Allowed
  
Merger Policy Impact

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  - Eliminates Competition --
  
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  - SWB/Pacific Telesis (7 becomes 6)

Merger Policy Impact

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  - Eliminates Competition --
  - SBC/Pacific Telesis (7 becomes 6)
  - NYNEX/Bell Atlantic (6 becomes 5)
**Merger Policy Impact**

- **Horizontal Mergers Allowed**
  - Eliminates Competition --
    - SBC/Pacific Telesis (7 becomes 6)
    - NYNEX/Bell Atlantic (6 becomes 5)
    - ATT/SBC (eliminates potential competition)
  - Removed Benchmark Competition
  - Economies of Scale?

- **Long Distance Competition**
  - Premature Entry of LEC?

- **Rural Issues**
  - Carriers' Waiver (2 % rule)
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  - Interconnection exemption
- Rural Competitive Entry Restricted
- Rural <= Urban Rates

- Carriers' Waiver (2 % rule)
- Rural Competitive Entry Restricted
  - Rural <= Urban Rates
  - Discourage Expansion
  - Competitive Response Limited
Video Policy

- No FCC Rate Review of Cable
- Redefinition of Video Competition
- Common Carriage VDT
- LEC’s Video Rates?
- No Separate Subsidiary, Programming

Policy Assessment: Positive

- Interconnection Required
Policy Assessment: Positive

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  - Agreements mandated

Policy Assessment: Positive

- Interconnection Required
  - Agreements mandated
  - Non-pricing rules established

Policy Assessment: Positive

- Interconnection Required
  - Entry Policy Encouraged (in part)
    - Cross-ownership

Policy Assessment: Positive

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    - Cross-ownership
    - Exchange/toll entry

Policy Assessment: Positive

- Interconnection Required
  - Entry Policy Encouraged (in part)
    - Cross-ownership
    - Exchange/toll entry
    - Horizontal/vertical mergers

Policy Assessment: Negative

- Interconnection Policy Incomplete
  - Price rules indeterminate
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  - (Economic) principle undefined

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Policy Assessment: Negative

- Interconnection Policy Incomplete
- Entry Policy Distorted
- Price Policy Distorted
  - Universal service obligations

Policy Assessment: Negative

- Interconnection Policy Incomplete
- Entry Policy Distorted
- Price Policy Distorted
  - Universal service obligations
  - Cross-subsidies (schools/institutions)