Chapter 7

Viewing divestment from afar

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No country has gone so far, or so quickly, in restructuring its telecommunications sector as has the United States. Indeed, the recent history of telecommunications policy in the United States is at once awe-inspiring, on account of the scale of the changes wrought by divestiture, and bewildering, because the divestiture agreement was contested before the ink was dry. These developments should not be treated as purely domestic issues since their effects are being felt, albeit unevenly, throughout the world. Although many countries have embarked on regulatory reform, we argue here that the United States experience is unique. This is because the US has witnessed not so much regulatory reform as regulatory turbulence, and this can be attributed to the coexistence of competing centers of regulatory power, itself the product of an inordinately diffuse policymaking structure - what we call its open network policy regime. We use the term 'regulatory turbulence' to refer not just to the celebrated turf fights within government, but to a situation in which radically different regulatory signals are being transmitted to the domestic telecommunications community.

In this chapter we examine the political dilemmas facing United States policy at home, where the main challenge is to devise a coherent and sustainable telecommunications policy, and abroad, where the United States faces the formidable political challenge of creating a level playing field in the international telecommunications arena. We focus first on domestic policy in the post-divestiture era and, second, on United States efforts to overcome regulatory asymmetry in the world market.

Instead of subsuming all regulatory change under the banner of deregulation, it may be more helpful to speak of parallel regimes of regulation at the federal level, the traditional regime of the FCC, and the new Court regime of Judge Greene. Conflict between these two regimes

was not envisaged by the authors of the original divestiture script, that is, the Department of Justice and AT&T. If anything, the Department of Justice saw divestiture as the ultimate form of deregulation in that it would be a substitute for traditional regulation. For the Department of Justice the quintessential purpose of the divestiture was to draw a bright line between the monopoly and competitive segments of the telecommunications industry by vesting each in separately owned companies. In this scenario the *Modification of Final Judgment* (MFJ) should have removed 'the structural problems that have given rise to the controversies between the United States and AT&T over the last three decades.'[1]

As we know, the actual divestiture signally failed to deliver any such line. That it failed to do so provides a graphic illustration of the scope for policy mutation and this, in turn, speaks much about the fragmented policymaking process. One of the main reasons why the Department of Justice's vision failed to materialize was that the original agreement that it struck with AT&T made dubious assumptions about the post-divestiture behavior of parties that had not been privy to the agreement. Quite simply, these other parties refused to 'play the roles assigned to them.'[2] The main delinquents here were the Court and the Regional Bell Operating Companies (RBOCs). Concerned about the RBOCs' ability to sustain universal service, the Court tabled ten amendments to the original *Modified Final Judgment* (MFJ), the two most important being the decision to give the RBOCs the lucrative (and competitive) Yellow Pages business and the decision to waive the restrictions on the RBOCs upon a showing that they could not use their monopoly power to impede competition in the market(s) they sought to enter. Thus the MFJ had already breached the bright line about which the Department of Justice cared so much.

As regards the RBOCs, they were to confound all their critics. Animated by the desire to shed their pedestrian image, they exploited the Court's waiver mechanism to the full; so much so that even before the first triennial review of the MFJ, the Court had sanctioned well over 100 waiver requests, allowing the RBOCs into an array of businesses. Indeed, this waiver process encouraged the RBOCs to set their sights on markets that were forbidden to them under the terms of the MFJ, namely, interexchange, manufacturing, and information services. Before we examine this threat to the MFJ, it is worth elaborating on the respective regulatory policies of the FCC and the Court.

The centerpiece of the FCC's regulatory policies, all of which are geared to deregulation, is its *Computer III* decision, adopted in May

1986. Put simply, *Computer III* was a response to the problems associated with the FCC's previous *Computer II* ruling, which had distinguished between (regulated) basic and (unregulated) enhanced services. In an effort to ensure that carriers did not subsidize their unregulated ventures from regulated earnings, the FCC required structurally separate subsidiaries if carriers wished to offer enhanced services. However, in response to strong pressure from AT&T and the RBOCs, who argued that separate subsidiaries entailed excessive costs, the FCC dropped this requirement in favor of the nonstructural safeguards of *Computer III*.

Without a doubt the key regulatory mechanism in the FCC's current policy arsenal is Open Network Architecture (ONA). An extremely ambitious concept, ONA involves the overall design of a carrier's basic regulated network to permit all users, including competing enhanced service providers, to interconnect with basic network functions on an equal access basis. Although ONA is very much the jewel in the FCC's regulatory crown it is still at a primitive stage of development. Indeed, judging by the criticism that greeted the RBOCs' first ONA plans, this regulatory concept will need all the political support it can muster.

Among the main criticisms made were that the RBOCs have simply put an ONA gloss on features and functions that were already available; that they have not sufficiently unbundled these basic service elements; that ONA offerings vary from one RBOC to another; and that some of the RBOCs were engaging in strategic pricing of their ONA offerings.[3] Although disappointed by this adverse reaction, the FCC still approved the RBOCs' plans, albeit with certain caveats, like asking for more uniformity with respect to terminology, technical characteristics, and deployment of ONA services.

Phenomenally complex issues, and deeply antagonistic interests, are involved in this ONA challenge. For example, how far should local networks be unbundled when other forces, like ISDN, appear to be pushing in the direction of greater integration? Who will decide which tradeoffs are to be made between uniformity and diversity in ONA offerings across the country? Then there is the highly sensitive issue of regulatory jurisdiction as between federal and state authorities, the latter being deeply suspicious of the FCC's motives in this field. Indeed, the New York, Californian, and Michigan state commissions have jointly challenged the FCC's *Computer III* decision in the Court of Appeals, in which they assert state jurisdiction over intrastate ONA services, including the right to retain or remove structural separations on the RBOCs!

ONA is turning into a political challenge, not just for the RBOCs, who see it as a quid pro quo for getting into the forbidden information services market, but for the entire United States telecommunications system because no other country has placed such a high premium on the parts over the whole, on competition over coordination. ONA clearly raises a whole series of unanswered questions, and, in doing so, it creates a new wave of turbulence and uncertainty for government, industry, and users. If ONA is ever going to be successful, there will have to be a much greater degree of cooperation between federal and state authorities and between the RBOCs, enhanced service vendors, and users.[4]

The ONA cause has also suffered from the fact that the FCC lacks credibility as a regulatory enforcement agency because the Office of the Chairman became so politicized during the tenure of Mark Fowler, who was associated with a policy of deregulation at all costs. This credibility problem, which was severely exacerbated by the FCC's decision to repeal the fairness doctrine in broadcasting, helps to explain why potentially sound new policies, like the proposal to substitute price cap for rate of return regulation, command so little political support. Alongside the FCC the Court has emerged as a powerful new regulatory force. In several important rulings Judge Greene has earned himself a reputation as a robust and politically subtle jurist. Although opponents seek to disparage Greene as an inflexible regulatory czar, it is worth recalling that it was his decision to insert the famous section VIII(C) amendment into the divestiture agreement, without which the RBOCs would be operating under a much more draconian set of MFJ restrictions. This amendment covered the waiver mechanism to which we have already referred and allowed for the MFJ restrictions to be reviewed every three years by the Department of Justice and the Court.

The tension inherent in this system of parallel regulation first surfaced at the time of the triennial review. In its triennial report to the Court, the Department of Justice, which by this time had undergone a political metamorphosis, wanted to dismantle most of the MFJ restrictions. These, it argued, had been rendered futile by the growth of competition and the advance of technological alternatives. The Court, however, came to a radically different conclusion: In a major rebuff to the RBOC camp, Greene refused to make any fundamental change in the MFJ because, he argued, there was no evidence that the RBOCs' monopoly over the local network had been eroded since divestiture. Whereas the Department of Justice had expressed confidence in the FCC's regulatory capacity, Greene questioned its ability to control

anti-competitive abuse, citing as evidence inadequate FCC resources and the weakening of regulatory safeguards, like the dropping of separate subsidiaries. The only concession to the RBOCs was Greene's decision to dilute the ban on information services by allowing the RBOCs to engage in the transmission (but not the content) side of information services. So while the FCC regime allows the RBOCs to participate fully in information, or enhanced services, the Court regime only allows them to play a gateway role.

Further conflict occurred when the Court delivered a ruling on the meaning of 'manufacture' in the divestiture agreement. AT&T had asked Greene to clarify what the term included, because a similar request to the Department of Justice had not been acted on in nearly two years. In the face of intense pressure from the RBOC camp, which wanted a narrow definition, Greene defined the term broadly, saying that the divestiture agreement intended 'to bar the Regional Companies from the entire manufacturing process, including design, development, and fabrication.'[5]

This manufacturing ruling was particularly notable for the way in which the Court assailed the Department of Justice and the FCC. Greene chided the former for its failure to enforce the ban, but he saved his main ire for Dennis Patrick, the FCC chairman, who, said Greene, 'took the unusual, if not unprecedented, step for the head of a federal regulatory agency, of exhorting those whom the agency regulates to refuse to comply with orders duly issued by this Court.'[6] Here Greene was counter-attacking. Earlier in the year Patrick had accused the Court of having abused its position and of having preempted the authority of Congress and the FCC, and he expressed surprise that the RBOCs were acquiescing in the 'ongoing administration of the MFJ.'[7] These are not harmless turf fights. What we have here is the spectacle of two centers of regulatory power locked in a fundamental conflict, each giving the industry radically different signals.

As things stand, government and industry are both internally divided over the future direction of domestic telecommunications policy. On one side a powerful anti-MFJ coalition has emerged, consisting of the RBOCs, the Department of Justice, the FCC, and the National Telecommunications and Information Administration (NTIA). The NTIA seems to have assumed the role of chief political choreographer in this coalition, partly because it is responsible for coordinating telecommunications policy in the Executive. Indeed, the NTIA was the first federal agency to question the wisdom of the divestiture agreement because it sees the MFJ as warehousing half the nation's telecommunications

industry at a time when the United States position in high technology is under threat. This coalition has launched several legislative initiatives to get all or parts of the MFJ rescinded. For example, the so-called Dole Bill, which was an unsuccessful attempt to transfer control of the MFJ from the Court to the FCC, was actually prepared by the agencies mentioned above. One of the main reasons why the Dole Bill was stopped in its tracks was the enormously successful opposition campaign waged by the No-Name coalition. This coalition, a pro-MFJ lobbying force, was specifically set up to counter the Dole Bill, and it has stayed together to protect the integrity of the MFJ. The No-Name coalition represents the widest cross-section of corporate interests ever formed in the United States telecommunications sector, including strange bedfellows like AT&T and MCI, trade associations like ADAPSO, and user groups like the ICA. In many ways this is an unholy alliance, the one common denominator being a shared fear that the RBOCs represent a threat if the MFJ is ever rescinded. Not surprisingly this coalition preaches virtues of antitrust, its motto being 'Remember the Sherman Act.'

These contending interests are the main forces shaping United States regulatory policy. Resonant themes are being tapped on both sides. The pro-MFJ camp appeals to notions of fair competition, level playing fields, and to an antitrust tradition which the Reagan Administration tried its best to bury. The RBOC camp, on the other hand, appeals to notions of free competition and deregulation in an attempt to portray the MFJ as an obstacle to a better trade balance and a threat to intelligent (public) networks. The Reagan Administration tried, but failed, to resolve this contest in favor of the RBOCs. Its successor may find that the real challenge lies not just in composing a new telecommunications policy, but in getting the various branches of government to play the same tune.

If regulatory turbulence is the main feature of the domestic telecommunications environment, then regulatory asymmetry is what characterizes the international level. As the first country to dismantle its regulatory barriers to entry, the United States unwittingly exposed itself to what we might call the burden of deregulation in one country. Notwithstanding the benefits that have flowed from deregulation and divestiture, this experience has not been without its costs, many of which can be traced back to regulatory asymmetry (i.e., to the fact that the US was deregulating in a highly regulated, and therefore largely closed, world telecommunications market).

The conventional wisdom in Western Europe seems to be that deregulation and divestiture were the product of strategic decisions from governments bent on unleashing American firms onto the world market. However, there are two problems with this conception. On a factual level, deregulation and divestiture were prosecuted as matters of domestic policy with little or no reference to the international trade dimension. On a more theoretical level, such a contention exaggerates the degree to which concerted action is possible within government itself or between government and industry. Let us be clear: We are not suggesting that the United States government is not trying to play a more forceful role in support of its multinationals abroad, only that it faces great problems doing so given the extraordinarily diffuse United States political system. In short, the US capacity for cohesiveness is low, especially in telecommunications, where at least two dozen agencies could claim to be involved in the development and implementation of policy. However, we maintain that enormous efforts are underway to secure greater cohesiveness within government and between government and industry; in each case the aim is to export as much of the United States regulatory model as possible. It is in this way that the United States hopes to be able to remove, or at least ease, the burden of deregulation in one country.

The dangers of pursuing regulatory reform without any reference to the external trade dimension were evident at the time, and no one did more to draw attention to these dangers than Senator John Danforth. Backed by the equipment industry, Danforth bemoaned the fact that divestiture and deregulation had been driven by purely domestic considerations. In the context of introducing a new telecommunications bill (S. 2618), he said:

> In this interdependent world we cannot afford to make decisions in a vacuum. We cannot afford to let trade be the stepchild of domestic policy decisions. . . . In trade terms, the break-up of AT&T is more than just the unilateral elimination of a major barrier to imports. It also means that on January 1, 1984, we may have discarded the only trade concession that could ever be effective negotiating leverage for the US to gain reciprocal market access for our telecommunications exports. It is hard to imagine any other US concession providing as much incentive for foreign telecommunications manufacturers and their governments to really open up domestic markets.[8]

It was not that the Administration was wholly unaware of the potentially adverse trade effects of divestiture: It would be nearer the truth to say that it underestimated how quickly the trade deficit would subsequently mount, for two reasons. First, the Administration did not fully appreciate the negative effect on United States exports of a strong dollar. Second, it was too optimistic about the prospects for removing regulatory barriers to entry in overseas markets.

Whatever the precise reasons, the trade front has been a bounty for the prophets of doom. The telecommunications equipment trade balance has progressively deteriorated from a surplus in 1980 to a deficit of $2.7 billion in 1988, while in the same period the trade deficit increased from $36.2 billion to over $171 billion. Accustomed for so long to being the global leader in high technology industry (i.e., R&D-intensive sectors), the authorities were shaken by the fact that this high technology trade balance was also slipping badly.[9] We should not forget, however, that this dismal trade picture refers not to the declining fortunes of firms but, rather, to the decline of the United States as a place of production.[10] It seems that a significant part of the high technology trade imbalance can be attributed to American firms making greater use of their Southeast Asian subsidiaries, where labor costs are much lower than in the United States. Hence AT&T is one of the top 'Taiwanese' exporters in telecommunications and IBM is the largest 'Japanese' exporter in computers. The deepening trade deficit created a more fertile ideological climate for those who wished to fashion a domestic regulatory policy that was more compatible with United States trade interests. The NTIA has been the most vociferous advocate of such a change in policy, arguing that:

> the US today is engaged in the functional equivalent of economic warfare with certain of its traditional trading partners, particularly in the critical telecommunications and computer, or information industry sector. By virtue of self-inflicted wounds, Government actions proven imprudent in hindsight, and persistent foreign restrictions on US-based competition, there is a significant chance America's future in this 'sunrise,' high-tech sector will be eclipsed if current policies are not changed.[11]

If the trade deficit created a new climate, the event that persuaded the Administration to step up its offensive against foreign telecom regimes was the CGCT affair. AT&T had set a high premium on acquiring CGCT, a publicly owned French telecom firm, and it seemed well poised to do so because it had received reassuring signals to this effect

from France Telecom. The contest turned into a major political dispute, though, when the Bonn government began lobbying in favor of Siemens, the German national champion. In an attempt to placate American and German feelings, the French government eventually decided to allow an Ericsson-dominated alliance to acquire CGCT in April 1987. The CGCT affair convinced the Administration that telecommunications had moved into the realm of high politics.

The CGCT affair had two other effects on the Administration. First, it encouraged the formation of the Breakfast Club, an informal gathering of the heads of all agencies with a major stake in telecommunications policy formation. This was yet another attempt to achieve greater interagency cohesiveness, the main aim of which was to try to present a common face to the external world on international policy issues. The fact that this club was thought to be necessary speaks volumes for the inefficacy of the Senior Interagency Group on International Communications and Information Policy (SIG), which was set up in 1984 with the aim of bringing greater coherence to United States policy formation in this area.

Second, the CGCT affair encouraged the FCC to try to expand its own authority in the field of international trade regulation. The FCC's ambitions in this field had been fueled by the new mood in Congress, which seemed to indicate growing support for sector-specific trade legislation like the Telecommunications Trade Act of 1985, which was introduced by Senator John Danforth.

It is worth dwelling on the FCC's initiative because it illustrates the potential for jurisdictional fights within the government and because it sheds light on how difficult it is for industry to agree to a common political platform. The clearest indication of the FCC's ambitions came in December 1986, when it voted to issue a notice of inquiry and proposed rulemaking with respect to what action it should take to persuade foreign governments to open their markets to United States firms.[12] Admitting that its authority in the trade arena was at best ambiguous, the FCC nevertheless suggested that it should develop an international model that would represent an ideal to be sought in international telecommunications and a benchmark against which national and international policies and practices may be compared. The Commission also invited comment as to whether it could or should vary access to the United States market for foreign firms depending on the degree to which their countries of origin were open to US firms. Among the proposed rule changes the FCC wanted to increase reporting require-

ments, the aim of which was to gain a better picture of foreign penetration of the United States equipment and services market, and this was eventually introduced in February 1988.

In all, forty-nine parties filed comments, and the vast majority of them objected to the FCC's proposal to restrict access to the United States market. The RBOCs, for example, saw the proposal as a threat to their freedom to procure equipment from wherever they wished, while companies with extensive overseas interests feared a protectionist backlash from foreign governments. Many other parties, prominent among which were federal agencies, claimed that the FCC did not (and should not) have the authority to take unilateral initiatives based on trade factors. What concerned the traditional trade players, like the United States Trade Representative (USTR), the State Department, and the Commerce Department, was that the FCC lacked the diplomatic skills necessary in international negotiations and that another player would make it more difficult to achieve interagency cohesiveness. The traditional trade players were also defending their political turf against the claims of an aspiring new player.

This was not the first time that the FCC had tried to create a more prominent role for itself in the international arena. For example, a major interagency dispute broke out in 1985, when the United States Administration decided to initiate a Market Access Fact Finding (MAFF) exercise, consisting of bilateral talks with countries whose telecom markets were thought to be closed to United States firms. Although the Department of Commerce led the first of these MAFF talks (with Germany in 1985), a battle arose between the FCC, Commerce, and USTR over which agency should assume the lead with other countries: The FCC insisted that its technical expertise made it the natural chairman; while Commerce, itself divided between the NTIA and the ITA, argued in favor of its wider expertise in trade negotiations. Instead of resolving the issue, however, an informal deal was struck whereby each agency assumed the lead role with different countries, for example, USTR with the European Community itself, NTIA with Spain and South Korea, ITA with Sweden and Italy, FCC with the UK and France.

This arrangement did nothing to resolve tensions in the system. Although these tensions undoubtedly reflect the jurisdictional wars so common in the American system, they reflect much more than this. At bottom these agencies have different political priorities and, as often as not, the main contrast is between the FCC and the State Department. With its narrow sectoral remit the FCC can afford to adopt a more aggressive line in international negotiations on telecommunications;

indeed, the FCC has been one of the main advocates of sectoral reciprocity in telecom trade talks, a concept to which the Reagan Administration was very much opposed. Being the principal foreign policy advisor to the President, the State Department occupies a radically different position, being obliged to take a far more panoramic view, and, not infrequently, the narrow material interest of the nation is subordinated to diplomatic or military exigencies. For example, State appears to have had a moderating influence on the Reagan Administration's attitude to telecom talks with Germany because it did not want to antagonize the Germans prior to sensitive negotiations in the North Atlantic Treaty Organization.

Not surprisingly, the telecommunications industry has been deeply critical of the fragmentation of political authority in this sector, a problem compounded by the lack of an institutional memory brought about because of the high turnover of expert staff within government. In such a fragmented political system there is a powerful incentive for corporations to forge coalitions through which to educate government as to the corporate agenda. Perhaps the most effective of the many coalitions in United States telecommunications is the US Council for International Business, which represents over 300 of the largest American-based corporations in and beyond telecommunications. The Council's telecommunications committee consists of companies that use, manufacture, and provide equipment and services. The leading firms on this committee are drawn from IBM, Citibank, Nynex, and GTE, each of which represents a specific segment of the telecommunications industry. The Council is the US affiliate of the International Chamber of Commerce and the Business and Industry Advisory Committee to the Organization for Economic Cooperation and Development (OECD). It can justly claim to have driven the telecom agendas of both these international organizations.

Because the Council's telecommunications committee is so broad-based, however, it has mirrored the conflicts in the wider United States telecommunications industry as to how best to respond to regulatory asymmetry. For example, there is a good deal of conflict about whether to proceed multilaterally or bilaterally through sector-specific initiatives like MAFF. This debate has divided the Council itself, especially between the equipment suppliers and the rest; the former favored sector-specific action in the Trade Bill, although many users and service vendors feared that their external interests would suffer if the equipment firms' interests were pushed too aggressively. The Council has played an important role in at least two ways: first, in bringing together the

disparate segments of the industry so each has become more alive to the other's interests; second, in helping to forge a greater degree of cohesiveness between government and industry. The most tangible sign of this trend toward unity is the Telecommunications Trade Task Force that was formed under the auspices of the United States Chamber of Commerce near the end of 1987. The industry side of this task force is carefully balanced to reflect the main segments of the industry - users, equipment suppliers, and service providers – and the membership base includes individual companies (like AT&T, IBM, Nynex, Control Data) and trade associations (like ICA, ADAPSO, the United States Council for International Business). On the government side the main agencies involved are those with a major responsibility in the trade policy field, namely, USTR, Commerce, State, and the FCC.

The task force emerged at the time when the government was soliciting views from industry about what agenda should be adopted for the MAFF initiative. Since then its membership has grown quite significantly and it is now the chief forum for developing a common industry response to a wide range of telecommunications trade policy issues. The main aims of the task force are to obtain:

- market access on reasonable terms for telecommunications equipment providers and value-added and information service vendors;
- non-discriminatory access to and use of telecommunications transport services;
- freedom to choose customer premises equipment;
- safeguards to prevent anti-competitive behavior toward foreign providers by government-controlled monopolies;
- transparent and reasonable domestic regulations starting with the separation of regulatory and operational functions;
- unrestricted movement of information among countries and companies.

Along with these substantive aims - indeed, in order to achieve them – the task force sets a high premium on making the government's interagency policy process more coherent and consistent, thus reducing the scope for debilitating turf fights, and on forging a more structured relation between government and industry. If the most sophisticated thinking on regulatory asymmetry has been done in forums like the task force and the United States Council, however, the tide of events has often been driven by more elemental forces, such as the neomercantilist current in Congress, which has lobbied, in part successfully, for the Administration to adopt a much tougher trade policy stance. Some of the neomercantilist demands have been met, albeit in an attenuated fashion,

by the passage of the Omnibus Trade and Competitiveness Act of 1988. In the emerging repertoire this new trade legislation is the most distinctive weapon, partly because of its provisions for unilateral action on the part of the United States. Thus in an effort to overcome regulatory asymmetry the nation has launched offensives on three distinct political fronts: the unilateral, the bilateral, and the multilateral, each of which merits attention.

As regards unilateral action, pride of place must go to the 1988 Trade Act, described by its sponsors as the most assertive trade legislation since 1945, and which America's trade partners consider to be the most protectionist. However, the Act is not protectionist in the classical sense of restraining imports; it aims, rather, to expand exports by forcing other countries to open their markets. In other words, the Trade Act is an attempt to systematize a policy hitherto pursued on a sporadic and *ad hoc* basis.[13] Although the Reagan Administration claimed to be resolutely opposed to any sector-specific trade measures, it eventually accepted the provisions designed to promote the telecommunications industry. Simply stated, the Act obliges the Administration to identify objectionable Acts, policies, or practices and requires these to be negotiated away under threat of sanctions: Special emphasis is accorded to countries with large trade surpluses and to issues like trade in telecommunications, intellectual property rights, and public procurement.

Under the terms of the Trade Act the USTR had five months after the date of enactment to identify priority foreign countries, that is, countries which were said to be denying mutually advantageous market opportunities to United States products and services. The first priority countries to be selected under the Trade Act were South Korea and the European Community, the rationale being their high volume of exports to the United States, their potential for United States sales, and their barriers to telecommunications trade. Arriving at this selection was not an easy task. In fact the USTR was inundated with recommendations for different priority countries by the agencies that constitute the interagency Trade Policy Review Group: among the countries cited were France, Germany, Spain, and Italy.

The USTR's decision to cite the European Community, rather than a particular member state, was a shrewd piece of diplomacy because the European Commission sees itself as the locus of authority for trade negotiations. Even so, some members of the Trade Policy Review Group are anxious for the Administration to keep the pressure on individual European countries, especially since the USTR review found that telecommunications trade barriers varied so much within the

Community, with Germany and France situated on the illiberal side of the spectrum as viewed through American eyes. All the ingredients are here for a telecommunications-related trade war between the United States and the European Community. The European Commission is deeply troubled by the Trade Act, particularly by the provisions which allow the United States to make unilateral decisions on what constitutes a trade barrier, and by the espousal of sectoral reciprocity in telecommunications, a concept which contravenes the GATT according to the Commission.

At bottom the Commission believes that the United States offensive against the Community is misdirected. It is at pains to stress that the Community's share of United States telecommunications imports has been on a declining curve and is of minor significance compared to the scale of imports from the Pacific Basin. On top of this the Commission argues that the United States has enjoyed a steadily growing telecommunications trade surplus with the Community, which stood at $320 million in 1986, a surplus that would be larger still if data processing equipment were added to the picture (and the Commission maintains that it should be included given the convergence between these sectors). In short the Commission feels that the United States is firing indiscriminately at its trading rivals when, in reality, the source of the trade problem is the Pacific Basin, and more fundamentally the chronic budget deficit.[14] As we see later, one paradoxical effect of the Trade Act has been to strengthen the hand of the neomercantilist lobby within the Community.

Because the Trade Act took some three years to get enacted, the Administration was forced by growing Congressional activism to take more immediate action on the telecom front, hence the Market Access Fact Finding (MAFF) exercise, which was launched in 1985. This is the bilateral front, where the US has tried to educate countries about the benefits of deregulation, to assess how much their markets are open to United States firms, and to pressure them to liberalize their telecom markets. What made bilateral action all the more appealing was the fact that telecommunications is not yet subject to the General Agreement on Trade and Tariffs (GATT), which meant that the payoff from multilateral action was too distant.

As we have seen, the first MAFF exercise was conducted with Germany in December 1985. The Germans agreed to these talks only after the United States had threatened to initiate Section 301 actions against the FRG on the grounds that the Bundespost was engaged in restrictive regulatory practices. The United States followed this in 1986

with MAFF talks with France, Spain, and Italy. Each of these member states has been advised by the Commission to refrain from further bilateral talks with the United States because trade negotiations must be handled at Community rather than member state level. As if to placate the Commission, the USTR has been careful with its political vocabulary: The MAFF exercise, it insisted, was all about 'talks' not 'negotiations.' But this distinction did nothing to allay the fears of the authorities in Brussels that the United States was using bilateral pressure to divide and rule the member states of the Community.

Fortunately for the United States, however, the Community is far from being a monolithic political bloc. On a spectrum of liberality the UK and the Netherlands are the most liberal and Germany, France, and Spain are the least liberal in terms of their telecommunications regimes. Because the UK is closer to the United States than it is to Germany as regards regulatory ideology, it was only a matter of time before they reached a bilateral agreement, which they duly did in 1988 with respect to international value-added networks (IVANs). The most notable feature of this deal was the fact that it took nearly two years to get it signed: One of the main reasons for this inordinate delay was the inability of the government agencies to agree among themselves, particularly in regard to what many of them saw as the FCC's uncompromising demands on international leased lines, demands which the UK government was reluctant to accept. The FCC's stance infuriated the United States Council; the latter felt that even without the FCC's demand the IVAN pact with the UK represented a very good deal for the United States. In other words an interagency turf fight had had a deleterious effect on United States interests. However, the United States is not about to give up on its bilateral offensive, especially since it is beginning to yield tangible results in Europe and Japan.

Last but not least is the multilateral arena, where the United States is engaged in much longer term initiatives. Because the United States is intent on prying open telecommunications markets worldwide, it is necessarily involved in the task of reforming (or perhaps even bypassing) the international institutions that have regulated these markets. For the United States this is especially the case with the International Telecommunications Union (ITU), the main regulatory and standards-setting body. Quite simply, the United States sees the ITU as a major obstacle to its deregulatory goals because it believes the ITU is overly influenced by public monopolies. Hence one of the main aims of the United States is to try to get the telecommunications sector subjected to the GATT process; from a United States standpoint this would force the

telecommunications debate 'into a broader, and perhaps more congenial, policy milieu.'[15]

The United States has worked long and hard to get the public telephone monopolies covered by the GATT Government Procurement Code, which provides for a non-discriminatory tendering process for government purchases. The United States has also tried to improve the situation with respect to non-tariff technical barriers to trade because the GATT Standards Code does not cover network equipment. Finally, the United States is the major driving force behind the attempt to develop a GATT framework for telecommunications services in the Uruguay Round of trade negotiations. In the absence of a GATT framework some of the main multilateral battles have occurred in the ITU, especially in the run up to the ITU's World Administrative Telegraph and Telephone Conference (WATTC), which met in December 1988 to try to define the regulatory regime for new telecommunications services. The main conflict here was between those countries (like France) which wanted to extend the hand of regulation and those (like the United States and the UK) which wanted as few regulations as possible. While the outcome was sufficiently ambiguous for each country to carry on as before, WATTC demonstrated two things: First, the United States vision of regulatory reform was still being highly contested; second, the multilateral road was as laborious as ever.

To the extent that the United States travels down this multilateral road, therefore, it will be more than ever anxious to get the issues debated in liberal trade forums, like the GATT, rather than in the more technical and illiberal ITU type of forum. Even so, it is highly unlikely that the ITU apparatus will be bypassed in the event of a GATT-based telecommunications trade agreement. Rather, the likelihood is that there will be a growing overlap of jurisdictional boundaries, a situation which is bound to spawn continuous turf fights between the two organizations and their respective allies.

In an attempt to ease the burden of deregulation in one country, the United States has taken it for granted that the GATT is ineffective. It has thus pursued unilateral, bilateral, and multilateral action at the same time. This scatter-gun approach seemed the only way to deliver the goods – in this case the opening of foreign telecommunications markets. But some of these initiatives appear to be politically inconsistent with one another, especially between the unilateral and multilateral levels. For example, if the United States wishes to strengthen the multilateral trading system – and its enthusiasm for the Uruguay Round suggests that it does – then, logically, it must accept multilateral surveillance of its

own actions. Logic, however, is a poor guide in the tempestuous waters of international trade politics. The United States conundrum may be summed as follows: 'Logic dictates that the United States has to change its own (trade) legislation. Political realities mean that the prospects of this are, unfortunately, remote.'[16]

Quite apart from their lack of consistency some of these initiatives appear to be having counter-productive effects. For instance, the unilateral provisions in the Trade Act seem to have strengthened the hand of neomercantilist elements in the European Community. This was all too clear when the Commission announced its directive on public procurement in October 1988, which covers the purchasing activities of entities providing water, energy, transport, and telecommunications services. The directive says that member states can reject any bid if the value of at least half the products and services comes from outside the Community. Even if a bid meets the 50 percent requirement, bids by European companies will be preferred as long as they are deemed to be equivalent and not more than 3 percent higher in price.[17] In other words, the directive embodied a much tougher line on trade than had been expected, and this was attributed to the hawkish United States Trade Act.

A trade war serves the interest of neither the United States nor Europe, yet early skirmishes have already begun. Telecommunications may well be at the forefront because it is a sector where the United States has chosen to seek bilateral reciprocity, as determined by the United States, rather than the GATT concept of multilaterally agreed non-discriminatory reciprocity. More generally the United States seems to be moving closer to the concept of managed trade, as is the Community. In short, there is little to choose between the ways in which United States and European trade policies have evolved: Both have adopted discrimination as a norm.[18] Much will depend on how the Community implements its 1992 proposals for a single European market. If the United States feels that a Fortress Europe is emerging (i.e., external barriers go up while internal barriers come down), European firms can ready themselves for a terrible backlash in the United States market.

In this chapter we have examined some of the political dilemmas of America's open network policy regime at home and abroad. One of the main conclusions is that deregulation does not necessarily involve less government intervention: At the federal level the role of government is changing rather than diminishing. For example, while the traditional regulatory role of the FCC is being scaled down, the rise of the

Court-based regime signals a form of reregulation. Although deregulation and divestiture have delivered real benefits – especially for the business user community – these policy changes carry costs as well, on the trade front especially. There is also the intangible cost of regulatory turbulence, which renders corporate planning more difficult than it would otherwise be.

The diffuse, pluralistic nature of the United States political system has many strengths – it is a bulwark against centralization and it offers great scope for policy experimentation, to name but two. Recently, however, the opportunity costs of this system have become more prominent. At a time when other countries are upgrading their telecom infrastructures and streamlining their regulatory processes, the United States regulatory system is inordinately time-consuming, in part because it affords firms unrivalled opportunities to contest regulatory decisions. The regime of parallel regulation at the federal level compounds this problem because the FCC and the Court have been emitting radically different signals to the industry.

The opportunity costs of such turf wars may have been easier to bear when the United States rode high in world markets, but that time has passed. Its extraordinarily diffuse political system means that America has a low capacity for political cohesiveness within government and between government and industry. Compared to the more centralized systems of Japan and France, which have strong government–industry interfaces, the United States system may find it more difficult to develop infrastructural technologies, like ISDN and High Definition Television (HDTV), which have high up-front costs and involve a degree of collaboration unprecedented in the past. This dilemma is now a resonant issue in the United States; indeed, it has induced elements in government and industry to press for new public–private partnerships to exploit ISDN and HDTV.[19] These initiatives are a modest attempt to overcome the opportunity costs of America's open network policy regime, associated as it is with regulatory turbulence and political fragmentation.

At the international level the government has been forced to become more, not less, interventionist, especially in the areas of standards-setting, communications trade policy, and market access. This is motivated by a renewed determination to create a level playing field – to remove the regulatory asymmetries in the global telecommunications market. However, this is going to be an arduous task, not least because it touches the sensitive issue of national sovereignty. Although the United States has made some progress in concerting itself here, its unilateralist actions on the trade front may prove to be counter-

productive. As we have seen, the passage of the Trade Act fortified mercantilist elements in the European Community.

At domestic and international levels, then, it is naive to think that deregulation will remove telecommunications from the political arena. If anything, the reverse is true, namely that telecommunications issues are becoming the stuff of high politics at home and abroad. Time alone will tell whether America's open network policy regime, in which political power and regulatory authority are highly fragmented, is the most optimal system to carry the United States into the new era of international competition in telecommunications.

NOTES

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