Comments on

"A CRITIQUE OF STRUCTURE REGULATION IN COMMON CARRIER TELECOMMUNICATIONS"

WERNER Z. HIRSCH*

My comments on Trebing's paper seek to transcend its scope by relating it to other issues raised by the other stimulating and informative articles.

The Trebing article is, to me, interesting though somewhat puzzling, particularly in relation to what its theoretical underpinnings might be. Its major contribution lies in its impressive marshalling and organizing of complex facts and events. On the other hand, it includes only a few, rarely defined, theoretical concepts. As it deals with both legal and economic issues, I am hard pressed to group the article with any of the conventional kinds of efforts in law and economics. It does not engage in efficient rule formulation, but neither does it undertake a systematic estimation of the effects of present structural regulations and of those that have been proposed. Neither does the author pursue a neo-institutional approach which, in exam-

---

*Werner Z. Hirsch is a Director of the Institute of Government and Public Affairs and Professor of Economics at UCLA. He has held positions at the United Nations and at the Brookings Institution, and visiting appointments at Harvard, Cambridge, and the Rockefeller Study Center. He served as a consultant to Rand, OECD, the Los Angeles County Board of Supervisors, and to many Congressional committees and executive departments. He was president of Western Regional Science Association, is a member of the National Academy of Science and the Board of the Edmund Brown Institute of Government, and is on the editorial board of the *International Review of Law and Economics*. His numerous publications center on local public finance and on law and economics. He received a BS and PhD from the University of California.

ining structure regulation, would emphasize transaction cost in a manner suggested by Oliver Williamson and Victor Goldberg. Such an approach would be process oriented, dynamic, and evolutionary in seeking to identify and evaluate principal factors that have been responsible for institutional developments leading up to the divestiture decree. The Trebing article does not fit into any of these categories.

I would like to raise four specific issues. First, Trebing's article is entitled, "A Critique of Structure Regulation in Common Carrier Telecommunications"; however, I cannot find in it an articulation of a set of criteria on which the critique is based. Unfortunately, the same can be said about the other articles. They fail to establish explicit criteria by which they seek to evaluate regulation, whether of the old or of the new telecommunications network. What I find instead is an almost universal worship of competition in the telecommunications industry. But is not competition a means to an end rather than an end in itself? Don't we still have to consider what mix of allocative efficiency, X-efficiency, and distributive justice over what time horizon is our ultimate end? Are we perhaps too enamored of the virtues of competition through deregulation, or too intoxicated with the potential good that competition in the new telecommunications industry can do?

These are questions that have crossed my mind several times in my considerations of these articles. Yet I decided that what on first blush might appear as an overemphasis on competition through deregulation is not so much a fetish as it is a considered judgment and necessity. It is the realization that great innovations are coming down the pike at an accelerating pace and with snowballing force, and that deregulation is needed if we are to benefit to the greatest possible degree from these innovations. In short, a perception underlying an advocacy of deregulation is not that competition is needed to unleash innovation, but rather that the massive onslaught of innovation can only be harnessed effectively if we restructure the industry and remove some of the old shackles.

The following question has also occurred to me a number of times: Aren't we perhaps too impressed and overwhelmed by the AT&T divestiture proposal? Clearly, the telecommunications industry is much broader than even the imperial AT&T, and I was therefore concerned about the prominence of AT&T in our deliberations.

In the end, though, I concluded that we are right in focusing on the AT&T consent decree and emphasizing the opportunities it offers. In particular, I believe that it is promising to focus on process rather than merely on substance. Today's pricing structure of telecommunications services is controversial, particularly because it involves large hidden subsidies. These have evolved over time, not necessarily according to a widely agreed upon master plan, but in a nearly random fashion. The huge subsidies give signals to service users and result in substantial inefficiencies. The consent decree promises increased competition and is likely to let in fresh air. One would hope that a new subsidy pattern, if such is to result, will be arrived at after more explicit deliberations as to who is to be subsidized and by how much. As a result, substantial efficiency gains are likely.

Let me confess to a third stubborn thought. Would it not be nice to have a more rigorous analytical framework, or even model, by which to analyze the new telecommunications industry? Admittedly, the Noll and Shepherd articles go further in this direction than does the Trebing. Such a framework could take into explicit consideration some of the more fundamental issues and at the same time permit analysis of the effects under various scenarios. In relation to the former, I would hope that such a framework would be responsive to the question about the extent to which information and telecommunications services are social goods. Yes, they involve joint consumption and yes, they generate externalities; but to what extent are they merit goods and subject to declining costs?

The framework could also help us deal more effectively with a variety of scenarios attractive to experts. For example, Trebing's article appears to suggest that there will be relatively little competition for local distribution, perhaps because he assumes that old-fashioned phone service will dominate in the future. Yet, after discussions with a number of engineers, I can visualize active competition from cellular radio systems and other new techniques. Clearly, articulating these differences is likely to be rewarding to the analyst.

I might add a fourth and final unruly thought, or perhaps speculation. I foresee a near future in which major new risk takers will seek to enter the dynamic telecommunications industry. The reasons relate to attractive depreciation provisions of recent tax law changes and to a reduction in the all-time high interest rates, which I believe will have to come down sooner or later. These two developments will give newcomers to the industry an advantage over the established telecommunications firms that are burdened by old equipment and costly debt. The result will be a further explosion of innovation in this most dynamic industry.