

PART I: REGULATION OF COMMON CARRIERS

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* The authors gratefully acknowledge the contributions of Leslie Taylor, Esq. in preparing Chapter II, and of Mr. W. Edward Singletary in preparing Chapter III.

Introduction

Inspired by Lockean principles of natural law, classic American ideology seeks individualism, fragmentation of private power, limitation of government (with the notable exception of guaranteeing physical security) and protection of property rights and contracts. As applied to communications policy, this philosophy has justified a governmental role that is far narrower than in most other countries and has based government's residual role largely on the grounds of market failure and national security.

Market failure exists when the traditional competitive mechanisms for limiting economic power cannot operate, due to the peculiarities of an industry. In the case of telecommunications, these peculiarities include: the absence of property rights in the electromagnetic spectrum; the natural-monopoly characteristics often found in telecommunications networks; and the public-good externalities of universal service.

Until the mid-1970s, these were the fundamental goals of U.S. telecommunications policy. More recent trends, however, have shifted them in two contradictory directions. On the one hand, many of the market-failure arguments have been discarded as either inherently flawed or obsolete through technological change and entrepreneurial initiative. On the other hand, national-security arguments have become more important to U.S. policy makers.

For many other Western countries, however, the trends have been the opposite. National security concerns now have a lower priority, while a government's role in telecommunications often has become the foundation for industrial policy in the electronics field.¹

There have been other divergences. U.S. efforts to protect individual privacy have been applied vigorously against the state but not as against private parties. The U.S. Constitution only occasionally applies.² Protections are mostly by adaptation of the common law or by heterogeneous state legislation dealing with specific abuses.³ Many other Western countries reverse these priorities; they are vigilant about private power and often more tolerant of government authority.

The United States thus has diverged from European countries recently in

1 *E.g.*, S. NORA & A. MINC, L'INFORMATISATION DE LA SOCIÉTÉ (1978).

2 *E.g.*, *Griswold v. Connecticut*, 381 U.S. 479 (1965).

3 *E.g.*, A. WESTIN, PRIVACY AND FREEDOM (1967).

its general outlook on basic telecommunications policy, as it has moved from a somewhat social-democratic New Deal to a marketplace ideology. Since no country is an ideological island, this has led to problems of adjustment and coordination. An excellent example of this is the international flow of electronic information, at present subject to several multilateral harmonization efforts.

To shed light on this area, it is necessary to understand the rules governing information flows in the United States. This survey describes U.S. regulatory policies for those information flows using telephone, telegraph and other point-to-point communications, excluding the mass media. It begins with a survey of the basic regulatory scheme and is followed by a discussion of regulations in areas such as national security, privacy, common law and statutory restrictions. A host of other U.S. domestic laws – such as stock-trading regulations and the Uniform Commercial Code as to sales of goods – potentially impact on international information flows. But coverage of all these topics would require a multi-volume treatise. This survey thus focuses upon the domestic U.S. legal and regulatory structures and some of their aspects that impact on international telecommunications – export licensing, national security and privacy statutes.

This piece distinguishes between conduit and content – i.e., between medium and message – in examining U.S. restrictions on international telecommunications. It begins by reviewing U.S. regulatory and economic restrictions on the methods of point-to-point transmission into or out of the United States. It then considers a wide variety of piecemeal limitations on the content of these information flows.

The survey concludes that U.S. governmental control over the channels of communication is rapidly disappearing, that various common-law and regulatory restrictions also are declining and that national-security concerns apply more strictly than before.

Chapter I: The U.S. Carrier System

A. Overview

The basic framework of government involvement in U.S. telecommunications is simple in theory and complex in reality. The public sector does not own or operate civilian telecommunications services, except for a few small municipally-owned cable television operations, rural telephone systems and educational television broadcasting stations.

Although almost all civilian telecommunications facilities are privately owned, their use is often – but not always – subject to licensing and regulatory oversight. These regulations are set on the federal, state and, occasionally, local levels.

Federal policy emanates mainly from the Federal Communications Commission (FCC), a body of five commissioners appointed by the president but independent of that office. It operates as a hybrid within the American constitutional order, with some legislative powers (adoption of regulations), some executive authority (enforcement of its rules) and some judicial powers (adjudication of cases). The Commission allocates frequencies and regulates all broadcasting, satellite and other civilian uses of the electromagnetic spectrum.⁴ The FCC is also in charge of *interstate* telephony – that is, transmissions from one state to another – and everything affecting interstate communications. The FCC has some jurisdiction over cable television.⁵

State regulatory commissions, which also are usually independent in status, play an important role in regulating *intrastate* telephone and, in some instances, also cable television.⁶ Municipal authorities regulate cable television through their powers to grant franchises to lay cable in their streets.⁷

On the executive level, the Commerce Department's National Telecommunications and Information Agency (NTIA) helps to coordinate the presi-

4 47 U.S.C. §§ 214, 301 (1982).

5 *E.g.*, FCC v. Midwest Cable Co., 440 U.S. 369 (1979).

6 *E.g.*, N.Y. Exec. Law § 811 *et seq.* (1979).

7 *E.g.*, New York City Charter § 362 (1985).

dent's - that is, the executive branch's - overall telecommunications policy. It plays a role in international communications, together with the Office of the U.S. Trade Representative and the State Department, which is the lead agency in international negotiations.⁸ Despite its international visibility, the NTIA cannot match the FCC's domestic regulatory powers.

In addition, the executive branch's Department of Justice plays a major role through its Antitrust Division, which oversees much of the telephone industry by way of enforcing the 1982 court order that broke up AT&T.⁹ The primary authority in that case is federal district court Judge Harold Greene, who frequently decides whether telephone companies and other parties are complying with the AT&T divestiture decree and who has thus become a major presence in telecommunications matters.¹⁰

Conforming to a broader policy trend in the U.S. governmental decision-making process, federal courts - particularly the U.S. Court of Appeals for the District of Columbia Circuit - have become a significant locus of telecommunications policy making. (The circuit courts hear appeals from trial courts and administrative agencies; their decisions can be reviewed only by the Supreme Court, which hears only a few percent of circuit court decisions.)¹¹ For example, the D.C. Circuit forced the FCC to allow non-AT&T equipment manufacturers to sell terminal units for connection into the local AT&T exchanges, making competition in the equipment market possible.¹² The Justice Department and the Federal Trade Commission also play a role in regulating industry competitive behavior and structural changes - primarily mergers and acquisitions - and in forcing divestitures, as with AT&T.¹³

Most important for telecommunications policy, at least in theory, is the U.S. Congress. The primary legislation for U.S. telecommunications is the Communications Act of 1934.¹⁴ This Magna Charta of U.S. telecommunications has rarely been amended, despite many attempts. Policy making in light of changed circumstances has been left largely to the FCC's and the courts' discretion. Congress often wields its power indirectly, however, by

8 See GOVERNMENT SERVICES ADMINISTRATION, GOVERNMENT ORGANIZATION MANUAL (1985)

9 See discussion in text at note 27 *et seq. infra*.

10 See S. SIMON, AFTER DIVESTITURE 31 *et seq.* (1985).

11 See discussion in text at note 52 *infra*.

12 Hush-a-Phone v. FCC, 238 F.2d 266 (D.C. Cir. 1956).

13 See L. SULLIVAN, HANDBOOK OF THE LAW OF ANTITRUST 751 *et seq.* (1977).

14 47 U.S.C. § 151 *et seq.* (1982).

giving signals to the FCC through bills, resolutions, hearings and the budgetary process. Congress can reduce an agency's budget unless it adopts certain policies, a power that obviously can have a strong influence on an agency.¹⁵

This multiplicity of decision-making governmental bodies frustrates coordinated and comprehensive policy making. But this process also accommodates decentralized and ad hoc decisions, many of which are responses to specific problems rather than part of a grand design. This has permitted a fairly rapid reorientation of U.S. telecommunications policy, without major upheavals – except perhaps for the AT&T divestiture.

B. *Regulatory Authorities*

Most telephone service in the United States is provided by firms regulated as »common carriers.« This concept requires some explanation. The Communications Act of 1934 defines a »common carrier« merely as a »common carrier for hire, in interstate or foreign communication by wire or radio or in interstate or foreign radio transmission of energy.«¹⁶ In less circular terms, a common carrier is a firm that either holds itself out or is required by law to provide transmission services to any financially qualified customer.¹⁷

A common carrier offers to lease transmission facilities to the public on a nondiscriminatory basis, usually under a tariff of rates and services approved by the Federal Communications Commission and/or a state regulatory agency. A common carrier does not control the content of the information transmitted over its facilities. Local-exchange telephone operators, domestic as well as international long-distance networks and communications satellites are common carriers, despite the widely divergent services they offer.

Because of traditionally federalist U.S. policies, carriers are regulated by several levels of government – federal, state and local. Local-exchange operators – primarily, of course, the divested AT&T companies, called

15 *E.g.*, E. KRASNOW, L. LONGLEY, & H. TERRY, *THE POLITICS OF BROADCAST REGULATION* (3d ed. 1982).

16 47 U.S.C. § 153(h) (1982).

17 *National Ass'n of Regulatory Util. Comm'rs v. FCC*, 525 F.2d 630 (D.C. Cir.), *cert. denied*, 425 U.S. 992 (1976).

Bell Operating Companies (BOCs) – must secure state and occasionally even local approval of their operations. (Whether local approval is necessary depends upon whether a state has authorized cities to grant authorizations – generally termed »franchises« or »consents.« Although local franchising was quite common during the early days of telephony, virtually all states today have prohibited local regulation of telephony.)¹⁸

The states in turn have created specialized administrative agencies – usually called »public utilities commissions« or »public service commissions« – to regulate telephone companies' rates and practices. State agencies may regulate only *intrastate* activities – that is, activities occurring wholly within one state – such as charges for calls within or between exchange service areas in a state.¹⁹ Both local-exchange and long-distance service providers must apply to the state agencies for approval of their tariffs and for »certificates of public convenience and necessity.«²⁰

Rate setting is a complex matter. Rates usually are designed to generate enough aggregate revenues to cover costs and depreciation, plus a reasonable profit on invested capital. Rate cases often involve protracted battles to define and measure costs, depreciation and investments and to define a reasonable profit, given the risk characteristics of the business. Furthermore, the allocation of costs and profits to some services and not to others can have major implications as to whether some customers subsidize others and whether a competitive communications offering receives a subsidy by shifting some of its costs to a securely monopolistic service.

The FCC must approve any interstate carrier's rates and practices.²¹ Although the Commission largely has abandoned its strict rate-of-return regulation, tariff filings and »section 214 certificates« still are necessary.

This »content-neutral« or »conduit« status of common carriers often creates a set of public-policy problems totally unrelated to a carrier's basic-service obligations. For example, the last few years have witnessed a variety of disputes over local telephone companies' provision of »dial-it« recorded messages – that is, local numbers that a customer can call, at a charge, to hear a recorded message provided by a third party. Some of these services contain sexually oriented or »dial-a-porn« material.²²

18 W.K. JONES, CASES AND MATERIALS ON REGULATED INDUSTRIES 30-35, 74-76 (2d ed. 1976).

19 *E.g.*, 47 U.S.C. § 152(a) (1982).

20 *E.g.*, N.Y. Public Service Law art. 8 (1979).

21 47 U.S.C. § 214 (1982).

22 *E.g.*, 47 U.S.C. § 223 (Supp. 1985).

Because of its passive nature as a conduit, however, a telephone company cannot censor such material.

Regulation of the telephone industry historically has been justified by the existence of economies of scale – i.e., the view that some services are most inexpensively delivered by a single firm or monopoly since it can achieve the lowest average costs.²³ Interstate telephone service traditionally has been regulated by the FCC, while local or intrastate service is subject to regulation by state public utilities commissions.²⁴ To the extent that a call involves both interstate and intrastate facilities, the FCC and state authorities collaborate in setting the rate for the call.²⁵ Regulators must publish rate applications and conduct public hearings prior to rendering decisions. In theory, tariffs are designed to give a common carrier a fair rate of return on its capital investment.²⁶

C. AT&T

The U.S. telecommunications industry was a simple affair for a very long time. There was one telephone company, the American Telephone and Telegraph Company (AT&T). Despite its name, it was barred from telegraphy, which was the domain of Western Union; internationally, Western Union was excluded from the telegraph market in favor of a handful of so-called international record carriers.

This was a structure of stability, in which companies were carefully excluded from each other's markets. Instead of competition, federal and state regulation kept the various companies – most particularly, AT&T – from exploiting their market power. Over the past two decades, however, this traditional arrangement increasingly has exploded in a mutually reinforcing process of competitive entry and government liberalization and has given way to a highly dynamic structure of overlapping markets, which also has affected United States international telecommunications.

American Telephone and Telegraph had operated for twenty-five years pursuant to a 1956 Consent Decree, which terminated an antitrust suit

23 E.g., Handler, *Regulation vs. Competition*, 44 U. CIN. L. REV. 191, 206 (1975).

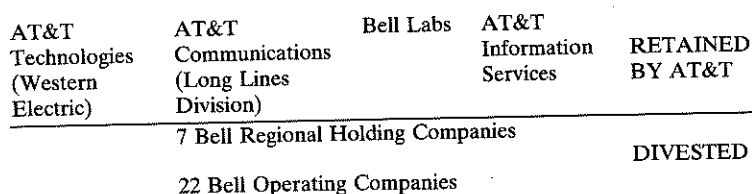
24 47 U.S.C. § 152(a) (1982).

25 W. BOLTER, TELECOMMUNICATIONS POLICY FOR THE 1980's 181 (1984).

26 *FPC v. Hope Natural Gas Co.*, 320 U.S. 591 (1944).

brought by the Justice Department in 1949.²⁷ The pre-divestiture AT&T was substantially different than today's often confusing mixture of entities. AT&T was perhaps the most vertically integrated telecommunications corporation in the world, since it provided almost everything from equipment service to long-distance transmission and local service. Western Electric (now AT&T Technologies) produced both terminal and switching equipment; Long Lines Division (now AT&T Communications) provided ninety percent of the nation's long-distance traffic; Bell Labs (the only AT&T entity to survive without a name change) did basic research through a complex set of contracts with the other AT&T components; and twenty-two wholly or majority-owned local telephone companies – such as New York Telephone Company or Southern Bell – provided local-exchange service to one or more states.²⁸

The divestiture ended the most significant portion of AT&T's vertical integration – namely, the common ownership of the local-exchange companies and equipment as well as long-distance service providers. At least in theory, this removed a number of perceived conflicts of interest, such as local-exchange companies' paying inflated prices for Western Electric equipment.²⁹ Put in a simplistically graphic way, the diagram below shows the major separation created by the of divestiture of AT&T:



The divestiture came about in a relatively complicated procedural fashion. In 1982, AT&T settled a 1974 antitrust case, under a Modification of Final Judgment (MFJ).³⁰ This technically was an amendment to the 1956 Consent Decree. The MFJ required AT&T to divest its twenty-two local-exchange Bell Operating Companies, which now are owned by seven Bell Regional Holding Companies (RHCs). (It is not yet clear whether an RHC is a common

27 See discussion in text at note 30 *et seq. infra*.

28 W. BOLTER, *supra* note 25, at 174 *et seq.*

29 See discussion in text at note 54 *et seq. infra*.

30 *United States v. AT&T*, Civ. No. 74-1698 (D.D.C. 1984), *modifying United States v. Western Electric Co.*, Civ. No. 17-49 (D.C.N.J. 1956).

carrier.)³¹ AT&T also kept several key entities: its research-and-development arm, Bell Labs; its manufacturing arm, Western Electric; its regulated long-distance operation, Long Lines Division; and a new entity for providing enhanced services (AT&T Information Services), which was later combined with AT&T Communications. The FCC supported the settlement but urged that the BOCs also be permitted to enter unregulated fields – a position for which there is increasing support.

While the Justice Department was pursuing its case, the FCC was imposing structural restraints on AT&T. The FCC found it necessary during the 1970s to decide how AT&T could provide data-processing and other »enhanced« services; under the 1956 Consent Decree, AT&T could provide only telecommunications transmission service. Because of the capabilities of electronic switching and of customer demand for new services, AT&T increasingly felt pressure to offer enhanced services. These services were provided at first through AT&T's common-carrier offerings – over the objections of the data-processing industry – and were considered communications services. The FCC addressed this dilemma in three so-called *Computer Inquires* (*Computer I*, *Computer II* and *Computer III*). In *Computer II*, the Commission developed a distinction between »basic« or communications services and »enhanced« or software-driven services. AT&T could provide only basic services through its regulated offerings. Enhanced services had to be provided by an unregulated and »fully separated« subsidiary.³²

Despite strenuous objections by U.S. service providers, the FCC in 1983 changed the effect of the *Computer II* »basic« and »enhanced« classifications. If a carrier provided »enhanced« rather than »basic« service, it no longer needed – and, indeed, no longer could obtain – an authorization pursuant to the certification processes of section 214. Since most new value-added carriers in fact were providing »enhanced« services by utilizing both data processing and telecommunications, they thus fell within this category. Because of this decision, providers of international enhanced services no longer could obtain FCC section 214 authorizations for their services. The service providers argued that lack of section 214 authority would impede their ability to obtain operating agreements with overseas PTIs since they would not be treated as common carriers under domestic U.S. law.

In August of 1985, the Commission initiated yet another rule-making pro-

31 *U.S. West, Inc. v. FCC*, Civ. No. 84-1448 (D.C. Cir. 1985).

32 See Amendment of Section 64.702 of the Commission's Rules and Regulations (*Computer II*), 77 F.C.C.2d 384 (1980); 84 F.C.C.2d 50 (1980); 88 F.C.C.2d 512 (1981); *aff'd sub nom.* CCIA v. FCC, 693 F.2d 198 (D.C. Cir. 1982).

ceeding, *Computer III*, to re-examine restrictions on both AT&T's and the BOCs' activities.³³ In general, the FCC's initial proposals would have allowed both AT&T and the BOCs not only to offer enhanced services jointly but also to operate without any requirement of a separate subsidiary in some circumstances. In addition, the Commission at least suggested abolishing the separate-subsiidiary requirement and replacing it with detailed regulatory requirements.³⁴

In the summer of 1986, the Commission did away with *Computer II*'s separate-subsiidiary requirement in the *Computer III* proceeding.³⁵ The FCC's view was that AT&T's market power was declining in the interexchange service market and that the separate-subsiidiary requirement imposed unnecessary regulatory burdens. One result of the Commission's decision was the merger of AT&T Information Services into AT&T Communications, with the aim of reducing some duplication. Side effects included the intensification of efforts to repeal the separate-subsiidiary limitations on the BOCs and to transfer jurisdiction over enforcement of the MFJ from Judge Green to the FCC, which had come to be viewed as more sympathetic to AT&T.³⁶

D. *The FCC's Jurisdiction*

There are telecommunications common carriers other than telephone companies. They take different forms and are not restricted to point-to-point transmissions. For example, a totally different type of common carrier is the Multipoint Distribution Service (MDS), which transmits omnidirectional microwave signals to multiple receivers with directional antennae. MDS operates on a small portion of the electromagnetic spectrum — 2150-2162 MHz — far above the frequencies that conventional television sets can receive. Authorized in 1962 for a variety of uses, MDS has been used until recently for »pay«-television programming and high-speed data transmission. An MDS licensee leases its facilities on a nondiscriminatory

33 *Computer III*, Docket No. 85-229, FCC 85-397 (Aug. 16, 1985).

34 See Marks & Casserly, *An Introduction to the FCC's Third Computer Inquiry*, THE COMPUTER LAWYER, Oct. 1985 at 1 *et seq.*; Wiley & Polsky, *Understanding the Computer III Inquiry*, TELEMATICS, Nov. 1985 at 3 *et seq.*

35 Report and Order, 102 F.C.C.2d 655 (1985); Memorandum, Opinion and Order on Reconsideration, Common Carrier Docket No. 85-229 (May 22, 1987).

36 S. 2565, 99th Cong., 2 Sess. (1986).

basis in accordance with FCC tariffs, although it usually has a pay-television service as its primary customer. The Commission prohibits an MDS operator from leasing more than half of its transmission time to any affiliated company.³⁷

The MDS example shows how technological developments and their applications have created strains on the FCC's traditional definition and treatment of communications services. Under the Communications Act of 1934, the FCC has at least five different types of regulatory jurisdiction. These distinctions, although technical in nature, can be important in determining what types of FCC regulations – e.g., common-carrier or broadcasting – apply to a particular communications service. This can make a great difference in the nature of regulation. In simplistic terms, broadcast status imposes content regulation but no economic restrictions or access requirements. On the other hand, common-carrier status often requires approval of rates and service conditions but does not restrict content.³⁸

In addition, the Commission has jurisdiction under title III of the Act over use of »any apparatus for the transmission of energy or communications or signals by radio,« – that is, any over-the-air use of the radio-frequency spectrum.³⁹ This jurisdiction in turn breaks down into three distinct sub-categories. The most visible type of title III jurisdiction is regulation of broadcast stations, and title III contains special provisions applicable only to broadcasters, such as the requirement of reply time under the fairness doctrine.⁴⁰ In addition, a license is necessary under title III for any title II common-carrier spectrum use – from a mobile telephone to an international satellite. Moreover, title III gives the Commission jurisdiction over spectrum uses that are neither broadcasting nor common carriage, under the general classification of »private radio.«⁴¹

Finally, the FCC has a very vague type of implied jurisdiction over activities that are not clearly within either title II or title III. The most significant example of this type of jurisdiction is the Commission's »reasonably ancillary« jurisdiction over cable television. As defined by case law, this jurisdiction appears to allow the FCC to regulate cable in order to prevent any adverse impact on broadcast television.⁴² Although the extent of this jurisdiction is unclear, it appears to be totally separate from – but implied

37 47 C.F.R. § 21.900 (1986).

38 See discussion in text at note 22 *supra*.

39 47 U.S.C. § 301 (1982)

40 47 U.S.C. § 315 (1982)

41 47 U.S.C. § 301 (1982); e.g., 47 C.F.R. § 95.401 *et seq.* (1986) (Citizens Band radios).

42 *FCC v. Midwest Video Corp.*, 440 U.S. 689, 696 (1979).

by — the Commission's other jurisdictions.⁴³ The scope of this jurisdiction may have been somewhat cast in doubt by the passage of the Cable Communications Policy Act of 1984, which enumerates certain limited powers for the FCC in the regulation of cable television.⁴⁴

The FCC's choice of a jurisdictional basis has a significant impact upon the legal status of a medium. If a medium is classified as broadcasting, it becomes subject to the wide variety of statutory requirements, such as the fairness doctrine, the political »equal time« reply requirements, the sponsorship-identification rules and the like.⁴⁵ On the other hand, classification as a common carrier requires an operator to file tariffs for its rates, subjecting it at least potentially to rate-of-return regulation.⁴⁶

The D.C. Circuit recently limited the FCC's discretion in choosing jurisdictional bases for the media. In *National Association of Broadcasters v. FCC* (*NAB* decision),⁴⁷ the court held that the Commission was required to regulate either direct-broadcast satellite (DBS) operators or their channel lessees as broadcasters, thus subjecting them to the full panoply of fairness, equal-time and other traditional broadcast regulations. The court reasoned that since »DBS systems transmit signals directly to homes with the intent that those signals be received by the public, such transmissions rather clearly fit the definition of broadcasting.«⁴⁸ Moreover, it noted that the Act »does not give the Commission a blank check to regulate DBS in any way it deems fit.«⁴⁹ At the same time, the court rejected analogies to regulation of MDS as a common carrier, suggesting that the Commission's initial classification of MDS may have been misconceived.

As a result, the *NAB* decision casts considerable doubt on the FCC's classification of the electronic media, in terms of common-carrier or other status. In the fall of 1985, the FCC initiated a rule-making proceeding in response to the *NAB* decision. The Commission recently proposed regulating both DBS and subscription television (STV) along the same lines as MDS, thus relieving them of any broadcast-style responsibilities.⁵⁰ Whether the FCC's proposal would withstand judicial review under the *NAB* decision is, of course, open to question.

Judicial review of FCC actions is quite simple in nature. In order to chal-

43 *E.g.*, *United States v. Southwestern Cable Co.*, 392 U.S. 157, 167 *et seq.* (1968).

44 47 U.S.C. § 601 *et seq.* (Supp. 1986).

45 *E.g.*, 47 U.S.C. § 315 (1982).

46 47 U.S.C. § 214 (1982).

47 740 F.2d 1190 (D.C. Cir. 1984).

48 *Id.* at 1194.

49 *Id.* at 1207.

50 Notice of Proposed Rulemaking, Gen. Dkt. No. 85-305 (Oct. 4, 1985).

lenge the Commission's adoption of a rule, a party need only file a »petition for review.«⁵¹ Review of a licensing decision under Title III of the Act, on the other hand, is by an »appeal.«⁵² Under section 402(a), a challenger may file its petition with any court of appeals in whose circuit it has a principal place of business. Under section 402(b), however, all appeals go to the District of Columbia Circuit Court, in order to allow one court to make national licensing policies. Both section 402(a) and section 402(b) proceedings are appellate in nature and thus involve merely the submission of briefs and the presentation of short oral arguments – rather than the introduction of evidence as in a trial court.⁵³

E. *Types of Networks*

1. *Public Networks*

Operation of the various types of telephone networks in the United States is highly decentralized.⁵⁴ Following the AT&T divestiture, the structure of networks is as follows:

a. *Local service*

(i) There are twenty-two Bell Operating Companies, such as the New England Telephone Company. They are organized into seven Bell Regional Holding Companies, such as NYNEX. The BOCs provide the bulk of local service, with more than 1000 small independent companies serving approximately 10% of the nation's geographic area and 20% of its population. The largest independent company is General Telephone & Electronics (GTE). Local companies are restricted to service within their Local Access and Transport Areas (LATAs) and may not enter long-distance or international communications. They are regulated by various bodies, primarily state commissions and the FCC.

(ii) Various private »bypassers« compete with the BOCs in providing local

51 47 U.S.C. § 402(a) (1982).

52 47 U.S.C. § 402(b) (1982).

53 47 U.S.C. § 402 (1982).

54 For a general description, see W. BOLTER, *supra* note 25.

service through a number of technologies.⁵⁵ These technologies include:

- a. Cable television;
 - b. Point-to-point microwave;
 - c. Digital Termination Service (DTS), a two-way point-to-point switched microwave service;⁵⁶
 - d. Fiber-optic links;
 - e. Infrared transmission, which does not require an FCC license; and
 - f. Cellular radio, primarily in the form of mobile car telephones.⁵⁷
- (iii) Shared tenant services (STS) is a hybrid new form of local transmission in which landlords resell local service using a private branch exchange (PBX) and lines leased from telephone companies or other carriers.

b. *Long-distance service*

- (i) AT&T controls more than 80% of the »interexchange« or »inter-LATA« service.⁵⁸
- (ii) Other common carriers (OCCs), such as MCI and Sprint, provide the rest.
- (iii) »Resellers« of long-distance service (including in part the OCCs, which often lease lines from AT&T) and many others buy long-distance service at low bulk rates and resell it to smaller users.
- (iv) Lessors of long-distance links include a growing number of railroads or highway authorities, which install fiber-optic lines on their routes.
- (v) Domestic record carriers, primarily Western Union and RCA, provide mostly telegraph services and, increasingly, data transmission.
- (vi) Specialized companies – including data networks and value-added networks such as Telenet and Tymnet – provide packet switching and other high-technology services over leased circuits.
- (vii) Satellite carriers (such as RCA), often operating as common carriers, lease transponder capacity to other common carriers and private users.

55 Noam, *The »New« Local Communications*, 6 COMPUTER L.J. 247 (1986).

56 E.g., D. IRWIN, TELECOMMUNICATIONS REGULATORY MONITOR II-29 *et seq.* (1985).

57 Davis, *Making Sense of the Telecommunications Circus*, HIGH TECHNOLOGY Sept. 1985, at 22-25.

58 *Id.* at 22.

c. *International carriers*

- (i) AT&T provides the bulk of international voice service and now also provides record service.
- (ii) Other common carriers, such as MCI International and Sprint, provide service to countries with whose postal, telegraph and telephone (PTT) authorities they have agreements. In the Pacific, the Hawaiian Telephone Co. handles much of the traffic.
- (iii) Comsat, the U.S. signatory to INTELSAT and INMARSAT, originally operated solely as a »carrier's carrier« and is now able to access users directly. For international civilian satellite communications (as distinguished from cable or microwave), INTELSAT was the sole link. U.S. carriers may go through either Comsat or a private carrier to access INTELSAT for international satellite service. As noted below, INTELSAT also now faces »bypass« from private satellite operators.⁵⁹
- (iv) International record carriers (IRCs), such as RCA, ITT, TRT and MCI International (formerly Western Union International), also offer telegraph and telex service. The IRCs originally were restricted to international record service. These restrictions now have been abolished.
- (v) Specialized carriers and value-added carriers such as Telenet use leased circuits to provide data-base and related services.
- (vi) Applications have been approved for new international satellite carrier systems; similarly, approvals have been granted for new transatlantic cable ventures.⁶⁰

None of these new carriers can function without a link to a foreign carrier. Hence, U.S. approval is not sufficient for actual service. These networks – local, long-distance and international – are substantially free to offer all types of telecommunications services, under restrictions that include the following:

1. Although AT&T can *carry* other companies' electronic publishing or videotex communications, it may not provide its *own* information service until 1989.⁶¹
2. The BOCs may provide such services as their own information services only through fully separated subsidiaries.⁶²

59 See discussion in text at note 172 *et seq. infra*.

60 See discussion in text at note 174 *infra*.

61 W. BOLTER, *supra* note 25, at 178 *et seq.*

62 Davis, *supra* note 57, at 22.

3. Under the Cable Communications Policy Act of 1984, local telephone companies may provide cable television service only in »rural« areas, which a cable company would find too unprofitable to enter. They are however free to construct and lease back cable facilities to cable companies, as long as the local telephone companies do not control the systems' programming in any way.⁶³
4. Since local telephone companies' rates are regulated, an expansion of their service offerings is subject to regulatory scrutiny if it affects rates.
5. For local transmission, the situation is very much in flux. Some states have instituted rules to restrict local »bypass« in favor of the local-exchange telephone companies. Bypass occurs when an unregulated company uses any of the means discussed previously to provide services within a LATA without using the local public switched exchange.)⁶⁴ In several instances, *intrastate* long-distance service entry – that is, service between LATAs – is also restricted to entry by additional carriers under state rules. Many of these regulations are now subject to litigation.

In addition, certain geographical service restrictions apply. BOCs and other local telephone companies have exclusive franchises for public switched service in their geographic areas, though this exclusivity is being undermined *de facto* by various forms of bypass and shared tenant services. BOCs cannot offer long-distance or international service, while AT&T cannot provide local service. GTE has provided both local and long-distance services but must do so through separate entities.

Common carriage provides access rights to all users, including resellers that compete with a carrier. Local-exchange companies must grant access to all long-distance carriers, as long as they pay for access. By the middle of 1986, equal-quality access – i.e., equal availability of all long-distance carriers to all telephone users – was required to have been provided to all long-distance carriers;⁶⁵ in fact, equal access was still being implemented in late 1986. Customers indicate their »primary« carrier, to which domestic and international long-distance calls automatically are routed by a local exchange. A customer thus is connected directly to the long-distance carrier of its choice without having first to enter elaborate access codes, as was necessary in the past. Customers also can utilize private branch

63 47 U.S.C. § 613(b) Supp. (1985).

64 See discussion in text at note 55 *supra*.

65 E.g., S. SIMON, *supra* note 10.

exchanges to select a different long-distant carrier for each call according to a »least-cost-routing« computer, which chooses the least expensive carrier for each route.

A form of universal-service obligation requires common carriers to accept all customers who pay their bills. Local telephone companies also must serve customers in undesirable locations. State rules vary on the extent of this requirement.⁶⁶ A typical arrangement is for customers to get a certain connection distance (e.g., up to three utility poles or their equivalent) as part of the basic installation charge, with additional distance requiring an extra fee.

As a matter of law, the FCC and state agencies do not currently impose any absolute universal-service obligations. As a matter of practice, however, both AT&T and local-exchange companies effectively must serve all customers. Over the last century, their networks have expanded to cover virtually the entire country, and, under both federal and state law, they may not withdraw service without the prior approval of the FCC or the relevant state authority.⁶⁷ Since the FCC requires a carrier to make a relatively difficult showing of economic necessity before discontinuing service, carriers effectively are locked into serving their present areas – which for AT&T includes interstate service for virtually the whole country.

Reselling of domestic local and long-distance transmission is allowed and extensive. Indeed, carriers must sell even to carriers that compete with them. Recent trends include the sharing of bandwidth on satellite transponders, the reselling of local transmission by shared tenant services and competing coin and credit-card public telephones.⁶⁸

Resellers do not require an authorization from the FCC. They merely need to file a notification with the FCC if they hold themselves out to the public generally.⁶⁹ Where there is no such general offering – e.g., one bank reselling its surplus transmission capacity to another – no FCC filing at all is necessary.

Of particular importance are the rates for access to local-exchange networks by long-distance carriers. In the past, complex financial accounting rules (»separations and settlements«) arguably provided an internal subsidy from AT&T's long-distance service to the BOCs. Complicated FCC tariffs also governed the access charges paid by the OCCs. After divestiture, this system was revamped, with equal access charges for carriers to be phased in

66 *E.g.*, N.Y. Pub. Serv. Law § 92 (1979).

67 *E.g.*, 47 U.S.C. § 214(a) (1982).

68 *E.g.*, Universal Payphone, 58 P&F RR2d 76 (1985).

69 D. IRWIN, *supra* note 56, at II-38 *et seq.*

as equal access to the BOCs for non-Bell long-distance carriers was introduced.⁷⁰ Furthermore, a new system of customer access charges partially replaces carrier-paid access fees for the use of local-exchange networks. At least in theory, introduction of customer access fees forces all long-distance carriers to compete on an equal footing, since they are not subject to different charges for use of local-exchange facilities. (The FCC has allowed state commissions to waive consumer access charges, however, for low-income users.)⁷¹ Because of the extremely large amounts of money at issue to the carriers and because of redistributive impact of access fees, these fees have become a very controversial subject. For example, the OCCs fear that by being forced to pay the same as AT&T – compared to roughly half as much in the past – they will lose their price advantage with consumers and thus suffer market erosion. The OCCs contend that the BOCs' provision of better technical facilities to them does not justify equalization of access costs – particularly since implementation of equal access has been behind schedule.

Various other telecommunications charges are regulated. The BOCs' rates and terms are regulated by state commissions on the principle of rate-of-return regulation. Due to the dominance of the local-exchange companies in local residential distribution, deregulation of these charges is unlikely in the near future.

The principle of rate setting is to permit a »fair« return on invested capital at a rate comparable to investments of similar risk. Rates thus include revenues that – after allowance for operating expenses, depreciation and taxes – result in a fair profit.⁷² Because this return is aggregated, not every service or customer category need pay its share of costs and return on capital. Internal subsidies are common. For example, rates often are lower for rural than for urban users and for residential than for business users. Since rate setting is meaningless without a definition of the product, federal and state agencies also set service-quality requirements.⁷³

Where local exchanges face competition from bypassers, their rates will probably be deregulated as well. In domestic and international long-distance service, rate regulation is already on its way out. The OCCs need only file tariffs with the FCC stating their rates. Internationally, only AT&T (and the Hawaiian Telephone Company on some Pacific routes) are subject to rate regulation. Only »dominant carriers,« i.e., those with monopoly

⁷⁰ *Id.* at II-13 *et seq.*

⁷¹ Report and Order, 97 F.C.C.2d 834 (1985).

⁷² C.F. PHILIPPS, *THE REGULATION OF PUBLIC UTILITIES*, 331 *et seq.* (1984).

⁷³ *E.g.*, 47 C.F.R. Part 68 (1985).

power, must secure prior approval of their rates.⁷⁴ In practice, rate regulation is handled quite laxly. Domestically, the goal of regulating AT&T's rates has shifted from protecting users against monopolistic price increases to protecting competitors from predatory price reductions. Long-distance rate regulation is likely to disappear as the OCCs establish themselves.

At least at present, the Communications Act requires all charges for interstate common-carrier services to be just and reasonable.⁷⁵ Under the statute, the reasonableness of charges is subject to review by the FCC, which has the authority to prescribe just and reasonable charges and to order rebates and refunds of overcharges.⁷⁶ In order to establish the reasonableness of their rates, carriers must submit to the Commission schedules of their rates. In the past, these filings were voluminous in nature, containing complex technological and economic showings prepared by experts. In today's deregulated environment, they tend to be much less formal. Changes in rates must be submitted to the Commission and do not become effective until the FCC approves a proposed rate change or until ninety days after filing of the proposed change.⁷⁷ In practice, only AT&T must file tariffs with the Commission.⁷⁸

2. Private Networks

Over the last few years, large-volume users of data- and voice-transmission services increasingly have utilized private-line telephone facilities. These operations often totally bypass the BOC or other local-exchange facility by direct connections to the uplink and downlink satellite installations of interexchange carriers. For example major brokers in New York use private lines to connect Manhattan offices directly with satellite transmission facilities in New Jersey. The local BOC plays no role in linking the terminal equipment to the satellite facility and consequently derives no revenue from the transmission.

The OCCs' uplink and downlink facilities are regulated by the FCC as interstate common carriers. State agencies may regulate them only to the limited extent that they provide intrastate long-distance services. (The FCC's power to preempt state regulation was recently slightly reduced by

74 D. IRWIN, *supra* note 56, at II-38 *et seq.*

75 47 U.S.C. §§ 201, 202 (1982).

76 47 U.S.C. §§ 203, 204, 205 (1982).

77 47 U.S.C. § 203 (1982).

78 D. IRWIN, *supra* note 56, at II-38 *et seq.*

a Supreme Court decision.⁷⁹) A non-carrier uplink or downlink, however, is subject to no federal regulation beyond the requirement of securing a license under the Communications Act to use the radio-frequency spectrum. As yet, satellite transmission services have not been used for private-line purposes because of these systems' high construction and maintenance costs. (This does not include the use of satellites by cable television programmers, however, which might be considered a type of private-line activity.) These private systems would not be subject to state or federal regulation as common carriers since they do not hold themselves out to the public; they thus would be unregulated in every sense except for needing FCC licenses under title III of the Act.⁸⁰

3. *Closed User Groups*

Closed user groups are located conceptually somewhere between a single user's private network on the one hand and a reseller's public services on the other. Since both are almost totally deregulated (except for a few restrictions in several states concerning local service), closed user groups are unregulated in terms of charges, access and content. No licensing is necessary, except to the extent that over-the-air transmissions are involved. Liability is based on contractual provisions or general commercial law.

There is no right of access to join a closed user group. If a group restrained trade by refusing to allow a competitor to join a group deemed to be an »essential facility,« however, traditional antitrust principles would require it to grant access.⁸¹ Some closed user groups' provision of value-added services might turn out to be natural monopolies, that is, single-firm production will prove to be substantially less expensive than multi-firm production, and no segment of users will be exposed to lower-priced and loss-free entry. In those cases, antitrust prohibitions on discrimination against competitors may apply.⁸² For example, the Supreme Court prohibited the Associated Press from refusing to sell news to its members' competitors, because no practicable substitute for its news service existed.⁸³

Defining a closed user group is extremely slippery; no legal definition

79 Louisiana Pub. Serv. Comm'n v FCC, 106 S.Ct. 1890 (1986).

80 47 U.S.C. § 301 (1982).

81 United States v. St. Louis Terminal Ass'n, 224 U.S. 383 (1912).

82 L. SULLIVAN, *supra* note 13, at 125.

83 United States v. Associated Press, 326 U.S. 1 (1945).

exists. There are literally thousands of electronic bulletin boards and specialized data bases through which private and commercial users communicate with each other via computers. Users range from major banks to antique traders to baseball fans. Some operate with leased lines, while others use conventional local and long-distance telephone services.

4. *Domestic Carriers and International Communications*

The U.S. experience has been that pro-competitive forces are expansionary. Once competition is permitted, pent-up user demand and entrepreneurial suppliers provide new services.⁸⁴

The federal government has been more deregulatory than the states and has continuously expanded the scope of its primacy over the states by invoking the doctrine of federal preemption, that is, invalidation of state laws inconsistent with federal laws, even where the federal policy is abstention from regulation.⁸⁵ Perhaps the most significant case establishing federal primacy was *North Carolina Utilities Commission v. FCC*,⁸⁶ which authorized the FCC to preempt most state telephone regulation.

Although it lacks similar preemption powers in the international sphere and cannot act unilaterally, the FCC has not been highly flexible and has not striven for international harmonization. The Commission has rather sought deregulation of U.S. firms where unilateral action was at all practical and has hoped that market forces would take care of the details.

There is no statutory distinction under the Communications Act between domestic common carriers that provide transborder transmission services and carriers that do not. No special regulatory requirements apply to carriers with transborder as well as domestic transmission capabilities. Any communications common carrier operating within the United States is subject to state and/or federal regulation.

Because they are common carriers, if U.S. carriers provide international service, they must grant access to domestic customers, including resellers.⁸⁷ Under most foreign administrations' current policies, however, resellers would not be able to link up at the other end; the carrier rather

84 E.g., Henry, *The Economics of Pay-TV Media*, in VIDEO MEDIA COMPETITION 19 et seq. (E. Noam ed. 1985).

85 Noam, *Federal and State Roles in Telecommunications: The Effects of Deregulation*, 36 VAND. L. REV. 949 (1983).

86 537 F.2d 787 (4th Cir.), cert. denied, 429 U.S. 1027 (1976). See also supra note 79.

87 See discussion in text at note 58 supra.

than the reseller would be viewed as the authorized user. But since neither a U.S. carrier nor a foreign administration would necessarily know whether a reseller were using a leased line, unsanctioned resale might be impossible to detect and thus to prohibit.

A U.S. carrier obviously needs a foreign carrier counterpart. Although a variety of U.S. carriers may want to operate internationally, they cannot provide service without foreign local and long-distance distribution. Foreign administrations are wary of introducing competitive complexity into their international service; furthermore, transactions with multiple U.S. carriers may impose extra costs. For example, European arrangements with MCI appear to involve primarily traffic inbound from the United States. A minimum amount of inbound traffic must be generated by MCI before a PIT will install outbound transmission equipment.⁸⁸

Access of foreign carriers to the United States is affected by several restrictions:

1. Foreign entities may not own more than 25 % of U.S. local telephone companies and long-distance carriers.⁸⁹ There do not appear to be any restrictions against foreign companies owning a U.S. value-added network or reseller, unless it functioned as a common carrier. Through such resale, foreign carriers could distribute their service within the United States.
2. In order to serve U.S. customers, foreign carriers have to link up with a U.S. carrier for long-distance service – such as AT&T and the IRCs (the traditional partners) or the OCCs (newer partners). They presumably also would need to deal with a BOC or a bypass operator for local distribution, unless a customer had its own satellite downlink. From the U.S. perspective, the only restrictions (except for those discussed below) are on direct links to the BOCs, due to the prohibition against their providing long-distance service.⁹⁰
3. The nature of foreign carriers' communications links to the United States is governed by the Cable Landing License Act of 1921, which goes back to 19th-century agreements concerning telegraphic cable.⁹¹ That Act requires bilateral reciprocity for carrier access. In practice, this has led to an FCC policy of approving only half-circuit access for foreign carriers in order to guarantee the other half circuit for a U.S. carrier in

88 Remarks of Mr. William McGowan, president, MCI, before IDATE, Montpellier, France, Oct. 23, 1984.

89 47 U.S.C. § 310(a) (1985).

90 See discussion in text at note 54 *supra*.

91 47 U.S.C. § 234 (1982).

the reverse direction.⁹² Beyond trade reciprocity, the half-circuit policy also has technical reasons, since control of a full circuit by a foreign carrier from a country with a congested telephone system might create burdens on domestic U.S. networks. Conversely, the half-circuit arrangement gives foreign carriers an economic incentive to upgrade their domestic network capacity. Capacity differentials might not be at issue if U.S. carriers had full landing rights in a foreign country. The United States might treat this as adequate reciprocity and give a foreign carrier similar rights in the United States.

The development of overcapacity in international circuits is likely to affect U.S. international carriers' activities in the future. U.S. international communications needs are rising by about 15 % annually. But TAT-8, the new INTELSAT satellites, private satellites, private oceanic cable and regional satellite projects will add more capacity than is demanded; they thus may create a glut. The existence of excess capacity and of marginal costs substantially below average costs may lead to price wars. In that situation, some form of U.S. rate regulation or other restraint on pricing might reemerge.

5. *The Equipment Market*

The connection of terminal equipment to the interstate network is regulated by the Communications Act⁹³ and FCC regulations.⁹⁴ Part 68 of the FCC's rules sets minimum technical standards that equipment must meet in order to be connected to any public switched network.⁹⁵ The FCC's objective is to provide uniform interconnection standards to protect the telephone network from improper terminal equipment and wiring.

Because interconnection standards are uniform, terminal-equipment users have nondiscriminatory access to the telephone network. Equipment sellers must register their products, however, with the FCC before marketing them.⁹⁶ Registration requires the disclosure of a unit's technical specifications, allowing the FCC staff to identify any possible system degradation prior to installation of the equipment; there is no approval process to go through. Moreover, there is a national-security exception to the registra-

92 *E.g.*, Report and Order, 93 F.C.C.2d 701 (1983).

93 47 U.S.C. § 201 *et seq.* (1982).

94 47 C.F.R. Part 68 (1986).

95 47 C.F.R. § 68.2(a)(1), (2), (3), (4) (1986).

96 47 C.F.R. § 68.200 (1986).

tion requirement. If a federal agency certifies that compliance with registration procedures would jeopardize national-security interests, equipment may be connected to the network without publication of technical data. Part 68's objectives and the registration requirements are relatively recent developments in U.S. common-carrier policy. Prior to *Carterphone*,⁹⁷ AT&T and the OCCs developed their own interconnection standards and manufactured or procured equipment compatible with those standards. Competitive terminal-equipment suppliers had no access to the telephone network since users could connect only equipment leased from AT&T. The U.S. market for central-office (i.e., local-exchange) equipment was characterized in the past by a fairly competitive situation only in the procurement of equipment for independent telephone exchange companies and independent telephone companies – that is, non-AT&T companies. AT&T was precluded from that market, but – perhaps as a result – many other companies were active in it, including such foreign suppliers as Ericsson and Northern Telecom. On the other hand, the vast Bell system and all of its customers – comprising 80% of the total market – were foreclosed to other suppliers by the former's ties to the AT&T manufacturing subsidiary, Western Electric. The *Carterphone* case and subsequent liberal equipment-approval policies opened up customer terminal equipment to a large variety of suppliers.⁹⁸ Today, one can buy a telephone for as little as four dollars on a New York City street corner.

The AT&T divestiture radically changed the market for local-exchange equipment. By severing the link between the BOCs and AT&T, it freed the former from having to buy from Western Electric (now AT&T Technologies). (Until recently, AT&T also marketed equipment through its fully separated subsidiary, AT&T Information Systems, a relic from prior FCC attempts to deal with AT&T's market power through internal restructuring.⁹⁹)

Although most analysts expected the BOCs to cling to AT&T as their equipment supplier, they in fact have embraced a wide variety of non-AT&T equipment quite rapidly.¹⁰⁰ They are responsible to their state regulatory commissions to use the least expensive qualified supplier. In one instance involving equipment allegedly affecting defense communications, the Defense Department reportedly used pressure to influence a carrier not to buy non-U.S. equipment. Nevertheless, the opening of the U.S. market to

97 *Carterphone*, 13 F.C.C.2d 420, *recon. denied*, 14 F.C.C.2d 571 (1968).

98 *E.g.*, *Universal Payphone*, 58 P&F RR2d 76 (1985).

99 *E.g.*, *CCIA v. FCC*, 693 F.2d 198 (D.C. Cir. 1982).

100 *Computer World*, Mar. 14, 1984, at 63.

non-AT&T and foreign network equipment generally has been rapid. Network standards are coordinated for the BOCs by Bell Communications Research (Bellcor). There appears to be no sign that Bellcor is using this role to favor AT&T or other U.S. manufacturers. Neither the executive branch, the FCC nor the state commissions have shown a desire to set standards beyond those already in place.

Procurement of network equipment by local telephone companies is governed by their obligation to state regulators to pay the lowest possible prices. Pressure is on them to keep rates low because of the loss of subsidies from long-distance service.¹⁰¹ The ability to compare cost trends for the twenty-two companies also forces them to seek low-cost equipment. The »gold plating« (overcapitalization) of the past is unlikely to persist in today's environment.¹⁰² Because of the divestiture, the BOCs no longer have any incentive to increase Western Electric's profits, since none of those profits are returned to the BOCs.

The opening of the U.S. telecommunications equipment market to foreign suppliers has not been matched by a reciprocal opening of foreign markets to U.S. producers. The U.S. balance of trade in telecommunications equipment thus has become increasingly negative, even though U.S. manufacturers have begun to sell equipment in countries such as Japan.¹⁰³ One response to these developments has been the introduction of proposed federal legislation to require reciprocity; several bills slowly moved through the Congress.¹⁰⁴ The United States also has exerted pressure on Japan to lower its non-tariff barriers in equipment procurement. For example, the U.S. International Trade Commission ruled that a number of Japanese manufacturers had »dumped,« i.e., sold below cost, cellular car telephones in the United States.¹⁰⁵ The decision allows the U.S. Customs Service to increase duties on these manufacturers' products. Similar stresses are likely to develop with European countries as they increase their U.S. market share. As has been the case in the automotive industry, one response to this problem may be for foreign manufacturers to open plants in the United States. Apparently a number of major Japanese firms are considering this option.¹⁰⁶

101 See discussion in text at note 70 *supra*.

102 C.F. PHILLIPS, *supra* note 72, at 633 f.

103 Communications Week, Dec. 30, 1985, at 1, 18; Communications Week, Dec. 23, 1985, at 1.

104 Communications Week, Dec. 2, 1985, at 8.

105 Communications Week, Dec. 9, 1985, at 10.

106 Interview with Mr. Michael Lactorin, analyst, DAIWA Securities, Inc., in New York City, June 18, 1985.

6. Role of U.S. Antitrust Policy

On the software side, both AT&T and the BOCs are subject to a number of significant restrictions under both the MFJ and the FCC's *Computer III* decision.¹⁰⁷ AT&T may not offer »electronic publishing« on its own until 1989.¹⁰⁸ Although the reason behind choosing this particular period of time is less than clear, the Department of Justice and Judge Greene, after extensive argumentation by the publishing industry, were concerned that AT&T would drive burgeoning new companies out of the software business. Furthermore, the FCC required AT&T under *Computer II* from 1983 to 1986 to offer all »enhanced« telecommunications services – such as data processing or value-added networks – only through a structurally fully separated subsidiary. This restriction was later deleted, as discussed above.¹⁰⁹ Similarly, BOCs may not offer enhanced services at all, except through a »fully separated subsidiary,« that is, a corporation outside of the BOCs' legal control, and only with the prior approval of Judge Greene under the MFJ.¹¹⁰

This new competition on both ends of the equipment supply market is fully consistent with the traditional U.S. emphasis on enhancing competition through the antitrust laws. Section 2 of the Sherman Act imposes both civil and criminal liability on any type of monopoly activity, including monopoly.¹¹¹ Precisely for this reason, the 1956 Consent Decree was necessary to immunize AT&T from liability because of the »captive consumer« relationship between Western Electric and the BOCs – a relationship with both monopoly and monopsony characteristics. Although the Antitrust Division of the Department of Justice and the Federal Trade Commission have primary responsibility for enforcement of the U.S. antitrust laws, the FCC and the state commissions must give at least some consideration to the antitrust aspects of regulated firms' conduct.

The effect of the antitrust laws has changed substantially with the advent of deregulation. In the past, the existence of a regulatory scheme often was held by the courts to protect a firm from antitrust liability under the general rubric of »primary jurisdiction.« As will be discussed, this doctrine has a variety of different aspects. Its central rationale, however, is simply that

107 See discussion in text at note 33 *infra*.

108 *United States v. AT&T*, 1982-2 Trade Cas. (CCH) para. 73,116.

109 See discussion in text at note 33 *infra*.

110 1982-2 Trade Cas. (CCH) para. 73,118.

111 15 U.S.C. § 2 (1982).

a court should not hold a firm liable for engaging in governmentally sanctioned activities.

»Primary jurisdiction« includes at least four major doctrines: primary exclusive jurisdiction, true primary jurisdiction, statutory exemptions and agency immunizations.¹¹² Under primary exclusive jurisdiction, a court loses all power over a case, except the very limited ability to review any ensuing agency action. On the other hand, true primary jurisdiction gives an agency the initial opportunity to consider a legal issue or to find facts but reserves for the court the ultimate power to render a judgment. A statutory exemption is simply a congressional act that bars antitrust claims against particular industries. An agency immunization has virtually the same effect of removing potential liability but is not self-executing and must be secured from an agency. Statutory exemptions and agency immunizations thus are quite similar in terms of both policy and impact. On the state level, legislation often also creates antitrust immunity under the »state action« doctrine.¹¹³

The original statement of primary exclusive jurisdiction came in the context of protecting Interstate Commerce Commission tariffs from collateral attacks in state courts. The putative parent of the doctrine is *Texas & Pacific Railway v. Abilene Cotton Oil Co.*¹¹⁴ In fact, the Court there held only that an aggrieved shipper could not challenge the validity of a railroad's tariff filing with the Interstate Commerce Commission in state court but instead had to commence a proceeding before the Commission.

Statutory exemptions and agency immunizations create inherent problems with regulated industries since the theories behind regulation and antitrust are naturally antithetical. Although the basic regulatory and antitrust schemes evolved at roughly the same time toward the end of the nineteenth century, the Supreme Court has recognized very properly that they represent »two regimes.«¹¹⁵ Since administrative agencies often apply anticompetitive standards, statutory exemptions and agency immunizations may result in approval of anticompetitive conduct.¹¹⁶ Every such decision is thus at least potentially anticompetitive.

The easiest cases naturally are those in which the status of an agency's immunization power or of an industry's statutory exemption is clear. When

112 McGovern, *Types of Questions over Which Administrative Agencies Do Not Have Primary Jurisdiction*, 13 ABA ANTITRUST SECTION 57, 61 (1958).

113 *Parker v. Brown*, 317 U.S. 341 (1943).

114 204 U.S. 426 (1907).

115 *Pan American World Airways, Inc. v. United States*, 371 U.S. 296, 310 (1963).

116 *Hughes Tool Co. v. Trans World Airlines, Inc.*, 409 U.S. 363 (1973).

a court finds that an agency could not conceivably immunize a violation of the antitrust laws, the court need not consider whether the agency must pass on the conduct.¹¹⁷ Conversely, many industries operate under express statutory exemptions from the antitrust laws.¹¹⁸

The situation becomes infinitely more complicated, however, either where the scope of an exemption is unclear or where an implied exemption may exist. Congress is often deliberately or carelessly vague in its language. In this area of comparatively free decision, the courts have established virtually no standards at all. The Supreme Court occasionally has suggested that immunization power should turn on whether an agency's regulatory scheme is sufficiently »pervasive.« But the Supreme Court has vacillated in using even this general test, applying or ignoring it as it has wished in order to retain or relinquish judicial jurisdiction.¹¹⁹ The cases indicate that the Supreme Court tends to look to an agency's effectiveness in protecting some public interest other than competition.

True »primary jurisdiction« exists only where there is concurrent jurisdiction between a court and an agency. In this situation, the question is which tribunal will proceed first, rather than which tribunal will proceed.¹²⁰ To be sure, primary jurisdiction has some impact upon the outcome of a case; after all, if an agency uses its »expertise« to find facts, review under the substantial evidence rule will restrict a court's role greatly. (The substantial evidence rule prevents a court from reversing an agency unless the court finds that the agency made a clear and material mistake.) A court may well be able to refer a case in such a way, however, as to preserve unlimited review powers.

One of the less visible but increasingly tangible effects of deregulation has been to remove the traditional protections of the primary jurisdiction doctrine. As federal administrative agencies – particularly the FCC – have removed regulatory requirements, they have opened the door to new antitrust suits. Although no definitive statistical data exists, the sheer volume of antitrust litigation has increased substantially during the last few years, particularly in the telecommunications field.¹²¹ One factor naturally is the loss of many defenses or immunities. Another is the need for an alternative forum to resolve private disputes that deregulatory agencies refuse to handle.

117 See *Maryland & Virginia Milk Producers Ass'n v. United States*, 362 U.S. 458, 464-71 (1960); *United States Alkali Export Ass'n v. United States*, 325 U.S. 196, 204-06 (1945).

118 Walden, *Antitrust in the Positive State*, 41 TEXAS L. REV. 741, 767-88 (1963).

119 E.g., *United States v. Radio Corp. of Am.*, 358 U.S. 334, 348-51 (1959).

120 See Comment, *New Twists on Old Wrinkles: Primary Jurisdiction and Regulatory Accommodation with the Antitrust Laws*, 15 B.C. IND. & COMM. L. REV. 80, 93-94 (1971).

121 See C.F. PHILIPPS, *supra* note 72, at 670-83.

Also, there is the prospect of treble damages and attorneys' fees for a successful plaintiff in an antitrust case. Indeed, some executives at regulated firms have commented informally that they would prefer returning to the old regulatory rules rather than coping with the new antitrust regime.