ANTITRUST’S FUTURE IN LOCAL EXCHANGE MARKETS: An Economist’s View

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‘96 Telecom Act Restructures the Local Exchange Industry

- Imposes duties on ILECs to facilitate entry
  + interconnection, unbundling, resale, reciprocity
  + number portability, dialing parity, ROWs
- Lifts RBOC L.O.B. restrictions
  + interLATA entry after checklist satisfied
  + manufacturing, e-publishing permitted
- Ends cable-telco cross-ownership ban
- Ultimate Goal: create competitors

8/5/97  Annual ABA Meeting -- San Francisco, CA
The Act Redefines the Antitrust Turf

- Realigns antitrust responsibilities & powers
  - vacates three DOJ consent decrees
  - rollbacks FCC authority over mergers
  - encourages coordination among carriers
- Affirms place for usual antitrust authorities
- Rewrites the ‘Regulatory Contract’
  - Extreme Example: New Zealand

The New Regime Will Set Off An Antitrust Frenzy

- Litigation is just one of many competitive strategies
- Attractive alternative in current environment
  - ILEC dominance is premise for action
  - regulatory and legal uncertainty/ambiguity
    - fuzzy, overlapping jurisdictions
    - ambiguous orders, rulings
    - multiple objectives and criteria at the FCC
  - “state action” immunity likely unavailable
The New Regime (Cont’d)

- Deregulation and competition create conflict
  - number of carriers multiplies
  - complex transactions and relationships
  - sales of essential inputs to direct competitors
  - co-tenants on one carrier’s facilities
  - asymmetries
    - in carrier sizes
    - in regulatory treatment
- **Consequence**: more antitrust litigation

The Frenzy Has Already Begun

- **CLECs charge** *monopoly exclusion*
  - nonprice foreclosure
  - price squeezes
  - tying and bundling
  - raise rivals’ costs
- **ILECs charge** *unfair regulation*
  - takings
  - asymmetric treatment
Consolidation is in Full Swing

Among ILECs
- BA + NYNEX, Pac Tel + SBC

Among CLECs
- AT&T + McCaw Cellular
- MCI + Brooks Fiber
- Sprint + TCI + Cox Cable + Comcast
- Worldcom + MFS

And various combinations
- US West + TW + Continental, GTE + BBN
- all sorts of joint ventures, strategic alliances

Expect Much More Litigation

CLECs likely will claim that ILECs ...
- misappropriate proprietary information
- leverage their dominant market share
- impose vertical restraints

ILECs likely will respond that CLECs ...
- merely re-bundle network services
- purchase services far below cost
Economic Cost of This Litigation

- Misallocation of resources
  - distorted pricing, product and investment decisions
- Protracted delays
  - subject to legal procedure
  - arbitration = regulatory proceeding
- Uncertain outcomes
  - risk of jury trials, judicial decisions

Challenges Facing Courts and Regulators in Near Future

1. Distinguishing “conventional commercial practice” from monopoly abuse when one party is dominant
2. Balancing scale/scope economies against abuse of market power
3. Weighing investment disincentives from breaking regulatory contract against the deregulatory imperative
Challenges (Cont’d)

4 Assigning liability for service problems when there are multiple component suppliers
5 Discerning unearned monopoly profits in markets characterized by “network effects” (a.k.a. “demand-side scale economies”)
★ Need for efficient division of labor between courts and regulators based on expertise and institutions

Advice for Antitrust Authorities
After the Act

✔ Resist temptation to tailor decisions to the realization of actual local competition.
✔ Avoid structural remedies which defeat the intent of the Act.
✔ Articulate general principles that apply broadly, steering clear of imposing pricing, investment rules.
✔ Streamline enforcement: screen cases, tighten arbitration
Summing Up

◆ Act clarifies some antitrust confusion, but opens door to much litigation.
◆ Carriers will rationally turn to the courts for relief causing significant economic costs.
◆ Courts will face industry specific issues better dealt with by regulatory agencies.
◆ Regulators may be drawn into antitrust beyond their expertise.
◆ Success of local competition requires commitment to principles of the Act.