

WAYS OUT: RECONCILING INDUSTRY RESTRUCTURING AND COMPETITION*

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2003 MICH. ST. DCL L. REV. 625

My name is Russ Neuman. I am the Evans Professor of Media Technology at the University of Michigan—to be kept distinct from Michigan State. We have combined forces between Michigan and Michigan State and brought down some spring weather from Michigan to Washington today. Enjoy a Michigan spring today. We may foreshorten the schedule this afternoon and speed things up just a bit. I will probably bring this session to a conclusion fifteen minutes early or so and we will move on a little ahead of schedule to our second to last session and then a wrap-up by our conference hosts. Professor Shelanski was unable to join us because of impairment of travel. We will have two speakers today in this session. We are going to start having had all of the difficult questions raised and articulated this morning and by Congressman Upton at our presentation at lunch. We are now going provide all of the answers and turn to two distinguished analysts and scholars of the telecommunications marketplace. The first to speak on our panel will be Gerald Brock from George Washington University who is a graduate of Harvard University. He has three books now from Harvard University Press going back to his first published in 1981 that got a number of us started and gave us some real perspective on the Kingsbury Commitment and Vail's influence on the issues that we are confronting today as was highlighted in the presentations this morning. The issue is now that we are going to use Vail as an adjective, we need to work on how to change the proper name Vail into an adjective. There is Vailish. There is Vailed. My personal choice is Vailiant. With that in mind, our first forward-looking presentation, not backward-looking, by Gerald Brock.

* Remarks prepared for Fourth Annual Quello Communication Policy & Law Symposium, held in Washington, D.C., on February 27, 2003.

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I am going to make one comment on Gerald's remarks and then introduce the next speaker. We will save the questions and answers until after both of our presenters have presented. You were rewarded just now because we are going to obviously set off the afternoon with a very different perspective. All of our speakers, if they would agree on anything this morning, agreed on what we have to avoid is regulatory uncertainty. Gerald says, "No, no. Regulatory chaos is good for you." We have a new fresh perspective for the afternoon. In that spirit, I turn to Randy May who is a senior fellow and Director of Communications Policy Studies at the Progress and Freedom Foundation.

This has all been very complicated and challenging to you to put into perspective changes in law and technology and regulatory history. Gerald brings us back to think about the robber baron era and the railroads. Randy reminds us of computer one, two and three and the evolution of the current system. I am going to make it all real simple for you and give you Neuman's rule of thumb for interpreting all of these complexities. I will use the three examples that came up from this morning and our presentation right here. This morning it was argued by a bunch of lawyers, consultants, and analysts that what you want is regulatory certainty. What they really mean is what you want is regulatory uncertainty because if you are a lawyer or lobbyist it is the uncertainty of the mark of regulatory marketplace that enhances your value as somebody who is tracking this. Then Gerald comes up and said, "No. What you want is regulatory chaos." What he really means is, "No, you do not because you have to keep writing those books and adding that last chapter." He really means the opposite. Randy's exposition is that what you want is marketplace chaos. Just look at those books that Michael Porter writes at the Harvard Business School which say, "What you really want is a sustainable, competitive advantage." That is not market chaos at all, but a sustainable advantage over all of the other guys. Neuman's rule of thumb is: they mean exactly opposite of what they say. Now that I have made it all clear, let us open it up for questions and answers. We have microphones and we are recording, so if you would please call for a microphone if you have got a question or a comment and identify yourself.

Question from audience

Richard McClellan. I like Gerald Brock's views on the role of anti-trust in telecom as we go forward.

Gerald Brock

I would agree with Randy's last comment, if I understood it right, which is we should be moving increasingly toward reliance on anti-trust, rather than industry specific regulation. We have competitive problems in this industry as we move it as it is now largely in the mode, not fully competitive, but in the policy structure of aiming for competition. There is an increasing role for the anti-trust laws and perhaps they should use that as an explanation of my comment on chaos, lest it be misunderstood. I consider the anti-trust laws somewhat chaotic too. That is, there is no single overarching principle that you start with this and then you can work it all out. We have some broad ideas thoroughly developed, including by many people in this room, and then we actually apply them to individual cases and controversies as they come up. We have been able to use that fairly effectively as competition policy and unregulated industries. It has clearly played a major role in communications already over many years. It should be increasingly relied upon as the primary intellectual reasoning and legal enforcement for competitive problems in the industry.

Question from audience

Steve Wildman. My question is directed towards what I perceive Gerald as saying, regulatory chaos is a good thing. It seems to me that regulatory chaos, as I interpret this, is a good thing because it arises, according to your examples, from dynamics and light industry, it creates uncertainty. Therefore, regulation has become out of whack, inconsistent with what is actually taking place. You are always a step or more behind. It is another thing to say that regulatory chaos is a principle that we should articulate and espouse, that we should create it. It seems in that case what you are doing is creating the problems that were complained about this morning. That it creates uncertainty for investors, you do not know what to do. Is my interpretation correct or are you actually advocating a principle regulatory chaos?

Gerald Brock

Your interpretation is correct. The one qualification that I might make is that I also have been in the position of having people come and say, "All I want is certainty. I do not really care what is done, I just want certainty. But, the certainty that I want is, move it this direction." Everybody wants certainty in their favored direction and I have never met a lobbyist yet that wanted to say, "If you would just guarantee that there is no movement, we would be completely happy. Leave everything else fixed and just move the part that I

want to move.” There is clearly a value of certainty, but my point is we cannot have complete certainty and complete freedom to innovate. Whether that be in the industry structure that we are allowing, or in the regulations that we are doing so that the price of rapid technological progress is going to have some inconsistency. Chaos is a strong word. I used that to try and get people’s attention. Really it is more that we cannot have a consistent, overarching framework, except by forcing things into that framework and limiting anybody stepping outside of it.

Question from audience

Steven Wildman. If I could just follow that up then. You view the chaos that comes from market dynamics as being a good thing, then would you have recommendations for policies that would be consistent with this lagging regulatory structure and market dynamics?

Gerald Brock

Yes, the overarching recommendation is to make regulation as little as possible, because it is always going to be backward-looking. It is built into the legal system. It is built into the way that we do things for two quite distinct reasons. First, that regulators, whoever they may be, cannot properly foresee the future. Secondly, even in so far as they do, it is very difficult to act on that. You have to get a record and work on things that are largely in the past. We work in regulatory terms with problems that have come up in the past. In my view, the Telecommunications Act of 1996¹ was primarily driven by an effort to neaten up problems that arose from the divestiture and all of the arguments about restrictions on the companies and so forth. About the time we solved the divestiture problems of 1984, now we are into internet and it was not looking at internet at all. The only broad principle I can draw from that is as little intervention as is feasible, which is why I would emphasize things in a transitional measure. Some things need to be changed. Spectrum reforms are a critical one. Whether you are looking forward or backward, we have got problems there. I would agree with Randy’s comment on limiting the unbundled network elements and thinking of them as a transition, and perhaps even at the moment have some transitional issues that have to be dealt with in a regulatory manner.

1. Pub. L. No. 104-104, 110 Stat. 56 (codified as amended in scattered sections of 15, 18, and 47 U.S.C.).

Question from Audience

My name is Rick Coy and I am a telecommunications lawyer in Michigan. My question goes to whether the post 1996 Act paradigm is working. We have many states now that have declared by virtue of recommending section 271² approval that their incumbent's local exchange markets are irrevocably open to non-discriminatory competition. Yet, we do not have any material competition by a regional Bell operating company and another Bell operating company's region that has been declared to be open. I would like to have your comments on why that is, what you think it will take, and whether it will ever occur under the current paradigm?

Randolph May

I am going to avoid a direct answer to your question a little bit. One thing that I did want to say more explicitly, when I said that competition was developing in all of these markets including local, I do feel strongly that so called intermodal competition is important. I would bet that ninety percent of the people in this room have one of these things in our pocket right now [displaying his cell phone]. We have them to make local telephone calls. Where cable companies have started to provide telephony, in some places they are going gang busters. That is competition. When we send e-mails, that is competition. That is competition in the same marketplace. Maybe not carrier pigeons, but e-mails, yes. In terms of why the regional Bell operating companies (RBOCs) have not gone into each others regions, I just think that they are probably afraid. Maybe they think that if they do not go there, the other one will not come into my market. I am not confident that in ten years the RBOCs are going to be around with all of these developments. That is not the test of whether the 1996 Act could work. Look at what is out there in the marketplace. When you do that, especially on an intermodal basis, competition is arriving quite quickly.

Gerald Brock

I have a brief comment on that one. My answer would be yes, it is working. That is because I had very modest expectations for it in the first place. It was not in any sense a revolutionary act. It was effectively formalizing what was already going on in state commissions at that time with regard to local competition and then saying, "Here are some conditions to get

2. 47 U.S.C. § 271 (2000).

out from under the manufacturing restrictions.” In that sense, it is working. No, not everything is wonderful, but especially since so much of it has been implemented at the state level and will continue to be now with the most recent Federal Communications Commission (FCC) decisions. We have not changed all that much from what would have happened if we had simply developed under state by state arrangements without ever passing the Act.

Russell Neuman

Please join me in giving a hand to our intrepid panelists.