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THE COMMUNICATIONS REGULATORY ENVIRONMENT IN THE 1980'S†

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Four major political and legal institutions are simultaneously affecting the communications regulatory environment of the 1980's: the Federal Communications Commission (FCC), Congress, the Department of Justice (DOJ), and the courts. The FCC recently concluded in its *Computer Inquiry II*[1] that all enhanced services and most interstate customer premises equipment (CPE) should be detariffed. Also, dominant carriers will be permitted to offer enhanced services and CPE only through a totally separate, unregulated subsidiary.[2] Congress nearly enacted the Communications Act Amendments of 1980 which would have required dominant concerns to offer enhanced services and CPE through a separate subsidiary, as well as effecting several other changes in the communications regulatory environment. Congress is continuing to study this area.[3] The third, and at present the most important, factor in the communications industry relates to the *United States v. AT&T* antitrust set-

1. This refers to an examination of the communications industry begun by the FCC in 1976. *See infra* notes 46-47 and accompanying text. *See also* Amendment of Section 64.702 of the FCC's Rules and Regulations, 77 F.C.C.2d 384 (1980), *modified on recon.* 84 F.C.C.2d 50 (1980), *further recon.* 86 F.C.C. 512 (1981), *appeal pending sub nom.* CCIA v. FCC, No. 80-1471 (D.C. Cir. 1980).

2. *See* G. BROCK, THE TELECOMMUNICATIONS INDUSTRY (1981). *See generally* Trebing, *Common Carrier Regulation—The Silent Crisis*, 34 LAW & CONTEMP. PROBS. 299 (1969) (contains an excellent and concise legal history of telecommunications in the United States).

3. S. 2827, 96th Cong., 2nd Sess. (1980).

tlement.[4] The parties have agreed on a divestiture plan in which the twenty-two Bell Operating Companies (BOCs) will be divested into seven separate companies, with AT&T retaining Bell Labs, Long Lines, Bell Headquarters, and Western Electric.[5] The legal structure of the communications regulatory environment in the 1980's will remain in a state of flux while the structure and role of the parent AT&T and the BOCs are refined within these four legal areas.

This Article presents a brief discussion of the history of the 1934 Communications Act followed by analyses of the FCC's *Computer Inquiry I*[6] and *Computer Inquiry II*. The congressional response to the changing communications technology will then be briefly examined. Finally, the interrelationship between the FCC decisions and the *United States v. AT&T* settlement[7] will be analyzed, followed by a general discussion of future trends in the communications industry based on the emerging legal environment.

I. HISTORICAL PERSPECTIVE

A. THE 1934 COMMUNICATIONS ACT

The Federal Communications Act of 1934[8] established the Federal Communications Commission (FCC) and empowered this regulatory agency with both rulemaking and adjudicatory authority. Under the 1934 Act, Congress outlined the basic rules for governing

4. 47 Fed. Reg. 4166 (1982). *See infra* notes 186-257 and accompanying text.

5. *Id.*

6. *See infra* notes 34-45 and accompanying text.

7. *See supra* note 4.

8. 47 U.S.C. §§ 151-55 (1976 & Supp. IV 1980). Section 151 explains that the FCC was created "[f]or the purpose of regulating interstate and foreign commerce in communication by wire and radio so as to make available, so far as possible, to all the people of the United States a rapid, efficient, nation-wide, and world-wide wire and radio communication service with adequate facilities at reasonable charges . . . ." *See* Berman, *Computer or Communications? Allocation of Functions and the Role of the Federal Communications Commission*, 27 FED. COM. L.J. 161 (1974); Davison, Babcock & Lesley, *Computers and Federal Regulation*, 21 AD. L. REV. 287 (1969).

The Supreme Court has recognized the FCC's broad authority. *See* United States v. Southwestern Cable Co., 392 U.S. 157, 167-69 (1968). The FCC had requested legislation to regulate the Community Antenna Television System (CATV), but no legislation was enacted. The legislators responded to the FCC's request by saying that the determination of jurisdiction was left to the courts. The FCC gradually exercised jurisdiction and subsequently issued revised rules for regulating CATV. The Court held that "the authority which we recognize today under § 152(a) is restricted to that reasonably ancillary to the effective performance of the commission's various responsibilities for the regulation of television broadcasting." Quoting 47 U.S.C. § 303(4), the Court further held that the FCC has the authority "to issue such orders as necessity requires." 392 U.S. at 178.

interstate and foreign wire and radio communications.[9] Interstate telephone service was established as a nationally regulated monopoly, but intrastate telephone operations remained subject to regulation by state public utilities commissions. Telephone companies were declared to be communications common carriers; these are firms which are regulated and which provide communications services to the public pursuant to a tariff.[10] Tariffs, or rates, are established through a procedure in which a regulated common carrier requests approval of its tariff proposals. The appropriate regulatory authority approves a tariff which affords the common carrier an opportunity to achieve a fair rate of return on its invested capital. This process provides a substitute for market forces which, in theory, regulate a competitive industry composed of many firms offering and buying the same or similar goods or services.

B. THE *1956 WESTERN ELECTRIC CONSENT DECREE*

Before examining the cases leading up to *Computer Inquiry I* and *Computer Inquiry II*,[11] an overriding, salient fact should be noted. Under the *1956 Western Electric Consent Decree*,[12] the Bell System was prohibited from offering, even through a separate subsidiary, any device that possessed the capability to perform a data processing function. The Bell System was also foreclosed from any

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9. 47 U.S.C. § 153 (1976). Section 153(a) provides that:

> "wire communication" or "communication by wire" means the "transmission of writing, signs, signals, pictures, and sounds of all kinds by aid of wire, cable, or other like connection between the points of origin and reception of such transmission, including all instrumentalities, facilities, apparatus, and services (among other things, the receipt, forwarding, and delivery of communications) incidental to such transmission."

Id.

Section 153(b) similarly defines radio communications as "transmission by radio or writing, signs, signals, pictures, and sounds of all kinds, including all instrumentalities, facilities, apparatus, and services (among other things, the receipt, forwarding, and delivery of communication) incidental to such transmission."

10. *See* 74 AM. JUR. 2d *Telecommunications* §§ 4-6 (1974); 86 C.J.S. *Tel. & Tel. Radio & Television* §§ 5-7 (1954).

11. *Computer Inquiries I* and *II* will be discussed in text accompanying *infra* notes 34-47.

12. The defendants were each:

> enjoined and restrained from commencing, and after three (3) years from the data of this Final Judgment from continuing, directly or indirectly, to manufacture for sale or lease any equipment which is of a type not sold or leased or intended to be sold or leased to Companies of the Bell System, for use in furnishing common carrier communications services, except equipment used in the manufacture or installation of equipment which is of a type so sold or leased or intended to be sold or leased. . . .

1956 Trade Cas. (CCH) ¶ 68,246.

direct or indirect activity in an unregulated market.[13] One interesting point is that the FCC, in establishing the legal distinction between data processing and communications, was in effect defining the limits of the *1956 Western Electric Consent Decree*. Thus, by indirect action, the FCC delineated the boundaries of the communications industry within which the Bell System could operate. If the FCC classified a data processing service or product as a communications service or product, then AT&T was able to offer the service or product under tariff. Consequently, the objective of the *1956 Western Electric Consent Decree*, which was to prohibit AT&T from entering the data processing industry, was thwarted.[14]

C. Early Cases

In 1956, the distinction between communications and data processing was relatively well-defined. But because of advances in communications and computer technologies made after 1956, the distinction between communications and data processing has changed.[15] Until these technological advances were made, AT&T offered end-to-end communication service. These technological developments gave rise to numerous cases involving the interaction of communications and computers in which the Bell System end-to-end service was challenged.

1. The Hush-a-Phone *Decision*

Hush-a-Phone Corp. v. United States[16] tested the legality of the tariff prohibiting all foreign attachments to the phone system. Hush-a-Phone manufactured and sold a device that when attached over the speaker of a telephone enabled the person speaking into the phone not to be overheard by third parties near the speaker. After the sale of numerous devices, various telephone companies threatened to suspend or terminate service to subscribers who con-

13. Under the *1956 Consent Decree*, AT&T was "enjoined and restrained from engaging, either directly, or indirectly through its subsidiaries other than Western and Western's subsidiaries, in any business other than the furnishings of common carrier communications services. . . ." *Id.*

14. *See AT&T's Access to New Markets Backed by Court*, Wall St. J., Sept. 8, 1981, at 1. *See also Judge Widens AT&T Business Scope*, Wash. Post, Sept. 5, 1981, at C-7. Judge Vincent P. Biunno of the United States District Court for the District of New Jersey ruled September 4, 1981, that the FCC's 1980 Ruling on Competition and the *1956 Consent Decree* did not conflict. Judge Biunno, ruling on the March 1980, request of AT&T that he interpret the *1956 Consent Decree*, held that enhanced services could be offered by AT&T because it is a communications service.

15. *See* Bylinsky, *The Second Computer Revolution*, Fortune, Feb. 11, 1980, at 230-32; *The Computer Society, A Special Section*, Time, Feb. 20, 1978.

16. Hush-a-Phone Corp. v. United States, 238 F.2d 266 (D.C. Cir. 1956).

tinued to use Hush-a-Phone based on the FCC tariff prohibiting foreign attachments. The FCC had concluded that the use of devices such as Hush-a-Phone was "deleterious to the telephone system" and would result in a general degradation of quality service.[17] On appeal, the decision was reversed and remanded to the FCC. The Court of Appeals for the District of Columbia stated that the tariff was "unwarranted interference with the telephone subscriber's right reasonably to use his telephone in ways which are privately beneficial without being publicly detrimental."[18] On remand, the FCC invalidated the tariff prohibiting foreign attachments, but only as the related to Hush-a-Phones.

2. The Carterphone *Decision*

Another early case involved the Carterphone Corporation's production and sale of a radio transmitter that would automatically switch on when the user was speaking and then would return the radio to receiving status when the speaker was finished. By connecting this device to the telephone system, a user was able to call any point on the telephone system from a remote radio.[19] After the sale of several thousand of these devices, common carriers claimed that the use of Carterphones on the telephone network was prohibited under the tariff prohibiting foreign attachments. Carterphone Corporation filed a private antitrust suit against the telephone companies to invalidate the tariff on antitrust grounds.[20] The court ruled that the FCC had primary jurisdiction and therefore referred the case to the FCC.[21] The FCC's hearing examiner approved the Carterphone radio transmitter for use on the telephone network, and he ordered the carriers to change their tariffs to allow the use of the Carterphone device.[22] On appeal the FCC, without a hearing, affirmed the decision of its hearing examiner and broadened the hearing examiner's decision to include all harmless attachments provided by customers.[23] The Bell and General Telephone (GTE) systems appealed the FCC's decision, but the appeal was later with-

17. Hush-a-Phone Corp. v. American Tel. & Tel. Co., 20 F.C.C. 391, 420 (1955).

18. Hush-a-Phone Corp. v. United States, 238 F.2d 266, 269 (D.C. Cir. 1956). *See* Smith, *Storming the AT&T Fortress: Can the FCC Deregulate Competitive Common Carrier Services?*, 32 FED. COM. L.J. 205, 221 (1980).

19. There was no electrical connection between the AT&T equipment and the Carterphone.

20. Carter v. American Tel. & Tel. Co., 250 F. Supp. 188 (N.D. Tex.), *aff'd*, 365 F.2d 486 (5th Cir.), *cert. denied*, 385 U.S. 1008 (1966).

21. *Id.* at 189.

22. Use of the Carterphone Device in Message Toll Telephone Service, 13 F.C.C.2d 430 (1967) *recon. denied*, 14 F.C.C.2d 571 (1968).

23. *Id.*

drawn when the parties settled out of court.[24]

After World War II, microwave communications grew slowly, and the FCC generally assigned frequencies to common carriers and to government agencies. By the 1950's, numerous corporations were applying for licenses to operate their own microwave systems.[25] In 1957, the FCC consolidated all the applications, and over the objection of common carriers changed its "no entry" policy to allow private firms entry into the microwave field.[26] Each applicant was assigned a portion of the radio spectrum above 890 millicycles. The private applicants, however, were not allowed to share facilities or use of a microwave system among themselves. If permitted to share facilities or use of a microwave system, groups of applicants (each not needing the entire capacity) could have combined together to provide themselves with a total microwave system. This combined microwave system would have been a major unregulated carrier in competition with the existing regulated common carriers. Even without the ability to combine and share a microwave communications system, however, each individual applicant posed an economic threat to the existing carriers. Consequently, those regulated common carriers reacted defensively to protect their shares of the communication revenues by applying for new service offerings with drastically reduced long distance rates.[27]

3. The MCI Dispute

In 1964, Microwave Communications, Inc. (MCI) applied to the FCC for permission to provide low cost voice and data communications links between urban centers. Substantial price reductions, as compared to the common carriers' rates, were proposed. Consumers would also have been granted complete flexibility in using the terminal equipment on an unqualified sharing of lines. Thus, a consumer needing only a portion of the MCI offering could purchase the service and resell what was not needed. In many instances, this sharing of lines would afford each customer substantial savings over AT&T's costs for similar lines on a nonshared basis. The FCC's hearing examiner approved a limited MCI application connecting

24. *See* Walker, Mathison & Jones, *Data Transmission and the Foreign Attachment Rule*, 16 DATAMATION, Feb. 1969, at 60.

25. *See* G. BROCK, THE TELECOMMUNICATIONS INDUSTRY 180-87, 198-210 (1981).

26. Allocation of Frequencies In the Bands Above 890 Mc, 27 F.C.C. 359 (1959), *recon. denied* 29 F.C.C. 825 (1959).

27. *See* American Tel. & Tel. Co., 37 F.C.C. 1111 (1964), *aff'd sub nom.* American Trucking Assn. v. FCC, 377 F.2d 121 (D.C. Cir. 1966), *cert. denied*, 386 U.S. 943 (1967). *See also* Note, *Regulation of Computer Communications*, 7 HARV. J. ON LEGIS. 208 (1970).

Chicago and St. Louis. In affirming the hearing examiner, the Commission stated that the proposed service by MCI would meet a significant unfilled communications need.[28]

After the initial MCI application was granted, other applicants petitioned the FCC for construction of commercial microwave systems. After realizing that it was faced with a general licensing question, the FCC in 1970 grouped together several of the applications.[29] Over the objections of the regulated common carriers, in 1970, the FCC established a policy of approving individual applications.[30] Subsequently, the FCC approved the application of numerous companies wanting to offer commercial microwave services.[31] In a defensive response, the existing communications common carriers announced plans to construct nationwide digital data networks.

4. The Bunker-Ramo Dispute

While the MCI dispute was in progress, a dispute arose between Bunker-Ramo Corporation (an unregulated firm) and AT&T, Bunker-Ramo had previously provided a national stock quotation service on lines leased from AT&T. But in 1965, Bunker-Ramo included a buy-sell provision in its service offering so that brokers using the stock quotation service could also transact business. AT&T contended that the additional service proposed by Bunker-Ramo was within its traditional communications monopoly. Consequently, Bunker-Ramo was denied access to the necessary communications lines. Bunker-Ramo finally withdrew its "message-offering" petition. Then in 1967, Western Union, which was substantially regulated by the FCC, filed a tariff which would provide the same service that Bunker-Ramo had requested to provide. The Western Union tariff

28. Applications of Microwave Communications, Inc., 18 F.C.C.2d 953 (1969), *recon. denied*, 21 F.C.C.2d 190 (1970).

29. Establishment of Policies and Procedures for Consideration of Applications to Provide Specialized Common Carrier Services in the Domestic Public Point-to-Point Microwave Radio Service and Proposed Amendments to Parts 21, 43 and 61 of the Commission's Rules, 24 F.C.C.2d 318 (1970).

30. Establishment of Policies and Procedures for Consideration of Applications to Provide Specialized Common Carrier Services in the Domestic Public Point-to-Point Microwave Radio Service and Proposed Amendments to Parts 21, 43 and 61 of the Commission's Rules, 29 F.C.C.2d 670 (1971), *aff'd sub nom.* Washington Util. & Transp. Comm'n v. FCC, 513 F.2d 1142 (9th Cir. 1975), *cert. denied sub. nom.* National Ass'n of Regulatory Util. Comm'rs v. FCC, 423 U.S. 836 (1975). *See* Smith, *Storming the FCC Fortress: Can the FCC Deregulate Competitive Common Carrier Services?*, 32 FED. COMM. L.J. 205, 223 (1980).

31. Comment, *Federal Communications Regulation of Domestic Computer Communications: A Competitive Reformation*, 22 BUFFALO L. REV. 947 (1973).

was approved over the objection of Bunker-Ramo.[32]

These early cases penetrated AT&T's end-to-end service monopoly. The FCC had allowed Hush-a-Phone to enter the limited mechanical phone attachments market, Carterphone to connect (although non-electrically) with the phone system, and MCI to establish voice and digital communications service between major cities. Thus, even though the FCC had not permitted Bunker-Ramo to establish a message-switching service in addition to its stock-quotation service, a major shift in FCC regulatory philosophy had occurred.[33] Based on this new FCC policy of free entry, both regulated communications common carriers and some nonregulated communications carriers were permitted to compete for parts of the communications traffic which had previously been in the exclusive domain of AT&T in its end-to-end communications service offerings.

II. *COMPUTER INQUIRY I*

Against this backdrop of rulings, the FCC determined that a full examination of the computer and communications interface was needed. In 1966, the FCC initiated an Inquiry (hereinafter *Computer Inquiry I*) designed to answer the following two questions:

1. Under what circumstances should data processing, computer information, message switching, or any particular combination thereof, be deemed subject to regulation pursuant to the provisions of the Communications Act?

2. Would the policies and objectives of the Communications Act be served better by such regulations or by such services evolving in a free, competitive market; and, if the latter, would changes in existing provisions of the law or regulations be needed?[34]

A. THE FCC'S *FINAL DECISION*

The FCC received over 3,000 pages of correspondence and submitted these responses to the Stanford Research Institute (SRI) for analysis.[35] In its *Final Decision*, the FCC made three major rulings:

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32. Western Union Tel. Co., 11 F.C.C.2d 1 (1967).

33. *See* Comment, *Computer Services and the Federal Regulation of Communications*, 116 U. PA. L. REV. 328 (1967). *See also* Smith, *Interdependence of Computer and Communications Services and Facilities: A Question of Federal Regulation*, 117 U. PA. L. REV. 829 (1969).

34. Regulatory and Policy Problems Presented by the Interdependence of Computer and Communications Services and Facilities, 7 F.C.C.2d 11, 17 (1966) (Notice of Inquiry). An additional issue relating to privacy was originally raised, but it was later dismissed as being beyond the jurisdiction of the FCC.

35. Dunn, *Policy Issues Presented by the Interdependence of Computer and Com-*

(1) it retained broad jurisdiction over those aspects of the computer industry relating to communications; (2) it decided that common carriers could not favor their own affiliates if they chose to enter the data processing industry; and (3) it established the principle of maximum separation so that the data processing affiliates were to be totally separated from their parent common carriers.[36]

In deciding to regulate the communications aspects of the data processing industry, and thereby limit AT&T to communications offerings only, the FCC was forced to define the difference between data processing and message switching. "Data processing" was defined as:

> the use of a computer for the processing of information as distinguished from circuit or message-switching. "Processing" involves the use of the computer for operations which include, *inter alia*, the functions of storing, retrieving, sorting, merging, and calculating data, according to programmed instructions."[37] "Message switching" was defined as follows: "the computer-controlled transmission of messages, between two or more points, via communications facilities, wherein the content of the message remains unaltered."[38]
>
> The FCC further refined the difference between message switching and data processing by defining "hybrid data processing service" and "hybrid communications service." These two categories were defined as follows: "(i) Hybrid Data Processing Service is a hybrid service offering wherein the message-switching capability is incidental to the data processing function or purpose;" and "(ii) Hybrid Communications Service is a hybrid service offering wherein the data processing capability is incidental to the message-switching function or purpose."[39] The overall effect of the data processing definition was that firms whose primary thrust was data processing would not be regulated. The FCC assumed that communications common carriers would police the line between hybrid data processing and hybrid communications.[40]

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munications Services, 34 LAW & CONTEMP. PROBS. 369 (1969); Dunn, *the FCC Computer Inquiry*, 15 DATAMATION, Oct. 1969, at 71.

36. Regulatory and Policy Problems Presented by the Interdependence of Computer and Communication Services and Facilities, 28 F.C.C.2d 291 (1970) (Tentative Decision); 28 F.C.C.2d 267 (1971) (Final Decision), *recon. denied*, 34 F.C.C.2d 557 (1972). *See* B. GILCHRIST & M. WESSEL, GOVERNMENT REGULATION OF THE COMPUTER INDUSTRY 70 (1972); Note, *The FCC Computer Inquiry: Interface of Competitive and Regulated Markets*, 71 MICH. L. REV. 172 (1972).

37. 28 F.C.C.2d at 287; 47 C.F.R. § 64.702(a)(1) (1973).

38. *Id.* § 64.702(a)(2).

39. *Id.* § 64.702(a)(5).

40. 28 F.C.C.2d at 274. *See* Berman, *Computer or Communications? Allocation of Functions and the Rule of the Federal Communications Commission*, 27 FED. COM. L.J. 161 (1974).

B. *GTE Service v. FCC*

After exhausting administrative procedures, the communications common carriers appealed the FCC's decision in *Computer Inquiry I*. *GTE Service Corp. v. FCC*[41] affirmed the authority of the FCC to regulate communications common carriers who entered the data processing field, but held that the FCC could not regulate data processors who merely used communications networks. Furthermore, the court upheld the FCC's requirement that communications common carriers entering the data processing industry establish a totally separate data processing subsidiary.[42] However, the attempt by the FCC to prohibit the separate subsidiary from using the parent company's name was invalidated. Consequently, the separate subsidiary could obtain the goodwill benefits of its parent's name. Also, carriers were permitted to purchase data processing services from their separate subsidiaries.

C. Post *Computer Inquiry I* Developments

In the 1960's and 1970's, communications and computer technologies advanced even more rapidly.[43] The data communications equipment section has been at the forefront of this technological advancement, and data communications technology has attained a high degree of specialization. Front-end computers dedicated solely to communications functions act as buffers between powerful mainframes and intelligent communications networks and perform many sophisticated functions including line control, character and message switching and handling, conversion of data and protocols, error control, message editing, and message queuing.[44] Computer mainframes, relieved of these communications functions, can specialize on various data processing functions. Given these technological developments, the legal distinction between data processing and message switching which the FCC had carefully established in *Computer Inquiry I* became "technologically outdated."[45]

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41. GTE Service Corp. v. FCC, 474 F.2d 724 (2d Cir. 1973), *decision on remand*, 40 F.C.C.2d 293 (1973).

42. Note, *Federal Communications Commission—Review of Regulations Relating to Provisions of Data Procession Services by Communications Common Carriers—GTE Service Corp. v. FCC*, 15 B.C. Indus. & Com. L. Rev. 162 (1973).

43. *See generally* Frank, *Alive and Well*, 26 Datamation, June 1980, at 112.

44. *Id.* at 112, 114.

45. *See* Wiley, *Competition in Telecommunications*, 47 Antitrust L.J. 1283, 1285 (1979).

III. *COMPUTER INQUIRY II*

Based on these technological developments and the realization that the demarcation points between data processing, hybrid categories, and communications defined in *Computer Inquiry I* were no longer technically valid, the FCC initiated *Computer Inquiry II*.[46] In *Computer Inquiry II*, the FCC asked the industry for comments and new definitions dealing with data processing functions.[47]

A. DATA-SPEED 40/4 CONTROVERSY

As the FCC initiated *Computer Inquiry II*, AT&T announced it would offer the Data-Speed 40/4 communications terminal as a tariffed communications item. However, many terminal manufacturers believed that the Data-Speed 40/4 was a "smart" data processing terminal, and pursuant to *Computer Inquiry I*, only properly offered through a separate subsidiary. The opponents of AT&T were really arguing that the Data-Speed 40/4 was a major entrance by AT&T into the data processing industry. The *1956 Western Electric Consent Decree* had prohibited AT&T from offering data processing equipment or services. The Chief of the FCC Common Carrier Bureau agreed with the competitors of AT&T. The FCC, however, ultimately disagreed, and it determined that the Data-Speed 40/4 could be offered by AT&T as a tariffed item.[48] The Second Circuit Court of Appeals upheld the decision of the FCC.[49] As a result of the Data-Speed 40/4 dispute, an additional notice to the *Computer Inquiry II* was issued to deal specifically with the problem of terminals possessing communications and data processing capabilities.[50] Comments were also sought as to whether customer premises

46. *See* Amendment of Section 64.702 of the FCC's Rules and Regulations, 61 F.C.C.2d 103 (1976) (Notice of Inquiry and Proposed Rulemaking).

47. *Id.* The FCC acknowledged the "technological advances, in hardware and software, which are tending to cause a blurring of the distinctions between data processing and communications. . . . In particular, the dramatic advances made in large scale integrated circuit technology, . . . minicomputers, microcomputers, and other special purpose devices. . . ." 61 F.C.C.2d at 103.

48. American Tel. & Tel. Co., 62 F.C.C.2d 21 (1977). The initial vote by the FCC was tied, but the FCC finally voted that the Data-Speed 40/4 was properly classed as a tariffed communication item.

49. IBM Corp. v. FCC, 570 F.2d 452 (2d Cir. 1973). In interpreting Section 203(a) of the 1934 Communications Act, the court held that the FCC's classification of a complex of small machines with communicative capacity to send and receive messages from a central computer as "communications" as opposed to "data processing" was not improper.

50. Amendment of Section 64.702 of the Commission's Rules and Regulation, 64 F.C.C.2d 771, 773 (1977). The FCC stated that "new technology has clearly made it possible for terminals to automatically perform many processing operations which

equipment (CPE) which performed any information processing function besides conversion should also be regulated.

B. Enhanced Services and Customer Premises Equipment (CPE)

The *Final Decision* to *Computer Inquiry II* abandoned the procedures established under *Computer Inquiry I* for distinguishing between communications and data processing.[51] Instead, the *Final Decision* classified all network services as either basic or enhanced, and it set forth the following:

> Basic service is limited to communications common carriers offering transmission capacity for the movement of information, whereas enhanced service combines basic service with computer processing applications that act on the format, content, code, protocol or similar aspects of the subscriber's transmitted information, or provide the subscriber additional, different, or restructured information, or involve subscriber interaction with stored information.[52]

In December 1980, the FCC further refined the distinction between basic and enhanced services by comparing basic service to a "transmission pipeline," as opposed to enhanced services which are dependent upon basic service, but are different in kind from the pipeline service.[53]

Regarding CPE, the FCC had noted in its *Final Decision* of May 1980, that "in general, no regulatory distinction should be made between various types of carrier-provided CPE."[54] In the *Supplement*

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they previously performed poorly or not at all by employing techniques previously limited to central computers."

51. Amendment of Section 64.702 of the Commission's Rules and Regulations, 77 F.C.C.2d 384 (1980) (Final Decision).

52. *Id.* at 387. In the Tentative Decision, the FCC had distinguished three categories of service—voice, basic non-voice (BNV), and enhanced non-voice (ENV). Carriers owning transmission facilities would have been required to provide ENV through a separate corporate entity. In addition, the FCC proposed new definitions for distinguishing between communications and data communications for ENV. Resale carriers would have been allowed to offer both ENV communications and ENV data processing services through common computer facilities. The FCC, however, opted for the basic/enhanced dichotomy as a more simplified terminology. *See* Amendment of Section 64.702 of the Commission's Rules and Regulations, 72 F.C.C.2d 358 (1979) (Tentative Decision and Further Notice of Inquiry and Rulemaking).

53. Amendment of Section 64.702 of the FCC Rules and Regulations, 84 F.C.C.2d 50, 54 (1980) (Memorandum Opinion and Order).

54. 77 F.C.C.2d at 388. In the *Tentative Decision* the FCC had proposed to define CPE based on whether the CPE performed more than a basic media conversion (BMC) function. After public comments, the FCC concluded that:

> [T]he public interest would not be served by classifying CPE based on whether or not more than a basic media conversion function is performed. We conclude that, in light of increasing sophistication of all types of CPE and

of December 1980, however, the FCC did create two subcategories for use during the transition period for detariffing CPE.[55] Equipment placed in service after January 1, 1983, and federally tariffed CPE will be detariffed as of January 1, 1983.[56] CPE which is tariffed at the state level and subject to the separations process is classified as embedded CPE.[57] Embedded CPE will not be subject to the January 1, 1983, detariffing deadline imposed on new CPE and interstate CPE, and a separate implementation proceeding will be instituted for the FCC.

By March 1, 1982, all carrier provided CPE had to be "unbundled" from other service offerings, and carrier provided CPE was also to be detariffed.[58] To prevent the rate base from being improperly inflated, the investment of "unbundled" CPE was required to be removed at the then current book value from the jurisdictional rate base of each of the respective carriers. Note that the FCC only detariffed, but did not deregulate enhanced services and CPE.

C. Corporate Separations Requirements

Given the "significant potential to cross-subsidize or to engage in other anti-competitive conduct," the FCC initially required both

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the varied uses to which CPE can be put while under the user's control, it is likely that any given classification scheme would impose an artificial, uneconomic constraint on the design and use of CPE. In general, no regulatory distinction should be made between various types of carrier-provided CPE.

Id.

Full analysis of the problem of CPE is made impossible by the leaps in technological advancement that have taken place in the computer communications industry in the past five years. *See supra* note 15.

55. 84 F.C.C.2d at 66-67. The FCC acknowledged that under the bifurcated approach some customers during the transition period may pay different rates for equivalent CPE.

56. Amendment of Section 702 of the FCC's Rules and Regulations, 88 F.C.C.2d 512 (1981) (Memorandum Opinion and Order on Further Reconsideration). In 1981, AT&T proposed to detariff all CPE at one time. This one step process was called the "flash cut" approach. The FCC, however, rejected this approach and reiterated its determination to follow its bifurcated approach in detariffing CPE.

57. The Jurisdictional Separations process divides exchange and interexchange investment into local and interstate categories, and then further apportions the interstate component between the message and private line service categories on the basis of techniques described in a manual which is incorporated by reference in section 702 of the FCC's Rules. *See* 77 F.C.C.2d at 447-50. In June 1980, the FCC established a Federal-State Joint Board. *See* Amendment of Section 702 of the FCC's Rules and Regulations, 78 F.C.C.2d 837 (1980) (Notice of Proposed Rulemaking and Order Establishing a Joint Board). *See also* 77 F.C.C.2d 224 (1980) (Second Supplemental Notice); 89 F.C.C.2d 1 (1982) (Second Further Notice of Proposed Rulemaking); 90 F.C.C.2d 52 (1982) (Decision and Order).

58. 77 F.C.C.2d at 447-50. *See* 84 F.C.C.2d at 65-67.

AT&T and GTE to establish separate corporate entities to provide enhanced services or CPE.[59] Subsequently, the separate subsidiary requirement was applied to AT&T alone because of the risk that the largely captive monopoly ratepayers might be burdened by anti-competitive conduct by AT&T.[60] The AT&T subsidiary would not have been permitted to own or to construct its own transmission facilities; thus, all transmission capacity had to be obtained from an underlying carrier pursuant to tariff. However, if no common carrier offered a specific basic service which the Bell subsidiary needed as part of an enhanced offering, the Bell subsidiary could request from the Commission a waiver of the prohibition of the Bell subsidiary owning or controlling any transmission facilities.[61]

The 1980 *Supplement* to *Computer Inquiry II* further curtailed the possibility of anticompetitive behavior by modifying the FCC's initial position on research and development of hardware, firmware, and generic software. The *Final Decision* had required that all research and development by a parent for a subsidiary be performed on a compensatory basis; however, the subsidiary had to perform its own design and development of nongeneric software.[62] In the 1980 *Supplement*, the FCC followed the GTC/Telenet merger authorization procedure by requiring the separate subsidiary: (1) either to perform internally or to have performed by an outside non-Bell affiliated contractor all software and firmware development; and

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59. 77 F.C.C.2d at 388-89. The FCC stated that in weighing "the public interest benefits of our objectives and the economic tradeoffs inherent in a separate subsidiary requirement, we have determined that limited imposition of the requirement will best serve the communications ratepayer and the public interest more generally."

60. 84 F.C.C.2d at 72-75. The FCC explained its rationale for applying the separate subsidiary requirement only to AT&T by stating that the following factors were considered:

> (a) a carrier's ability to engage in anti-competitive activity through control over "bottleneck" facilities, i.e., local exchange and toll transmission facilities, on a broad national geographic basis; (b) a carrier's ability to engage in cross-subsidization to the detriment of the communications ratepayer; (c) the integrated nature of the carrier and affiliated entities, with special emphasis upon research and development and manufacturing capabilities that are used in conjunction with, or are supported by, communications derived revenues; and (d) the carrier's possession of sufficient resources to enter the competitive market through a separate subsidiary.

84 F.C.C.2d at 75.

61. 84 F.C.C.2d at 78-79. The test for granting a waiver to the prohibition of the AT&T subsidiary owning transmission facilities was whether "any negative effects on ratepayers which may arise from grant of a waiver are outweighed by the possibility of imposition of unreasonable costs upon consumers, or unavailability of an enhanced service if waiver is not granted."

62. 77 F.C.C.2d at 479-81. Nongeneric software is often called applications software in the data processing industry.

(2) either to perform internally or to have performed by any outside firm (including a Bell System affiliated firm), research and development of equipment into which the software could be inserted. The separate subsidiary could purchase any equipment from its parent as long as any software or firmware contained in the equipment was not customized, but was the same as that sold "off the shelf" to any interested party.[63]

Furthermore, the FCC set forth rules regarding the information flow between parent and subsidiary as follows: (1) the basic network had to be released to everyone on the same basis and at the same time; (2) research and development had to be paid for on a fully compensatory basis; (3) proprietary information (i.e., customer lists) of the parent AT&T had to be disclosed to all interested parties at the same time and under the same terms and conditions; and (4) a record of each transaction between the parent AT&T and its unregulated subsidiary had to be filed with the FCC.[64] No restrictions were placed on transactions between unregulated Bell subsidiaries. The 1980 *Supplement* also revised the restriction prohibiting affiliated Bell entities from purchasing equipment from the separate subsidiary by prohibiting affiliated Bell entities from purchasing equipment from the separate subsidiary only if the equipment was not manufactured by the separate subsidiary. Finally, AT&T was ordered to account for all of its costs in establishing any separate unregulated subsidiaries.[65]

Overall, *Computer Inquiry II* favors AT&T by permitting AT&T to enter the rapidly growing enhanced services and CPE communications sectors. The restriction separating the parent Bell affiliates and the separate Bell subsidiary necessary to prevent cross-subsidization will be modified to fit the divestiture of the Bell Operating Companies (BOC's) from the parent AT&T. These same separations requirements can be expected to form the basis of the future rules that the FCC will implement to continue its regulation of the Long Lines Division as the parent AT&T begins to compete in the unregulated sectors of the telecommunications industry.[66]

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63. 84 F.C.C.2d at 79-81.

64. *Id.* at 81-83. *See* Application of General Telephone and Electronics Corp. to Acquire Control of Telenet Corp. and its Wholly-Owned Subsidiary, Telenet Communications Corp., 72 F.C.C.2d 111 (1979), *modified*, 72 F.C.C.2d 516 (1979).

65. 84 F.C.C.2d at 84.

66. *See* 77 F.C.C.2d at 475-86. In the *Final Decision* of May 1980, the FCC, consistent with its enunciated policy of maximum separation, ruled that this degree of separation required (1) separate maintenance of records and books of account, (2) no joint or common personnel, (3) separate offices, (4) that administrative services (such as legal services) be provided by the parent on a cost reimbursement basis, (5) no sharing of computer services, (6) no joint use of the same physical space,

The divestiture procedure whereby the assets of the Bell System will be divided between the parent AT&T (Bell Headquarters, Western Electric, Long Lines, and Bell Labs) and the BOC's will be reviewed by the United States District Court for the District of Columbia and by the Department of Justice. Congress and the FCC can also be expected to review the division of the Bell System's assets and to monitor the effects of the divestiture of the Bell System pursuant to the settlement of the *United States v. AT&T*[67] case.

IV. FCC ACTIONS PARALLEL TO *COMPUTER INQUIRY II*

A. AT&T PRICE STUDIES

In 1974, the FCC sponsored a study by Touche Ross & Company to analyze Western Electric.[68] The Touche Ross Report concluded that Western Electric was able to avoid "certain costs incurred by outside manufacturers [in its] expense build-up."[69]

In 1977, the FCC approached the problem of cross-subsidization from the perspective of analyzing the price comparisons that AT&T used to insure that the prices Western Electric charged to the BOCs were competitive with Bell nonaffiliated product sources.[70] The FCC concluded that these costs studies were not valid.[71] However, the Commission did not make any specific order regarding how AT&T should perform these studies in the future. Instead, the Commission required AT&T to submit a proposal for achieving maximum separation of its equipment procurement and manufacturing functions, short of divestment of Western Electric.[72] Given the poor quality of the AT&T price studies, this proceeding also focused on the "make/buy" decision. Subsequently, in July 1981, the FCC approved an inquiry notice to examine the purchasing practices of the BOCs. In approving this inquiry notice, the Commission relied heavily on the previous proceeding in which the Commission had concluded that the BOCs purchasing system created a bias in favor of Western Electric products and that Western Electric had an input

(7) that any technical information disclosed to the separate subsidiary be released to competitors of the subsidiary at the same time and on the same terms and conditions, and (8) that no software or firmware be designed by the parent for the subsidiary except if the software or firmware was embedded in or integral to some of the CPE obtained from the parent.

67. *See supra* note 4.

68. Touche Ross & Co., Final Report on the Comprehensive Review of the Western Electric Co. (Jan. 3, 1974) (F.C.C. Contract RC-10195).

69. *Id.* at 68.

70. American Tel. & Tel. Co., 64 F.C.C.2d 1 (1977) (Final Decision and Order).

71. *Id.* at 61-101.

72. *Id.* at 43-45.

into virtually every step of the "make/buy" decision-making process.[73]

Therefore, although not specifically related to *Computer Inquiry II*, these proceedings indicate the philosophical approach that the FCC has taken to formulate conduct changes in the Bell system. Under *Computer Inquiry II*, the FCC will have to be careful to establish procedures which prevent the unregulated decisions to favor itself at the expense of rate-payers using Long Lines.[74]

B. Uniform System of Accounts (USOA)

In 1978, the FCC also began to examine and revise the Uniform System of Accounts (USOA), which had remained virtually unchanged since its adoption in 1935.[75] The Commission noted that the USOA was based on a company-wide breakdown of costs.[76] Given the multi-service telecommunications environment, the Commission determined that due to the introduction of competition in the specialized services and terminal equipment areas, more specific service-related cost and revenue information, with interstate and intrastate (as opposed to the company-wide data as provided by the USOA) breakdowns of cost for each service was required for proper regulation.[77] The ultimate goal of the revised USOA is a single database for state and federal regulators and the elimination of the cost studies that AT&T had been required to perform to justify its requests for rate increases.[78] In addition to the goals of a single

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73. *See* 64 F.C.C.2d 1.

74. *See* Comment, *Communications—The FCC, As an Alternative to Divestment of Western Electric, Ordered Greater Autonomy for the Bell Operating Companies in Purchasing Divisions*, 27 Cath. U.L. Rev. 1521 (1977).

75. Revision of the Uniform System of Accounts and Financial Reporting Requirements for Telephone Companies (Parts 31, 33, 42 and 43 of the FCC's Rules), 70 F.C.C.2d 719 (1978) (Notice of Proposed Rulemaking). In making its revision, the FCC includes an examination of the early history of the USOA.

76. *Id.* at 721. Historically, the primary rate-making criteria were overall investment and expense levels, property valuations, and depreciation rates. In recent years, rate cases have dealt increasingly with rate levels and rate structures of specific services. The starting point in setting appropriate rate levels and rate structures for specific services is the relative cost of providing the services.

77. *Id.* at 724-25.

78. The FCC stated:

> [To remedy] the inadequacies of the current USOA, we are proposing a comprehensive modification of the existing accounting system as a whole. . . . It is our intention that the revised accounting system which will result from this proceeding will constitute a single data base serving the following functions:
>
> (1) It will form the basis for financial reports, including both balance sheet and income statement reporting. (2) It will serve as a data base and a foundation for managerial decision-making and internal management reports by

database and the elimination of AT&T's cost studies, in light of *Computer Inquiry II*, the USOA will be revised so as to prevent cross-subsidization between the regulated Long Lines Division and the unregulated divisions of AT&T. The FCC is continuing its study of the USOA through various proceedings.[79]

C. Manual and Procedures for the Allocation of Costs

In another related matter, in 1979, the FCC initiated a proceeding to develop procedures for AT&T to use in allocating costs among its various services.[80] The cost allocation procedures that AT&T was to follow were the general guidelines established by the FCC in Docket Number 18128.[81]

In 1980, the FCC issued a *Notice of Proposed Rulemaking*.[82] The

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> the carriers. (3) It will provide sufficiently detailed disaggregated cost and revenue information for derivation of costs and revenues of individual services and rate elements, for pricing decisions and other managerial decision-making by the carriers. (4) It similarly will provide detailed disaggregated cost and revenue information for derivation of costs and revenues of individual services and rate elements, for rate review and continuing surveillance purposes of this Commission (and other regulatory bodies which adopt the revision) and provide a basis for rate prescription, where appropriate. (5) It will facilitate the breakdown of costs between interstate and intrastate jurisdictions ("Jurisdictional Separations"). (6) It will permit analysis of facility and plant utilization, including studies of the causes for each category of expenditure and review of service quality and service efficiency. And (7) it will be structured so as to allow for regulatory and independent auditing and tracing of questioned entries.

Id. at 724-25.

79. Another aspect of the USOA, depreciation, has also recently been examined. *See* Amendment of Part 31 (Uniform System of Accounting for Class A and Class B Telephone Companies), 83 F.C.C.2d 267 (1980).

80. American Tel. & Tel. Co., 73 F.C.C.2d 629, 630 (1979) (Notice of Inquiry). In its *Notice of Inquiry*, the FCC noted that:

> competitive methods for diverse telecommunication services remain in their infancy. Dominant carriers still possess sufficient market power to cross-subsidize among services and users. Such cross-subsidization might nullify or otherwise restrain the emergence of fully-developed competitive telecommunication markets. Consequently, the implementation of Commission-approved costing principles for dominant carriers generally, and AT&T in particular, is crucial to the promotion and further development of sustainable, competitive telecommunication markets of the future.

Id. at 630.

81. *See* American Tel. & Tel. Co., Long Lines Dept., 81 F.C.C.2d 587 (1976), *recon.*, 64 F.C.C.2d 971 (1977), *further recon.*, 67 F.C.C.2d 1441 (1978), *aff'd sub nom.* Aeronautical Radio, Inc. v. FCC, 642 F.2d 1221 (D.C. Cir. 1980), *cert. denied*, 451 U.S. 920 (1980). The FCC had attempted in Docket 18128 to establish basic principles and standards of general applicability for determining cost of service and corresponding rate levels by service category. 451 U.S. at 976.

82. American Tel. & Tel. Co., 78 F.C.C.2d 1296 (1980) (Notice of Proposed Rulemaking).

Commission stated that the cost allocation manual which they had proposed, although not a "perfect solution," was necessary to allow the Commission to fulfill its statutory obligations.[83] This proposed manual was to be an interim manual, and more suggestions and comments were sought on long-term approaches to the potential problem of cross-subsidization. The Commission was most concerned with cross-subsidization of private line services by message services. The chief concern was that AT&T's dominant position in the provision of message service would allow it to overcharge message customers in order to cross-subsidize private line service, and thereby weaken or prevent competition in this area.[84]

Therefore, private lines are to be aggregated into a single category for reporting purposes. To simplify, but still have the data verifiable, the FCC proposed to increase reliance on separations for allocation purposes. This interim manual does not lessen the burden on AT&T to demonstrate the validity of its tariff filing."[85]

Three major types of allocation procedure were suggested by the commenting parties,[86] but the FCC concluded that each accounting method suffered fatal shortcomings.[87] The FCC required, there-

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83. *Id.* at 1297.

84. *Id.* at 1298.

85. *Id.* at 1298-99. The FCC also noted that the simplification of reporting requirements and added flexibility did not constitute a "carte blanche" to AT&T to engage in unjust, unreasonable or unlawfully discriminatory pricing practices. The Commission's "interest in eliminating unnecessary complexity is related to our intent that the allocation of costs be verifiable and not unduly subject to management discretion . . . while existing separation procedures . . . may be amended in the near future, they nevertheless constitute an existing, externally mandated system of allocation which is readily subject to audit." *Id.* at 1299.

86. *Id.* at 1307-12. AT&T proposed to modify the existing system, but the FCC viewed AT&T's proposed modified system as still impossible to understand and monitor. The second method, proposed by Walter Hinchman & Associates, Inc., was extremely complex, and in some areas went beyond an allocation technique and involved restriction on AT&T. The third method was Western Union's "top-down" approach. Although a simplified method, this "top-down" approach required identification of factors that would lead to the division of the interstate costs to various services; these factors were not identified in the report.

87. In its Summary, the FCC concluded:

> A system of cost allocation must be understandable, verifiable, and, insofar as it assigns costs based upon forecasts and other inputs which are strongly subject to management discretion, capable of being checked for accuracy . . . . AT&T's cost allocation methods have prevented us from prescribing new rates in situations where filed tariffs have been found unlawful . . . . We believe that a cost allocation mechanism must be sufficiently understandable to permit us to take appropriate remedial action if we find that improper rates have been filed.

Id. at 1329.

fore, that an interim plan be implemented by AT&T.[88] Under the interim plan, AT&T is required to allocate interstate revenues, investment, and expense to four service categories: MTS, WATS, Private Line, and ENFIA.[89] This FCC proceeding concerning the establishment of a revised Manual and Procedures for the Allocation of Costs continues.

D. *EXECUNET* CONTROVERSY

The *Execunet* controversy showed the further development of the FCC's free-entry policy while *Computer Inquiry II* was being decided.[90] In *MCI Telecommunications Corporation v. FCC*[91] (hereinafter *Execunet*), the Court of Appeals for the District of Columbia ruled that the FCC could not deny specialized carriers the right to expand intercity telephone services in the absence of a finding by the FCC that such expansion was not in the public interest. Later, in a *Declaratory Ruling*,[92] the FCC ruled that AT&T was under no obligation to provide the local physical interconnections necessary for MCI's Execunet service. AT&T, relying on the FCC's *Declaratory Ruling*, refused to supply MCI the local physical interconnections required for the Execunet service. MCI then challenged the *Declaratory Ruling* in federal court.[93] The court specifically invalidated the FCC's ruling that AT&T was under no obligation to provide local distribution facilities for MCI's Execunet service.[94] Consequently, while *Computer Inquiry II* was progressing within the FCC, the effect of the court's decision was to allow MCI to offer specialized services such as Execunet.[95]

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88. *Id.* at 1311-12.

89. ENFIA was developed as a temporary category pending completion of the FCC's access charge investigation. *See* AT&T Manual and Procedures for the Allocation of Costs, 84 F.C.C.2d 384, 406 (1980) (Report and Order), 86 F.C.C.2d 107 (1981) (Order), *recon. in part*, 86 F.C.C.2d 667 (1981) (Order on Reconsideration).

90. *See* G. BROCK, THE TELECOMMUNICATIONS INDUSTRY 224-30 (1981).

91. MCI Telecommunications Corp., 60 F.C.C.2d 25 (1976), *rev'd sub nom.* MCI Telecommunication Corp. v. FCC, 561 F.2d 365 (D.C. Cir. 1977), *cert. denied*, 434 U.S. 1040 (1978). A push button telephone subscriber to "Execunet" is able to reach any telephone in a distant city served by MCI by dialing a local MCI number, followed by an access code and the phone number in the distant city.

92. Petition of AT&T for a Declaratory Ruling and Expedited Relief, 67 F.C.C.2d 1455 (1978) (Memorandum Opinion and Order).

93. MCI Telecommunications Corp. v. FCC, 580 F.2d 590 (D.C. Cir. 1978).

94. *Id.* at 591.

95. *See* Warren, *Intercity Telecommunications Competition After Execunet*, 31 FED. COM. L.J. 117 (1978).

E. MTS AND WATS MARKET STRUCTURE

In response to the *Execunet* controversy, in 1978, the FCC instituted a proceeding to determine "whether the public interest would be better served by conferring single source status upon MTS and WATS, in whole or in part, or by authorizing some other kind of industry structure."[96] Subsequently, in 1979, the FCC issued a *Supplemental Notice* requesting comments by interested parties on the optimal industry structure and entry policy for the MTS-WATS market.[97] The FCC concluded that, except for the Alaskan interstate market, the MTS-WATS market was open to entry, effectively permitting individual and corporate consumers to enter the MTS-WATS market.[98]

F. COMSAT AND SBS

Computer system vendors and communications common carriers are interested in satellite communications technology because satellites provide an attractive opportunity for major cost reductions.[99] Significant reductions in the costs of communications are particularly attractive to computer system vendors as they expand their computer design options. The Communications Satellite Act of 1962[100] established the Communications Satellite Corporation (COMSAT), which is owned half by the general public and half by overseas carriers. COMSAT is still in operation and has launched several satellites and established a communications network.[101]

In the late 1960's, the FCC conducted a four-year study of the role of satellites in domestic communications, and in 1970, it concluded that satellites could play a major role in domestic communi-

96. MTS and WATS Market Structure, 67 F.C.C.2d 757, 758 (1978) (Notice of Inquiry and Proposed Rulemaking). "MTS" stands for Message Telecommunications Service, and "WATS" stands for Wide Area Telephone Service.

97. MTS and WATS Market Structure, 73 F.C.C.2d 222 (1979) (Supplemental Notice of Inquiry and Proposed Rulemaking). The FCC encouraged the parties to describe regulatory policies that the Commission should adopt with respect to entry policy for the MTS-WATS market.

98. *See* MTS and WATS Market Structure, 77 F.C.C.2d 224 (1980) (Second Supplemental Notice of Inquiry and Proposed Rulemaking); MTS and WATS Market Structure, 81 F.C.C.2d 177, 202-03, 214 (1980) (Report and Third Supplemental Notice of Inquiry and Proposed Rulemaking); MTS and WATS Market Structure, 90 F.C.C.2d 135 (1982) (Fourth Supplemental Notice of Inquiry and Proposed Rulemaking).

99. *See* Kelley, Satellites Save Money, 26 INFOSYSTEMS, July 1979, at 42. *See also The Gold Mine in Satellite Services*, BUS. WEEK, April 6, 1981, at 89, 90.

100. Communications Satellite Act of 1962, Pub. L. No. 87-624, 76 Stat. 419 (1962) (codified as amended at 47 U.S.C. § 701 (1976)).

101. *See* Socol, *Comsat's First Decade*, 7 GA. J. INT'L & COMP. L. 678 (1977).

cations.[102] The FCC then invited potential satellite applicants to submit concrete system proposals. In its 1972 *Domsat II* decision, the FCC, recognizing that each potential applicant presented possible antitrust problems, rejected the suggestion that entry be limited to one or a small number of entrants.[103] Instead the FCC asserted that "there may well be advantages to and need for voluntary considerations or sharing arrangements (such as "launch risk pools")," and it indicated its willingness to approve applications involving joint ventures so long as they were consistent with its policy of encouraging multiple entry and competition.[104]

AT&T and COMSAT proposed a domestic satellite system wherein AT&T would lease communications satellites and associated services from COMSAT.[105] To prevent antitrust abuses in the AT&T and COMSAT joint venture, the FCC required that: (1) COMSAT be a minority participant in the joint venture; (2) no AT&T officer or director could serve as a director of COMSAT; and (3) COMSAT establish a separate corporate entity to operate the domestic satellite system.[106]

COMSAT had previously entered into a joint venture (called CML Satellite Corporation) with Lockheed Aircraft Corporation and MCI Communications Corporation to operate a domestic satellite communications system. In 1974, COMSAT and IBM filed a joint petition for FCC approval of changes in the corporate structure of

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102. Establishment of Domestic Communication—Satellite Facilites by Non-governmental Entites, 22 F.C.C.2d 86 (1970) (Report and Order) ("Domsat I"). *See* Orr, *Satellite Communications Takes a Big Leap Forward*, 73 A.B.A. BANKING J., Jan. 1981, at 76; Evans, *Satellite Communications—The Legal Gap*, 11 JURIMETRICS J., Dec. 1970, at 92.

103. Establishment of Domestic Communications—Satellite Facilities by Non-governmental Entities, 35 F.C.C.2d 644, 647 (1972) (Second Report and Order) ("Domsat II"). The FCC stated: "the presence of *competitive* sources of supply of specialized services, both among satellite system licensees and between satellite and terrestrial systems, should encourage service and technical innovation and provide an impetus for efforts to minimize costs and charges to the public." (emphasis added) After the *Domsat II* decision, the FCC approved the applications of AT&T, RCA, Hughes Aircraft Company, GTE, and American Satellite. *See* Satellite Business Sys., 62 F.C.C.2d 997, 1063-73 (1977); American Tel. & Tel. Co., 42 F.C.C.2d 654 (1973); RCA Global Communications, Inc., & RCA Alaska Communications, Inc., 42 F.C.C.2d 774 (1973); Hughes Aircraft Co. (National Satellite Services, Inc.) & GTE Satellite Corp., 43 F.C.C.2d 430 (1973); and American Satellite Corp., 43 F.C.C.2d 348 (1973). The lack of an FCC evidentiary hearing was upheld by the Court of Appeals for the District of Columbia. *See* Network Project v. FCC, 511 F.2d 786 (D.C. Cir. 1975).

104. 35 F.C.C.2d at 850; *see also* 62 F.C.C.2d at 1037.

105. The application of AT&T and Comsat was filed in response to Domsat I, 22 F.C.C.2d 86 (1970) (*Report and Order*), *See* 35 F.C.C.2d at 851-53.

106. 38 F.C.C.2d 655, 676-88 (1972). (Memorandum Order and Opinion). *See* American Tel. & Tel. Co., 42 F.C.C.2d 654 (1973).

CML.[107] It was proposed that after the withdrawal of Lockheed and MCI from the CML venture, COMSAT and IBM would operate a joint venture for a domestic satellite system. In 1975, the FCC rejected the COMSAT/IBM proposal, but it delineated the conditions under which COMSAT and IBM could participate in a joint venture for a domestic satellite system. These conditions included requiring: (1) the joint venture to provide for interconnection of its customers' data processing and communications systems on reasonable terms and without discrimination; (2) the details of the interconnection to be submitted in advance to the FCC; (3) IBM to create a separate subsidiary to operate the satellite system; and (4) COMSAT and IBM to conform to one of three permissible forms of business organization.

In compliance with the FCC's fourth requirement, the two companies chose the "balanced CML option" (one of the three permissible forms); and in December 1975, COMSAT, IBM, and Aetna Casualty and Surety Company (through its subsidiary, Aetna Satellite Communications, Inc.), applied to the FCC for a license to operate a domestic satellite system as a joint effort under the name Satellite Business Systems (SBS).[108] Opponents objected to the SBS proposal on numerous grounds, including antitrust considerations.[109] Yet, in February 1977, after extensive filing, the FCC denied the request by opponents for a formal evidentiary hearing, and it granted SBS a license.[110] Although American Satellite, Western Union, AT&T, and the Department of Justice appealed the FCC *SBS Decision* on the grounds that the FCC had not properly reviewed the antitrust considerations of the SBS joint venture in an evidentiary hearing. The Court of Appeals for the District of Columbia upheld the FCC decision to permit SBS to operate a domestic satellite communications system.[111]

The various FCC proceedings involving applications for satellite communications systems are yet another example of the FCC's open entry policy. The requirements for entry into this market are limited to a basic fitness requirement. Although the FCC will not impose a structural requirement that each entrant be a separate corporation. Rather, the FCC can be expected to closely regulate all satellite entrants, to evaluate each entrant, and to adopt appropriate

107. Petition for Approval of Changes in Corporate Structure of CML Satellite Corp., 51 F.C.C.2d 14 (1975). CML stood for the three initial partners in the COMSAT joint venture: COMSAT, MCI, and Lockheed.

108. Satellite Business Sys., 62 F.C.C.2d 997, 998 (1977).

109. 62 F.C.C.2d at 1014-15.

110. 62 F.C.C.2d at 1029-32, 1061-99.

111. United States v. FCC, 652 F.2d 72 (D.C. Cir. 1980).

conduct constraints, such as the requirement imposed on SBS to treat all prospective customers equally.

G. SUMMARY

While the *Computer Inquiry II* was in progress, the FCC was holding numerous related proceedings. The FCC will need to monitor carefully the procurement decisions of Long Lines to avoid unfair favoritism by Long Lines to its unregulated parent—AT&T. The USOA will also need to be modified by the FCC to prevent cross-subsidization between the regulated portions of Long Lines and the unregulated AT&T. Finally, the proceedings concerning the *Manual and Procedures for Allocation of Costs* will need to continue.

V. THE CONGRESSIONAL SCENE

A. CONGRESSIONAL EFFORTS TO REVISE THE 1934 COMMUNICATIONS ACT

After the Department of Justice filed the *United States v. AT&T*[112] antitrust case in 1974, Congress began to study the telecommunications industry, and consequently, several bills were introduced.[113] Some of these early bills nearly passed in the House of Representatives or the Senate. An analysis of these initial legislative efforts reveals the evolution of present communications law.

One of these early attempts to revise the 1934 Communications Act was the 1976 AT&T-supported Consumer Communications Reform Act.[114] Opponents charged that the bill should have been called the Monopoly Protection Act of 1976 because it would have removed most of the FCC's authority over the national communications network and given this authority to the states' public utilities commissions. Specifically, the bill would have: (1) transferred jurisdiction over station equipment and terminal equipment from the FCC to the states; (2) given the states authority to set intercommunications rules, to define station equipment, and to dictate the terms under which the equipment could be marketed; and (3) permitted states to control the interconnection of interstate specialized common carriers to the AT&T local distribution networks.[115] Opponents

112. *See supra* note 4.

113. *See infra* notes 114-83 and accompanying text. *See generally* Loeb, *The Communications Act Policy Toward Competition: A Failure to Communicate*, 1978 DUKE L.J. 1 (contains an excellent review of the historical origins and passage of, and developments affecting, the Communications Act of 1934 through the mid-1970s).

114. S. 3192, 94th Cong., 2d Sess. (1976).

115. *See* Biddle, *Computer Industry Association Position Statement [Consumer Communications Reform Act of 1976]*, TELECOM., Nov. 1976, at 18; Ellinghaus, *What the*

of the legislation sponsored a Pro-Competition Resolution, and after hearings in committees on communications in both houses, the bill died.[116]

A 1978 bill in the House of Representatives would have required AT&T to divest Western Electric,[117] and an early 1979 House bill would have required AT&T to deal at arms length with all of its subsidiaries.[118] AT&T claimed that both bills were seriously deterimental to the ability of AT&T to operate the national core communication network; both bills were defeated.[119] In December 1979, H.R. 6121 was introduced and successfully moved through subcommittee, but was adversely reported by the Committee of the Judiciary due to antitrust concerns.[120] In 1977 and 1978, the Senate also attempted to establish communications policy, and it introduced several bills and held numerous hearings; these bills, however, suffered a fate similar to the House bills.[121]

Although both the House and Senate bills adopted the concept of a separate subsidiary, they differed over the degree of separation that should be required. Both would have modified the *1956 Western Electric Consent Decree*, but the House bill was stronger on limiting AT&T in mass media. Although both agreed on the concept of supporting the local urban networks through access charges, the first six years of developing access charges were to be administered differently. And both the House and the Senate agreed that to maintain reasonable rural telephone rates a subsidy for rural networks would be necessary.[122]

B. THE 1981 PACKWOOD BILL (S. 898)

In 1981, Senator Packwood introduced Senate Bill 898, the "Tele-

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Public Should Know About the Consumer Communications Reform Act, TELEPHONY, Oct. 4, 1976, at 84.

116. H.R.J. RES. 285, 95th Cong., 1st Sess. (1977) (introduced by Tim Wirth (D-Colo.)); S.J. RES. 30, 95th Cong., 1st Sess. (1977) (introduced by Gary Hart (D-Colo.)).

117. *See* H.R. 13015, 95th Cong., 2d Sess. (1978).

118. See H.R. 3333, 96th Cong., 1st Sess. (1979).

119. *See* Sarasohn, *Telecommunications Rewrite Tries to Unfetter Industry*, CONG. Q., Feb. 16, 1980, at 389.

120. *See* H.R. 6121, 96th Cong., 2d Sess. (1980); H.R. Rep. No. 1252, 96th Cong., 2d Sess. 3 (1980).

121. For a discussion of these cases, see O'Riordan, *An Examination of the Application of Common Carrier Regulation to Entities Providing New Telecommunication Services*, 29 CASE W. RES. L. REV. 577 (1979).

122. *See* S. 2827, 96th Cong., 2d Sess. (1980); H.R. 6121, 96th Cong., 2d Sess. (1980). *See* Sarasohn, *AT&T Restructured: New Objections Show Dare of Communications Rewrite*, CONG. Q., July 12, 1980, at 1943.

communications Competition and Deregulation Act of 1981."[123] Senator Packwood announced at the bill's introduction that "it has been our view that Congress, not the courts or the Federal Communications Commission, should establish national communications policy."[124] In effect, the bill was an attempt to deregulate the telecommunciations industry and to offer parameters for future regulation of the telecommunications field.[125] Under the bill, the FCC would have been encouraged to foster competition in the market for interexchange telecommunications, with regulation only as necessary. For example, regulation would have been required in the case of a market where no alternative carriers were available to provide telecommunications services, but regulation was not a foregone conclusion where more than one service was available.[126] Carriers would have been regulated according to the classifications set forth in the bill.[127] The FCC would have retained the power to regulate all markets to insure the availability of telecommunications services at reasonable rates[128] and the power to regulate dominant carriers defined in the bill.[129] AT&T was specifically designated as a dominant carrier, and thereby kept within the regulatory authority of the FCC by specific intention.[130]

Senate Bill 898 proposed several amendatory additions to the Communications Act of 1934, each specifically directed toward AT&T.[131] For example, the bill would have required AT&T to establish a separate subsidiary to compete in deregulated markets[132] and would have provided procedures for AT&T to follow in conducting its research and development and its manufacturing activities during the interim period until full separation from the affiliates was achieved.[133] Requirements for a "fully separated affiliate" were clearly defined,[134] with a timetable provided for the telecommunications giant to follow in the process of cutting loose its operating companies.[135] Nothing in the language of Senate Bill 898 required

123. S. 898, 97th Cong., 1st Sess. (1981).

124. 127 CONG. REC. 83,544 (1981).

125. *See* Trienens, *Deregulation In the Telecommunications Industry: A Status Report*, 50 ANTITRUST L.J. 409 (1982).

126. S. 898, 97th Cong., 1st Sess., 102, 201.

127. *Id.* §§ 201, 205.

128. *Id.* § 203.

129. *Id.* § 204.

130. *Id.* §§ 205, 229.

131. *Id.* § 223.

132. *Id.*

133. *Id.* §§ 223, 227.

134. *Id.*

135. *Id.* §§ 223, 228. Section 228(a) stated that "until such time as the American

the total divestiture of the subsidiary companies, although strict requirements were established for the relationship of the "affiliates" to the parent company; these requirements were to apply to the subsidiary that would offer enhanced services. The fully separated affiliate and the parent: (1) could have only one common director (similar to the 1980 House Bill)[136]; (2) could not have any joint officers or employees (similar to both the 1980 House and Senate bills)[137]; (3) would have to maintain separate books and records, and records which have to be fully auditable (similar to both the 1980 House and Senate bills)[138]; (4) could not have any joint or common property except for international telecommunications facilities or properties (slightly different than either the 1980 House or Senate bill)[139]; and (5) could only engage in joint institutional advertising on a compensatory basis (similar to both the 1980 House and Senate bills).[140] Consequently, the dominant regulated carriers were to be prohibited from conducting business with their fully separated affiliates on a preferential basis and were to be prohibited from cross-subsidizing the unregulated separate subsidiary.[141] Under Senate Bill 898, the FCC role in the reorganization of AT&T would have been that of a watchdog. Before offering unregulated services, AT&T would have had to receive FCC approval of a plan for complying with the transition to fully separate affiliates.[142] The FCC would have been permitted to waive the proposed statutory transition schedule if intervening forces rendered AT&T incapable of compliance.[143]

The *1956 Western Union Consent Decree* was to be construed so as to permit AT&T to enter the data processing computer field through an unregulated subsidiary.[144] Consequently, AT&T and its affiliates would have been permitted to provide telecommunications services or equipment,[145] as well as information services, so long as these services and products were offered by fully separated affili-

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Telephone and Telegraph Company and its affiliates (hereinafter referred to in this section as AT&T) establish fully separated affiliates pursuant to this section and section 227, the provisions of this section shall apply in any case . . . ."

136. *Id.* §§ 223, 227(a)(1).

137. *Id.* §§ 223, 227(a)(2).

138. *Id.* §§ 223, 227(a)(3).

139. *Id.* §§ 223, 227(d)(1).

140. *Id.* §§ 223, 227(d)(2).

141. *Id.* §§ 223, 227(e)(1).

142. *Id.* §§ 223, 228.

143. *Id.* §§ 223, 228(c)(6)(A),(B). Examples of intervening forces were labor strikes, war, severe economic depression, and acts of God.

144. *Id.* §§ 223, 229.

145. *Id.* §§ 223, 229(d)(2)(B).

ates.[146] Although in October 1981, the Senate passed Senate Bill 898, no further action as taken on the Packwood bill because of subsequent court action.

C. THE 1981 WIRTH BILL (H.R. 5158)

In December 1981, Representative Wirth introduced House of Representatives Bill 5158 (hereinafter H.R. 5158), a bill to reform Title II of the Communications Act of 1934.[147] In January 1982, the Justice Department and AT&T announced a proposed settlement of the seven-year antitrust litigation. The agreement would have required AT&T to divest its twenty-two local operating companies, which constituted two-thirds of AT&T's assets, in return for the Justice Department's lifting of the restrictions imposed on AT&T in the *1956 Western Electric Consent Decree*. These restrictions had kept AT&T from entering the telecommunications field or any other unregulated activity.[148] The subcommittee hearing which followed became a focal point for the debate over the adequacy of the proposed settlement. In March 1982, the subcommittee unveiled a substitute bill which dealt with the perceived deficiencies of the proposed settlement in *United States v. AT&T*.[149]

The subcommittee began a comprehensive review of competition in the telecommunications industry, and it printed the results in a lengthy staff report.[150] The substitute H.R. 5158 was designed (1) to protect the viability of the local operating companies after divestiture; (2) to prevent local rates from increasing dramatically due to the loss of subsidization from long distance revenues; and (3) to guard against AT&T taking anti-competitive actions, especially in the unregulated sectors of the communications industry.[151] H.R. 5158 was approved unanimously in March 1982, and it went substantially beyond both the proposed *United States v. AT&T* settlement and S. 898.[152]

The purpose of H.R. 5158 was to guarantee the public a reliable, efficient, and diverse telecommunications service at reasonable and

146. *Id.* §§ 227-29.

147. H.R. 5158, 97th Cong., 1st Sess. (1981).

148. *See* Sarasohn, *House Panel Approves Bill Adding New Limits to AT&T*, CONG. Q., March 27, 1982, at 688.

149. *Id.* at 688. *See supra* note 4.

150. *House Comm. on Energy and Commerce, Subcomm. on Telecommunications, Consumer Protection and Finance, Telecommunications in Transition: The Status of Competition in the Telecommunications Industry*, 97th Cong., 1st Sess. (1981).

151. H.R. 5158, 97th Cong., 1st Sess. §§ 201, 205 (1981).

152. *See supra* notes 4 & 123.

affordable rates.[153] To achieve this goal, the forces of open and competitive markets were to be relied upon rather than regulation.[154] Under H.R. 5158, the FCC was directed to deregulate competitive markets and to promote competition in those markets lacking competition.[155]

1. Regulatory Authority of the FCC

Under H.R. 5158, the FCC's authority over exchange, interexchange, and international transmissions would have been limited.[156] State public utilities commissions and the FCC were to be (1) forbidden from considering the revenues or profits derived from the offering of any unregulated products or services (except for *Yellow Pages*) by any affiliate or separate subsidiary of a regulated carrier when determining the revenue requirements of any regulated service of such carrier and (2) prohibited from regulating new terminal equipment, new inside wiring, and resale or shared use of any transmission service or enhanced service.[157] The FCC would also have been required to classify carriers that owned interexchange transmission facilities as either dominant carriers, regulated carriers, or deregulated carriers (AT&T would have been the only dominant carrier under the bill).[158] Telephone companies that were currently providing joint long distance and local exchange services were to be classified as regulated carriers.[159]

2. Interexchange Transmission

After an initial transition period of five years, the FCC would have exercised sole authority over all interexchange (toll) transmission, whether intrastate or interstate, except for intrastate toll transmissions of exchange carriers serving not more than 500,000 customer access lines. Deregulation of any given carrier would have depended upon a determination by the FCC that there were adequate alternatives to the service/facility.[160] Alternatives would have been considered adequate if they were substitutable in quality and comparable in both economic cost and geographic range to the relevant service or facility.[161] Regulated carriers would have been com-

153. *Id.* § 201(a).
154. *Id.*
155. *Id.* § 201(b)-(c).
156. *Id.* § 211.
157. *Id.*
158. *Id.* § 212.
159. *Id.*
160. *Id.*
161. *Id.* § 213.

pelled to furnish, upon reasonable request, "regulated services" or those for which there were inadequate facilities available.

The tariffs established for these services were required to be just, reasonable, and nondiscriminatory.[162] No tariff for a given regulated service could include any costs associated with the provision of any other service or product, and the burden of showing a tariff to be just and reasonable was placed on the carrier.[163] Carriers offering enhanced services would have been compelled to do so on an unbundled basis. To prevent cross-subsidization, facilities constructed for the purpose of enhancing service, as opposed to transmission, would not have been included in the regulated rate base.[164]

3. Exchange Transmission

To prevent the use of local exchange facilities to create a bottleneck to restrict interexchange, enhanced services, or terminal equipment competition, H.R. 5158 would have required exchange carriers after 1986 to offer all interexchange carriers access on an equal basis including equal access in type, quality, and range of supporting functions. Exchange carriers would have also been required to interconnect any terminal equipment, inside wiring, or transmission services or facilities that met federal technical standards.[165]

In order to protect exchange carriers, all interexchange transmission offered by a dominant carrier would have been required to originate and terminate through the facilities of exchange carrier until 1988. This would prevent a dominant carrier from "bypassing" a local exchange for the sole benefit of large users of long distance service. To subsidize the costs of exchange service in rural or remote areas, all interexchange carriers would have been required to contribute to a National Telecommunications Fund.[166] The payments from this fund wre also intended to ease the transition from the current jurisdictional separation rules to a system which allocated costs between exchange and interexchange services. Exchange access charges would have been frozen subject to the Consumer Price Index until such time as the access charges took effect.[167]

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162. *Id.* §§ 212-13, 221-23, 226.

163. *Id.* §§ 223, 226.

164. *Id.* §§ 222, 226, 228.

165. *Id.* §§ 232, 233.

166. *Id.* § 234.

167. *Id.* §§ 232, 233.

4. Telecommunications Equipment

The FCC would have retained authority to establish technical standards for transmission facilities and services, and interconnection of terminal equipment.[168] After a transition period of two years, no regulated carrier nor any regulated exchange carrier would have been able to file a tariff which included any cost associated with or caused by the provision of terminal equipment or inside wiring.[169] Terminal equipment would have had to have been offered on an unbundled basis.

To promote the development of a domestic competitive industry for the manufacture of transmission facilities, the bill would have required regulated carriers and regulated exchange carriers affiliated with facilities manufacturers to procure all products on a nondiscriminatory basis.[170] These carriers would also have had to provide specifications to all manufacturers in order to foster competitive procurement.

5. Dominant Carriers

The bill would have required AT&T to offer transmission facilities and services only through a separate subsidiary.[171] Not more than 50% of the subsidiary's board of directors could consist of employees, officers, or directors of AT&T.[172] All transactions between the parent and subsidiary were to be on an arm's-length basis.[173] Joint ventures by AT&T and the subsidiary would have been prohibited.[174] The subsidiary would have been required to conduct its own marketing, sales, advertising, installation of equipment, hiring and training of personnel, maintenance, operations, manufacturing, and research and development.[175] Finally, the subsidiary would have had to maintain its own books, records, and accounts.[176]

All of AT&T's transmission facilities and services would have been required to be offered through the subsidiary on a regulated basis, and AT&T would have been forbidden from constructing, owning, or operating duplicate, unregulated transmission facilities until effective, facilities-based competition came into being.[177]

168. *Id.* §§ 241, 242.
169. *Id.* § 242.
170. *Id.* § 243.
171. *Id.* § 251.
172. *Id.* § 252(b).
173. *Id.* § 252(d).
174. *Id.* § 252(g).
175. *Id.* § 252(h).
176. *Id.* § 252(c).
177. *Id.* § 253.

6. Telecommunications Industry

Carriers would have been allowed jointly to meet, plan, and agree, under the auspices of the FCC, on matters affecting the design, maintenance, management, development, and coordination of any network of telecommunications services or facilities. Meetings with the purpose or effect of violating federal or state antitrust laws, however, were prohibited.[178] To promote the widest possible diversity of information sources, no dominant carrier or its separate subsidiary would have been allowed to offer any information services over its own transmission facilities except for (1) limited directories; (2) time or weather information; (3) printed directory advertising; (4) electronic directory information; and (5) audio information services.[179] Mergers between owners of transmission facilities would have been limited by the FCC, and regulated exchange carriers would have been barred from providing cable television or broadcasting services in areas in which they were offering exchange services, with an exception for carriers serving rural areas.[180]

7. Protection of Ratepayers and Employees in Transition

To protect ratepayers in the transition to a competitive marketplace for telecommunications, installed terminal equipment would have had to be made available to the customer under regulation until it was fully depreciated. Alternatively, customers would have had the option of purchasing installed equipment for a price determined by a state commission. State public utilities commissions would have had the authority to auction fully depreciated or returned installed equipment so as to aid in the orderly development of a competitive secondary market in terminal equipment, and to ensure that ratepayers were fully compensated for the transfer of equipment to carriers' unregulated activities.[181]

The bill would also have established a transitional joint board, composed of three FCC commissioners and two state commissioners (1) to review exchange area boundary disputes; (2) to establish the formulas for funding, and to establish procedures for distributing funds from the National Telecommunications Fund; (3) to modify the jurisdictional separation and settlements procedures as necessary for the orderly transition to the system of exchange access charges; (4) to determine joint and common costs for long distance services; (5) to advise the FCC on equal exchange access; and

178. *Id.* § 261.
179. *Id.* § 263.
180. *Id.* § 264.
181. *Id.* § 271-72.

(6) to evaluate the assets of regulated carriers.[182] The legislation would have given ratepayers the fruits of the research they had funded at Bell Labs by requiring AT&T to grant nonexclusive licenses for all patents currently existing or developed within two years of passage of the bill for products manufactured in the United States.

8. Viability of Operating Companies

Prior to asset valuation, AT&T would have been required to distribute to its shareholders securities which represented interests in the assets or businesses of the newly created operating companies. By requiring such divestiture before valuation of the assets, the officials of the operating companies would have had a legal duty to promote and protect the independent corporate interests of the operating companies. No particular form of reorganization was imposed; the bill simply required that divestiture occur, and that after reorganization, no operating company's securities include any interest in another operating company or in AT&T.[183] A key component in asset valuation would have been the allocation of debt, some of which AT&T would have had to assume in return for its acquisition of billions of dollars of the operating companies' assets. The bill provided that AT&T take an equitable distribution of the operating companies' debt with respect to the interest rate and dates of maturity of the debt instruments.

VI. ANTITRUST LITIGATION

A. PRIVATE PLAINTIFF ANTITRUST LITIGATION AGAINST AT&T

During the last several years, AT&T has continuously been involved as a defendant in anywhere from twenty to sixty active antitrust suits.[184] Given this large number of antitrust suits, and the obvious drain on the AT&T management in supporting this level of litigation, there appears to be a trend in the late 1970's and early 1980's for AT&T to settle, where and when appropriate, as many cases as possible. In June 1980, increased pressure was put on the settlement trend by AT&T's antitrust trial loss in *MCI Communications, Inc. v. AT&T*,[185] which after trebling, amounted to 1.8 billion

182. *Id.* § 273.

183. *Id.* §§ 252(j)-(k), 253(e)-(f).

184. *See* Current Case Table, TRADE REG. REP. (CCH) (Sept. 13, 1982). Twenty-nine cases are listed in the Current Case Table, and others are listed in the main Case Table.

185. See TELECOM. REP., March 3, 1980, at 5 (No. 9), which discusses a settlement in which AT&T agreed to purchase two billion dollars of telecommunications products

dollars. AT&T has appealed this decision.[186]

B. *UNITED STATES V. AT&T*

In November 1974, the Department of Justice filed an antitrust suit against AT&T in the United States District Court for the District of Columbia. The Department of Justice alleged that AT&T used its position of dominance in the telecommunication industry to suppress new competition and that it maintained and enhanced its monopoly in violation of Section 2 of the Sherman Act.[187] The Department of Justice sought divestiture of (1) Western Electric; (2) Bell Labs; (3) the Long Lines Division; and (4) some or all of the Bell Operating Companies (BOCs).[188] After divestiture, AT&T would no longer be a vertically integrated firm, nor would AT&T be able to offer end-to-end telecommunications services.

In 1978, after appeal to the Supreme Court, the parties finally began exchanging documents. After three years of discovery and almost a year of stipulation negotiations, there appeared to be an eleventh hour settlement in January 1981.[189] The parties, however, were not able to reach a settlement, and in March 1981, trial began. In June 1981, the Department of Justice ended its case in chief, and in August 1981, after AT&T's motion for summary judgment was denied, AT&T began the presentation of its case.

1. Reopening of the 1956 Western Electric Consent Decree

In January 1956, the Department of Justice and AT&T had entered into a consent decree in which AT&T agreed not to engage in "any business other than the furnishing of common carrier communications services."[190] In March 1981, AT&T filed a motion with the United States District Court for the District of New Jersey (Judge

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and services offered by ITT, if competitively priced, over a ten year period. A deposit of two hundred million dollars was required of AT&T which is returned to AT&T at the rate of 10% of any AT&T purchases. The remaining balance would be returned in either 1990 or 1995 pursuant to the detailed terms of the agreement. The two billion dollars of purchases by AT&T from ITT over ten years represent less than 2% of Western Electric's annual sales to the Bell System over the ten year period.

186. *See* ANTITRUST & TRADE REG. REP. (BNA) A-3 (June 19, 1980).

187. *See* Department of Justice, Plaintiff's First Statement of Contention and Proof—U.S. v. AT&T, Western Electric Corp., Inc., and Bell Laboratories Inc. 3 (1974).

188. *Id.* at 527. Specifically, the Department of Justice seeks

> the separation of AT&T's ownership of intercity facilities from its ownership of local facilities and the separation of the current providers of telecommunications services from the manufacturer of telecommunications equipment and its allied research and development facilities.

189. ANTITRUST & TRADE REG. REP. (BNA) A-15 (Jan. 22, 1981).

190. United States v. Western Elec. Co., Inc., 1956 TRADE CAS. (CCH) ¶ 68,246 (Part

Victor Biunno presiding) seeking a construction of the *1956 Western Electric Consent Decree* which would not bar AT&T from "furnishing [or manufacturing equipment and facilities in connection with providing] 'customer premises equipment' and 'enhanced services' " as defined by the FCC in its *Computer Inquiry II*.[191] The FCC believed that detariffing, rather than deregulating, enhanced services and CPE would permit AT&T, pursuant to the terms of the *1956 Western Electric Consent Decree*, to offer these services and products through a separate subsidiary.[192] Various motions were filed by the parties, and amicus curiae briefs by non-parties. AT&T asked for an expedited hearing of its motion which the Department of Justice opposed. Judge Biunno then ruled that the FCC decision in *Computer Inquiry II* and the *1956 Western Electric Consent Decree* were not in conflict with each other, and the Department of Justice filed an appeal.

In January 1982, Assistant Attorney General William Baxter submitted to Judge Biunno a proposal for the modification of the *1956 Western Electric Consent Decree*. Judge Biunno accepted Baxter's proposal, and transferred supervision of the *Consent Decree* to the federal district court in Washington, D.C., for consolidation with the AT&T antitrust case already underway in that court (Judge Harold Greene presiding).[193] Baxter's proposed modifications were placed before the district court in the form of a stipulation for voluntary dismissal between the parties.

2. *The* Proposed Decree

The proposed modifications to the 1956 *Decree*, hereinafter referred to as the *Proposed Decree*, would have eliminated all provisions of the *1956 Western Electric Consent Decree* and replaced them with provisions which would have required AT&T to divest itself of its twenty-two operating companies (BOCs) "by means of a spin-off of stock of the separated BOCs to shareholders of AT&T, or by other

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V). *See* 2 A. KAHN, THE ECONOMICS OF REGULATION: PRINCIPLES AND INSTITUTIONS 295 (1971).

191. Notice of Motion and Motion for Construction of Judgment of January 24, 1956, United States v. Western Elec. Inc. (filed March 4, 1981, by AT&T).

192. The National Telecommunications Information Administration (NTIA), part of the Department of Commerce, is the principal advisor on telecommunications policy to the President, and it is charged with the responsibility of insuring that the views of the Executive Branch are effectively presented to the FCC. The NTIA responded to the *Petition for Reconsideration* of the *Second Computer Inquiry*, by supporting the FCC in its construction of the *1956 Western Electric Consent Decree*. *See* The National Telecommunications and Information Administration Petition for Reconstruction of the Second Computer Inquiry, 43 Fed. Reg. 24,348 (1978).

193. ANTITRUST & TRADE REG. REP. (BNA) 82, 110 (Jan. 14, 1982).

disposition."[194] These divested BOCs would assume control of the intrastate localized exchange systems, while AT&T retained ownership and control over its Long Lines Division, Western Electric, and Bell Laboratories. AT&T would also have been permitted to provide customer premises equipment (CPE). AT&T was given eighteen months for internal reorganization, after which the divestiture of the local operating companies would take place. AT&T's plan for this reorganization was to be submitted to the Department of Justice within six months after the effective date of the *Final Decree*.

The *Proposed Decree* would have required the divested companies to provide access to all intercity carriers on an equal basis with that afforded AT&T.[195] The operating companies were also required not to discriminate against AT&T's competitors when procuring or interconnecting equipment or services;[196] when establishing or disclosing technical specifications;[197] or when planning new facilities or services.[198] After divestiture, the BOCs would be required to provide, through a centralized organization, a single point of contact for coordination of all operating companies in order to meet the requirements of national security and emergency preparedness.[199]

The divested BOCs would have been allowed to provide only exchange and exchange access services,[200] and other natural monopoly services that were regulated by tariff. This would have precluded the BOCs from offering any form of interchange services, information services, or CPE.[201] These markets were left to AT&T to pursue. The BOCs were permitted to provide directory services (within the definition of "exchange access"),[202] but this provision was generally interpreted as "White Pages" services rather than the lucrative "Yellow Pages" services which were left in the control of AT&T.[203]

After divestiture of the BOCs, AT&T, within the *Proposed Decree*, would no longer be precluded (as it was in the *1956 Western Electric Consent Decree*) from entering any sort of business it might

194. Department of Justice, Antitrust Division—United States v. Western Electric; Proposed Modification of Final Judgment; United States v. American Telephone and Telegraph Co.; Stipulation for Voluntary Dismissal, 47 Fed. Reg. 4166 (1982).

195. *Id.* at 4167.

196. *Id.*

197. *Id.*

198. *Id.*

199. *Id.*

200. 47 Fed. Reg. at 4167-68 (*Decree*, sec. II(D)).

201. *Id.* at 4168 (*Decree*, sec. II(D)(1)(2)).

202. *Id.*

203. L. GLASSER, AT&T SETTLEMENT: TERMS, EFFECTS, PROSPECTS 346-47 (1982).

choose.[204] Antitrust prohibitions against ownership by AT&T of cable television, broadcast, electronic news, or other mass media were reduced to normal antitrust criteria, rather than the antitrust restrictions imposed by the *1956 Western Electric Consent Decree*.

Within six months after the entry of the *Final Decree*, the plan for divestiture of the BOCs was to be submitted to the Justice Department for approval. The completion of the divestiture had to occur within eighteen months after the entry of the *Final Decree*.[205] Under this plan, the BOCs had to be provided with whatever facilities, personnel, systems, and rights to technical information which would be necessary to provide all intercity carriers with equal access to interexchange facilities.[206] Although AT&T and the various BOCs could not share ownership, personnel, facilities, or accounting records, joint ownership of multifunction facilities as among the BOCs could occur via lease or other arrangements if each BOC maintained control over its own exchange telecommunications and its exchange access functions.[207]

Under the *Proposed Decree*, all supply and license contracts between the BOCs and AT&T's remaining subsidiaries would have been terminated.[208] The BOCs would have retained priority status in all dealings with AT&T, Western Electric, and Bell Laboratories until September 1, 1987. This priority status was to enable the BOCs to fulfill the requirements of the proposed *Proposed Decree* in continuing, at the BOC level, research, development, manufacturing, and other support services.[209]

Once separated from AT&T, the twenty-two BOCs would not have been restricted in consolidating into one national or several regional companies.[210] The BOCs, whatever their final configuration, could share costs to support a centralized organization for engineering, administration, and other services in order to insure a viable national communications network.[211] The BOCs could not discriminate between AT&T and other interexchange carrier when offering or procuring products or services. The BOCs would have been required to provide equal services at equal tariffs to all inter-

204. *Id.* at 347.

205. 47 Fed. Reg. 4167.

206. *Id.*

207. *Id.*

208. *Id.*

209. *Id.*

210. *Id.* Given later developments, in all likelihood there will be seven regional BOCs.

211. *Id.*

exchange carriers.[212] Although all exchange access rates were to be cost based,[213] the BOCs could seek court relief from this requirement when equal access was not possible (this relief from the requirement for equal charges is found in Appendix B to the *Proposed Decree*).[214] Where access by an interexchange carrier was not equal, the BOCs could offer a lower charge to a carrier requiring less exchange access.[215]

The *Proposed Decree* did not specify whether regulation of these requirements was to be left to the FCC or to the state utilities commissions. Assistant Attorney General Baxter has claimed that it is his understanding that BOC tariffs are within the jurisdiction of the FCC under the Communication Act.[216]

3. Problems of the Proposed Decree

a. *Language Ambiguities*

The *Proposed Decree* introduced new terminology without providing specific definitions of all terms. The BOCs were permitted to provide "exchange telecommunications" and "exchange access." AT&T was permitted to offer "interexchange communications" and "customer premises equipment" (CPE). There was no clear delineation between the realms of "exchange" and "interexchange" telecommunications. It was also within the realm of AT&T or part of the amorphous "exchange telecommunications" reserved for the BOCs.

b. *The Divestiture Plan*

Six months after the settlement was final, AT&T was permitted to formulate a divestiture plan. This provision would have permitted AT&T unilaterally to decide how the divestiture would proceed, thereby precluding control or review by Judge Greene. The critics of this arrangement feared that AT&T would intentionally structure the divestiture so as to insure the continued weakness of the BOCs as independent companies. Competitors of AT&T requested that Judge Greene withhold final approval of the settlement until after the divestiture plan was finalized. AT&T argued that the Justice Department would have final approval of the divestiture, and that AT&T's obligation to its shareholders ensured a fair division of assets because the shareholders of AT&T would also be shareholders

212. *Id.*
213. *Id.* at 4170.
214. *Id.*
215. *Id.*
216. L. GLASSER, *supra* note 203, at 350.

in the new companies.[217]

c. *The Long-Term Viability of the BOCs*

There has been concern as to how financially viable the BOCs will be once they are separated from AT&T. One technique to ensure the viability of the BOCs is to increase the access charge which the interexchange carriers incur in order to interconnect with the local exchanges.[218] Further technological advances, however, may preclude the need for these carriers to connect with the BOCs. AT&T's Chairman Brown has already warned that if local telephone companies attempt to charge AT&T "unreasonable" interconnect fees, AT&T would emply these technological alternatives to bypass the local networks.[219]

AT&T's and Assistant Attorney General Baxter's initial proposals for the removal of "Yellow Pages" advertising, terminal equipment rentals, and intrastate toll services from the BOCs would have effectively denied the BOCs access to traditional sources of revenue.[220] Confining the BOCs to local telephone services could effectively condemn them to financial ruin within a few years since technological advancements may make their present services unnecessary.[221] Without the opportunity to expand or augment services, the BOCs might be faced with severe financial difficulties.

d. *Potential For Higher Local Telephone Rates*

The loss of the terminal equipment rental market and "Yellow Pages" advertising revenues,[222] and the loss of long distance subsidies,[223] may force the BOCs to increase local telephone rates as much as 46% to maintain current revenue levels.[224] AT&T may also be permitted to bypass local exchanges and thereby deal directly with portions of the local services market, which would siphon off a very profitable portion of the BOCs market revenues.

e. *The Nationwide Telecommunications Network*

There may be a need for legislation to ensure cooperation and

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217. THE SCOTT REPORT, April 1982, at 11-12.

218. *See* Pearee & Verveer, *Some Policy-oriented Reflections on the AT&T Antitrust Settlement*, 29 FED. B. NEWS & J. 372, 373-74 (1982).

219. *See* Wall St. J., Jan. 29, 1982, at 2.

220. THE SCOTT REPORT, *supra* note 217, at 13.

221. *See* Katsh & Barney, *The Proposed AT&T Consent Decree: A Preliminary Analysis*, 9 MEDIA L. NOTES 2 (1982).

222. *See* L. GLASSER, *supra* note 203, at 19.

223. THE SCOTT REPORT, *supra* note 217, at 14.

224. *See* Chavez, *Rise in Local Rates May Come Rapidly*, N.Y. Times, Jan. 7, 1982, at 36.

reduction of interconnection problems between interexchange carriers and the BOCs. Under the proposed settlement, the BOC's, left with the local exchanges would be under state as well as federal regulation.[225] Inconsistencies in regulation may develop between the local exchange carriers and the Long Lines facilities.[226]

f. *Regulation of BOCs and Independent Telephone Companies*

Given the new economic and regulatory environment, the question arises as to whether continued regulation of the independent phone companies and the BOCs would promote the expansion of the telecommunications industry. Some industry observers feel that permitting competition among the independents and the various BOCs would promote the expansion of the telecommunications industry.[227] Others feel that allowing expansion of BOC's into any communications market would place too much power into the hands of the BOCs.[228]

g. *Patent Licensing and Competitive Problems*

The *1956 Western Electric Consent Decree* required that all components manufactured by Western Electric have patents that were automatically available to competing equipment manufacturers. The proposed settlement contained no similar requirement. Consequently, AT&T would have been able to use the revenues obtained from patent licensees to support research and development (R&D) work. This would have led to additional patents for AT&T to use in order to ensure its competitive advantages. AT&T currently holds the patents for basic semiconductor and laser technologies which will permit AT&T to extract large license fees (if it will even grant licenses) for these patents. If AT&T chooses not to license its patents to competitors, these competitors may be precluded from producing equipment capable of connecting with the AT&T network.

h. *Cross-subsidization by AT&T of New Operations*

If AT&T were permitted to move into unregulated markets, it would surely be tempted to fund its new operations with the revenues from the Long Lines Division. Competitors in these unregulated markets may rightfully assert that, given this tremendous financial base, AT&T's new operations would have an unfair advantage. Competitors have already strongly argued for the separation

225. *See* L. GLASSER, *supra* note 203 at 351.

226. THE SCOTT REPORT, *supra* note 217, at 15. *See* 356 TRADE REG. REP. (CCH) 4-5.

227. L. GLASSER, *supra* note 203, at 27.

228. THE SCOTT REPORT, *supra* note 217, at 16.

of Western Electric and Bell Labs from AT&T.[229]

i. *Access to Technical Information by Competitors*

The *Proposed Decree* would require the BOCs to share information regarding future equipment needs with all manufacturers, but it would not place the same requirement on AT&T and Long Lines. Frequently, two or more years of lead time is necessary to place such equipment in service. If Western Electric was given advance notice of equipment specifications, Western Electric would have an unfair advantage over other manufacturers in the production and sale of this equipment.

j. *AT&T's Possible Expansion into Electronic Publishing and Cable Television*

AT&T may, depending on the interpretation of the *Proposed Decree*, be permitted to enter the electronic publishing and cable television markets. Technically, the language of the *Proposed Decree* would permit AT&T to expand its operations into these markets. Numerous legislators and newspaper organizations oppose permitting AT&T to have access to the publishing market.[230] Some believe that First Amendment issues may exist. Representative Tim Wirth has stated: "The settlement fails to adequately safeguard against the threat to information diversity from AT&T being permitted to engage in information publishing over its remaining monopoly transmission facilities . . . its long distance lines."[231] AT&T has denied its ability to monopolize these markets, claiming that divestiture will eliminate this possibility.[232] The *1956 Western Electric Consent Decree* prohibited AT&T from owning cable television facilities in areas that it serviced. Since AT&T will no longer own local telephone services, this prohibition no longer applies.

4. FCC Perspective on the Proposed Decree

The FCC reviewed the *Proposed Decree* and concluded that there were three major areas of concern.[233] First, the BOCs exchange areas would each be limited to individual states, unless Judge Greene permitted an exchange area to cross over into an ad-

229. *Id.* at 17.

230. *Id.* at 18.

231. *See* L. Schwartz, Stacked Competition and Phony Regulations for AT&T: The Proposed "Telecommunications Competition and Deregulation Act of 1981 (Dec. 1981) (preliminary draft of as yet unpublished manuscript).

232. THE SCOTT REPORT, *supra* note 217, at 18.

233. FCC Analysis of AT&T Antitrust Consent Decree (1981), *reprinted in* L. GLASSER, *supra* note 203, at 344-62 [hereinafter cited as FCC Analysis].

joining state.[234] In theory, then, one could argue that each of the seven BOCs is merely a holding company for groups of state-oriented local exchange areas, with state public utilities commissions exercising exclusive authority over each exchange area. If each exchange area were under the regulation of an individual state's public utilities commission, then the FCC would have no jurisdiction over either the individual exchange areas or over the seven BOCs. The position of the FCC is that it has authority over the seven BOCs, based on the FCC's continued "superintendency of the national phone network."[235]

Second, the FCC has also voiced concern about the structure and pricing levels for access charges into the local exchange areas.[236] Judge Greene, the FCC, and state public utilities commissions could all, in theory, attempt to enforce their individual views on proper access tariffs. The FCC has stated that it alone has authority to regulate these tariffs. As the BOCs file tariffs, the role of the FCC in setting access tariffs will continually evolve.[237] Given the new structure of the communications industry under the *Proposed Decree*, the FCC will also need to modify its "separation, accounting, and depreciation policies."[238]

Third, the FCC is also concerned about timing issues between various dates set in *Computer Inquiry II* and dates discussed in the proposed *United States v. AT&T* settlement. Such timing issues will require a great deal of attention to prevent different dates for similar changes being enforced by the FCC and by Judge Greene.[239] The FCC has stated that it would be helpful if Judge Greene would include a "Terminal Railway" clause in the final decree to ensure that interpretations by AT&T and the BOCs of the decree are subject to lawful agency orders issued by the FCC.[240] The FCC has stated that

234. United States v. Western Elec. Co., Proposed Modification of Final Judgment; United States v. American Tel. & Tel. Co., Stipulation for Voluntary Dismissal, 47 Fed. Reg. 4166, 4169 (1982).

235. FCC Analysis, *supra* note 233, at 351.

236. *Id.*

237. *See* Procedures for Implementing the Detariffing of Customer Premises Equipment and Enhanced Services, 89 F.C.C.2d 694, 699 (1982).

238. FCC Analysis, *supra* note 233, at 351.

239. *Id.* at 352.

240. *Id.* at 373. The "Terminal Railroad" clause concept is taken from *Terminal R.R. Ass'n v. United States*, 266 U.S. 17 (1924). Paragraph 6 of the decree stated that:

> Nothing in this decree shall be taken to affect in any wise or at any time the power of the Interstate Commerce Commission over the rates to be charged by the Terminal Railroad Association, or the mode of billing traffic passing over its lines, or the establishing of joint through rates or routes over its lines, or any other power conferred by law upon such commission.

Id. at 25.

Computer Inquiry II and as many as twelve of its ongoing proceedings are "substantially affected" by the proposed settlement.[241]

5. *Congress and the* Proposed Decree

a. *H.R. 5158*

The most recent form of H.R. 5158 represented an attempt by the House Telecommunication Subcommittee to deal with the alleged deficiencies of the modification of the *1956 Consent Decree* contained in the proposed *United States v. AT&T* settlement.

Unlike the proposed settlement, H.R. 5158 would have provided that *Yellow Pages* advertising remain with the BOCs because such listings are a natural function of the local companies and would provide them with revenue to keep local phone rates low.[242] The *Yellow Pages* produce an annual national revenue of approximately $2 billion. Pay telephone operations and maintenance would also have

241. FCC Analysis, *supra* note 233, at 356. A complete checklist of the impact of the *Consent Decree* on major FCC matters follows (see below for explanation of table):

CC Docket No. 78-72 (Access Charges)	S P
ENFIA III	S P
BSOC Tariffs Nos. 9 & 10	S P
CC Docket No. 80-286 (Joint Board)	P
Docket No. 20828 (Computer II)	S P
CBI-SNET Reconsideration	S P
Docket No. 20188 (Depreciation/ELG)	P
CC Docket No. 78-196 (USDA)	P
CC Docket No. 79-105 (Station Connections)	P
CC Docket No. 79-318 (Cellular)	P
CC Docket No. 80-742 (License Contracts)	S P
CC Docket No. 80-53 (Procurement)	S P
WPC-3071 (Fiber Optics Filing)	U
Rate of Return Regulation	U
CC Docket No. 79-187 (1978 Earnings)	U
CC Docket No. 79-245 (Cost Manual)	U
Interstate Service Tariffs	U
CC Docket No. 79-252 (Competitive Carrier)	U
CC Docket No. 78-72 (Alaskan Entry)	S
CC Docket No. 81-2126 (Registration)	S
NTIA Joint Planning/Ownership Petition	S
CC Docket No. 80-634 (Comsat)	S
CC Docket No. 80-176 (International Resale)	S
CC Docket No. 80-632 (TAT-4)	
Cable TV Cross Ownership	S

S—Substantively Affected (i.e., new policies may be necessary),
P—Procedurally Affected (i.e., new mechanisms may be needed to achieve established policy goals)
U—Generally unaffected.

242. *House Panel Approves Bill Adding New Limits to AT&T*, CONG. Q., March 27, 1982, at 688.

remained with the local operating companies. As with the provision for *Yellow Pages*, this would have given the local companies more revenue and ameliorated their need to charge higher local rates. All installed terminal equipment would have remained with the BOCs, and it would have continued to be provided under tariff until fully depreciated. After five years, the operating companies would have been permitted to sell, but not to manufacture, new terminal equipment, including computers, through separate subsidiaries. The bill would have provided protection for employees' rights and benefits during the transition period to deregulation (labor protection provisions would have been extended to all carriers which were permitted to establish a separate entity). AT&T would have been prohibited from setting up its own information services and offering these services over company phone lines. This provision, lacking in the proposed settlement, had been sought by newspaper publishers and others who viewed AT&T's ability to provide such services as anticompetitive.

b. *Reaction to H.R. 5158*

The Wirth bill, which attempted to deal with what was viewed as deficiencies in the proposed settlement, was met by strong opposition from AT&T. According to AT&T, the bill would have disrupted the nation's phone system by placing undue burdens on long distance lines. Congressman Wirth contended that committee members were sympathetic to AT&T and that they caused procedural delays which included forcing the reading of the 130 page bill line by line and demanding extensive debate on each amendment.[243] As a result of these efforts by the opponents of H.R. 5158, Wirth, in a surprise move, withdrew his bill from consideration and claimed that AT&T had waged a campaign of "fear and distortion," and that "[t]he only way to pass legislation [in the time remaining] would be to accept an agreement dictated by AT&T."[244]

6. Modifications of the Proposed Decree *by Judge Greene*

Judge Greene insisted in his August 1982, opinion that the proposed settlement plan be modified in several critical areas. These areas addressed many of the concerns found in the Packwood and Wirth bills. Congressman Wirth praised Greene's opinion as a positive first step, yet he cautioned that Congressional action was still

243. *See Supporters of AT&T Bill Block Major Change*, CONG. Q., July 17, 1982, at 1696.

244. *See AT&T Bill Dropped, Killing Rewrite Efforts*, CONG. Q., July 24, 1982, at 1773.

needed to establish a comprehensive telecommunications policy.[245]

Although Judge Greene recognized that he had no power to order changes to the *Consent Decree*, he was able to insist on modifications to the settlement agreement by threatening the parties with a resumption of the trial if they did not agree to his modifications (Judge Greene gave the parties fifteen days to consider whether they would accept his modifications).[246] Because Judge Greene's opinion contained several statements indicating that there was sufficient evidence to support the government's position, AT&T, faced with Judge Greene's ultimatum and recognizing the very real possibility that it could lose the case on the merits if the trial were to be resumed, agreed to his modifications.[247]

Judge Greene set forth ten modifications to the order, four of which constitute major changes to the proposed *Consent Decree*[248]:

1. AT&T is to be barred for seven years from "electronic publishing" activities using its own transmission lines (this prohibition would not include the offering of directory or time/weather services). Judge Greene noted the potential for AT&T to discriminate against competitors and to deter potential competitors, although he also noted that AT&T, at the present time, had no plans to enter this field;[249]

2. Divestiture, the keystone of the settlement, was considered by Judge Greene to be an appropriate remedy, and he noted that the charges that AT&T may have monopolized the intercity communications and telecommunications product market "may be well taken."[250] As part of this divestiture, the BOCs would be given the following powers:

a. to provide but not to manufacture, customer premises equipment (CPE);

b. to publish the *Yellow Pages* (AT&T must personnel, systems, and rights to the information are necessary to produce the advertising directories); and

c. to request the court to remove the restrictions on the local companies from providing long distance service and maintenance;[251]

3. The local companies are to have debt ratios of approxi-

245. *Courts AT&T Ruling Refocuses Attention on New Legislation*, CONG. Q., Aug. 14, 1982, at 1986.

246. *Judge's Power in Settlements Outlined in AT&T Decision*, Nat'l L.J., Aug. 23, 1982, at 3.

247. *Id.*

248. ANTITRUST & TRADE REG. REP. (BNA) 317 (Aug. 12, 1982).

249. *Id.* at 318.

250. *Id.*

251. *Id.* at 317.

mately 45%, and the quality of the debt is to be equal to that of AT&T;

4. The local companies' billing services must indicate to customers that they may choose an independent carrier for long distance service. These carriers must be given the same access as AT&T receives, or in the alternative, price discounts. Finally, the order reserves the court's jurisdiction to insure that the purposes of the *Decree* are carried out, and it prohibits the implementation of a reorganization plan without the court's approval.[252]

Judge Greene supported the removal of the restrictions imposed on AT&T by the *1956 Western Electric Consent Decree*, finding that AT&T's monopoly power had its root in AT&T's control of the local operating companies, and "with the divestiture of these local exchange monopolies, continued restrictions are not required unless justified by some other rationale."[253]

In late August 1982, the Justice Department sent Judge Greene a proposed order incorporating all of his conditions.[254] The Justice Department had feared that the local companies would monopolize the selling of complex exchange equipment used by businesses. But Judge Greene rejected this position, noting that the remote possibility of such monopolization was due to "the certainty that [the local companies] would provide healthy competition for AT&T."[255]

In October 1982, AT&T filed a four volume plan which laid out the seven regions in which the local companies would operate.[256] The AT&T plan also outlines Local Access and Transport Areas (LATA's) within which the local companies will provide services. Other carriers will be allowed to provide long distance service linking the LATA's. The filing of this plan by AT&T was the first major step in the divestiture which is to be concluded by February 24, 1984.[257]

VII. A COMPARISON OF DIFFERENT PROPOSALS FOR RESTRUCTURING AT&T

Although not complete in every detail, Table I sets forth a comparison of major provisions of *Computer Inquiry II*, the *United States v. AT&T Consent Decree* (the "Proposed Decree"), the Wirth Bill (H.R. 5158), and the Packwood Bill (S. 898).

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252. *Id.*
253. *Id.* at 318.
254. ANTITRUST & TRADE REG. REP. (BNA) 381 (Aug. 26, 1982).
255. *Id.*
256. N.Y. Times, Oct. 5, 1982, § D, at 1, col. 6.
257. *Id.*

Table I

COMPARISON OF DIFFERENT PROPOSALS FOR RESTRUCTURING AT&T

CRITICAL QUESTION	COMPARISON OF PROPOSALS			
	Computer Inquiry II	1982 Consent	Wirth Bill	Packwood Bill
1. What will be the role of market competition?	CPE & Enhanced Services	AT&T Deregulated	AT&T Partially Deregulated	AT&T Deregulated
2. Who will own Bell Labs?	AT&T	AT&T	Initially separate company	AT&T
3. Who will own the Bell Operating Companies?	AT&T	Separate companies	Initially separate companies	AT&T
4. Who will own Western Electric?	AT&T	AT&T	Initially separate company	AT&T
5. Who will own Long Lines?	AT&T	AT&T - Partially separate subsidiary	AT&T	AT&T
6. Who will own Yellow Pages?	AT&T	BOCs	AT&T	AT&T
7. Who will control the pay telephones?	AT&T	BOCs	AT&T	AT&T
8. What will be the role of the FCC?	Continued active	Many questionable areas	Active regulator	Active regulator
9. What will the states be able to do?	Lesser role as CPE is deregulated	Active in exchange areas in access charges	Active at state level	Active
10. How will the employees be protected?	AT&T left intact	Neutral	Statutory protections	Neutral

11.	How will the stockholders be protected?	AT&T still dominant	AT&T Must set up BOCs as financially viable	Neutral	Neutral
12.	How will equipment be transferred upon divestiture?	FCC will need to interface *Computer Inquiry II*	Yes	——	
13.	Who will be able to sell customer equipment?	AT&T separate subsidiary	AT&T not BOCs	AT&T separate subsidiary	AT&T separate subsidiary
14.	Where will research and development take place?	Bell Labs	Bell Labs & BOCs	Bell Labs	Bell Labs
15.	What will happen to existing Bell Lab patents?	AT&T will keep them	AT&T will keep them	Open to public license	AT&T will keep them
16.	What will be the BOCs' responsibilities?	—	Manage local exchange areas	—	—
17.	What will happen to the AT&T/BOC license agreements	Will remain	Leased	Revised	Revised
18.	Will telecommunications carriers be required to interconnect?	Yes	Yes	Yes	Yes
19.	Will AT&T be allowed to go into data processing?	In a separate subsidiary	Yes	In a separate subsidiary	In a separate subsidiary
20.	Will any safeguards against price discrimination be established?	FCC will monitor	Court & FCC will monitor	FCC will monitor	FCC will monitor
21.	How will the public be protected?	FCC	FCC & court	FCC	FCC
22.	Will telecommunications carriers be allowed pricing flexibility?	Some	Yes	Yes	Yes

VIII. FUTURE TRENDS IN THE TELECOMMUNICATIONS INDUSTRY

A. EMERGING LEGAL STRUCTURE

In his historical analysis of AT&T's development and growth, Gerald Brock reviewed the numerous strategic decisions made by AT&T's management throughout AT&T's existence.[258] One such decision was AT&T's acceptance of the 1913 "Kingsberry Commitment" in which AT&T agreed not to continue its attempt to take over the telecommunications industry; as a result, the competition between AT&T and the independent telephone companies was greatly reduced.[259]

Given a history of strategic decisions by AT&T's management, it is not surprising that, during deliberations with Congress and the FCC over the future structure of AT&T, AT&T was not only willing to accept a separate subsidiary as part of the revised structure of AT&T; it also proposed procedures to establish the separate subsidiary and began to create a separate AT&T subsidiary.[260] AT&T agreed with Assistant Attorney General Baxter to spin off the BOCs, thereby retaining Western Electric, Bell Labs, Long Lines, and Bell headquarters instead of risking an unfavorable ruling in the *United States v. AT&T*[261] antitrust litigation.

Initially, the AT&T separate subsidiary, under *Computer Inquiry II* and both the Packwood and Wirth bills, would have been the deregulated portion of AT&T, while AT&T would have remained subject to FCC and state public utility commission regulation. After the *United States v. AT&T Proposed Decree*,[262] however, the AT&T parent companies (Bell headquarters, Western Electric, Bell Labs, and the portion of Long Lines offering enhanced services pursuant to *Computer Inquiry II*) will be deregulated, while the portion of Long Lines offering basic services (and enhanced services until the procedures established under *Computer Inquiry II* have been fully implemented) will be regulated. Thus, the future legal structure of AT&T will reflect AT&T's status as a substantially unregulated corporation. As the FCC continues its deregulation of the telecommunications in-

258. G. BROCK, THE TELECOMMUNICATIONS INDUSTRY (1981).

259. *Id.* at 155-58. In more detail, under the 1913 "Kingsberry Commitment," AT&T unilaterally agreed to dispose of its Western Union stock, to allow interconnection with competing independents, and to refrain from further purchases of competitors in return for the U.S. Attorney General's decision not to pursue antitrust litigation against AT&T and the Bell System.

260. Copithorne, *Key Word at AT&T is "Bus,"* 26 DATAMATION, May 1980, at 64.

261. *See supra* notes 186-257 and accompanying text.

262. *Id.*; 47 Fed. Reg. 4166 (1982).

dustry under *Computer Inquiry II*, the size of the AT&T separate regulated subsidiary will gradually decrease.

The two-part legal structure imposed upon AT&T must be extremely flexible to encourage advancement in communications technology, but it must be rigid enough to prevent cross-subsidization from regulated to nonregulated affiliates. Cross-subsidization would harm monopoly rate payers and unfairly enhance the competitive position of the unregulated separate subsidiary.

In addition to the FCC's regulation of basic services and deregulation of enhanced services pursuant to *Computer Inquiry II*, the FCC will remain active in the regulatory arena through its proceeding to revise the Uniform System of Accounts (USOA), its proceeding involving the Manual and Procedures for the Allocation of Costs, and its administration of access charges for the local exchange areas. The FCC will continue to exercise overall supervision of the national telecommunication network, as well as numerous other related communications areas. Given this pervasive enforcement of the nation's communications policy, the FCC will undoubtedly continue to play a major role in regulating the seven regional BOCs, despite the fact that practically all local exchange areas will be within individual states. Customer premises equipment (CPE) will be deregulated, and AT&T will be allowed to offer CPE. The BOCs will be able to offer CPE under tariff only where unregulated CPE providers are unwilling to provide CPE (e.g., in isolated or unprofitable areas).[263]

B. Emerging Communications Technologies

The 1980's will witness an enormous growth in the information industry because the capabilities for gathering, manipulating, and disseminating information are based on advancing computer and communications technologies which comprise many different technologies including, but not limited to, satellites, fiber optics, cellular, Digital Electronic Message Service (DEMS), teletext (over-the-air one way transmission of material such as airline schedules and stock market news), and videotexts (involving two-way communication such as CATV).[264] Communications technology will continually increase the capability of carrying larger amounts of data at greater

263. For example, in remote rural areas, where there is limited demand for CPE, it may not be profitable to offer CPE, and thus the BOC's may need to offer CPE on a tariff basis.

264. *See Micro Electronics: A Survey*, The Economist, March 11, 1980, at 3; Noyce, *Microelectronics*, Sci. Am., Sept. 1977, at 63, 68.

speeds and with lower unit costs.[265] All of these technologies require a flexible and fair legal structure if they are to develop to their fullest potential.[266] As these technologies develop further, they will have a dramatic impact on the legal and regulatory structure and environment of the telecommunications industry. The BOC legal structure, for example, is premised on the continued technological and economic viability of the local exchange areas. AT&T, however, has stated that if access charges into local exchange areas become too high, AT&T will use technology presently available to bypass the local exchange areas, and instead connect its Long Lines directly to its customers.[267]

C. INTERMIX OF THE EXPECTED LEGAL ENVIRONMENT AND FUTURE COMMUNICATIONS TECHNOLOGY

Given the emerging legal structure of deregulated inter-local exchange (i.e., between cities), communication and customer premises equipment (CPE), and regulated intra-local exchange (i.e., intracity) communication, an ever increasing variety of communications technologies can be expected to appear in the communications marketplace. Although AT&T and the BOC's will dominate their respective areas, numerous competitors offering new products and services can be expected to enter, or even to create, new markets for these goals and services.[268] A shake-out of these new competitors is inevitable.[269] In addition, the effects of the asset division between AT&T and the BOCs can be expected to continue well into the late 1980's, as will the effects of *Computer Inquiry II*.

CONCLUSION

Overall, the pace of change in the market for communications technology can be expected to increase rapidly in the 1980's. The intermix of FCC and state public utility regulation, therefore, will

265. *See* Hindin, *Large Scale Integration Latches on to the Phone System*, ELECTRONICS, June 5, 1980, at 113. *See also* Branscomb, *Computer Technology and the Evolution of World Communications*, 47 TELECOM. J. 206, 208 (1980).

266. *See* Hardman, *A Primer on Cellular Mobile Telephone Systems*, 29 FED. B. NEWS & J. 385 (1982); Senter, *Private, Intracity Data Communications Networks*, 29 FED. B. NEWS J. 414 (1982); Pace, *A Bold New World for Video*, N.Y. Times, April 14, 1982, at D1.

267. *See* Uttal, *What's Ahead for AT&T's Competitors*, FORTUNE, Dec. 28, 1981, at 79.

268. *See Telecommunications: Everybody's Favorite Growth Business—The Battle For a Piece of The Action*, BUS. WEEK, Oct. 11, 1982, at 60.

269. *See* Oren & Smith, *Critical Mass and Tariff Structure In Electronics Markets*, 12 BELL J. ECON. 467 (1981) (theoretical analysis of minimum size to offer successful communications services).

need to remain flexible in order to adapt to changing communications technologies and to changes in the economics of the communications marketplace.