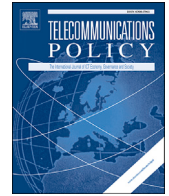


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An unsung success story: A forty-year retrospective on U.S. communications policy

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ABSTRACT

This paper looks back at forty years of U.S. communications policy, and concludes that all of the challenges that were salient when *Telecommunications Policy* published its first issue—the lack of competition in CPE, long distance, local telephone service, television networks, and multichannel video program distribution—have essentially been addressed. The other technology that has grown in importance since 1976—the Internet—is widely regarded as a raging success. Although no history is completely uniform, the past forty years illustrates the key considerations underlying the choice between whether to impose access regulations or whether to rely on facilities-based competition. Moreover, the paper considers the important role that U.S. courts have played in promoting competition and consumer welfare. In many cases, timely judicial intervention has forced regulators to retreat from positions that protected incumbents and limited competition. The paper concludes with outlooks on new issues and debates that will continue to arise.

1. Introduction

Since the very beginning, the goal of *Telecommunications Policy* has been to provide a venue for academics to offer policy guidance to key actors (Day, 1976a). It arose at a time when government officials, academics, and industry actors were just starting to create venues to explore the increasingly complex issues posed by developments such as the emergence of cable television and the impending breakup of AT&T.¹ The Journal has consistently offered a home for influential articles that have framed and shaped a wide range of critical regulatory decisions.

One inevitable consequence of such a mission is that the articles that have graced the Journal's pages have looked forward and concentrated on the next set of challenges that must be surmounted. The result has been a tendency to focus on the part of the glass that remains half empty and to downplay, if not ignore, the part of the glass that has become half full. This special issue commemorating *Telecommunications Policy's* fortieth anniversary provides a welcome opportunity to look backward instead of forward and to offer a long-term assessment of how far U.S. communications policy has come.

Recall the central challenges that dominated the telecommunications policy agenda in December 1976. For voice, U.S. policymakers were trying to promote competition in customer premises equipment (CPE)² and long distance both through regulation and the ongoing

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¹ Another prominent example was the Airlie House Conference that would eventually evolve into the annual Telecommunications Policy Research Conference (TPRC). Like *Telecommunications Policy*, TPRC has the goal of bringing together academics, policymakers, and industry leaders to engage with one another over cutting-edge research. Initially supported by the White House Office of Technology Policy, the Federal Communications Commission, and the Markle Foundation, this conference was described by this Journal as “a unique focus for policy research” (Dordick, 1977) as well as “the most important annual gathering of individuals interested in the specifics and scope of telecommunications policy research in the USA and, to a much lesser extent, internationally” (Day, 1976b).

² CPE includes both residential equipment, such as handsets, as well as business equipment, such as switches known as public branch exchanges (PBXs).

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antitrust case that would eventually lead to the breakup of AT&T. At this point, competition in local telephone service was still viewed as impossible.

With respect to video, one major concern was the decades-long dominance of three broadcast television networks and the potential for them to exercise vertical market power against the movie studios and local broadcast stations. Moreover, cable television had existed for nearly three decades, but had yet to achieve widespread consumer acceptance and remained in regulatory limbo because of the lack of a clear resolution of the scope of the Federal Communications Commission's (FCC's) jurisdiction over this new technology.

Waiting in the wings was the technology that would fundamentally change all of communications policy and would eventually become one of the most pervasive influences in modern life: the Internet. As of 1976, however, the Internet remained more dream than reality, and technologies that combined communications with computing power had just begun to attract regulatory attention.

Looking back from the vantage point of forty years down the road, what is perhaps most striking is the extent to which these challenges have largely been solved. In most cases, the solution has been the result of structural changes that enhanced facilities-based competition rather than agency-imposed behavioral requirements. Moreover, close inspection reveals that in most cases, prodding by the courts often served as a key institutional catalyst for change.

2. Voice

Regarding conventional telephone service, the policy problems confronting the U.S. in December 1976 were somewhat different from those confronting the rest of the world. Other countries were striving to increase low telephone penetration rates and to improve the poor performance of government-owned systems that would eventually lead to the privatization wave that swept the industry during the 1980s and 1990s. The U.S., in contrast, had already achieved a household penetration rate of over 90% by 1970 ([U.S. Census, 1975, 783](#)) and had long been home to the only major telecommunications system in the world that was completely privately owned.³

Instead, the focus in the U.S. was on the breakdown of the previous belief that all aspects of the telephone system constituted a natural monopoly and the accompanying realization that multiple providers could serve portions of the network efficiently. In particular, regulators and antitrust courts had begun to focus on promoting competition in CPE and long distance. The possibility of competition in local telephone service would not emerge until later and would find its most concrete manifestation in the Telecommunications Act of 1996.

What is most striking is the extent to which each of these policy challenges have largely been resolved over the past forty years. The mechanism of change has been more the result of facilities-based competition than government-mandated behavioral requirements. Furthermore, a review of the history reveals how well-timed judicial interventions have played a critical role in driving these changes.

2.1. Customer premises equipment (CPE)

Until the late 1960s, few questioned the conventional wisdom that the entire telephone represented an integrated natural monopoly, all aspects of which had to be coordinated and controlled by a single entity. Consistent with this belief, the Bell System maintained strict control over all devices attached to its network. All handsets had to be manufactured by and leased from AT&T's equipment subsidiary, Western Electric.

The Bell System enforced these requirements by including so-called foreign attachment provisions in its tariffs that prohibited subscribers from connecting equipment made by any other manufacturer to the network. These restrictive policies regarding CPE had already led the 1949 government antitrust suit that was settled in 1956 by an agreement that allowed it to keep Western Electric, but required that it refrain from entering the computer business.⁴

Since that time, remarkably little innovation had occurred in handsets, which was limited to the introduction of the Princess phone in 1959 and the Trimline phone in 1965. Interestingly, Bell Labs had developed answering machine technology in 1950, but suppressed it out of concern that it would reduce telephone calling.

Over time, key decisionmakers began to recognize that the telephone network was more properly regarded as a series of separate, vertically related markets consisting of CPE, local service, long distance service, and the content and other collateral services provided through the network. Many of these markets were potentially open to competition. Of these, CPE was the most obvious candidate for reform.

By 1976, the Bell System's control over CPE was already under significant pressure, triggered by a seemingly trivial device known as the Hush-a-Phone. The Hush-a-Phone was a plastic cup that could be attached to a handset to limit the extent to which one person's phone conversation would interfere with and be disrupted by other conversations taking place in the same room. After considering the case for seven years, the FCC accepted the argument that this device violated the foreign attachment provisions contained in the Bell System's tariffs, only to see that decision struck down on judicial review because the U.S. Court of Appeals for the D.C. Circuit decided that consumers should be left to judge for themselves how best to use the network so long as that use did not interfere with others. Indeed, the proffered alternative (cupping your hand around the mouthpiece) had the same deleterious effects as the Hush-a-Phone itself.⁵

The next landmark dispute over CPE arose with respect to the Carterfone, a device that extended the reach of the wireline telephone

³ For an analysis of the exceptional year during World War I when the federal government took over the U.S. telephone system, see [Janson and Yoo \(2013\)](#).

⁴ *United States v. W. Elec. Co.*, 1956 Trade Case. (CCH) ¶68,246 (D.N.J. Jan. 24, 1956).

⁵ [FCC \(1955\)](#), *rev'd*, 238 F.2d 266 (D.C. Cir. 1956).

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