

Special Review Memorandum

Re: FCC Reforms: What Can Be Done?

Foreword

Last month, Senator Jay Rockefeller commendably said he wanted to make reform -- even possible restructuring -- of the Federal Communications Commission (FCC) a priority. The Senator was upset over the FCC's planned (and, since adopted) changes in media ownership rules, and well-publicized shortcomings in broadband service availability (or, more accurately, reported or claimed shortfalls). Repeatedly, the Senator said the FCC just isn't working.

Ossa on Pelion

This past week, the House Commerce Committee's leadership -- both Democrats and Republicans -- also announced a full-fledged "investigation" into how the FCC's been operating. They'll probably not address our decades-old concern -- the fact the FCC (a) never convenes fact-based, trial-type hearings and (b) all too much is decided secretly, through a mysterious "circulation" process. As Senator Obama's commendably said, "The public's business should be handled in public." But maybe the House process inquiry will yield something. Man, even woman, must always live on hope, right?

Now, it seems unlikely a badly fractured Congress in an election year (or even later) would tackle a complicated matter such as "attic-to-basement" FCC reform -- especially as there's no real constituency for "good government," and none of the companies regulated by the FCC are really clamoring for major change. They want tweaks -- a few nips-and-tucks. But not much more. It's not just "Stockholm syndrome," either; they're worried about agency retaliation if they were to say more.

But neither Senator Rockefeller nor the Commerce Committee leadership are that far off, are they, in assuming that fundamental changes need to be made. So here's the first of a series of well-considered suggestions regarding ways the current FCC system might be seriously -- and, productively -- changed.

Revisiting the Ash Council Recommendations

The last time there was a serious examination of the FCC and its structure was in the early 1970s, when the Nixon Administration asked former Litton CEO Roy Ash to review how Government was regulating -- and, what changes might be appropriate. It was the Ash Council report which laid the basis for the "single administrator" system which is the most common regulatory approach these days.¹

¹ The 1988 NTIA Telecom 2000 report reviewed the FCC's international communications activities, and concluded that most of those should be transferred to the U.S. Departments of State and Commerce. In 1996, the House Telecommunications & the Internet Subcommittee heard recommendations that the FCC's frequency management operations and those of the Executive branch be merged. Remember, most of what the FCC actually does is oversee the frequency

Remember, the Government now relies on single administrators, appointed by the Administration and confirmed by the Senate, to run the Environmental Protection Agency, the Food & Drug Administration, the National Highway Traffic Safety Administration, the Federal Aviation Administration, the Occupational Safety & Health Administration, and most bank regulatory operations (through the Office of the Comptroller of the Currency and the Federal Deposit Insurance Administration). Thus, by far a majority of Federal regulation in this country isn't handled by bipartisan, independent regulatory commissions -- and, that's been true for decades.

The Ash Council said they thought a single administratorship might be able to handle most of the FCC's responsibilities. They said it'd be speedier, more in-line with standard notions of Presidential powers and responsibilities. But when it came to certain media functions, they said, a bipartisan collegial approach might be better. At that time, remember, there still was a "Fairness Doctrine," the FCC was heavily involved in regulating the TV programming industry (both production and distribution), and the agency had numerous license renewal challenges before it (mostly petitions to deny, but a few comparative applications as well).

What About Today?

Now, the FCC's far less involved in regulating media and its content these days, of course. The FCC also seems to get into "political broadcasting" less often. So one of the chief predicates for carving out an exemption for the FCC -- its media functions -- is less valid now than when the Ash Council was debating the matter.

But assuming it's desirable to maintain some sort of bipartisan, collegial system to handle media matters, what about the rest of the FCC? What about its Wireline Competition Bureau -- the remnants of what used to be called the Common Carrier Bureau.

Various Arcane Operations

The FCC's Wireline Competition Bureau handles a variety of arcane functions. They oversee operation of the national telephone numbering system, for instance. They work with the Federal Trade Commission's Consumer Protection Bureau on do-not-call and similar rules. The FCC's Bureau duplicates the review of telephone industry mergers which is usually undertaken by the Justice Department's Antitrust Division. The FCC's Bureau also strives to come up with new and innovative reasons to deny any and all forbearance requests -- these folks, after all, have a keen sense of slot and position preservation, you know.

It's worth noting, too, what the FCC's Wireline Competition Bureau does not do and, indeed, has never shown much interest in doing. For example, they do not

management activities of private frequency coordinator groups. That oversight could as well be performed by NTIA's IRAC, of course.

police the financial activities of FCC regulatees. When the collapse of WorldCom produced the biggest corporate failure in U.S. commercial history, FCC Chairman Michael Powell responded to a House Financial Services Committee inquiry by acknowledging a quite fantastic list of omissions.

The FCC's Wireline Competition Bureau has no standardized procedures for dealing with the Securities & Exchange Commission, any of the stock exchanges, or the U.S. Attorney for the Southern District of New York. The Bureau has very limited engineering resources. In recent years, an effort has been made to improve the volume and timeliness of FCC reports on the industry. But the FCC -- unlike other regulatory agencies -- doesn't track research and development, investment, or even industry coverage.² They're an "expert agency" without a great deal of in-house subject-matter expertise (the FCC's expertise regarding its own rules is another matter, right?).

Are These Functions Really Necessary?

From a budget standpoint, the Wireline Competition Bureau is primarily engaged in these "big ticket" activities:

- :: Regulating Terminating Access. AT&T, Verizon, and even smaller phone companies still say the prices charged to terminate long-distance calls need to be policed, because the carriers terminating such traffic all enjoy a "natural monopoly bottleneck." (Heard that before?) Now, you might think that protecting Verizon from being overcharged by AT&T isn't exactly the most compelling "public interest" proposition. It also isn't clear why possible overcharging in South Succotash, Idaho, say, has to be made a Federal matter. Why couldn't the Idaho Commission police that? But major phone companies -- and, certainly the FCC bureaucracy -- think this price control function is just critical, and it has to be kept Federal. And, don't worry. There's nobody at the FCC even contemplating a disengagement from this increasingly competitive field.³

- :: Overseeing USAC. Before the Bell System breakup in 1982-84, part of AT&T's Long Lines Department handled almost all the

² The Senate Commerce Committee just last fall approved legislation to mandate "broadband mapping" -- developing public information on the availability of high-speed Internet access -- because of dissatisfaction with what the FCC had been doing. This responsibility was assigned to the Commerce Department, incidentally, and not the FCC.

³ As your Review has noted, more than 14 million people now rely on cable television systems for their phone service, and the FCC doesn't police what those systems are charging to handle other companies's traffic. There also are an increasing number of wireless-to-wireless calls which bypass the public switched telephone network altogether. Do you think that if South Succotash Phone Co. ran amuck, traffic might shift to competing systems and companies? Please be assured there's no one at the FCC who seems able to imagine that!

"separations and settlements" matters which are now subsumed by the Universal Service Fund operations, run by the quasi-nongovernment Universal Service Administrative Company (USAC)(which the FCC ordered the industry to create). Today, about \$8 billion a year is collected, then distributed according to complicated formulas, etc. One goal is to maintain wireline service in rural and small town America -- where the U.S. Department of Agriculture also has major communications support programs. Another goal is to ensure the urban poor all have access to wireline phones -- even if most of them use cellphones (including prepaid ones) these days. The FCC staff, in theory, oversees all this. They don't actually do much, but they liaise, monitor, and oversee what USAC is up to. Sound useful and productive?

- :: Subsidizing schools, libraries, and nonprofit health care. Then, there's the \$2.65 billion a year which USAC disburses to underwrite use of the Internet by schools, libraries, and nonprofit health care operations. This program was supposed to be an "initial capital grants"-type program but, like most, has morphed into an ongoing support proposition. The FCC, incidentally, doesn't particularly coordinate with the Department of Education, the Department of Health & Human Services, state agencies, governors, or the Bush Administration. But overseeing this USAC function, again, generates FCC work.
- :: Supporting the wireline competitors. Finally, the FCC spends a good deal of time and attention on local competition issues -- or, more accurately, making sure that incumbent carriers like AT&T give some of their competitors special facilities access and pricing deals. In effect, the FCC runs a small business support effort -- and, it's been quite successful, at least as far as these small businesses and their shareowners are concerned.⁴

Reassigning and Terminating Functions

Now, do you really think there's a strong public policy case to be made for maintaining these "big ticket" activities by the FCC's Wireline Competition Bureau? It seems to us that the Federal Government really has no business running an operation which has, as a major program goal, protecting one giant multinational corporation from the hypothetical depredations of another. Airlines, railroads, motor carriers, pipelines, and ocean/water shipping companies all seem able to work out

⁴ The FCC has had very little to do with the development of cable television-provided telephone services, somewhat more to do with the wireless alternatives, and a great deal to do with classic "CLECs" (competitive local exchange carriers). Cynics note that there are a lot more Common Carrier/Wireline Competition Bureau alumni working for this subset of the local exchange business than cable or wireless.

the equivalent of "terminating access" issues -- and, without the active involvement of 250-odd civil servants and five Presidentially appointed Commissioners in Washington. For heaven's sake, why wouldn't the marketplace take care of these communications industry relationships just as effectively?

Sure, we understand the argument against "flash cut" deregulation. In President Carter's air passenger and air freight legislation, various functions of the Civil Aeronautics Board (CAB) were terminated, but according to a calendar -- after January 1, 1979, thus and such was terminated; after January 1, 1980, the following, and so forth. It was a variant on Admiral Hyman Rickover's plan for Pentagon reform -- close down its corridors, one by one.

Former Missouri Commission Chairman John Shapleigh has said that, given the certainty of a fixed "drop dead" date, communications carriers can almost certainly work all these "terminating access" issues out. Carriers are also quite capable of resolving the related issue of "intercarrier compensation." We think, too, that Verizon official Link Hoewing has a good point -- that as long as companies know the bureaucracy's prepared to intervene to help them, they have much less incentive to talk and negotiate seriously.

Thus, Senator Rockefeller ought to (a) provide that all these "big ticket" functions will be eliminated, according to a time table; and (b) also provide that if there are problems, the relevant state PUC will be responsible to handle them. It seems to us they're at least as able to handle these matters as the FCC, probably better -- as, among other things, they use credible trial-type fact-gathering procedures.

Network Maintenance and Development

Please note, we want the FCC out of the USF/USAC process, please. We're opposed to having regulatory agencies engaged in the "operations" part of the business. The old Atomic Energy Commission was broken up, among other things, because Congress concluded that regulation and operations just don't mix. Ditto the separation of the Federal Maritime Administration and Federal Maritime Commission. And, please note that when the Federal Power Commission was folded into the U.S. Energy Department, it was not placed in the position of supporting the growth, development of the electric, natural gas, or other energy businesses.

We're at a loss to rationalize the current regime. It seems to us that if your objective is to maintain and develop networks -- a business operations and development chore -- that's best undertaken by the Government's business department, if anyone. Thus, we'd transfer all the FCC's duties to oversee the Universal Service Administrative Company to the Secretary of Commerce. That would certainly make more sense than the current arrangements.

Get the FCC Out of Education, Etc.

The notion of subsidizing education, book publishing and libraries, and health care through everyone's phone bill also strikes us as fundamentally crazy. What in the world does an independent regulatory agency know about these fields - - much less the Administration's goals and policies?

It seems to us the best way to deal with this administrative anomaly would be to transfer the various programs to the Executive agencies with the relevant, underlying expertise. But if that's impractical -- because it'd entail treading on Congressional committee jurisdictions -- then we'd shift this, too, to the Secretary of Commerce. At the same time, we'd require the Commerce Secretary actually to cooperate and collaborate with the Secretaries of Agriculture, Education, and Health & Human Services. Doesn't that make sense?

Incidentally, if the Commerce Secretary thought it made more sense to let USAC continue to run all these efforts, that'd be fine. But, again, we expect the Commerce Secretary and his Cabinet colleagues are much more suited to oversee these activities than an independent regulatory agency.

Supporting the Competition

Finally, if it's still necessary to subsidize local telephone competitors, couldn't we at least place this Federal support program on a glide path to oblivion?

Remember, it's one thing to have a set of rules, then abruptly to change them. If that's the situation, a due regard for "transitional equities" is in-order. But here, companies have entered a business with full knowledge and understanding that they were facing an uphill battle.

If a company appeared and said it wanted to compete with GM, Ford, and Toyota, would the Federal Government feel obliged to carve out some portion of the vehicles market to help it? Would we order Toyota to supply parts at a discount? Or, GM to assemble the competitors vehicles on the cheap?

We wouldn't undertake in other sectors the sort of corporate welfare program that the FCC has developed in the local exchange business. Thus, again, we'd take the approach recommended for "terminating access" and "intercarrier compensation" regulation -- fine, for the moment, but as of X-date, it's all coming to an end.

To Summarize, Briefly

If Congress were systematically to examine the FCC's wireline industry activities, we're pretty sure they'd conclude that (a) the FCC's doing a lot of things which ought to be phased out, or (b) shifted to Executive branch agencies that have the subject-matter expertise. It's worth remembering, too, that a number of these

activities at the FCC are of relatively recent origin. And, there's virtually nothing here which state commissions couldn't handle more speedily.

Now, we appreciate that the idea of relying on markets and Federal agencies with expertise might be scary. As General "Buck" Turgidson declared in Dr. Strangelove, "Why, Mr. President, they could see the Big Board!" But as we noted, the surface and air transportation sectors, the pipelines, the banks, the securities firms -- they, plus a generally unregulated marketplace, seem able to sort all of this out. As Dr. Paige Wenrich famously commented, "Markets are quite able to devise complicated -- but effective and efficient -- solutions to complicated problems."

To the extent Federal support programs are still warranted, they ought to be run by agencies with subject-matter expertise. Thus, we'd shift the USAC functions to the Commerce Department, with the admonition that they ensure the Departments of Agriculture, Education, and Health & Human Services are involved.

Conclusion

Remember, there've been vast, sweeping changes in areas of FCC regulatory activity in the past. In 1982, Congress passed legislation which terminated the FCC's elaborate international carriers regulatory regime. No more "International Quota Bureau" allocating unrouted public message telegrams. No more "carrier of the week," or "circuit-by-circuit" activation.

Before that legislation passed, international record carriers and their Washington advocates hypothesized an industry only slightly less delicately balanced than the innards of a Breitling chronograph. They suggested that any change would be about as helpful as sticking a pencil point into the workings of that extravagant watch. But Congress changed the laws anyway. And, what happened? Services expanded, prices fell, options increased -- and, these days, hardly anyone can even remember what the international communications regulatory regime used to be like.

The lesson? Terminate and reassign functions along the lines suggested here and we're more than a little sure it'd be good for America. Next? The reforms which need to be made on the consumer affairs front.

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