

Before the United States House of Representatives

Committee on the Judiciary

Telecommunications and Antitrust Task Force

Testimony of

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Mr. Chairman and members of the Task Force: My name is Earl Comstock and I am the President and CEO of COMPTEL. COMPTEL is a non-profit trade association that was formed by the merger of three trade associations, each of which represented segments of the competitive communications industry. Today COMPTEL has 180 voting member companies and stands as the only trade association representing a broad cross section of the competitive industry. Our members are taking action to advance communications through innovation and open networks, and are responsible for introducing many of the innovative services that consumers and businesses take for granted today.

Introduction

It is a pleasure to be here to testify about Net neutrality and its importance to the preservation of the Internet and America's competitive position in the global marketplace. As a former Senate staff attorney who worked on the Telecommunications

Act of 1996, I can hopefully provide some insight into how the world has both changed and stayed the same in the 10 years since that landmark legislation was enacted.

COMPTEL would like to commend the Judiciary Committee for its creation of this Task Force and for its recent letter to Chairman Majoras of the Federal Trade Commission asking the FTC to re-examine its role in protecting consumers and competitors from abuse by entrenched network operators. As that letter notes, the Committee's inquiry was spurred by the Supreme Court's recent decision in *Brand X*¹ and actions by the Federal Communications Commission that severely limit the FCC's authority over broadband communications services. The FTC's response was encouraging, and stated that they believe the *Brand X* decision supports the conclusion that the FTC is now the primary enforcement authority with respect to Internet access services because the common carrier exclusion in the Federal Trade Commission Act no longer applies to the provision of those services. The FTC's involvement provides a backstop, but its role needs to be strengthened if the Internet as we know it today is to be preserved.

Since the Committee's letter to the FTC was written, the Chairman of the FCC on March 19 used a provision in section 10 of the Communications Act² to allow a forbearance petition by Verizon to take effect without any written decision by the FCC. As a result of that action, Verizon was relieved of common carrier obligations that the FCC had previously preserved in the *Wireline Broadband Order*, and is now subject to less regulation than any of its far smaller competitors. This unprecedented dereliction of

¹ *National Cable & Telecommunications Ass'n v. Brand X Internet Services*, 125 S. Ct. 2688 (2005).

² 47 U.S.C. 160.

the FCC's duty to protect consumers and promote competition further highlights the need for active oversight and intervention by Congress.

Unfortunately, the subjugation of the economic rights of the many to the interests of the few has not been limited to the FCC. The Department of Justice abandoned the Reagan administration's commitment to telecommunications competition at a particularly sensitive juncture. Given the FCC's recent decisions to abjure historical conduct regulation of firms with market power, the DOJ's decision to abandon a commitment to competitive market structure, by allowing –virtually unopposed – the recent AT&T/SBC and Verizon/MCI mega-mergers and with minimal divestiture of certain unused assets, could not have come at a worse time. The anticompetitive effects of vertical integration in the telecommunications industry were starkly revealed only after divestiture—when services that relied on the divested, but regulated, local networks flourished. Long distance prices plummeted, because competitors were free to build more efficient long distance networks, and the local monopolies had to interconnect with them in a nondiscriminatory manner, which finally brought the benefits of price competition to consumers. Perhaps even more importantly, though, the divestiture allowed for the development of new industries which the integrated Bell system would have found little use for—the wireless market and the Internet.

The original 1984 divestiture, with its equal access and non-discrimination requirements, showed the enormous social and economic benefits of network neutrality as applied to the communications industry. In only 20 years, the way people communicate has changed dramatically for the better, and in ways that no one could have predicted as the result of that original decision in favor of network neutrality. As the

Committee considers the importance of network neutrality on innovation, consumer welfare, and American competitiveness, the most important point that the Committee should keep in mind is the nature of the harm to be avoided—in this case exclusion from the market. Exclusionary conduct is especially pernicious, because there is seldom an adequate ex post remedy. Thus, ex ante rules are the preferable way to address exclusionary behavior. We have voting rights legislation, because, when some Americans can't vote, democracy suffers. Similarly, when efficient firms are foreclosed from the Internet market, America's information services economy suffers.

The opponents of network neutrality rules – what we now refer to as “Net neutrality”—will say there are no costs to not adopting fair access rules, and that there is no reason to address this issue at this point. These opponents will flippantly argue that Net neutrality is a “solution in search of a problem.” However, as our recent history has shown, the costs that we can't quantify—the costs of innovation, opportunity, and efficiency foregone—are often the most expensive for society to bear. Indeed, as we've seen through the original network neutrality rules at work over the last 22 years, when welfare loss can be avoided, and productivity and innovation can be promoted through rational economic rules, then there is no excuse to deny American consumers and innovators the benefits of such rules.

Nonetheless, before divestiture and the first network neutrality rules, the apologists for market power told us that “the system is the solution.” Now, as before, in order to justify an unprecedented accretion of market power we are told by Ed Whitacre, the head of AT&T, that “no partnership between two independent companies, no matter how well run, can match the speed, effectiveness, responsiveness and efficiency of a

solely owned company."³ In light of history, Mr. Whitacre's quote should be a clarion wake-up call to legislators, law enforcement, and regulators. This Committee has a key role to play in taking steps to ensure history does not repeat itself.

Net Neutrality—What It Is and Is Not

First, let me explain briefly what I mean by Net neutrality. It is a term that is often heard these days, but most people don't explain exactly what they mean when they use the term. What COMPTEL means by Net neutrality is reinstatement of the basic legal requirements that the Internet was founded on – nondiscrimination, interconnection on reasonable terms and conditions, service upon reasonable request, the right to attach devices to the network, and the right to innovate and provide service without having to obtain the permission of the network operator. This is not to say that the network operator is without rights – many COMPTEL members are themselves network operators, and in order to remain in business they all expect to be paid for their services. Network operators are entitled to charge, on a non-discriminatory basis, for the transmission services they provide and to charge more for larger amounts of bandwidth. Network operators are also entitled to offer consumers whatever content and services they want. What Net neutrality would not allow a network operator to do, however, is to favor transmission of their own or affiliated content or services, to act as gatekeepers on who can provide content or services, to discriminate against unaffiliated content and services in the allocation of transmission capacity, or to force consumers to buy unwanted content and services in order to obtain basic transmission services.

³ *AT&T, BellSouth to Merge*, Press Release, available at <http://att.sbc.com/gen/press-room?pid=4800&cdvn=news&newsarticleid=22140>

It is also helpful to consider some of the mischaracterizations of Net neutrality. For example, as I've noted, the Bell companies and the cable operators say that Net neutrality is "a solution in search of a problem" and then tell you that Net neutrality rules would hurt broadband deployment. But they never say exactly what Net neutrality means or how it would hurt broadband deployment. They also don't mention that data reported to the FCC shows that, as of June 30, 2005 (almost a year ago), high-speed cable modem service was available to 91 percent of the homes passed by cable and that high-speed Digital Subscriber Line (DSL) service was available to 76 percent of the homes that have telephone service.⁴ Those numbers indicate to me that the United States already has significant deployment of broadband facilities. Where the United States is falling behind other developed countries is in broadband *penetration* (i.e. subscription to broadband service), which is largely due to the lack of significant price competition in the provision of broadband services.⁵ Again, a point neither the Bell companies nor cable representatives tend to make.

To make this point, regarding price competition and broadband penetration, I want to highlight for you part of a news article in Communications Daily just last week:

Verizon's recent price increase for its low-end DSL service is "rational" and highlights that the market is less competitive than expected -- not a bad thing, according to an industry briefing released Mon. by Wachovia. Jacking the price up to \$18 from \$15, plus a \$19.95 activation charge, shows the competitive environment for broadband is "more rational than anticipated," Wachovia said. The bank said "the last mile operates under an attractive duopoly structure" which will inevitably push competition

⁴ *High-Speed Services for Internet Access: Status as of June 30, 2005*, Industry Analysis and Technology Division, Wireline Competition Bureau, FCC, April 2006, at 3.

⁵ See D. Turner, "Broadband Reality Check: The FCC Ignores America's Digital Divide", Free Press (2005), at 8, available at http://www.hearusrnow.org/fileadmin/sitecontent/broadband_report_optimized.pdf

away from irrationally low prices. It added it had heard rumors that Verizon was having trouble meeting demand for its \$15 offer.⁶

Restricting output is indeed “rational” if you are “having trouble” meeting demand—if there are too many customers at a given price point, it is much easier to just raise the price to make less customers, than to hire more workers and buy more equipment in order to produce more of the service. However, it is the “attractive duopoly structure” of the market that gives Verizon this luxury of choice. In a market with a competitive structure, the choice would belong to the consumer, and not the producer. Thus, it appears that with or without Net neutrality rules, the network operators have a lot to say about whether penetration rates will improve in the near future.

The FCC hasn’t defined Net neutrality either, but has decided that Net neutrality can be addressed by issuing a “policy statement” that has no legal force or effect.⁷ That policy statement, while acknowledging that the Internet “has had a profound impact on American life”⁸ and that the Internet “plays an important role in the economy,”⁹ simply offers “guidance and insight”¹⁰ into the FCC’s approach to ensuring “that broadband networks are widely deployed, open, affordable, and accessible to all consumers...”¹¹ The FCC’s four principles are that consumers are entitled to: 1) access lawful Internet content of their choice; 2) run applications and use services of their choice, subject to the needs of law enforcement; 3) connect their choice of legal devices that do not harm the

⁶ Communications Daily, April 18, 2006.

⁷ *In the Matter of Appropriate Framework for Broadband Access to the Internet over Wireline Facilities*, Policy Statement, CC Docket 02-33, FCC 05-151, released September 23, 2005 (*FCC Policy Statement*).

⁸ *Id.* at 1.

⁹ *Id.* at 2.

¹⁰ *Id.*

¹¹ *Id.* at 3.

network; and 4) competition among network providers, application and service providers, and content providers.¹² Because the Commission decided in the order that was the subject of the *Brand X* case, and more recently in the *Wireline Broadband Order*,¹³ that any network operator (both cable and telephone) that *forces* consumers to purchase transmission services as part of a bundled offering with an information service is no longer a common carrier (i.e., the network operator is not a common carrier so long as it *refuses* to offer the transmission service on a stand-alone basis for a separate price), it is not clear what legal authority the Commission has left itself to implement these principles should it chose to attempt to do so.

While the FCC's principles are a good start, they fall woefully short of the mark when you consider the fact that the FCC has now abandoned the common carrier framework that allowed the Internet to flourish. It is the recent loss of that framework, combined with the unprecedented (in the Internet age) vertical integration between the dominant "last mile" providers and the dominant Internet backbone providers, that is generating the sudden interest in Net neutrality by so many consumer groups, competitors, and content providers. This unprecedented vertical integration, has substantially increased the ability and incentives of these large dominant firms to exclude competitors, restrict output, and raise prices across an even larger range of services. Thus, at the very time that access rules are most needed, the FCC has abandoned its role

¹² *Id.*

¹³ See *In the Matter of Appropriate Framework for Broadband Access to the Internet over Wireline Facilities*, Report and Order and Notice of Proposed Rulemaking, 20 FCC Rcd 14853 (2005), consolidated appeal pending *sub nom Time Warner v. FCC*, 05-4769 (3rd Cir. Oct. 26, 2005) ("*Wireline Broadband Order*").

as regulator, and the antitrust agencies have only allowed this now-unconstrained market power to concentrate further through larger and larger acquisitions.

Given the FCC's ongoing efforts to abdicate the responsibilities that Congress gave it in Title II of the Communications Act, and the Supreme Court's apparent willingness to allow the FCC's irresponsible behavior, it is imperative that Congress provide new guidance to the courts and the Federal agencies that are supposed to protect the public. One way Congress could do that would be to re-instate the common carrier rules that the FCC has abandoned. Unfortunately, it appears from the subcommittee markup in the House Commerce Committee on April 5th that, for the moment at least, the Bell companies and the cable operators have prevailed in convincing that Committee not to adopt meaningful Net neutrality requirements or re-instate common carrier requirements. Another way Congress could address Net neutrality falls squarely in this Committee's jurisdiction, and that would be to provide meaningful antitrust remedies against network operators who abuse their market power.

Congress is at a Crossroads in Communications Policy

America currently leads the world in high technology. The question that is being increasingly asked today is whether our changing national communications policy will allow America to stay at the cutting edge of the Information Age. Our economy is increasingly service oriented, and new information services based on computer applications are a critical driver of our future growth. If businesses and consumers have access to reasonably priced transmission capacity, then any person can invent the next

Google, Amazon, eBay, or Yahoo and hope to succeed. If rural areas can get access to adequate transmission capacity, then rural States and communities can share in that economic opportunity and growth.

Whether or not America will continue to be a world leader in the 21st century's Information Age economy will depend in large measure on if, and how, Congress rewrites our communications and antitrust laws. The Supreme Court's *Trinko*¹⁴ decision has been interpreted by some courts as limiting the availability of the antitrust laws to protect consumers and competition in the communications arena. The Court reasoned that no antitrust action arose because the FCC and a State regulatory body were actively regulating the anti-competitive behavior being complained of, and dismissed the case without ever examining the effectiveness of that presumed regulatory oversight. Yet the FCC has recently made significant changes to the structure of our Nation's communications laws through its interpretations of specific provisions Congress added in the Telecommunications Act of 1996, effectively removing any regulatory constraints on the behavior of incumbent telephone and cable network operators, and the Supreme Court in *Brand X* appears to support the FCC's decision not to regulate.

As a result of the FCC's abdication of authority and the Court's apparent indifference, Congress has a basic choice to make. In rewriting the law, it can reaffirm the pro-competitive policies that led to the creation of the Internet and the tremendous explosion of innovation and growth that accompanied the Internet by re-imposing common carriage and antitrust remedies, or it can reaffirm the FCC's recent decision to abandon those policies and trust that the private business interests of a few network

¹⁴ *Verizon v. Trinko*, 540 U.S. 398 (2004).

operators – namely the Bells and the cable companies – will protect consumers, provide access to competing content and service providers, and enable the next generation Internet to be built. If history and basic business behavior are any guides, the approach taken by the FCC will prove catastrophic.

The Internet Depends on a Common Carrier Framework

The FCC’s new approach will prove catastrophic precisely because the Internet depends on basic common carrier rules to ensure the availability of an essential facility, namely the transmission networks over which Internet applications reach businesses and consumers. Those basic rules required all common carriers – incumbents and competitors alike – to provide non-discriminatory service upon reasonable request, to permit attachment of devices to the network, and to interconnect their networks with other operators on a non-discriminatory basis. Without this historic legal foundation, the Net neutrality principles that the FCC has articulated to “protect” the Internet fall well short of that goal, and the robust competition in information services that has been the hallmark of the past 25 years will soon be replaced by the limited innovation and higher prices that are the hallmarks of duopolies and monopolies.

Congress’ decision to act or not to act will in many senses determine America’s economic future. Communications is increasingly at the heart of America’s economy. Companies depend on communications networks to offer content and services to consumers, advertise, manage inventory, and transmit voice, video, and data between locations. Today everyone takes for granted that they will be able to buy transmission services and use those services without interference. That is no longer the case under the

FCC's new approach. Under the FCC's new interpretation of existing law, no longer will AT&T, BellSouth, or other companies that use public rights of way and spectrum to offer service to the public be required to act as common carriers with an obligation to offer non-discriminatory service upon reasonable request.

Without that obligation, network operators like AT&T will be able to refuse service to, or discriminate against, anyone offering competing content or services, just as the cable operators do today. The CEOs of the various Bell companies have already been saying publicly how they intend to do just that – namely that the Bell companies will decide who can get content or service delivered via the Bells' "higher" quality "private" networks.

This will cause a radical change to the Internet and the information services market. Information services – the content and services made possible by computer applications – all depend on transmission networks to reach consumers. The information services market has been robustly competitive – with tremendous innovation as a result – because the FCC in its 1980 *Computer II* order¹⁵ required all public network operators (both incumbents and competitors) to provide their transmission services to anyone who wanted to buy them on non-discriminatory terms and conditions. By regulating the much smaller class of transmission networks – which everyone needs in order to offer their services to users – the FCC did not have to regulate any person's (even an incumbent network operator's) provision of information services. The FCC's recent decision to abandon its *Computer II* unbundling requirements now makes it possible for the small

¹⁵ *Amendment of Section 64.702 of the Commission's Rules and Regulations*, 77 FCC 2d 384 (1980) and subsequent orders on reconsideration, *aff'd sub nom. Computer and Communications Industry Ass'n v. FCC*, 693 F.2d 198 (D.C. Cir. 1982), *cert. denied*, 461 U.S. 938 (1983) (collectively "*Computer II*").

class of network operators to become gatekeepers on the Internet and use their network control to dominate the much larger information services market.

The FCC's Reliance on Inter-Modal Competition is Unfounded

The FCC's reversal of its 25-year old *Computer II* decision is predicated on a flawed assumption, namely that the barriers to entry for transmission networks are so low that anyone who wants to compete can build their own network. Nothing is further from the truth. The truth is that all three of the wired networks that exist today – telephone, cable, and power – were each built in a monopoly environment. The builders were protected from competition by law, and could build their networks with the assurance that they would get every customer who wanted service over those networks. Each of those entities is now entrenched in their market with ubiquitous facilities and 70 percent or more of the customers, and therefore a substantial revenue stream. Further, to improve their transmission capability incumbents merely have to upgrade existing infrastructure using ongoing customer revenue.

In contrast, in the absence of any rules requiring access to and sharing of existing infrastructure on reasonable terms and conditions, a new entrant has to build entirely new facilities from scratch with no customers and no revenue, and then has to win any customers from the incumbent. That is a very high barrier to entry. Even the FCC has acknowledged that, when it preempted a pre-1996 Texas statute that required certain large entrants to “build out” to each customer in a 27 square mile area,

enforcement of the build-out requirements would ‘have the effect of prohibiting’ [competitors] from providing service contrary to section

253(a) due to the substantial financial investment involved and the comparatively high cost per loop sold by a new entrant.¹⁶

The Bells have made the same arguments with respect to Congressional proposals for limited geographic area build-outs with respect to video franchising. It goes without saying that the larger the geographic territory concerned the higher the entry barrier created by a mandatory facilities build. It is, thus, well recognized that even dedicated, high-capacity telecommunications networks (such as those deployed to serve a central business district) are characterized by substantial economies of scale and scope.¹⁷

Moreover, the “sunk” aspect of the high capital costs that are characteristic of competitive fiber deployment are additional entry barriers.¹⁸

¹⁶ *In the Matters of the Public Utility Commission of Texas, et al., Petitions for Declaratory Ruling and/or Preemption of Certain Provisions of the Texas Public Utility Regulatory Act of 1995*, CCB Pol. Docket Nos. 96-13, 96-14, 96-16, and 96-19, Memorandum Opinion and Order, (Rel. October 1, 1997) at ¶ 78.

¹⁷ In one of the early antitrust cases it was determined, “that there are three reasons for [incumbent] defendants having achieved such clear economies of scale. First, as [the incumbent] defendants' witnesses explained, higher levels of demand allow efficient use of high-capacity facilities and technologies which provide transmission service at progressively lower unit costs. Second, the process by which the network is configured allows for the fullest utilization of these high-capacity, low-cost facilities. Finally, [the incumbent] defendants supply the entire spectrum of communications services, and through the networking principle, demand for all those services is concentrated or pooled so that it can be transmitted and switched over the same facilities. This last phenomenon is referred to by economists as “economies of scope”. Economies of scope exist when it is cheaper to produce two or more goods or services together than to produce each one separately. *Southern Pac. Communications Co. v. American Tel. & Tel. Co.*, 556 F. Supp. 825, 861-862 (D. D.C 1982). Furthermore, the FCC has found, “competitive carriers with lower amounts of traffic aggregation, such as new market entrants, face economies of scale that can act as a barrier to entry.” *In the Matter of Unbundling Obligations of Incumbent LECs*, Order on Remand, 18 FCC Rcd. at ¶ 377 & n. 1155.

¹⁸ The existence of high, or proportionately high, sunk costs is generally recognized as a barrier to entry. See, e.g., Larson, *An Economic Guide to Competitive Standards in Telecommunications Regulation*, 1 CommLaw Conspectus 31, 52 (“if entry requires the incurrence of capital costs, and a ‘high’ proportion of these are sunk costs for entrants, then entry barriers exist.”) c.f., Bolton, Brodley, and Riordan, *Predatory Pricing: Strategic Theory and Legal Policy*, 88 Geo. L.J. 2239, 2265 (August, 2000)(“if

The FCC points to satellite, terrestrial wireless and powerline operators (all of which own facilities that reach the end user directly) as potential competitors. But an examination of the facts regarding satellite, broadband over powerline (BPL), and terrestrial wireless make clear they are not real competitive threats for the foreseeable future. First and foremost, there is the empirical evidence. The US is not the only testing ground for new technology. Nowhere in the world are BPL or terrestrial wireless being commercially used as the primary means for data or video communications. In the US, the annual FCC reports on broadband show that wireless, BPL, and satellite account for less than 3 percent of the market, and that their share of the market is actually declining.¹⁹ The reality is that there are significant technical difficulties that remain to be resolved with BPL, and you also need significant investment to deploy the needed facilities.

Likewise, a review of the empirical evidence shows that terrestrial wireless is a complement to wired services, and not a replacement. First and foremost, both satellite and terrestrial wireless services are more expensive on per-minute (in the case of voice) or per-byte (in the case of data and video) basis. People are willing to pay more for wireless because of the mobility, but almost no one uses wireless to replace wired service where wired service is an option. The number of business users that rely entirely on wireless is limited to those that can only get service by satellite, and in the consumer market fewer than 5 percent of customers have chosen terrestrial wireless only.

challenged by new entry, the incumbent will rationally disregard such [sunk] costs in its pricing decisions rather than lose the business. The entrant . . . must now incur such costs, and therefore faces risk of underpricing by an incumbent with sunk costs. Thus, as a result, sunk costs may act as an entry barrier, giving the incumbent the ability to raise price above the competitive level.”)

¹⁹ FCC Reports on High-Speed Services for Internet Access, available at <http://www.fcc.gov/wcb/iatd/comp.html>

The FCC also likes to cite WiMax (a wide area wireless network standard) as a potential wireless competitor providing broadband service. Again, the facts don't support its enthusiasm. WiMax, which like BPL and fixed wireless many of COMPTTEL's members are seeking to use, has numerous barriers to entry that must be crossed. First, a final standard needs to be agreed to. Second, any competitor needs to obtain spectrum rights, which must be acquired at auction. Third, a competitor would need to build out a regional or national network. Fourth, any customers competitors gain must be won over from a Bell company or a cable company. And finally, this must be done in the face of competition from incumbent wireless companies owned by the Bells.

Put simply, the FCC is betting America's future on the good will of the Bell companies and large cable operators. Counting on companies to act for the public good against their own financial interest has been tried before, and it has never worked. The FCC believes that robust competition between these two entrenched incumbents will ensure that unaffiliated content and service providers will continue to get access to consumers. Yet in the 10 years since the passage of the 1996 Act not one large cable company has voluntarily let any competitor offer competing service over its network, and not one Bell has voluntarily negotiated an interconnection agreement with a cable company or a large competitor.

The reason is understandable – no CEO is going to voluntarily help a competitor. In fact, it would be a violation of the CEO's fiduciary duty to his investors and shareholders if the CEO voluntarily helped the competitor take market share or drive down prices. In the absence of some legal duty to permit competitors to use their networks on reasonable terms and conditions, the reality is that any network operator

with market power – and the incumbent local exchange carriers and cable operators each have 70 percent or more of the customers for the core service provided by their respective networks – is going to use that market power to restrain competition. That is why action by Congress is needed.

The Risk is Not Hypothetical

Network operators have already demonstrated on many occasions that, in the absence of regulatory restraints, market forces will lead them to discriminate. The refusal by AT&T to connect its long lines network with competing carriers was one of the driving forces behind section 201 of the Communications Act of 1934²⁰, and anticompetitive actions by AT&T resulted in three different antitrust actions by the United States government over the course of 70 years. In fact, Judge Greene, who oversaw the implementation of the 1984 Consent Decree that resulted from the most recent of those actions, cogently observed fifteen years ago that:

“In the opinion of this Court, informed by over twelve years of experience with evidence in the telecommunications field, the most probable consequences of such entry by the Regional Companies into the sensitive information services market will be the elimination of competition from that market and the concentration of the sources of information of the American people in just a few, dominant, collaborative conglomerates, with the captive local telephone monopolies as their base. Such a development would be inimical to the objective of a competitive market, the purposes of the antitrust laws, and the economic well-being of the American people.” *U.S. v. Western Electric Co.*, 767 F. Supp. 308 (D.D.C. 1991) at 326.

As members of this Task Force will recall, section 601 of the Telecommunications Act provided that “all conduct or activities that are currently subject to [the 1984 AT&T Consent Decree, the GTE Consent Decree, and the McCaw Cellular Consent Decree]

²⁰ 47 U.S.C. 201.

shall, on and after the date of enactment [of the 1996 Act] be subject to the requirements and obligations of the Communications Act and shall no longer be subject to the restrictions and obligations of the respective consent decrees.”²¹ Given the FCC’s decision to no longer enforce the provisions of the Communications Act that replaced the restrictions in the AT&T Consent Decree (for example, non-discrimination and reasonable prices under section 201, interconnection and unbundled network elements under section 251, and the local competition checklist under section 271, among other requirements)²² with respect to the Bell companies, it is appropriate for this Task Force and the Judiciary Committee to re-examine the need for antitrust oversight of the rapidly re-emerging Bell monopoly.

And the Bell companies are not alone. Since the 1996 Act, cable operators have largely excluded independent Internet service providers (ISPs) from providing service over their cable networks by refusing to negotiate agreements to provide transmission services and by requiring consumers to purchase the cable operators’ affiliated ISP service as part of the price of buying cable modem transmission service. The cable companies were able to do this because the FCC refused to apply common carrier regulation to the cable companies’ provision of transmission service used for Internet access and voice services, even though Congress clearly anticipated, and in fact sought to facilitate, cable company entry into phone services (including data transmission) and telephone company entry into cable services as part of the 1996 Act.²³

²¹ House Report 104-458, “Conference Report to Accompany S. 652” (1996) at 198.

²² See 47 U.S.C. 201, 251, and 271.

²³ *House Report, op cit*, at 201 (“in the future, the conferees anticipate that cable companies will be providing local telephone service and the [Bell operating companies] will be providing cable service. Mergers between these kinds of companies should not be

Even Internet backbone network operators that do not control the last mile connections to consumers are not immune from market forces that prompt discriminatory behavior. Late last year an Internet backbone network operator, Level 3, disconnected another network operator, Cogent, with which it had a dispute, causing disruptions to customers on Cogent's network.²⁴ Voice over Internet Protocol (VoIP) providers have also experienced discriminatory behavior by network operators, for example in one particular case where the FCC actually took enforcement action to stop port blocking by a small incumbent local exchange carrier. In that case, which the FCC resolved prior to issuing its *Wireline Broadband Order* by using its Title II authority over common carriers, the FCC forced the offending common carrier to agree in a consent decree not to engage in the practice in the future.²⁵ In the aftermath of the *Wireline Broadband Order* and the FCC's determination that the broadband Internet access services over which the VoIP service at issue is provided is no longer a common carrier service, it is not clear under what legal authority the FCC could prevail should it attempt to use the same approach again.

New Antitrust Amendments Are Necessary

While the antitrust laws have been used to successfully promote telecommunications competition in the past, some changes will be necessary if the

allowed to go through without a thorough antitrust review under the normal Hart-Scott-Rodino process.”).

²⁴ See “The Cogent-Level 3 Peering Dispute” available at http://www.isp-planet.com/business/2005/cogent_level_3.html (visited April 5, 2006) (“My feeling is this is more of a competitive attack on Cogent,” Berninger said. “These are two companies that have opposite business models. Cogent is a low-cost player that essentially undercuts the price of the market. Level 3 is an elite player that charges a premium to connect to them.”).

²⁵ See *Madison River LLC and Affiliated Companies*, File No. EB-05-1H-0110, Order, FCC Rcd 4295 (Enf. Bur. 2005).

antitrust laws are to become the primary means through which competition will exist.

There are at least three changes to the existing antitrust laws that this Committee should consider over the next several months.

First, while competition is undeniably being eliminated and concentration is increasing at alarming rates, for antitrust standing purposes, we are not yet back to the era of the one, fully-integrated, Bell system. In that era, everyone was a direct customer of the Bell system; thus, standing was not an issue. Now, however, it is quite conceivable—even likely—that the Bells’ will target their anticompetitive refusals to deal, or efforts to raise rivals’ costs/reduce rivals’ revenue to firms that are not direct customers of the Bells, but whose Internet backbone providers must be able to obtain interconnection on fair and reasonable terms with the Bell companies. These firms—if preyed upon by the Bells—will potentially face an indirect purchaser barrier to antitrust standing. The Committee should consider a limited exception to the “Illinois Brick” line of precedent to grant standing for those indirect-purchaser private litigants bringing cases against formerly-regulated dominant firms.

Similarly, for dominant carriers for which the FCC has eliminated common carrier regulations, this Committee should introduce legislation clarifying that these firms no longer enjoy the liability limitations they currently enjoy under the “filed rate doctrine” where the rates in lawfully-filed tariffs are presumed reasonable. Rather, if the de-regulated monopolies are engaging in anticompetitive conduct that forecloses entry, unlawfully restricts output, or otherwise leads to supra-competitive pricing as a result of antitrust violations, then the damages—which are subject to trebling—must be based on

the difference between the supracompetitive rate and the competitive rate that the Bell company has foreclosed.

Finally, the Committee must clarify that anticompetitive exclusionary conduct carries significant anticompetitive consequences and should be vigilantly enforced. The “*Trinko*” precedent in favor of tolerating increasingly aggressive exclusionary behavior, for fear of deterring “efficient” monopoly behavior, must be repudiated. As one scholar has presciently observed, “[p]recisely because it can be so difficult for courts to restore competition once it has been lost, the true cost of exclusion to consumer welfare--and its benefit to dominant firms--are likely to be understated.”²⁶

Thus, the modifications described above are necessary to ensure that the antitrust laws continue to allow efficient firms to freely enter and vigorously participate in the free-enterprise system as it relates to our information economy. Similarly, the suggested modifications will ensure that the antitrust laws are fully enforced as originally intended by Congress, with respect to this vital segment of our economy. The antitrust laws are unique in that they create a critical role for “private attorneys general”—through tremendous rewards for successful private litigants. Furthermore, the antitrust laws rely on vigorous private enforcement—in partnership with federal and state antitrust enforcement agencies to ensure that the antitrust laws are fully implemented.

²⁶ Issue 1 Symposium: Integrating New Economic Learning with Antitrust Doctrine, Gavil, Andrew I., 72 *Antitrust Law Journal* 3 (2004) Professor Gavil goes on to explain that the costs of tolerating exclusionary conduct “may be especially aggravated in cases of new and resourceful entrants and may be particularly acute in fast-moving technology industries, where once an opportunity for competitive challenge is lost, the conditions that produced it may be difficult, if not impossible, for courts or enforcement agencies to recreate. Indeed, the convergence of factors that spawned that competition may never come again--the competitive “moment” may be lost, and the dominant firm’s position fortified for years to come.”

Conclusion

Everyone who provides content and services over the Internet requires access to transmission networks in order to reach consumers. Ownership of the essential transmission network leads to tremendous market power with respect to each individual consumer served by that network and with respect to unaffiliated providers who need to use that network to reach those consumers. Transmission networks are a limited resource in part because they require access to limited public rights of way and spectrum in order to reach consumers. Perhaps more important, transmission networks are a limited resource because the presence of entrenched incumbents makes competitive entry by new network operators difficult, even with rules that promote that entry.

With government protection from competition, incumbent local exchange carriers had sixty years to construct and upgrade networks that reach every home and business in this country. Likewise, incumbent cable operators enjoyed more than 15 years of government protection from competition and more than 25 years of below cost access to poles, ducts and conduits in which to build and upgrade their cable networks to nearly every home in this country. That is a tremendous head start over the competitors that Congress hoped to encourage to enter the phone and cable marketplaces with the passage of the 1996 Act.

Now, ten years after the passage of the 1996 Act, instead of seven Bell operating companies and one large independent local company (GTE) there are now only four, and that number will drop to three if the AT&T- Bell South merger is approved. Two of the three major long distance operators at the time of the 1996 Act have been swallowed

whole by the two largest Bell operating companies, further diminishing the ranks of the competitors. Those same two Bell operating companies, AT&T and Verizon, own the two largest wireless carriers, further enhancing their market power and their ability to use bundled service offerings to cross subsidize and engage in anti-competitive pricing in areas where they do face competition.

Anti-competitive behavior is already rampant in the business markets, where the Bell companies enjoy a virtual monopoly on transmission services. Cable companies and unaffiliated wireless companies, along with competitive local exchange carriers and large businesses who operate their own private networks for internal use, all have to depend on getting special access services from the incumbent Bell companies. The FCC has largely abandoned any oversight of special access pricing or terms and conditions, leaving the Bells free to raise competitors' costs with impunity. This increase in costs will ultimately be borne by consumers, not only in terms of increased price, but also in terms of diminished options as competitors are forced out of business. Competitors have sought relief from the Commission in a pending proceeding on special access, but to date the FCC has given no indication as to when, or even if, it will issue an order to provide relief.

COMPTEL hopes that the Task Force will schedule further hearings to look specifically at the Bell companies' behavior in the business marketplace. In the meantime, the record is clear that the Task Force and the Judiciary Committee should take affirmative steps to protect the Internet. COMPTEL urges the Committee to introduce and adopt legislation creating a specific antitrust remedy to enforce Net neutrality by prohibiting anticompetitive behavior by transmission network operators. By

using the private enforcement mechanisms and treble damages available under the antitrust laws, Congress can create an effective alternative to the FCC's apparent unwillingness to implement the pro-competitive rules adopted by Congress in the 1996 Act.²⁷ Further, the Committee should also include specific language to address the misperception created by the *Trinko* case, and adopt new legislation that makes clear that the antitrust laws continue to apply in addition to any regulatory regime that may or may not be implemented by a regulatory agency. Compliance with a specific regulatory regime that is actually being enforced by a regulatory agency should be available as an affirmative defense to an antitrust claim, but the mere presence on the books of a regulatory regime that is not being enforced should not be allowed to nullify the pro-competitive effect of the antitrust laws.

Thank you. I look forward to answering any questions.

Testimony by Earl W. Comstock
President and CEO
COMPTEL
April 25, 2006

APPENDIX

²⁷ Unfortunately, this unwillingness is not new behavior on the part of the FCC. It was similar inaction by the FCC that led Judge Greene to actively oversee the 1984 AT&T Consent Decree. See P. Weiser, "The Relationship of Antitrust and Regulation In a Deregulatory Era", *Antitrust Bulletin*, Vol. XX (2005) at 8 ("Judge Greene examined the actual capabilities of the FCC with regard to regulating the Bell System and concluded that, as demonstrated by years of regulatory indecision, 'the Commission is not and never has been capable of effective enforcement of the laws governing AT&T's behavior.'")(footnote omitted). It appears history is once again repeating itself.

Ways Network Operators Can Discriminate

There are many ways in which a network operator can discriminate. As a result, the concept of Net neutrality must deal with each of them. Some, like bit discrimination and port blocking, are addressed by both the narrow FCC approach and the broader neutral network approach. However, the FCC approach stops there, far short of what is needed. To ensure that the Internet we have today continues to grow and flourish, there are several other discriminatory tactics that need to be addressed. These include:

Attachment of devices is a concept that refers to the ability to attach devices to a transmission network. Telephone network users generally have the right to attach any device to the network without obtaining the network operator's permission so long as the device will not harm the network or other users of the network and conforms to certain minimal specifications. In contrast, cable network operators can control what kind of devices are allowed to attach to their network, and that is the reason there is limited competition in set top boxes and cable modems and why many cable users still rent their devices. The ability to attach devices without approval or interference from the network operator is essential for continued innovation.

Bit discrimination is a term used to describe actions by the network operator to either favor its own content and services or to degrade the content or services of other providers by using information conveyed in the individual bits of a message to identify which messages to favor or degrade. Bit discrimination can be accomplished in any one of several ways. A network operator could, for example, instruct its routers (machines which direct the flow of information to its destination) to delay all traffic bound for Google.com by sending it to another network operator rather than carrying it directly to

the address. In the alternative, the network operator could use the sender's address to favor its own services by instructing its routers to give priority to all packets that originate from a Verizon.net address.

Port blocking is a term used to describe a specific form of discrimination in which the network operator uses information in the message header which tells the receiving computer which software application to use to open the information. The computer knows which software to use by the "port" through which the message enters the computer's communications hardware. If a network operator wishes to block a particular application, for example a Voice over Internet Protocol (VoIP) telephone call, it can do so by blocking messages destined for the port used by that application.

Quality of service is a term that is generally used to describe service offerings in which the transmission component is managed with respect to bandwidth, latency, jitter, priority, or other technical aspects of the transmission in order to ensure the quality of a particular service offering. Quality of service (QoS) is used to differentiate service offerings from the baseline standard for Internet transmissions, which operate on a "best-efforts" basis. In cases where bandwidth constraints or other factors result in congestion in the transmission network, QoS can be used to prioritize the delivery of certain types of services (for example VoIP or video services).

Many network operators are attempting to market QoS as an alternative to the "best efforts" approach of the Internet. Best efforts means that all traffic has the same priority, and the network uses its best efforts to deliver all of the traffic. The problem created by QoS is that it requires additional protocols and network management software in order to provide it, thus increasing the cost and complexity of the network.

Perhaps more importantly, QoS negates one of the key benefits of the Internet, which is the use of a common protocol (IP) to allow unimpeded transmission across multiple networks. When QoS is added, it helps balkanize the Internet because transmissions across multiple networks require cooperation among the network operators to ensure that each is using the same QoS protocols. Six years ago Internet2 (an organization tasked with designing and testing next generation Internet technologies) took a close look at QoS technology, and concluded that the cheaper solution to congestion problems was to add bandwidth and continue to use best efforts.

Bandwidth starvation is a term used to describe actions by a network operator to degrade or block applications or services by limiting the bandwidth (capacity) available to provide those services. One way to think of bandwidth starvation is in terms of trying to drink through a straw instead of a garden hose. Bandwidth starvation can be accomplished in a number of ways. At the consumer end, network operators can limit the upstream (sending) capability of user equipment in order to prevent consumers from providing content to other users, or can limit the bandwidth available for downstream content in order to prevent consumers from being able to access competing content. Examples of this would be limiting upstream transmission so that large bandwidth transmissions like digital video content takes much longer to send, thus limiting consumers ability to send movies, or limiting downstream transmission so that video streaming can't compete with the network operator's cable offerings. On the network end, the network operator can create bandwidth starvation by limiting the capacity of its interconnection points, so that content coming from a competing network provider has to squeeze through a narrow choke point, or by creating a two-tier network (as some Bell

company officials have proposed) where the bulk of the bandwidth is reserved for the network operator's "private" network and remainder is allocated to the "public" network.

Interconnection is a term used to describe the physical linking of two transmission networks. The Internet is a series of interconnected transmission networks that all use a common addressing protocol (the Internet Protocol or IP) to facilitate seamless transmission across the disparate networks. The primary issues with respect to interconnection are the bandwidth (capacity) of the interconnection and where the interconnection will occur. If the connection between the two networks is too small for the amount of traffic being sent from one network to the other, congestion will occur and transmissions can be degraded or lost. Likewise, if a network operator can only interconnect with another operator at a single location or at distant locations, congestion and/or degradation can occur because of the concentration of traffic across a single point or the additional distance traffic must travel. Historically, if a network operator is under no legal obligation to interconnect its network, voluntary interconnection rarely occurs.

Caching is a term that refers to the local storage of information that is frequently requested by an end user. By storing frequently accessed information, in particular large files like pictures or graphics, at a local storage site near the end user, caching allows the content provider to reduce network congestion (to the extent there is any) and reduce the time needed to run an application (for example, web pages appear faster and file downloads take less time). Caching arises as an issue in net neutrality discussions in two ways. First, because caching must be done on devices located closer to the end user, in general these devices are physically located in a facility under the control of the local network operator (for example in a central office or a cable head end). In the alternative,

if the caching is done at a physical location not under the network operator's control, then the local storage device needs to be interconnected with the local network. As a result, in the absence of a right for competitors to physically collocate equipment or to interconnect with a local network, a network operator could use local caching to favor their own content and services.

Each of these potential discriminatory actions by themselves would be sufficient to seriously inhibit, if not prevent entirely, competition in the provision of information services. The **attached diagram** illustrates in red the many different potential choke points that can come into play in the absence of strong Net neutrality requirements. Interconnection issues occur at the incumbent local exchange carrier (ILEC) central offices (numbers 2 and 4) and at the interconnection point with the ILEC network (number 3). Bandwidth starvation is illustrated by the narrow red "ILEC public Internet" lines connecting homes to the central offices and the central offices to the interconnect point. The broader blue pipes of the ILEC illustrate how the ILEC reserves more capacity for itself and its service offerings.