

Competition versus Regulation: “Mediating Between Right and Right” in the Wireless and Wireline Telephone Industries*

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I.	INTRODUCTION	107
II.	THE RISE AND FALL OF AT&T THROUGH GOVERNMENT REGULATION.....	109
	A. <i>The Growth of AT&T in the Telecommunications Industry as a “Natural Monopoly”</i>	109
	B. <i>The Beginning of the End: The Breakup of AT&T</i>	112
	C. <i>Post-Divestiture Developments in the Long-Distance Market</i>	112
III.	COMPETITION, DEREGULATION, AND THE WIRELESS MARKET ..	113
	A. <i>The Development of the Regulatory Scheme in the Wireless Phone Industry</i>	113
	B. <i>Wireless Number Portability: The Last Piece of the Puzzle</i> . 116	
	1. The Seven-Year Struggle over the Implementation of Number Portability	116
	2. Possible Effects of WLNP	117
IV.	WIRELINE REGULATION V. WIRELESS COMPETITION	119
	A. <i>The Methods of Control: A Brief Overview of the Regulatory Approaches Taken in the Wireless and Wireline</i>	

* Paul A. Freund, *Legal Frameworks for Human Experimentation*, EXPERIMENTATION WITH HUMAN SUBJECTS 106 (Paul A. Freund ed., 1970).

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	<i>Industries</i>	119
B.	<i>Different, but Why? An Analysis of the Regulatory Approaches Taken in the Wireless and Wireline Industries</i> ..	120
1.	Policy Goals behind the Development of the Wireline Regulatory Framework	120
2.	A Shift in Focus: A Different Scheme Emerges	122
3.	Regulation Sets the Stage for Competition	123
V.	THE NEW ROLE OF THE FCC	124
VI.	CONCLUSION	125

I. INTRODUCTION

In November 2003, wireless telephone providers in the 100 largest Metropolitan Statistical Areas ("MSAs") began allowing customers to transfer, or "port," their telephone numbers to different companies when switching providers. Though wireline telephone providers began offering number portability in 1998, the new wireless portability has met with much fanfare, as many believed that the last barrier to wireless phone competition had finally been lifted.¹

Wireless local number portability ("WLNP") is one of many provisions stemming from the Telecommunications Act of 1996 ("Telecommunications Act"),² a bill that by its own description was designed to "provide for a pro-competitive, de-regulatory national policy framework . . . by opening all telecommunications markets to competition, and for other purposes."³ The Telecommunications Act ended over sixty years of regulatory policy and introduced sweeping changes to both the telecommunications and broadcasting industries.⁴ Where regulation had once been seen as the best way for these industries to flourish, competition and an open market were now gaining favor among politicians and others inside the telecommunications industry. When the Telecommunications Act was passed, the wireless industry had already evolved into a competitive market, though the traditional telephone industry had been

1. Grant Gross & Stephen Lawson, *WLNP Is a Boon to Customers*, InfoWorld.com (Nov. 26, 2003), at http://www.infoworld.com/article/03/11/26/47NNportable_1.html.

2. Telecommunications Act of 1996, Pub. L. No. 104-104, 110 Stat. 56 (codified at scattered sections of 47 U.S.C.) [hereinafter Telecommunications Act].

3. From the original title of the Telecommunications Act of 1996, as introduced by Senator Larry Pressler. S. Res. 652, 104th Cong. (1995) (enacted), available at <http://thomas.loc.gov/cgi-bin/bdquery/z?d104:SN00652:@@T> (last visited Sept. 29, 2004).

4. MICHAEL J. ZARKIN, SOCIAL LEARNING AND THE HISTORY OF U.S. TELECOMMUNICATIONS POLICY 1900-1996 147 (2003).

heavily regulated for nearly 100 years.⁵ While this regulation created arguably the most sophisticated and complete telephone system in the world, many felt that regulation had been a failure and the only way to “fix” the situation was through increased competition.⁶

This Note argues that differing policy concerns are responsible for the different regulatory approaches taken in each industry. Furthermore, regulation and lack of competition were beneficial to the creation of the wireline telephone industry. Had the wireline industry been open to direct competition from its inception, as the wireless industry essentially has, the wireline industry would not be as strong as it is today. As a result of this weakness, the growth and success of the wireless industry, as well as many other peripheral industries, would have suffered. Part II details the history of regulation in the wireline telephone industry. It begins by noting the telephone industry’s early status as a “natural monopoly,” it continues through the breakup of AT&T in 1984, and concludes with an analysis of the post-breakup period. Part III provides background information on the wireless industry, with a brief discussion of the implications of the number portability requirement. Part IV analyzes the different regulatory approaches used in these two industries, and illustrates the reasons for and benefits of treating the two industries differently. Part V looks at the new role of the Federal Communications Commission (“FCC”) in telecommunications regulation as illustrated by the recent WLNP implementation.

II. THE RISE AND FALL OF AT&T THROUGH GOVERNMENT REGULATION

A. *The Growth of AT&T in the Telecommunications Industry as a “Natural Monopoly”*

From its invention in 1876 until the original Bell patents expired in 1894, the telephone system operated as a monopoly.⁷ As the technology became available, competition grew quickly and by 1907, Bell’s share of the marketplace fell below 50 percent.⁸ Competition, however, came with a price. The telephone system was in a state of disarray. Customers were

5. PETER W. HUBER ET AL., THE TELECOMMUNICATIONS ACT OF 1996: SPECIAL REPORT 6 (1996).

6. See ZARKIN, *supra* note 4.

7. ROBERT BRITT HORWITZ, THE IRONY OF REGULATORY REFORM: THE DEREGULATION OF AMERICAN TELECOMMUNICATIONS 97 (1989).

8. GERALD R. FAULHABER, TELECOMMUNICATIONS IN TURMOIL: TECHNOLOGY AND PUBLIC POLICY 2 (1987).

frequently unable to call people on competing networks because there was no network interconnection, due in part by lack of attempts to connect the networks and in part by a lack of technology.⁹ Competition also led multiple companies to build duplicate infrastructures in the same localities.¹⁰

Due to mounting dissatisfaction with the service provided by local telephone companies, as well as high service prices, there was growing public sentiment that some type of reform must take place in the telephone industry.¹¹ Eager to create a dominant phone company, Theodore Vail, president of AT&T, embarked on a bold mission to buy up all existing telephone-related patents, and to then deny his competitors access to AT&T's long-distance network.¹² As a result, AT&T lured many customers away from competing networks and bankrupted a large number of competitors.¹³

Though AT&T's marketing plan was very successful, American society was becoming very distrustful of monopolistic corporations.¹⁴ Sensing the public's concern, Vail pushed the idea that telephone service was a "natural monopoly" that could best be provided by a single phone company.¹⁵ The concept of a natural monopoly emerged from Progressive Era economic principles that had found favor in the American public during the early years of the Industrial Revolution.¹⁶ Vail's strategy was successful: Congress passed the Willis-Graham Act in 1921 granting the Interstate Commerce Committee ("ICC") the power to consolidate local telephone systems.¹⁷ By the time the Communications Act of 1934 ("Communications Act") created the FCC,¹⁸ regulatory policy in the telephone industry was well established.¹⁹

9. ZARKIN, *supra* note 4, at 52.

10. FAULHABER, *supra* note 8, at 2.

11. ZARKIN, *supra* note 4, at 53.

12. *Id.*; FAULHABER, *supra* note 8, at 2.

13. *Id.* at 4.

14. This concern is evidenced by the Sherman Antitrust Act of 1890, the Clayton Act, and the breakup of Standard Oil in 1911. *See* FAULHABER, *supra* note 8, at 5.

15. ZARKIN, *supra* note 4, at 54.

16. *Id.* Progressive Economic Theory found its roots in late 19th century European thought and advocated increased government regulation of private industry in order to stabilize society and assist in human progress. *Id.* at 47.

17. The ICC, a regulatory body in the early twentieth century, later became part of the FCC. FAULHABER, *supra* note 8, at 7.

18. Communications Act of 1934, ch. 652, 48 Stat. 1064 (codified at 47 U.S.C. § 151 (2000)).

19. The telephone industry was allowed to exist as a regulated monopoly, while the radio broadcast industry, also controlled by the FCC, was kept separate from the telephone industry and functioned as a competitive marketplace. ZARKIN, *supra* note 4, at 56-57.

AT&T flourished as a regulated monopoly, with its grasp on the telephone industry remaining practically unchecked until the mid-1950s.²⁰ In that time, AT&T had cornered the market on telephone technology, and through the process of cross-subsidization²¹ had been able to keep the cost of local service artificially low by overcharging for long-distance service.²² This practice was in line with the social goals of the Progressive Era economists, who believed the telephone industry's aim should be universal service, something that could not be guaranteed in a free market.²³ However, with the goal of universal service coming closer to completion and a growing number of competitors encroaching on AT&T's market, the sanctioning of these less-than-ethical business practices would not last forever.

While attitudes regarding the effectiveness of regulation slowly soured, advances in technology created additional problems for AT&T's regulated monopoly status. The development of microwave technology as a means of communication during World War II, as well as the advances in computer technology, brought on a fresh batch of competitors, all seeking a share of AT&T's market.²⁴ While the FCC had previously protected AT&T from outside competitors, the Commission began creating special exceptions allowing new companies to compete in areas once thought to be the lone province of the telecommunications giant.²⁵

20. Although AT&T was widely hailed as the "model of a modern corporation" for much of the 1920s and 1930s, it was not without its detractors. The first successful challenge of AT&T's supremacy stemmed from an antitrust suit filed in 1949. The suit sought divestiture of Western Electric, the manufacturing arm of the Bell Corporation. To avoid the divestiture, AT&T signed a consent decree in 1956 that forced them to "freely licens[e] its Bell Labs technology," and "restric[t] its business to only regulated utility operations." FAULHABER, *supra* note 8, at 8.

21. Cross-subsidization involves using profits from one business venture to support another venture that is not cost efficient, or operating at a loss. *Id.* at 25-27.

22. *Id.* at 16.

23. See ZARKIN, *supra* note 4.

24. See HORWITZ, *supra* note 7, at 222-24.

25. Three decisions in particular threatened the AT&T monopoly. The first decision created a special category for private microwave systems that offered corporations the ability to create private networks to handle interoffice communication. Allocation of Frequencies in the Bands Above 890 Mc., Report and Order, 22 Rad. Reg. 2d (P & F) 2069 (1959). In the second decision, the prohibition against allowing other companies to connect to AT&T's terminal equipment was relaxed, opening a small window for outside manufacturing companies. Use of the Carterfone Device in Message Toll Telephone System, *Decision*, 13 Rad. Reg. 2d (P & F) 597 (1968). The third decision expanded the rule in *Above 890*. Specifically, it allowed smaller firms to gain access to the microwave communication system, which had previously been available only to large companies. Establishment of Policies and Procedures for Consideration of Application to Provide Specialized Common Carrier Services, *First Report and Order*, 29 F.C.C.2d 870 (1971). See also FAULHABER, *supra* note 8, at 24-33.

B. *The Beginning of the End: The Breakup of AT&T*

In 1974, the influence of Chicago School economics, favoring free market competition over government regulation, as well as pressure from the growing number of competitors, led the Department of Justice ("DOJ") to file an antitrust action against AT&T.²⁶ The complaint alleged that AT&T had discriminated against other long-distance carriers and telecommunication equipment manufacturers through its monopoly control of local telephone service, and that AT&T had engaged in pricing without regard to cost.²⁷ These charges directly mirrored the accepted business practices that AT&T had relied on for over seventy years. It was the feeling of those in the DOJ that regulation was a failure and was responsible for the anticompetitive business practices of AT&T.²⁸ The DOJ felt that if the competitive long-distance carrier (AT&T) could be separated from the noncompetitive monopoly (Bell), then the ability and desire to engage in these anticompetitive practices would disappear.²⁹

Though AT&T expended great effort to maintain its status, it eventually succumbed to divestiture on January 1, 1984.³⁰ AT&T was to maintain service in the competitive long-distance market, and the Bell Corporation was split into seven Regional Bell Operating Companies ("RBOCs"), which would maintain monopoly control over local telephone service.³¹ While the end of AT&T in its traditional form did not mean the end of regulation in the telephone industry, it was certainly a large step in that direction. The challenge then became how to ensure that access to the market was truly unencumbered so that the newly created free market in telecommunications could thrive, as those in the DOJ and FCC had envisioned.³²

C. *Post-Divestiture Developments in the Long-Distance Market*

The years directly following divestiture saw an incredible restructuring of the long-distance market. Where once AT&T was essentially the lone player in the field, hundreds of new long-distance providers have come into existence in a matter of a few years.³³ This

26. ZARKIN, *supra* note 4, at 108.

27. *Id.* at 110-13.

28. *Id.* at 109.

29. FAULHABER, *supra* note 8, at 88.

30. JAMES SHAW, TELECOMMUNICATIONS DEREGULATION 35 (1997).

31. *Id.*

32. ZARKIN, *supra* note 4, at 115.

33. By 1987, there were 223 long-distance companies competing in the open market. That number increased to 621 in 1996, when the Telecommunications Act was made law.

increase in competition spurred immediate reduction of long-distance rates, as AT&T dropped its rates by 6.4 percent in 1984, a small amount compared to the overall 40 percent drop in rates by 1990.³⁴ Furthermore, even though AT&T's market share slipped from 91 percent in 1983 to only 44 percent in 1997, its revenues increased in that time from over \$36 billion to nearly \$46 billion.³⁵ The overall long-distance market revenues increased from \$9 billion in 1983 to \$96 billion in 1998.³⁶ Whether or not this growth would have happened if AT&T had retained its monopoly status is simple speculation. However, it is very telling that in the same period, local telephone service, still subject to monopoly control by the seven RBOCs, saw its prices remain steady or increase slightly.³⁷

III. COMPETITION, DEREGULATION, AND THE WIRELESS MARKET

A. *The Development of the Regulatory Scheme in the Wireless Phone Industry*

Though wireless telephone technology has existed since the 1940s,³⁸ the regulation of the modern form of wireless telephone did not begin until 1968. The FCC's first step toward regulation was the exploration of possible bandwidth distribution and the distinctions between private and common carriers in the emerging field.³⁹ Specialized mobile radio ("SMR") providers, created in 1974, were able to deliver service to users as a private

JAMES ZOLNIEK ET AL., FEDERAL COMMUNICATIONS COMMISSION, LONG DISTANCE MARKET SHARES: FOURTH QUARTER 1998 (Mar. 1999) *available at* http://www.fcc.gov/Bureaus/Common_Carrier/Reports/FCC-State_Link/IAD/mksh3q98.pdf.

34. AT&T Corporation *at* <http://att.com/history/milestones.html> (last visited Aug. 26, 2004).

35. ZOLNIEK, *supra* note 33, at 16-20.

36. *Id.*

37. SHAW, *supra* note 30, at 36. Competition in the local service industry has not brought the drastic changes seen in the long-distance market. As of 1999, there was only a 6 percent increase in independent providers for local service, but that number jumped to 10 percent by 2001. The FCC also cites the high incidence of consumers using their wireless phones as substitutes for local service as a contributing factor to the relatively slow development of competition in the local service industry. The Commission remains hopeful that further regulatory measures will increase competition in the local market. *See* Biennial Regulatory Review 2002, *Staff Report of Wireline Competition Bureau*, WC Dkt. No. 02-313, at 32 (Dec. 31, 2002), *at* http://hraunfoss.fcc.gov/edocs_public/attachmatch/DA-03-804A1.pdf.

38. Thomas W. Hazlett, *Is Federal Preemption Efficient in Cellular Phone Regulation?*, 56 FED. COMM. L.J. 155, 161 n.17 (2003).

39. An Inquiry Relative to the Future Use of the Frequency Band 806-960 MHz, *Notice of Inquiry and Notice of Proposed Rule Making*, 14 F.C.C.2d 311 (1968).

carrier.⁴⁰ SMR was intended to be limited to eligible users, such as doctors or taxi drivers, thus differentiating it from common carriers, who were bound to hold their service open to all customers.⁴¹

While there was a definitional distinction between private and common carriers, functionally they offered the same services. This created a great deal of trepidation on behalf of the common carriers, as private and common carriers were subjected to vastly different regulatory schemes. For example, common carriers were required to provide service in a nondiscriminatory fashion, with reasonable rates, terms, and conditions.⁴² Furthermore, common carriers were subject to individual state regulation of rates and market entry.⁴³ Private carriers, on the other hand, were not subject to any such state regulation and could structure their service terms as they saw fit.⁴⁴ This disparity in regulation led to a court challenge in 1976, but the classification was upheld.⁴⁵ While the court may have been satisfied that there was a proper distinction between common and private carriers, the boundaries of this distinction would prove to be a source of confusion in the coming decade.⁴⁶

In 1984, the FCC began distributing licenses for cellular service.⁴⁷ The Commission did not adopt the natural monopoly approach that had been used to create the wireline telephone industry, opting instead for limited competition.⁴⁸ While this structure produced adequate cellular service, the cost of service remained high. Cellular license holders began to feel disadvantaged, as the distinction between the services they offered and the services offered by the private carriers blurred even more. Over time, the FCC relaxed the restrictions on private carriers, who had started to offer essentially the same services but without the state regulation.⁴⁹ The Commission had essentially created a highly competitive marketplace in

40. E. Ashton Johnston, *Regulatory Treatment of Mobile Services: The FCC Attempts to Create Regulatory Symmetry*, 2 COMMLAW CONSPECTUS 1, 6 (1994).

41. *Id.* at 6-7.

42. *Id.* at 7-8.

43. *Id.* at 8.

44. *Id.*

45. Nat'l Ass'n of Regulatory Util. Comm'rs v. FCC, 525 F.2d 630 (D.C. Cir. 1976).

46. Because of the problems experienced by the courts and regulators, Congress unsuccessfully attempted to clarify the situation in an amendment to the Communications Act in 1982. Johnston, *supra* note 40, at 7.

47. The 306 Metropolitan Service Areas were licensed between 1984 and 1986, while the 428 Rural Service Areas were licensed between 1988 and 1989. Hazlett, *supra* note 38, at 161.

48. The FCC issued two licenses per Metropolitan Service Area to allow for some competition. *Id.*

49. Johnston, *supra* note 40, at 10-11.

which some actors (common carriers) were unable to effectively compete.

In the 1993 Budget Act, Congress sought to remedy these competition problems by ending state control over price regulation.⁵⁰ While the state could still regulate other aspects of the common carrier's service, the cellular companies were free to compete with the private carriers on the basis of price.⁵¹ This move was consistent with the stated policy of the Clinton Administration, which believed that access to telecommunications was vitally important to the future of the United States. The Clinton Administration also believed that private investment and open competition were the best ways to ensure this access.⁵²

The impact of deregulation on the wireless industry was immense. In the year following deregulation, there were approximately 25 million cellular telephone customers;⁵³ that number jumped to 141.8 million in

50. "[N]o State or local government shall have any authority to regulate the entry of or the rates charged by any commercial mobile service or any private mobile service. . . ." Omnibus Budget Reconciliation Act of 1993, 47 U.S.C. § 332(c)(3)(A) (2002).

51. See 42 U.S.C. § 332. It is interesting to note that this statute allows states to petition for the ability to resume regulation of the wireless industry. If a state is able to make the requisite showings, then the FCC "shall" permit such regulation. Section 332(c)(3)(A) reads in part:

[A] . . . State may petition the Commission for authority to regulate the rates for any commercial mobile service and the Commission shall grant such petition if such State demonstrates that—

- (i) market conditions with respect to such services fail to protect subscribers adequately from unjust and unreasonable rates or rates that are unjustly or unreasonably discriminatory; or
- (ii) such market conditions exist and such service is a replacement for land line telephone exchange service for a substantial portion of the telephone land line exchange service within such State.

The Commission shall provide reasonable opportunity for public comment in response to such petition, and shall, within 9 months after the date of its submission, grant or deny such petition. If the Commission grants such petition, the Commission shall authorize the State to exercise under State law such authority over rates, for such periods of time, as the Commission deems necessary to ensure that such rates are just and reasonable and not unjustly or unreasonably discriminatory.

This language suggests that Congress may not have been as confident in the free market as they would have us believe. This faith in regulation seems to mirror the "natural monopoly" approach that defined the wireline telephone industry for much of the 20th century.

52. Larry Irving et al., *Steps Toward a Global Information Infrastructure*, 47 FED. COMM. L.J. 271, 272 (1994).

53. In 1995, there were approximately 25 million cellular customers, though the total number of wireless customers reached more than 65 million when pagers and other wireless radio communication devices were included. Implementation of Section 6002(B) of the Omnibus Budget Reconciliation Act of 1993, *First Report*, 10 F.C.C.R. 8844, para. 10 n.9 (1995) [hereinafter *6002(B) First Report*].

2003.⁵⁴ In that same time frame, the price per minute of cellular service decreased from \$.51 per minute to \$.12 per minute.⁵⁵ Furthermore, where the original pattern of regulation called for only two competing networks in each service area, 95 percent of the population then lived in a county that had at least three operators available, and 83 percent of the population lived in a county with five competing networks. Finally, the introduction of personal communications services (“PCS”) technology in the mid-1990s,⁵⁶ and the consolidation of national networks during this time frame,⁵⁷ added to the increase in service and price reductions. Despite these introductions, it would be hard to argue that deregulation did not have an immediate and immense impact on the wireless telephone industry.

B. Wireless Number Portability: The Last Piece of the Puzzle

1. The Seven-Year Struggle over the Implementation of Number Portability

Arguably, the Communications Act of 1996 most directly impacted the RBOCs because the promotion of local competition effectively ended their monopoly control over local telephone service. Nonetheless, the wireless industry was not left unscathed. Though the wireless industry had been effectively competitive since its inception, or at the very least since the Budget Act of 1993, local number portability (“LNP”) created a large stir among wireless providers.⁵⁸

LNP, as mandated by the Telecommunications Act, was originally meant to apply to Local Exchange Carriers (“LECs”).⁵⁹ Even though wireless providers were not included in the definition of an LEC, the FCC

54. As of 2001, the top ten wireless providers accounted for approximately 110 million of these customers with numerous other providers splitting the remaining 31.8 million customers. Implementation of Section 6002(b) of the Omnibus Budget Reconciliation Act of 1993, *Eighth Report*, 18 F.C.C.R. 14783, app. D, tbl. 4 (2003) [hereinafter *6002(b) Eighth Report*].

55. Hazlett, *supra* note 38, at 165 tbl. 3.

56. *Id.* at 163-64.

57. *Id.* at 168.

58. The FCC has issued numerous orders and reports dealing with LNP. See Telephone Number Portability, *First Report and Order and Further Notice of Proposed Rulemaking*, 11 F.C.C.R. 8352 (1996) [hereinafter *Telephone Number Portability First Report*]; Telephone Number Portability, *First Memorandum Opinion and Order on Reconsideration*, 12 F.C.C.R. 7236 (1997); Telephone Number Portability, *Second Memorandum Opinion and Order on Reconsideration*, 13 F.C.C.R. 21208 (1998); Telephone Number Portability, *Memorandum Opinion and Order on Reconsideration and Order on Application for Review*, 17 F.C.C.R. 2578 (2002).

59. Telecommunications Act, *supra* note 2.

decided that LNP would also apply to wireless phone providers as well.⁶⁰ In its first report on wireless local number portability, released July 2, 1996, the Commission set an original compliance date of June 30, 1999.⁶¹ On February 9, 1999, in response to a petition filed by the Cellular Telecommunications Industry Association ("CTIA"), the Commission moved the compliance date to November 24, 2002,⁶² due in part to the increased competition in the wireless industry, low customer demand for WLNP, and the need for additional time to develop the necessary technology for implementation of WLNP.⁶³ In the summer of 2001, Verizon Wireless filed a petition with the FCC seeking permanent forbearance from WLNP.⁶⁴ Verizon believed that the wireless industry was already highly competitive and that WLNP was not cost effective.⁶⁵ The Commission did not grant a permanent forbearance, but it did push the compliance deadline back an additional year to November 24, 2003.⁶⁶ After an unsuccessful court challenge to the FCC's final decision,⁶⁷ WLNP became a reality in the fall of 2003.

2. Possible Effects of WLNP

Due to the extremely short existence of WLNP, it is impossible to gauge what kind of long-term effects number portability will have on the wireless market. There are some early indications that the transition to number portability has been a rocky one, even after seven years of preparation. The FCC received 4,734 informal complaints in the first two months following the implementation of WLNP, with some carriers experiencing far more problems than others.⁶⁸ The FCC is quick to point

60. *Telephone Number Portability First Report*, *supra* note 58, at para. 4.

61. *Id.*

62. Cellular Telecommunications Industry Association's Petition for Forbearance From Commercial Mobile Radio Services Number Portability Obligations and Telephone Number Portability, *Memorandum Opinion and Order*, 14 F.C.C.R. 3092, para. 1.

63. *Id.* at paras. 19-30.

64. Verizon Wireless's Petition for Partial Forbearance from the Commercial Mobile Radio Services Number Portability Obligation, *Memorandum Opinion and Order*, 17 F.C.C.R. 14972, para. 10 (2002).

65. *Id.* at paras. 10-11.

66. *Id.* at para. 1. WLNP was to be made available in the 100 largest MSAs as of November 23, 2003, with May 24, 2004, (six months after portability is introduced in the 100 largest MSAs) as the deadline for the remaining service areas. Press Release, FCC, FCC Provides Information for Consumers on Wireless Local Number Portability (Nov. 4, 2003), at http://hraunfoss.fcc.gov/edocs_public/attachmatch/DOC-240702A1.pdf.

67. *Cellular Telecomms. & Internet Ass'n v. FCC*, 330 F.3d 502 (D.C. Cir. 2003).

68. Press Release, FCC, Wireless Portability Complaints: 4,734 Consumer Complaints Since Porting Began on Nov. 24 (Jan. 28, 2004), at http://hraunfoss.fcc.gov/edocs_public/attachmatch/DOC-243262A1.pdf. Furthermore:

out that even though there have been a substantial number of complaints; no wrongdoing has yet been proven.⁶⁹ It will be interesting to see how the industry will perform now that WLNP is available outside the 100 largest service areas.

Problems are not the only expected result of WLNP; wireless insiders speculate that WLNP will mean lower prices, better service, and more favorable terms for consumers as wireless providers try to compete for the wave of customers expected to switch carriers.⁷⁰ FCC Chairman Michael Powell has speculated that as many as 21 percent of wireless customers may switch service after WLNP is available.⁷¹ However, since full WLNP has only been in effect for a short period of time, credible evidence to support these figures is currently unavailable.

While there is not yet any data on the actual impact of number portability, claims of lower prices and better service are not without support. Hong Kong initiated number portability in 1999 and has seen a sharp rise in wireless subscribers and a marked decrease in price.⁷² When number portability hit Hong Kong in 1999, 45 percent of the population owned a wireless phone; now the number is in excess of 99 percent.⁷³ Hong Kong prices fluctuated initially, when carriers tried to find a price for service that would keep them out of the red but still in competition. Prices eventually settled at rates much lower than that of pre-portability service.⁷⁴ If the Hong Kong experience is any indication of things to come in the United States, consumers can look forward to much lower prices, and carriers can look forward to a huge jump in subscribers.⁷⁵

The carriers mentioned in at least 100 complaints are: AT&T Wireless (2297); Sprint PCS (1119); Verizon Wireless (739); Cingular Wireless (699); T-Mobile (625); Nextel (332); Qwest (195); ALLTEL (119). Many of the complaints concern more than one carrier so the total number of complaints received is smaller than the number of times a carrier is mentioned in a complaint.

Id.

69. *Id.*

70. Sarah Max, *Your Cell Number, Yours to Keep*, CNN/Money (Nov. 5, 2003), available at <http://money.cnn.com/2003/11/04/pf/cellphoneportability>; Gross & Lawson, *supra* note 1.

71. FOXNews.com, *Long-Awaited Cell Phone Rules Go Into Effect* (Nov. 24, 2003), at <http://www.foxnews.com/story/0,2933,103913,00.html>.

72. Dan Gillmor, *Hong Kong Offers Lesson in Number Portability*, THE MERCURY NEWS (Nov. 23, 2003), available at <http://www.mercurynews.com/mld/mercurynews/business/7331821.htm>.

73. *Id.*

74. *Id.*

75. Though the population of Hong Kong is a great deal smaller than that of the United States, a jump from 45 percent wireless subscription rate to a 99 percent subscription rate is nonetheless impressive. The increase in service may not be as pronounced in the United States, but it clearly indicates that some rise in subscription rate is on the horizon.

IV. WIRELINE REGULATION V. WIRELESS COMPETITION

A. *The Methods of Control: A Brief Overview of the Regulatory Approaches Taken in the Wireless and Wireline Industries*

The initial regulatory approach in the wireline telephone industry was a product of Progressive Era economics in the early twentieth century.⁷⁶ The social value of telephone service was placed above competition, as progressives had very little faith in the ability of the free market to adequately protect the consumer.⁷⁷ The initial period of competition only strengthened this belief, as competing providers brought poor levels of service, incompatible networks, and high prices.⁷⁸ Sensing the prevailing trend toward regulation, AT&T began to consolidate the industry, and the creation of the FCC in 1934 essentially vindicated AT&T's status as a natural monopoly.⁷⁹ Over the years, the FCC ensured that no competition interfered with AT&T's long-distance and manufacturing divisions, while state regulators saw to it that the RBOCs maintained control over local service.⁸⁰ This system allowed AT&T to create the most complete telephone network in the world, and all in the name of "universal service." As the network became secure, and universal service was in reach, the rationale behind the natural monopoly status began to fade.⁸¹ The FCC, the courts, and the DOJ eventually began to turn against AT&T until the company was broken apart in 1984.⁸² AT&T was thrust into the competitive world of long-distance service, while the RBOC's maintained monopoly control over the local service until 1996.⁸³

The wireless industry, though subject to early regulation, always had competition as a goal.⁸⁴ The classification of common and private carriers allowed private carriers to provide limited services on a competitive basis, while the licensing of two common carriers in each area produced some competition, though seemingly artificial in nature.⁸⁵ This distinction quickly fell apart, as private carriers offered essentially the same services

76. ZARKIN, *supra* note 4, at 47. *See also supra* text accompanying note 16.

77. ZARKIN, *supra* note 4, at 47-49. *See also supra* text accompanying note 16.

78. ZARKIN, *supra* note 4, at 52. *See also supra* text accompanying notes 9-10.

79. ZARKIN, *supra* note 4, at 57. *See also supra* text accompanying note 19.

80. ZARKIN, *supra* note 4, at 58.

81. *See* FAULHABER, *supra* note 8, at 16. *See also supra* text accompanying note 23.

82. SHAW, *supra* note 30 and accompanying text.

83. SHAW, *supra* note 30.

84. Hazlett, *supra* note 38. *See also supra* text accompanying note 48.

85. *See* discussion *infra* Section III.A.

as common carriers but in a competitive nature.⁸⁶ Seeing the success of the private carriers, Congress decided to end the quasi-regulation of common carriers and open the market to full competition.⁸⁷ The end of regulation, in conjunction with the introduction of PCS technology, led to a giant increase in subscribers, an increase in service quality, and a decrease in prices.⁸⁸

B. Different, but Why? An Analysis of the Regulatory Approaches Taken in the Wireless and Wireline Industries

While it is clear that the regulatory approaches taken in each industry were markedly different, the reason for these differences is not so clear. Did AT&T fool Congress, the FCC, state regulators, and the population for over eighty years with the belief that a single company, or “natural monopoly,” was the best way to ensure universal service? Is the success of competition in the wireless industry, as well as the long-distance market after divestiture, proof that competition would have produced the same or better results in the wireline industry? Are the goals of the wireless and wireline industry even the same, so that a comparison would be appropriate, or are we assuming that because both industries involve telephones, that a comparison of regulatory approaches is proper?

The regulatory scheme enacted in both industries was correct. Moreover, the success of wireless carriers and long-distance providers in a deregulated, open market is a result of the over-regulation of wireline that permeated much of the twentieth century. To explain these contentions, it is first necessary to examine the underlying goals of each industry, the manner in which these goals are best served, and whether or not the success of competition in the modern era is due in large part to the history of strict regulation of the wireline industry.⁸⁹

1. Policy Goals behind the Development of the Wireline Regulatory Framework

A particularly fitting law school mantra is “if the reason for the rule does not apply, then you do not apply the rule.” This statement illustrates

86. See Johnston, *supra* note 40, at 7.

87. Omnibus Budget Reconciliation Act of 1993, 47 U.S.C. § 332(c)(3)(A) (2002).

88. See 6002(B) *First Report*, *supra* note 53. See also 6002(b) *Eighth Report*, *supra* note 54; Hazlett, *supra* note 38, at 165-66 and tbl. 3.

89. Not everyone believes competition is successful in either the wireless or long-distance industries. Indeed, many books and journal articles would likely disagree with this premise. However, from a raw data standpoint alone, it is difficult to argue that competition has not been successful in these industries, and for the purpose of this Note, effectiveness of competition is assumed.

that it is first necessary to figure out the reason for the rule before it is possible to see if the rule applies. The clearest summation of the stated goals in the early regulation of the telephone industry is in the preamble to the Communications Act:

For 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, without discrimination on the basis of race, color, religion, national origin, or sex, a rapid, efficient, Nation-wide, and world-wide wire and radio communication service with adequate facilities at reasonable charges, for the purpose of the national defense, for the purpose of promoting safety of life and property through the use of wire and radio communications. . . .⁹⁰

From this, one can extract a good number of principles that Congress wanted to serve: mass availability, a single efficient system, reasonable fee for service, protection of national interests, and protection of personal interests (life and property).

Even though Congress laid out these numerous principles in the Communications Act, it was not a given that regulation was the best way to achieve each individual goal. National defense, though clearly a national concern, receives its innovations not through federal regulation, but from the private sector where companies compete to create the newest technologies. Protection of personal interests is another area where federal regulation would not seem to be the best way to achieve results. Protection of personal interests tends to be a very local issue. If a person is having a problem with an intruder or illness, his or her first concern is contacting someone in the immediate area for assistance, not making a collect call to Tempe from Kalamazoo. Protection of personal interests would not be best served by a national system, but from coordinated local services.

On the other hand, many of these goals can best be served through a regulated system: mass availability; a national, efficient system; and stable, affordable prices. In the sense that it is beneficial to have a single system available to all at a reasonable price, the federal government is well equipped to ensure compliance. A few good examples of this are the highway system and the railroads. If there were no guarantee that the highway would continue beyond state borders, what good would it be? The same holds true for trains; if the passengers had to change trains every time they left the state because the tracks were not the same size, rail travel would be inconvenient, and would likely not survive. Because the government deemed these functions important to the nation as a whole, it decided to intervene and regulate, instead of leaving the market to decide how and if these industries were to succeed. Similarly, the market cannot

90. Communications Act of 1934, 47 U.S.C. § 151 (2000) (emphasis added).

guarantee affordability or availability. If it is not profitable to provide service in an area, then the market will not provide service, or if it does, the price will be so high that the people in those areas may not be able to pay for it. The federal government, through price controls and subsidies, can take care of both of those problems. For the purpose of “universal service,”⁹¹ it would seem that government control is beneficial, at least at an early stage.

2. A Shift in Focus: A Different Scheme Emerges

Just as the Communications Act provides a basis for examining the regulatory scheme of the wireline telephone industry, the Telecommunications Act provides some insight into the goals behind the deregulatory approach in the wireless industry.⁹² The Telecommunications Act sought to echo the policies set forth in 1934, particularly the desirability of universal service and the role of the FCC.⁹³ The Telecommunications Act, however, had a decidedly different tone: the focus now was on the promotion of competition with less government interference.⁹⁴ In order to explore the rationale behind Congress’ sudden distaste for regulation, it is helpful to look beyond the Telecommunications Act to the position taken by the Clinton Administration regarding telecommunications policy. The Administration focused on “(1) encouraging private investment; (2) promoting competition; (3) creating a flexible regulatory framework that can keep pace with rapid technological and market changes; (4) providing open access to telecommunications networks for all information providers; and (5) ensuring universal service.”⁹⁵

Again, while Congress and the Clinton Administration articulated the above principles, it does not necessarily mean that Congress or the President are in fact concerned with each individual goal, or that the chosen course of action is best suited to meet these goals. Read together, the Telecommunications Act and the principles set forth by the Clinton

91. For the purpose of further discussion, universal service will be defined as a single system, available to all at a reasonable price.

92. Although the wireless industry was effectively deregulated in the 1993 Budget Act, the Telecommunications Act provides a better policy framework with which to analyze the rationale behind the trend toward deregulation.

93. SHAW, *supra* note 30, at 39.

94. The preamble to the Telecommunications Act states its purpose as “[t]o promote competition and reduce regulation in order to secure lower prices and higher quality services for American telecommunications consumers and encourage the rapid deployment of new telecommunications technologies.” See Telecommunications Act, *supra* note 2.

95. Irving, *supra* note 52, at 273.

Administration seem to value an increase in private participation in order to lower the costs of telecommunications for individuals as well as other emerging industries while still striving to provide universal service. Where the Communications Act focused more on the social benefits of the telephone industry, the contemporary policy of the 1990s focused more on economic aspects. While universal service remained important, it had now taken a new form. With the basic telecommunication framework already in place, the focus seemed to have shifted toward making access to that network as cheap and efficient as possible. No longer was the physical availability of service a driving force, rather the focus was now on maximizing the potential of the existing structure.

The existing regulatory framework was ill-equipped to bring about the new policy goals driving the telecommunications industry. While the government had been able to ensure the creation of a uniform, reasonably priced system, things like innovation and maximization of existing resources are typically the fiat of the open market. This was essentially the contention of the Progressive Era economists; they knew that the market was quite capable of, if not ideal for, spurring the development of new products and finding economic efficiency. The market, however, was scarcely able to take into consideration the social benefit of any particular product.

3. Regulation Sets the Stage for Competition

Though the reasons for the different regulatory approaches in the wireline and wireless industries are fairly evident, the reason why these differences came about is not yet clear. To simply say that policies shifted does nothing to explain why they shifted or what made this shift possible. In this instance, it can be fairly said that the reason the policy shifted, and was able to shift, was the regulatory approach taken by Congress and the FCC at the inception of the telephone industry. By initially favoring the social value of the telephone over the purely economic benefits, the government allowed AT&T to construct an extremely complex and wide-reaching network. Because this network was already in existence, additional equipment manufacturers, long-distance providers, and even the cellular phone industry needed only to design their products to attach to the existing network. Without interconnectivity to the existing network, the cost of starting and maintaining these peripheral industries would be greatly increased. The original idea of universal service led not only to the creation of the most impressive telephone system on the planet, but it also

allowed for innovation and competition in the wireless industry, the long-distance industry, manufacturing, the Internet, and a variety of other types of technology.

V. THE NEW ROLE OF THE FCC

Though the telecommunications industry is no longer subject to strict regulation, the FCC still maintains a great deal of power. Congress specifically sought to reaffirm the power of the Commission in the Telecommunications Act, perhaps as an acknowledgement that although the open market is best able to serve the current set of values, the telecommunications industry is too important to relinquish all governmental oversight. The new mission of the FCC is to ensure open access to the telecommunications market and to promote competition. This new role is opposite from the role served in the past, where it seemed the goal of the Commission was to keep competition away until AT&T was strong enough to survive on its own.

Nowhere is the image of the FCC's new role clearer than in the implementation of WLNP. WLNP by nearly all accounts is a good thing for competition. Portability will give the customers more bargaining power with their existing carriers, as well as with potential new carriers. But if WLNP increases competition, and competition is a good thing for the telecommunications industry, why is it that WLNP took seven years to implement? Here is a perfect example of how the FCC must now balance the desirability of competition with the social benefit of a successful telecommunications industry. If WLNP was thrust upon the wireless carriers too soon, it had the potential to wreak economic havoc. The technology costs, combined with the fact that many of the networks were still in their infancy in the mid-1990s, had the potential to bankrupt a good portion of the wireless companies. While a pure free-market advocate might say this is the ideal outcome for economic efficiency, it is clearly not the best outcome if one takes into account the social benefits of a thriving telecom industry. The FCC now has the stated ability to take into account these types of factors⁹⁶ instead of making clearly protectionist rulings in a somewhat dubious fashion.⁹⁷

96. Omnibus Budget Reconciliation Act of 1993, 47 U.S.C. § 332(c)(3)(A) (2002) (granting the FCC the ability to allow states to resume regulation of the wireless industry if certain conditions are met).

97. In the mid-1940s, AT&T sought to discontinue the use of the Hush-a-Phone device, a plastic attachment that provided additional privacy for those engaged in a telephone conversation. The device attached to the outside of the telephone unit and in no way affected the inner-workings of the telephone system. The FCC, however, found that the attachment did impair the telephone service, and thus the use of a Hush-a-Phone device was prohibited.

The implications of the new role for the FCC are yet to be fully actualized. The courts, as well as the DOJ, have a history of disagreeing with the FCC's decisions.⁹⁸ Will this trend continue now that the Commission's role is less as protector and more as mediator? Or will courts and politicians on the other side of the issues condemn the FCC for being too pro-competition at the expense of the public good? Only time will tell, and certainly in time, adequate data will be available to examine the full impact of the new policies shaping the FCC.

VI. CONCLUSION

A great many factors outside the scope of this analysis undoubtedly had an effect on the different regulatory schemes employed in the wireless and wireline telephone industries. However, this does not weaken the connection between the early regulatory/anticompetitive nature of the wireline industry and the success of the deregulatory/competitive approach in both the wireless and the wireline industries in recent years. The influence of a complete, unified telephone system on later technological developments cannot be overstated. Imagine if the Internet, long-distance providers, or the wireless industry had to adapt to competing telephone systems utilizing different technology. This would not only increase the types of technology that would need to be developed to be compatible with each network, but would force these new companies to contract for the services of multiple parties instead of a single, integrated system.

The high cost of multiple systems would not be borne by the telecommunications industry alone. The value of these services to the public would be much less if the system was not proprietary. One need only look to the early history of the telephone industry, when competing networks, lacking the ability to interconnect, created a system where an individual may not have been able to call his or her own neighbor. It was clear that the telephone would revolutionize the way the country interacted as a whole, but until an efficient system could be created that allowed everyone access to the entire country, the telephone would be little more than a luxury.

Because of these added costs and minimized benefits, it would not have been profitable or feasible to create these industries at all. Still, can

Hush-a-Phone Corp., *Decision*, 20 F.C.C. 391 (1955), *rev'd*, 238 F.2d 266 (D.C. Cir. 1956).

98. The decision in *Hush-a-Phone* was clearly a measure to protect AT&T, and the courts took notice. The FCC decision was invalidated by the Court of Appeals for the District of Columbia. *Hush-a-Phone*, *supra* note 97. The DOJ felt that regulation of AT&T had not been effective in stopping its abuses, and initiated the antitrust suit that eventually led to the breakup of AT&T. FAULHABER, *supra* note 8, at 60.

anyone imagine a world where the telephone is merely a luxury held by the rich, or life without the Internet, cell phones, or wireless modem capability? Perhaps this example overstates the ramifications the free market would have had on the developing telephone industry. Competition spells the demise of new technologies all the time. When Beta lost the battle to VHS, society managed to survive.⁹⁹ Sony, the producer of Beta, had the choice to either adapt its production to the VHS format, or to sell its manufacturing space to another industry. For telephone service providers, it is not this simple. The initial outlay to cover the nation with telephone poles and service lines was enormous. If each provider used different technology and one company folded, then those lines would be useless. The amount of waste created by the natural progress of the free market in this instance would be staggering. While it is easy to say that the situation would have worked out under the free market, it is equally as easy to imagine the very real consequences that could have reduced the telephone industry to ruins.

While looking to the past is always an interesting enterprise, its importance lies in what it can teach us about the future. What lessons can we learn from the evolution of the telecommunications industry? While the United States is rightly characterized as a capitalist society, there are times when government intervention can be very useful in providing for the early establishment of a particular industry. However, there does come a time when the reasons for government intervention are no longer valid, at which point the government needs to pull back. As is evidenced by the FCC's continuing role in the telecommunications industry, the government need not relinquish all control and, perhaps, should not. The ability of the government to act in a positive manner to ensure economic competitiveness can yield very positive effects. The seemingly successful implementation of WLNP is evidence of the positive effect a regulatory agency can have on an industry. The other advantage of continued government regulation is that, should the industry fall on hard times, it is easier for the government to give assistance to the industry without looking protectionist.¹⁰⁰

99. In the early 1980s, there were two emerging forms of video cassette recorders (VCRs), Beta and VHS. Beta was produced by the Sony Corporation, while VHS was made by JVC. Though Beta was thought to be the higher quality product, the marketing strategy employed by JVC eventually carried the day, and VHS became the preferred format in VCRs. The Sony Corporation began to market VHS products after the failure of Beta. WIKIPEDIA, *The Free Encyclopedia, Video Cassette Recorder*, at http://en.wikipedia.org/wiki/Video_tape (last visited Oct. 03, 2004).

100. Following the government bailout of the airline industry after the attacks on September 11, 2001 there was some concern as to the socialistic nature of the bailout. Susana Dokupil, *Rethinking the Airline Bailout*, The Federalist Society: National Security White Papers, available at <http://www.fed-soc.org/publications/terrorism/airlinebailout.htm>

As previously stated, it will be interesting to see how the FCC adapts to its new role, and how the different factions of the government adapt as well. But whatever early bumps in the road are experienced, it is clear that the current regulatory scheme is best suited to serve the goals of our changing society, and, without the path chosen nearly a century ago, it is very possible we could be living in a completely different world.

(last visited Oct. 6, 2004); J.D. Tuccille, *The Baneful Bailout*, Free-Market.Net, at <http://www.free-market.net/spotlight/bailout> (last visited Oct. 7, 2004.) Perhaps if the government retained more control of the industry, there would have been other, less controversial, methods of insuring the success of the airlines.

