PROPOSED ANTITRUST SETTLEMENT OF U.S. v. A.T. & T.

JOINT HEARINGS

BEFORE THE

SUBCOMMITTEE ON TELECOMMUNICATIONS, CONSUMER PROTECTION, AND FINANCE

OF THE

COMMITTEE ON ENERGY AND COMMERCE

AND THE

SUBCOMMITTEE ON MONOPOLIES AND COMMERCIAL LAW

OF THE

COMMITTEE ON THE JUDICIARY HOUSE OF REPRESENTATIVES

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PROPOSED ANTITRUST SETTLEMENT OF UNITED STATES VERSUS A.T. & T.

TUESDAY, JANUARY 26, 1982.

HOUSE OF REPRESENTATIVES, SUBCOMMITTEE ON TELECOMMUNICATIONS, CONSUMER PROTECTION, AND FINANCE, COMMITTEE ON ENERGY AND COMMERCE, AND SUBCOMMITTEE ON MONOPOLIES AND COMMERCIAL LAW, COMMITTEE ON THE JUDICIARY,

Washington, D.C.

The subcommittees met, pursuant to notice, at 9:30 a.m., in room 2123 of the Rayburn House Office Building, Hon. Timothy E. Wirth (chairman, Telecommunications Subcommittee), presiding.

Mr. WIRTH. The joint hearing will come to order.

Today is the first of two hearings being held jointly by the Subcommitttee on Telecommunications, Consumer Protection, and Finance and the Subcommittee on Monopolies and Commercial Law. This morning, with Mr. Brown and Mr. Trienens, and on Thursday, with Assistant Attorney General Baxter, we will examine the recently announced settlement of the Justice Department's antitrust suit against A.T. & T., and the proposed modification of the 1956 consent decree. We will look not only at the individual pieces of the settlement, but also at the larger issue of the settlement's ramifications for communications policy generally.

I would like to welcome Chairman Rodino and the members of the Monopolies Subcommittee here today. I am sure your expertise will prove invaluable as we explore the settlement.

By dramatically restructuring the Bell System, the modification of the consent decree will have an impact on the entire telecommunications industry. As with any plan so complex and far reaching, there are details and ambiguities in the settlement that the parties and the court must still resolve.

There are those who say that, consequently, Congress should refrain from taking any action now, that we should wait until the settlement is in final form. I, for one, disagree. I believe today, as I have since becoming involved in these issues, that the Communications Act of 1934 must be revised to serve in the coming decades as the underpinning for universal telecommunications service and the development of competition in this industry. Congress has the responsibility to establish policy in this crucial field regardless of court action.

The proposed settlement resolves the issue of the relationship between the local operating companies and the rest of A.T. & T.—an

important structural question—but it fails to address a long list of other problems, and it raises some new questions as well.

The settlement has not caused problems, but it has brought into sharp relief such issues as the continued availability of telephone service at reasonable rates; the maintenance and improvement, particularly at the local exchange level, of our telephone system's high quality; and the development of full and fair competition throughout the telecommunications industry. It is our purpose here today to examine the settlement's effect in each of these varied areas.

There is, in addition to the issues I have listed, a need to overhaul the FCC's regulatory machinery to keep pace with the rapid developments in telecommunications. The definition of Federal and State regulatory jurisdiction must be clear. Despite the dramatic changes required by the settlement, it does not—and cannot—change the FCC's jurisdiction, or enable the Commission to deregulate competitive markets.

Let me repeat what I said earlier. The antitrust settlement did not create the local rate issue or the need to maintain high-quality telephone service or the desire to encourage competition. All of these issues predated the settlement. We have been seeking solutions to them now for years. But the settlement has served to focus the issues for debate, and its short-order timetable makes resolution of those issues imperative.

We welcome Mr. Brown and Mr. Trienens, and look forward to their testimony.

I would ask Chairman Rodino if he has an opening statement he would like to make at this time.

Mr. RODINO. Thank you very much, Chairman Wirth.

I appreciate very much the hospitality of your subcommittee in hosting the first day of these joint hearings. We hope to return that hospitality on Thursday of this week, on the second day of the hearing. I would also like to take this opportunity to compliment you, Mr. Chairman, and your subcommittee, for the diligence with which you have been pursuing development of legislation in this area.

I have a number of concerns about the consent settlement which the Department of Justice and A.T. & T. have negotiated. These hearings will provide all of us a chance to address these concerns. But, I want to say at the outset that I am pleased that the parties were able to agree to a consensual resolution of this long litigation. The settlement, whatever its problems, is surely a momentus one, and it largely vindicates our system of antitrust enforcement that some have said was no longer effective in addressing large structural questions.

I have on a number of occasions urged both the Department of Justice and A.T. & T. to explore a settlement. Of course, any resolution of this proceeding, whether by consent or as an ultimate product of contested litigation will be unsatisfactory to some. This is a complex industry in which the interests of consumers, competitors and suppliers do not always coincide in the short term. A settlement has the undisputed advantage of ending the time and expense of prolonged litigation. It provides all of the interested par-

ties and the Congress the opportunity to concentrate on the remaining problems of the industry with a clearer focus.

So, I have no hesitation whatsoever in saying to Mr. Brown and Mr. Trienens, and the other officials of A.T. & T., that the decision to seek settlement of this proceeding was a wise and courageous one. I firmly believe that with the continuing good faith of all the interested parties we can bring this matter to a prompt and successful conclusion.

Chairman Wirth has already alluded to a number of questions about the settlement. Among these is the concern that it directly or indirectly will cause a substantial rise in local telephone bills. We cannot afford to see lower income Americans deprived of telephone service by aggressively rising rates. I will be most interested, therefore, in hearing what the witnesses will have to say about this central question.

The thrust of the settlement and of the telecommunications policy of the FCC in recent years is a restructuring of the industry in such a manner as to replace Government regulation with the potentially more effective regimen of natural competition. While the settlement is a substantial step in this direction, significant questions remain about the ability of others to compete on an equal basis with the largest company in the industry.

Finally, there is the question about the procedural steps taken to reach the settlement. In a case of this importance, the opportunity for public comment provided by the Tunney Act, which I cosponsored in the House, is vital. While I understand that the parties intend to comply with the act, I am bothered by statements suggesting that the parties might not consider themselves to be bound by the precise terms of the act. Indeed, I am deeply troubled by the contortions through which the parties appear to have gone to evade the literal requirements of the act. I would like to say in conclusion, Mr. Chairman, that again I thank you for the hospitality that you have afforded me and my subcommittee, and look forward to this hearing. I am sure we will develop the kind of information that will be important for us in our further consideration of these very important issues.

Thank you very much.

Mr. WIRTH. Thank you very much, Mr. Rodino.

Mr. McClory.

Mr. MCCLORY. Thank you, Mr. Chairman.

First, Mr. Chairman, I want to commend you on convening this joint committee meeting and I take pleasure in participating in it. Further, I would just like to say preliminarily that I hope that neither through litigation nor legislation nor settlements or any other way do we do any damage to the quality of the greatest communications service in the entire world.

In the last Congress, when the Judiciary Committee held hearings on the telecommunications bill, we expressed the hope at that time that settlement in the A.T. & T. antitrust case could be reached. I am pleased that this settlement has been reached for several reasons.

First, it saves a great deal of time and expense.

Second, it removes a major obstacle to the enactment of necessary telecommunications legislation.

Third, it will release the innovative forces of what will be the country's second largest corporation, which have been confined by the 1956 consent decree. This should benefit both A.T. & T. and the Nation.

Fourth, it will make this dynamic industry far more competitive than it has been.

Fifth, regulatory burdens should be eased greatly with the elimination of the heretofore unsolvable problems of cross-subsidies between Bell operating companies and other parts of A.T. & T.

However, my enthusiasm is mixed. The proposed settlement is but the barest outline. For a complex multifaceted issue, we are presented with an agreement to agree in 6 months' time. A.T. & T. is to draw up a plan for Justice Department approval. I suspect many of our questions will not be answered until then. The witnesses this week will not be able to answer many vital questions because they do not know what they will agree to 6 months from now. Certainly, divestiture can be accomplished in a number of different ways, some better than others. It is not possible to judge well what is not yet before us. I would hope that a second round of oversight hearings will be held after the definitive settlement is reached.

Much has been said in the newspaper about circumventing the Tunney Act. It now appears that Judge Green in Washington has salvaged its applicability by vacating the modification of the 1956 decree entered in the district court in New Jersey. But having worked on this legislation in the 93d Congress, I would hope the form of this proposed settlement, which I have characterized as an agreement to agree, will not thwart the effect of the Tunney Act. I would hope further that Judge Green would use his authority to decline entry of the proposed order so as to draw forth greater specificity or, alternatively, to require the consummation of the agreement to agree before making his determination.

I do not believe we should expect too much of a consent decree. No decree can or should answer every telecommunications question on the minds of this audience. It would be presumptuous of the parties, for example, to determine in their settlement who should regulate this or that. But we should see more in writing about precisely how the 22 local operating companies are to be divested. Only then is it possible to assess the viability of these companies and the resultant state of competition in those portions of this industry which are intended to be competitive. These are very serious questions. We should not be rushed to judgment in ignorance. And I do not believe that we will be.

While my primary concerns are with the unspecified details, some specifics give me pause. It appears that the Bell operating companies will lose their intrastate long distance lines to A.T. & T. Thus, Illinois Bell, which now administers virtually all the telephone lines in Illinois, will become a confederation of city systems dependent on A.T. & T. for connection. Will that serve to undermine the operating company's autonomy, or proclaimed impartiality? Since these intrastate lines are a monopoly, arguably a natural monopoly, this arrangement could preclude A.T. & T.'s competitors in long-distance communication services from offering the same universal service. While these competitors may not be ready to

offer such service in the next few years, circumstances may change rapidly. If the purpose of the proposed settlement was to free A.T. & T. of its natural monopoly powers, there may be some question whether the task was completed.

I look forward to the testimony, Mr. Chairman, and to the succeeding hearing, at which time you and members of your committee will join Chairman Rodino.

Thank you, Mr. Chairman.

Mr. WIRTH. Thank you very much, Mr. McClory. For those of you standing in the back perhaps you would like to come over and take the first five or six seats here. Would you like to do that?

Mr. Mottl.

Mr. MOTTL. Thank you, Mr. Chairman.

Chairman Wirth, Chairman Rodino. As we continue to interpret the implications of the A.T. & T. settlement with the Justice Department, it appears that we are witnessing the finest hour for A.T. & T. and its shareholders. Unfortunately, more than 200 million American consumers who rely on quality phone service at a reasonable charge may be entering the most costly and tricky moments ever experienced in their long history as customers of A.T. & T.

It is plain to see that A.T. & T. is taking every winner, each lucrative moneymaker with it into the new competitive arena, while socking the Bell operating companies, such as Ohio Bell, with what have been called the losers in the telephone business. What this will mean is that residential customers, including people on fixed incomes and others served by the remaining monopoly, will ring up a total of rate increases that will be staggering compared to previous rate hikes. A.T. & T. is armed with an impressive arsenal of successful enterprises developed at ratepayers' expense as it enters the information age.

When A.T. & T. calculates its balance sheet, it should include the Justice Department antitrust division as one of its biggest assets. First, there is long distance, a tried and true winner for Bell which Bell has repeatedly told us subsidizes local rates for residential customers. Long distance is apparently too lucrative to be kept with a regulated monopoly to help the persons on fixed incomes, so A.T. & T. and the Justice Department stripped it from the operating companies to compete with the rest of the long distance companies. The fact that A.T. & T. and its independent telephone company partners control over 96 percent of the market and have little incentive to cut long distance charges just to capture the remaining 4 percent of the market should be one indicator of how competition will impact both on long distance markets, and basic rates of American consumers.

Then there is the very profitable Bell publication called the Yellow Pages. Although the monopoly has made this best selling book possible, A.T. & T. and the Justice Department decided those revenues would be better off in the unregulated entity, instead of with Bell operating companies where they could have helped keep rates down.

A.T. & T. has reason to view fondly its pay phones which saturate our Nation. Pay phones become far more than a nickle and dime business once all the coins are faithfully collected, including

the quarters you can never get change for. While pay phones will continue to ring up profits for A.T. & T., the Bell operating companies can kiss goodbye to another steady subsidy for their local residential rates.

In case there was any doubt about the WATS profits, where they would be funnelled, A.T. & T. and the Justice Department cleared them up by, you guessed it, giving this handsome profitmaker to A.T. & T.

What did the local operating companies keep? First, there is the white pages. There is no charge for white pages and no profits. So, A.T. & T. didn't have any trouble deciding to let local operating companies keep them. The local office loops also stay with the company. These have been big losers, so Bell decided to throw it in with the rest of the deadweight in the monopoly. It is frightening to think of the horror stories we might be hearing from the local operating companies in the next couple of years as they soberly tell us how they will go out of business without a doubling or tripling of rates.

The monopoly has a guaranteed profit, however, so the operating companies need only go to the willing public utility commissions to turn what should be a loser into a steady profitmaker.

No clever marketing plan is required to find the needed extra revenues. Residential users will be captive customers of the monopoly and the profit will be taken out of the hide of the residential users including seniors and those on fixed incomes.

Mr. Chairman, the Bell juggernaut has steamrolled its way through countless State public utility commissions, through the Senate and now through the Justice Department's antitrust division. Let me tell you that I will work with you in every effort to give some badly needed subsidies to the operating companies so that this potential mass rape of the American consumers is averted.

Thank you very much, Mr. Chairman.

Mr. WIRTH. Thank you very much, Mr. Mottl. Mr. Tauke.

Mr. TAUKE. Thank you, Mr. Chairman.

Mr. Mottl is a some what difficult act to follow. At the time that the settlement between A.T. & T. and the Justice Department was announced, there seemed to be general expressions of approval circulating among the media from many officials in Government and officials in the various telecommunications companies.

It occurs to me that it is too early to shower accolades on the settlement because there are so many questions that remain. There are questions not just about the substance of the agreements that have been reached, but there are also questions about the procedures which will determine just what the substance of that agreement might be.

It occurs to me that it is always customary for people, whether viewing an agreement such as this, to attempt to determine who are the winners and who are the losers. While it is perhaps too early to also determine just who the winners and the losers are, it occurs to me as I have attempted to determine what the likely outcome is of this decree that potentially the big winners are A.T. & T., their competitors in certain aspects of the telecommunications system, and the major customers of telecommunication

services, the Fortune 500 companies if you will. It seems to me potentially the losers are the small users of telecommunications services, residential customers, the Bell operating companies and the other small telephone companies that provide services to the people of our Nation.

Although a lot of discussion has been centered upon the rate issue, it occurs to me that one of the things our subcommittee needs to view carefully is the viability of the Bell operating companies, because certainly the viability of those companies, as well as the impact of this decree on the small telephone companies of the Nation, is going to be very important in the long term as we view the impact on ratepayers.

I think that there is one other thing that needs to be mentioned. And that is that there is considerable question whether or not telecommunications policies of this nature should be set through legislation, or through court decree. It occurs to me that even if we believe that the court decree, if it is ultimately concluded, is beneficial, and it very well may be in many ways. Then it is still questionable whether or not that should be the avenue for determining telecommunications policy.

I am, therefore, pleased that the chairman of our subcommittee, Mr. Wirth, indicated today his desire to move forward with legislation, because I believe that legislation is needed not only to perhaps supplement, perhaps change some things in the decree, but also to provide some long-term basis for insuring stability in telecommunications policymaking by insuring that that policy is made through the legislative process primarily, not relying primarily on the court process to develop these policies.

Thank you very much, Mr. Chairman.

Mr. WIRTH. Thank you very much, Mr. Tauke.

Mr. Markey.

Mr. MARKEY. Thank you, Mr. Chairman.

I am glad that we have finally gotten this issue off the business page and on the front pages of the American media. It has taken 5 years and a Justice Department consent decree. But we finally have been able to get the public interested in these issues. At previous hearings before the Telecommunications Subcommittee, it was amply demonstrated our economy has changed markedly over the past 20 years. As we have heard in hearings, we are today enormously dependent on the ability of telecommunications and information products and services for our Nation's economic well being.

Perhaps no other region of the Nation better demonstrates this change and the area I represent in Boston and the Route 128 corridor which surrounds the city. The settlement of the A.T. & T. antitrust suit which was announced earlier this month will have a profound effect on the manner in which telecommunications and information products and services are offered in our country. Our subcommittee is meeting today in an attempt to determine the nature of this impact and to see what additional legislative steps need to be taken in this area.

Today's hearing is the first of several and I am hopeful that the subcommittee and the Judiciary Committee will see fit to make the

necessary alterations in H.R. 5158 in order to accomplish the following goals.

One, to keep local telephone rates low. The dire predictions of rates doubling or tripling in the next 2 or 3 years will pose an unmanageable burden on many of our Nation's elderly and poor. If these citizens are not to be seriously disadvantaged, home telephone rates must be kept affordable.

Two, make certain that large corporate users of telecommunications, products, and services can obtain what they need at reasonable prices.

Three, make certain that fields in which the new restructured A.T. & T. competes do not become less competitive as a result of the entry of this telephone giant. I am speaking in particular of the fields of computer manufacturing and data processing which are of great importance to the area that I represent, and many other areas in the country. I am concerned that while we may have divested the gorilla of 200 or even 300 pounds, it may still be in a position to sit wherever it wants. There are other issues as well. Issues such as employee protection, foreign trade, the new regulatory framework necessary to cope with this new industry structure.

I commend the gentlemen from Colorado and New Jersey for giving the settlement the action it deserves, and I look forward to their continuing efforts to bring this issue to the forefront so we will be able to protect the ratepayers and the competitors during the transition period before us.

Thank you, Mr. Chairman.

Mr. WIRTH. Thank you very much, Mr. Markey.

Mr. Seiberling.

Mr. SEIBERLING. Thank you, Mr. Chairman. I have little to add to Chairman Rodino's opening statement.

Of course, there are very many facets to this transaction. We must be concerned about the employees as well as the stockholders of the Bell System.

We must be concerned about the continued competitiveness of our economic system and the crucial role communications perform.

Above all, we must be concerned about the American consumer. I think that in the interest of getting on with these concerns, I will not add any other statement of my own at this time.

Thank you.

Mr. WIRTH. Mr. Scheuer.

Mr. SCHEUER. Thank you, Mr. Chairman.

I congratulate you and Chairman Rodino for organizing these hearings. It is perfectly obvious that the consent decree has the potential to dramatically change American communications law and the economic environment in which our telecommunications industry is going to function.

It raises a whole host of public policy issues that the Congress and the administration are going to have to face.

We are going to have to do a real juggling act, because many interests are concerned. We all are deeply concerned about the interest of the consumer.

We want reliable, swift, and inexpensive telephone service for the American public. We also want to maintain the integrity and

excellence of our telephone system which now is the best in the world.

Many Members of Congress have traveled to developing countries, and we have seen what telecommunications can be like in other countries that are not as advanced as we are.

I don't think any of us want to take the risk that our system is going to deteriorate. I also think that we are very concerned that America maintains its technological leadership and remains on the cutting edge of new technologies and new markets, and that our major telecommunications corporations are comparatively unfettered and unshackled so that they can compete in global telecommunications markets.

Now, they are not competing against a bunch of mom and pop stores. They are competing with Nippon Tel & Tel, with Hitachi, with Sony, with Panasonic, all from Japan.

Many of them enjoy significant assists from the Japanese Government, from MITI, the Ministry of Industry and Trade.

Ericson of Sweden. Semens of West Germany. Northern Telecom of Canada. Phillips of Holland. All are enormous telecommunications conglomerates that are competing actively in global competition in selling systems and technologies.

I think we all want to make sure that our American corporations stay at the forefront. It is not written in the heavens that they will.

We have seen foreign companies, in Sweden especially, Germany especially, Japan especially, outcompete us every which way in steel, automobiles, pharmaceuticals, and beginning to compete with us in computers.

I think we have to make sure that our economic environment enables Americans to keep our technological lead. A number of other public policy questions are raised.

Should we allow the 22 local Ma Bells or State Ma Bells to compete, not only in the providing of telephone lines, but also in the provision of services?

Shouldn't they be able to get into the business of cable television, Yellow Page distribution, computer services? Should A.T. & T., since they no longer control local lines, also be able to compete in the provision of those services? Is some form necessary to keep the increase in local rates to an acceptable level, since increases seem to be in the cards?

If so, what is the most rational form those subsidies should take? What should we do to make sure that the State utility commissions are capable of effectively and expeditiously adjusting to the dramatic change that has been produced by the consent agreement, and, at the same time, protecting the interests of local consumers as well as protecting the integrity of our telecommunications system?

Is there a real danger that the local regulatory commissions will be under such pressure to keep rates low that they will skimp on telephone rates, they will keep down the rates so that the local phone companies will not have the cash flow to purchase new equipment and even to maintain the equipment that they have? That is a trade off that we, both in the executive branch and the Congress, are going to watch very carefully.

Will there be a significant variance in the quality of services from State to State, with grave implications for the integrity of our national telecommunications network?

Should Congress or the FCC, all working together, attempt to set uniform national standards to guide State regulatory agencies so that we can be assured that the integrity of the system will be maintained?

Mr. Chairman, I applaud you for your leadership in arranging these hearings. There are just a host of other policy issues that are going to have to be faced up to.

We still don't know the dimensions and implications of the consent decree, but we certainly have our work cut out for us for 1982 and I look forward to working under your outstanding leadership.

Mr. WIRTH. Are there other members of either subcommittee who have statements they would like to make at this point?

[The following statements were received for the record:]

STATEMENT OF CARDISS COLLINS, A REPRESENTATIVE IN CONGRESS FROM THE STATE OF ILLINOIS

Good morning. I would like to thank Chairman Wirth and Chairman Rodino for scheduling this joint hearing so that we might hear first hand from A.T. & T. about the consent agreement and learn how this will impact the ever changing telecommunications arena.

Accordingly, I would like to welcome Charles Brown and Howard Trienens.

As my colleagues and the public are aware, much has appeared on television, in the newspapers, on the radio since the signing of the consent agreement reached by the Justice Department and A.T. & T. With the combined employment of A.T. & T., Illinois Bell, Western Electric and Bell Labs being close to 65,000 people, I am quite concerned about jobs and equally concerned over whether local telephone rates will go up after restructuring? Assuming that rates will go up, and I expect that they will, how much can we expect local telephone rates to increase? I am also interested in what is needed to save and restore jobs in American industry and on the future of residential telephone service in this country.

It is my belief that a sound, competitive telecommunications industry will help American industries improve their competitive position in the world marketplace. However, in opening the communications market to competition, we want to be sure that residential telephone rates will remain affordable to virtually everyone. We want to be sure that everyone who needs and wants a phone can afford one.

The hearings scheduled this week and the ones to follow will be needed so that we can obtain a full understanding of the details of the modified consent decree and restructure or structure appropriate legislation to deal with those areas not fully defined in the agreement.

STATEMENT OF MARC L. MARKS, A REPRESENTATIVE IN CONGRESS FROM THE STATE OF PENNSYLVANIA

I regret that because of treatment for a back ailment, I am unable to personally attend this hearing. However, I want it made known that I shall closely examine what occurs this morning, as we examine the long litigated A.T. & T. antitrust case and the current proposed settlement. There is no doubt but that we need these two hearing days and perhaps subsequent days as well to ask hard questions until complete and satisfactory answers are received. We must seek those answers, on behalf of the American people, so that it can be made known what is the immediate effect of this proposed settlement. As important, we must determine what is to occur in the future as a result of this proposed settlement. It is through this procedue that we in Congress can gain the information necessary to adopt legislation which ensures that the ratepayer is not the one to bear the cost for this proposal and that a competitive arena is created for the provision of telecommunication services.

One need only look at the trial record to know this proposed settlement calls out for public scutiny. Frankly, this settlement troubles me as to the possible "hidden" impact it may have on this nation. I find it indeed unfortunate that this proposal raises far more questions than it answers: Questions about the future of telecommu-

nication and the cost it exacts from ratepayers who have supported the activities of A.T. & T. over the decades.

More disappointing still is that to date, in spite of countless questions addressed to the parties to this proposal, the responses have often time appeared evasive and in large part designed to enhance the position of the parties before the public. That should not be allowed to happen in this forum and I trust we will elicit for the record, for all to read and understand, straight forward and direct responses to straight forward and direct questions.

Before today's testimony concludes, I desire answers to a number of questions:

1. Will this agreement in any way impinge on our national goal of making available, to all people of the U.S., efficient telephone service at affordable rates?

2. How does this proposal answer the A.T. & T. trial posture that divestiture would impair our phone network and endanger national defense?

3. What are the prospects that in another twenty years we will have the Bell operating companies before the Congress seeking relief from the terms of this proposal?

These and many more questions require answers. However, the one question more than any other which requires an answer is this:

Does it necessarily follow that what is in the best interest of the American Telephone Company, A.T. & T., is likewise in the best interest of this Nation?

Thank you Mr. Chairman.

Mr. WIRTH. Mr. Brown, Mr. Trienens, if you could join us at the witness table. We are pleased to have with us this morning Mr. Charles Brown, chairman of the American Telephone & Telegraph Co., who is very familiar to the subcommittee and has worked closely with us.

We greatly appreciate your being with us today. Mr. Brown is accompanied by Mr. Howard J. Trienens, vice president and general counsel, who is also no stranger to room 2123. Mr. Trienens, thank you for being here.

Mr. Brown, if you would proceed in whatever way you feel is appropriate, we will then follow, under the 5-minute rule, on the order by which people have appeared this morning.

STATEMENT OF CHARLES L. BROWN, CHAIRMAN, AMERICAN TELEPHONE & TELEGRAPH CO., ACCOMPANIED BY HOWARD J. TRIENENS, VICE PRESIDENT AND GENERAL COUNSEL

Mr. BROWN. Thank you, Chairman Wirth, Chairman Rodino, and members of the committee. Both of us appreciate the opportunity to appear before you to talk about this proposed Department of Justice modification and to answer your questions as to really why we accepted this decree in the first place.

We really believe that the action we have taken is a giant stride toward communication policies which, in no smaller measure, I believe, have emerged from the work of this committee.

We believe that this action greatly eases the task of Congress in its desire to supplant outdated communications law with new legislation.

First, let me summarize what this agreement proposed by the Justice Department and signed by us means.

First, A.T. & T. will divest the local parts of 22 operating telephone companies 18 months after approval by the court. The divested companies are to have sufficient people, facilities, technical information, and financial resources to do the job.

A.T. & T. and Bell Labs are to provide R. & D. and manufacturing services as required to implement this decree. A.T. & T.'s li-

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cense contract and supply contracts with these companies are to be terminated.

Divestiture can take any form, that is, spinoff, sale, or any combination. Nothing in this decree changes employee benefits, pensions, or existing union contracts.

The decree specifies that there is no admission of violation of any antitrust laws. A.T. & T. retains the long-distance network, the Bell Labs, and integrated Western Electric Co., and the terminal equipment. The 1956 consent decree limitations on the Bell System are largely removed.

Why did we agree to this Draconian decree? We believe the signals are clear with respect to emerging national policy and structure of the telecommunications industry. And we are confident that this action is consistent with the intent of Congress.

We believe the provisions of the consent decree modification clear the way to promptly accomplish some very specific objectives.

First, to encourage further competition where competition is desirable, without in the least diminishing the authority of regulatory agencies to insure good phone service at prices everyone can afford.

Second, to eliminate the potential for cross subsidy as among existing Bell Cos., thereby clearing away those cumbersome, and anticompetitive prohibitions which might otherwise be applied.

Third, to preserve the resources as well as the mechanisms which insure that our country's communications system can operate effectively and respond to the requirements of national security.

Fourth, to put in place now an industry structure which may help pave the way toward some deregulation in the future.

Fifth, to provide equal access to the local plant on the part of any and all intercity competitors who desire to use them.

At the same time, to insure that all who wish to use that plant, complete intercity calls, contribute equally to the revenues of the local operating companies.

And last, to retain the research, development, and manufacturing resources which currently give America its world leadership in communications technology.

It is my real opinion that when all is said and done, this is really the surest means to protect the jobs of American workers.

Let me sum it up this way. Divestiture is not our idea. Frankly, it goes down very hard. But what matters in the end is not whether we like it or not, what matters is how and how soon the Bell Cos. undertake to conform themselves to the requirements of what is clearly national policy.

In view of the options available to us, the consent-decree modification we have accepted accomplishes that.

Last, I would like to talk for a moment about this rate matter which has received a lot of attention, a good portion of it erroneous. It has been said erroneously that this decree will have a major effect on increasing local rates. This is not, this is not the case. The regulators maintain the power to control the subsidy of long-distance rates locally.

Although the Yellow Pages subsidy will be affected by this decree, this is also true under most legislative proposals. The only

thing affected is the timing, and we have promised to cure the problems there.

Entirely apart from this decree and as we have been saying for many years, rates will go up for other reasons. Rates have been rising at about 4 percent a year on the average, well below any inflation figures we all have seen in many, many years.

They will go up at about 8 to 10 percent for a few years. The causes are not this consent decree. The causes are inflation, offset to a high degree by Bell System productivity.

Second, changes over the years in the way regulators calculate the subsidy for local rates.

Third, accounting changes to put the cost of installation, and moves and changes in telephone service on the customers who ask for them, rather than on the customer body as a whole.

And fourth, depreciation. Competition and technology changes act to shorten equipment lives. This increases depreciation expense.

What all this comes down to to the average customers is a relatively small increase in local rates, having little or nothing to do with this consent decree.

The average monthly rate now for local service is about $10 a month across the country. Due to the factors I have just outlined, we would expect that to increase each year for the next few years by less than $1 a year.

Telephone rates are a bargain now. They will remain so in the future.

Mr. Chairman, I will be glad to answer any questions which may occur to you, Mr. Rodino, or the members.

[Testimony resumes on p. 26.]

[Mr. Brown's prepared statement follows:]

STATEMENT OF CHARLES L. BROWN ON BEHALF OF AMERICAN TELEPHONE & TELEGRAPH CO.

My name is Charles L. Brown. I am Chairman of the Board of the American Telephone and Telegraph Company. I am joined by Howard J. Trienens, Vice President and General Counsel.

We welcome the opportunity to appear before this joint Subcommittee meeting to discuss the agreement reached between the U.S. Department of Justice and AT&T which modifies the 1956 Consent Decree. Since your letter inviting me to testify sought our views on the impact of the decree on the cost and quality of telephone service and its effect on the development of a competitive marketplace for telecommunications products and services, my statement will address those points as well.

THE 1982 CONSENT DECREE

Description of the Decree -- For reasons I will discuss in a moment, the 1982 Consent Decree is the modification of a 1956 Decree. Under the terms of the modified decree, AT&T would divest the local operations of 22 Bell Operating Companies (BOCs) -- the facilities by which customers complete local calls and gain access to long distance and international networks. Such facilities represent approximately two-thirds of the Bell System's total plant, or over $80 billion in assets. The resulting Local Exchange Companies (LECs) are required to provide

access to their local services to all interexchange carriers -- AT&T included -- as well as to information service providers.

All Bell System interstate long distance facilities and a portion of the intrastate long distance facilities now owned by the BOCs, will remain with AT&T. Ownership of customer premises equipment also will be retained by AT&T, along with the Western Electric manufacturing subsidiary and Bell Laboratories.

The LECs are not permitted to establish or maintain a manufacturing affiliate under the terms of the modified decree.

Of the Bell System's approximately one million employees, about half will work for the new LECs upon divestiture while the other half will work for AT&T and the units affiliated with it.

According to the modified decree, the divestiture will take place within 18 months. A plan for reorganizing the Bell System to accommodate this divestiture must be filed with the Department of Justice within six months of the effective date of the modified decree.

Modified Decree Filing Procedures -- Removing the restrictions of the 1956 Decree is the cornerstone of the

agreement with the Department of Justice to divest local exchange properties and operations. Therefore, the 1956 Decree was modified to reflect the new agreement and the 1974 suit was dismissed.

At the same time the Department of Justice and AT&T filed a Stipulation for Voluntary Dismissal in the D.C. Court suit, we asked Judge Biunno in New Jersey to transfer the 1949 suit to the D.C. District Court so all proceedings pursuant to the 1956 Decree would be under its jurisdiction. Our purpose was to consolidate all consent decree matters in one convenient court here in Washington.

From the very start we have anticipated hearings permitting public comment and judicial review of the Decree. Under Judge Greene's order of January 21, these hearings will be held expeditiously. We want to get on with the business of restructuring the Bell System. We have a mammoth job to do to implement the decree. One million Bell System employees, three million shareholders, our bondholders, and millions of customers anxiously await resolution of this matter.

Effect of Removing the 1956 Decree -- Lifting the 1956 Consent Decree removes restrictions imposed by that Decree on AT&T. This action along with preserving Bell Laboratories and Western Electric as integral parts of AT&T

-- technologically integrated with the Bell System part of the nationwide network -- promises to be a key element in maintaining America's world leadership in the Information Age and in the technology on which that leadership is based.

Reasons For Negotiating A Decree -- Over the last several years there has been a continued blurring of the distinctions between communications and data processing technologies. The nationwide public switched network is in fact the world's largest special purpose computer with that special purpose being communications.

Clear signals have been emerging from the deliberations of Congress, actions of the FCC, and actions of the courts that the public interest is best served by a competitive marketplace -- a marketplace in which technology and entrepreneurial ingenuity can be exercised to their fullest to bring products and services of the Information Age to all Americans with regulation limited to basic telecommunications service.

The modified decree preserves the free flow of technology from the Bell Laboratories. It enables us to provide to the public Information Age products and services far sooner than if we had elected to seek resolution of the uncertainty surrounding the future role of the Bell System in other forums. The modified decree should simplify the

deliberations of the Congress as it seeks to update the outdated Communications Act of 1934. The issues of Bell System size and structure are no longer a stumbling block.

IMPACT OF THE MODIFIED DECREE ON THE COST OF SERVICE

At the outset let me state unequivocably, the upward pressure on telephone rates we all are hearing so much about is a result of today's competitive environment and inflation, not the modified consent decree.

The Bell System has a long, successful history of holding down the cost of services to the nation's telecommunications users. In a 1927 speech to the NARUC, then President of AT&T, Walter Gifford, spoke about the Bell System's obligation "to furnish the best possible telephone service at the lowest cost consistent with financial safety". The foremost principle underlying the Communications Act is that basic telecommunications services should be available to all people of the United States at reasonable rates.

In 1981 the average manufacturing worker in the U.S. had to work only about 22% as long as in 1940 to earn the basic monthly charge for residential service. This is a record envied by nations around the world.

Over the last decade, however, we have been experiencing an economic fact of life. Barring some form of subsidy, growth of competition in the telecommunications industry will have one inevitable outcome -- rates for services will be driven toward costs. In a competitive environment the firm which is forced to price its services above its costs will soon find it is unable to compete. The firm which prices below costs will not remain in business long.

In his appearance before the Subcommittee on Communications of the Committee on Interstate and Foreign Commerce on September 28, 1976, my predecessor as Chairman, John D. deButts pointed out this economic reality -- "...competition can have no other consequence than to force the rates for each of our services to a closer and closer match with the cost of providing that service".

In November 1979, NTIA under the direction of Henry Geller addressed the movement of rates to costs in a competitive environment with particular emphasis on the need to reevaluate the cost allocations referred to within the industry as "separations and settlements". In its "Primer" NTIA stated:

> As competition has been introduced into the provision of interexchange services, there is increasing pressure to

reevaluate these allocations. This is so because it will be necessary to price traditional long distance service more closely to the cost of providing that service in order to compete with other carriers offering alternative services.

Rates also will reflect the more rapid capital recovery necessary as competing firms employ technology seeking to use the latest advances to meet user expectations.

Also contributing to the upward pressure on rates were the cost allocations from intrastate to interstate which had been used as a means of subsidizing local service rates. Over the years regulators assigned an increasing proportion of local exchange plant to the interstate jurisdiction.

The new decree contemplates that tariffs will be filed which could be the means of support for the local exchange companies. The FCC currently has an access charge plan under review which is consistent with the decree requirements and would provide such support for local exchange rates. As you pointed out in your press conference of January 13, Mr. Chairman, care must be exercised to avoid creating incentives for large users to by-pass local exchange facilities. Burdensome access charges would provide such an incentive.

IMPACT OF THE MODIFIED DECREE ON THE QUALITY OF SERVICE

The Bell System has a long standing commitment to service which we must continue to honor to be successful in today's competitive environment. The companies which will be divested must be strong if they are to meet this commitment in the future.

Accordingly, the decree requires AT&T to assure that upon divestiture the LECs have sufficient personnel, facilities and rights to technical information to permit them to perform their functions. For a five-year transition period, AT&T, Western Electric and Bell Laboratories will provide on a priority basis the manufacturing, research and development services needed by the LECs to implement the Decree.

With established customer acceptance, an excellent management team, a strong balance sheet, strong revenue streams -- measured local service and access charges -- full freedom to apply technology, and the continued oversight of state regulatory bodies, the commitment to the best possible service at the lowest possible cost should continue undiminished in these new companies.

While on the subject of service, I should point out that the modified decree preserves the unified management of the nationwide public long distance network

and, by mandating a central point of coordination in the LECs takes explicit account of national defense and emergency preparedness requirements as charged by the Communications Act of 1934. As operational details of the divestiture are developed in greater detail, these national concerns will continue to be addressed. We, of course, will cooperate fully with the Department of Defense and all other agencies of the Federal Government which have responsibilities in these areas.

IMPACT OF THE MODIFIED DECREE ON THE DEVELOPMENT OF A COMPETITIVE MARKETPLACE

The modified decree is a positive contribution toward the growth of competition. The establishment of LECs barred from providing interexchange or information service eliminates any incentive or potential to use local exchange facilities as a bottleneck. Quite to the contrary, the incentive of the LECs will be to connect any and all users to local exchange facilities thereby enhancing their local access revenue stream -- a revenue stream which will be important to their financial viability.

The modified decree removes any incentive for a LEC to prefer any supplier/manufacturer due to corporate affiliation. This provides a far better solution to the question of opening BOC procurement quotas or contrived

"market tests" as provided in recent legislative proposals. Clearly, the Department of Justice agrees that the divestiture eliminates any procurement problems. The LECs will be able to buy the best products at the least cost with full assurance that arbitrary quotas will not contribute to higher costs in the provision of services to the nation's telecommunications users.

Recent FCC decisions which have been designed to reduce barriers to entry into the telecommunications industry are not affected by the modified decree. The recent decision to permit resale and sharing of Bell System private line, MTS and WATS services, of course, allows entrepreneurs entry into the business with a minimum capital investment. Similarly, the recent order requiring AT&T to unbundle its private line rates allows any potential customer or competitor to choose those pieces of private line rate offerings they wish and resell them as part of their own service package in competition with AT&T.

The concept of AT&T as a dominant carrier will not valid in the years ahead.

Under the terms of the modified decree the intercity enterprise has no corporate affiliation with the supplier of local exchange services. Thus, this potential for anticompetitive cross-subsidy is eliminated. The

extensive competition and ease of entry in long distance business removes any problem of cross-subsidy there.

As Assistant Attorney General Baxter said at the January 8, 1982 press conference announcing the modified decree,

> One can have a very, very large market share without having a significant degree of market power.

Barriers to entry into the market are low. Competition is flourishing in the long distance market.

- Between 1977 and 1981 cities served grew 15-fold -- 18 to 296.
- Nearly 90% of those living in the urbanized SMSAs -- the prime market -- have access to competitive alternatives.
- In 85 areas customers have a choice of AT&T and three other carriers.
- In 126 areas customers have a choice of AT&T and two other carriers.
- Growth rates of these competitors of 40% per year are common.

- 177 Reseller Applications are before the FCC.
- By 1986, AT&T's share of the deployed domestic satellite capacity will be only 15%.

Western Electric is not a dominant supplier of long distance technology -- supplying less than 25% of the radio equipment and none of the satellite equipment in the U.S. in 1980.

By these standards, I believe the time has come that AT&T should not be inhibited in ways any different from other organizations in the telecommunications and information related businesses.

* * *

The modified decree, I believe, is in the public interest. It removes many of the anticompetitive restrictions applied to the Bell System that were the result of an era of pervasive public utility regulation in a monopoly marketplace. Moreover, it provides the Congress with a far easier task as it strives to complete the job of revising the outdated statement of national policy -- the Communications Act of 1934.

Mr. WIRTH. Thank you very much, Mr. Brown. I would like to pick up immediately on the summary of your testimony which focused on the subject of increases in local telephone rates. This subject has, as you pointed out, received an enormous amount of attention.

I think everybody here, as you stated the other night on the air and elsewhere, is firmly committed to the universal principles of service and rates. We all share that goal and appreciate the history of the telephone company in providing what is clearly the best telephone service in the world, available to all Americans.

Mr. BROWN. Yes, sir.

Mr. WIRTH. In your statement this morning on page 5, you say: "Upward pressure on telephone rates is a result of today's competitive environment and inflation, not the modified consent decree."

What I wanted to clear up was how this squares with the statements made by a number of your colleagues in A.T. & T. from around the country.

For example, Mr. Staley, the president of New York Telephone, has said, "After divestiture, we will receive no subsidy. Local rates will have to double in the next five years to bear their share of the costs."

Mr. Grossman, A.T. & T. spokesman in New York, said: "The long-distance subsidy will be gone and obviously the local companies will be under a lot of pressure to raise rates."

Mr. William McDonald, president of Ohio Bell, said, "The days of telephone service as we have known them are all gone. Home telephone users will find their monthly bills at least doubled."

Mr. Robert Sellick, vice president of Mountain Bell, said, "Increases in rates will come faster as a result of the settlement."

A lot of people have been very concerned by this cacaphony of statements that have been made all across the country by A. T. & T. Perhaps you could clarify for us why these statements seem to differ so markedly from the statement you made today and made yesterday in front of the Senate Commerce Committee.

Mr. BROWN. I don't know as I can clarify them completely, Mr. Chairman, but I would make two observations. First of all, local rates are under control of regulators in different parts of the country. Each State, as you well know, has its own commission and regulates local rates there. The rates, therefore, differ among jurisdictions.

The rate I quoted to you and increases I quoted to you represent an average. So in some places, the rates will be higher, the increases will be higher, due to these factors I spoke about, than in other places where they may well be lower.

Second, I don't know the full context under which these remarks were made. If they were made without the caveat of it having nothing to do with the consent decree, then they were incorrect.

Mr. WIRTH. I think that we would all agree that, even had there been no settlement, there are other issues related to local rates that were there before the consent decree and remain.

I think there are four central ones. One, the access charge issue which we have all discussed. I believe that A.T. & T. agreed on this principle when we drafted H.R. 6121 as a way of assuring equal

competition in the long-distance market and equal payment for the same rates, terms and conditions of interconnection.

Mr. BROWN. Yes, sir; that mechanism, as you know, still remains.

Mr. WIRTH. Second is the installation of telephones and other terminal equipment. How that is treated is a second issue that has billion-dollar implications for the ratepayer.

The third element is Yellow Pages.

Fourth is the valuation of assets that are transferred out of the Bell operating companies. Part of this last item is to assure the full payback of Bell operating company customers for their contribution via the license contract for research and development.

It seems to me that we ought to be guided by these principles. In my opinion, and that of many of my colleagues, they must be included in legislation.

Legislation should specify the elements of an access charge and how that system will work, so we don't get a fragmented system of 50 different tariffs around the country. That would be very counterproductive, certainly counter to our notion of a national telecommunications system.

Do you have any comment on these components of the subsidy issue?

Mr. BROWN. Yes, sir; as far as the access charge mechanism is concerned, the mechanism for the access charge remains in the control of the regulator. As a matter of fact, the Federal Communications Commission has a docket involving access charges which brings issues of which you speak. Nothing about this decree changes the power of the regulators to apply an access charge precisely in accordance with existing subsidy if they so choose.

Second, the terminal matter, I have to say it was not our idea that the local telephone companies could not sell or lease telephones. This is an idea originated by someone else. Clearly the terminals will be out from the jurisdiction of the telephone company under regulatory decree, if nothing else.

Third, I did deal with the Yellow Page matter. That subsidy was in all legislative proposals I know about, intended to be phased out anyway. And we can make arrangements to be in accord with most legislative proposals on that score.

As far as valuation is concerned, I am a little bit puzzled about how this becomes a question. If you take the case of the New Jersey Bell Telephone Co., the American Co. owns the stock of the Bell Telephone Co. in New Jersey and, therefore, owns it. We are directed by this decree to spinoff or dispose of the local parts of it, local switching parts of it. What is left we still own. I do not understand what the valuation problem is.

Insofar as the customers' contribution is concerned, I guess from my standpoint, what the customers have paid for is good telephone service, and they have gotten this at a bargain rate over the years. The stockholders are the ones that own the Bell Laboratories.

Mr. WIRTH. In adherence to the 5-minute rule, we will come back around as well. Mr. Rodino.

Mr. RODINO. Thank you very much, Mr. Chairman, Mr. Brown and Mr. Trienens. In my opening statement I alluded to the fact that I was troubled by the question whether or not you feel bound

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by the provisions of the Tunney Act, whether or not you intend to comply.

I understand that you do intend to comply with the provisions, but you do not feel bound. Am I correct in that statement?

Mr. BROWN. This is somewhat of a lawyer question, Mr. Chairman. I would like Mr. Trienens to pick that up if we will.

Mr. TRIENENS. Yes, sir; on the question of whether we are bound by the Tunney Act, our position is that because we cannot stand the uncertainty, the fact that if this decree were approved by a Federal judge without going through the Tunney Act procedures, and I mean every comma of them, we could not afford the uncertainty that someone would then appeal and say the Tunney Act applies or does not apply. We insist the Tunney Act procedures be followed because we cannot stand the uncertainty of this, which we expect would be subject to further litigation over that question.

It is the Justice Department who is worried about 1,600 other old decrees that have raised this question of whether the Tunney Act in fact as a matter of law applies. You will have to ask Mr. Baxter about his concerns about other decrees because as to this decree he agreed with us, that the Tunney Act should apply by every comma.

Now there were about 10 days of confusion here. The papers made it up as a lot of confusion. But it was the purpose of the parties as shown by documents filed on January 8 that the Tunney Act apply in full and be administered here in Washington by Judge Green. It took 10 days to get that all accomplished.

Why was it complicated? The reason is there were two courts and two decrees involved. This is not a settlement of a 1974 case. This is an instance where the 1956 decree which was in New Jersey, the 1974 case is being tried here in Washington, a question of law as to why that should have been which was never, resolved on the appellate level. Never got to that.

The point is that the principal economic consequence of this overall settlement of our controversies with Justice was to be relieved from the old increasingly binding restrictions of that 1956 decree. So we had to go to New Jersey. We had to get that decree modified.

Now the question is, the case in New Jersey, the case here, desire to have the Tunney Act apply, and the desire to have it apply here. It took 10 days of motions to transfer, appeal in the third circuit. The remarkable thing was not that it was confusing but that it was all done in 10 days. The problem is over, the full Tunney Act procedures have been ordered and we are on our way.

Mr. RODINO. Mr. Trienens, granted. It bothers me, though, to think that we must get into such semantics here, talking about not being bound, yet, willing to comply. I am most concerned with the good faith of the parties, especially when you are involved in the question of a consent decree involving a matter of such complexity and magnitude.

While I do not want to pursue this—and I am going to pursue it with Mr. Baxter—it does bother me a little bit because I would hope that parties that enter into consent decrees do so in good faith without seeking an advantage one way or the other, saying the law might be this way but we can circumvent it by going through some contortion.

But, nonetheless, saying we are going to comply. Again, I do not want to pursue that.

Mr. TRIENENS. I just want to say there was never, from the outset, from the first papers that were filed 10:30 Friday morning, January 8, any question of evasion of the Tunney Act, any question of lack of good faith. It was all open on the court record that we desired to follow the Tunney Act and desire to follow it here in Washington. That was apparent from the beginning.

The problem of the technical applicability is one the Justice Department has. It is a problem I want no part of. And you will have to ask Mr. Baxter that.

Mr. RODINO. Whose idea was it to dismiss the 1974 case?

Mr. TRIENENS. Well, it was a natural, inevitable consequence of the fact we had to change the 1956 decree and, therefore, since you could not have two decrees in two places and you could not have a case going on when there was no controversy about it, it was the obvious and necessary consequence of modifying the 1956 decree.

Mr. RODINO. Did this emanate though from A.T. & T.? Where did it come from, the idea itself seeking dismissal?

Mr. TRIENENS. I cannot recall where it emanated in the sense that once it was decided that the 1956 decree, the restraints of that decree would be lifted and, therefore, we had to go and modify that decree, and since you could not have two decrees in two courts, two Tunney Act proceedings going on, the obvious thing since the 1956 decree had to be modified, the only way to get it in one case was to dismiss the other. It was just a natural consequence.

Mr. RODINO. Mr. Trienens, under the settlement provisions is a requirement for divestiture of the 22 operating companies. In the newspapers, the question was asked whether or not there were any plans—as to whether or not the spinoff would take place into one new firm, or whether you would spinoff 22 of them.

Do you have any plans? I know that the newspaper states that you will not spinoff the local operating companies into one new firm, but are you still evaluating the future structure?

Mr. TRIENENS. Let me repeat exactly what I said yesterday. The decree does not require a spinoff of 22 operating companies. What the decree requires is that A.T. & T., which owns these many assets around the country, divest itself of the local exchange and exchange-access operations, whether it is 22, 49, 1, or whatever.

What I said was that given the intensive planning and study now underway, which has not been decided as yet, the precise number and form of divested local exchange companies, that I did not expect it would be divested in the form of one local company. I do not expect that.

Mr. RODINO. My time is up.

Mr. WIRTH. Mr. McClory.

Mr. MCCLORY. Thank you, Mr. Chairman.

Pursuing the antitrust aspects of this litigation and this settlement, one of the provisions is to require the divestiture of 22 operating companies. Do you not think that it would be appropriate in this settlement to specify how this divestiture is to take place? There is speculation as to whether we are going to have one big holding company holding all of the 22 operating companies.

Would it not be far better to say that these 22 operating companies are to be individually owned and operated, and thus allay the fears people have about some second big monopolistic giant?

Mr. TRIENENS. Well, I have undertaken, Mr. McClory, as best I could, to allay the fear that somehow there is going to be one big company out there. That is not in the cards. And I so stated.

Now the reason you cannot dictate at this time precisely the mechanism by which this is spun off is that while it sounds convenient to say well, there are 22 companies, so let's just have 22 companies and spin it off. Two things. First, we are not spinning off the companies. We could do that today. We do not need a decree to order us to do that. We have the power to divest the stock. But the decree calls for separating out the exchange and exchange-access portions which are regarded by some as the monopoly, so-called, bottleneck. We do not think there has ever been an abuse of that bottleneck but it is a source of contention, and that is the problem we are putting behind us.

Just to illustrate one of the practical problems, we have got 1 of those 22 companies that is Diamond State. It serves Delaware. Can you imagine the financing of that company if you spun off that stock and said there you are Diamond State with 3 million stockholders. How do they go to the financial market with 3 million stockholders with a company that size? That is the kind of problem you consider with these companies when considering what form of organization these local exchange companies should take.

Mr. MCCLORY. There are two companies in which you do not own a majority of the shares. I think Cincinnati and——

Mr. TRIENENS. Southern New England Telephone Co.

Mr. MCCLORY. How are you going to carry out the import of this settlement if you are going to continue to own a substantial portion of these operating companies?

Mr. TRIENENS. The ownership is in the range of 20 percent and 30 percent respectively. They are not Bell operating companies within the meaning of the decree. They are not subject to this requirement of isolating out the local exchange portion. The American Co. would continue to own the stock as an investment. The license contract relationship is severed because they are defined as a subsidiary. The question of what to do with that investment, whether to retain it, is simply one that has not been addressed.

Mr. MCCLORY. If it were required, you would not have any problem with divesting?

Mr. TRIENENS. It is not provided in the decree and I am not willing to agree to it. That is a business judgment Mr. Brown and other people will make in light of what makes sense with that investment.

Mr. MCCLORY. You have indicated your desire to comply with the procedures of the Tunney Act. However, the Tunney Act authorizes the court to take testimony from witnesses, to appoint a special master, to authorize participation in the proceedings by interested persons and agencies. There is a whole range of participation by outside interests, and a competitive impact statement that must be developed and filed by the United States.

Are you planning to have those provisions of the Tunney Act complied with?

Mr. TRIENENS. The answer is "Yes, sir." The answer is further it is not a question of my plans or Justice Department plans. It is the subject of an order, an order of considerable detail that takes up each and every one of the provisions you mentioned, Mr. McClory. It was filed in the district court here on January 21 by Judge Greene. It orders each and every one of those procedures.

Mr. WIRTH. Thank you, Mr. McClory.

Mr. Mottl.

Mr. MOTTL. Thank you very much, Mr. Chairman. Golly, if I was fortunate enough to be a shareholder, Mr. Brown, of A.T. & T., I would be extremely pleased with the job you have done, especially on this settlement.

But, unfortunately I am not a shareholder. So I think my concern is about the senior citizens and the people on fixed incomes in our society. And my closest senior citizens, my parents, recently read Mr. MacDonald's statement, president of Ohio Bell, which Mr. Wirth alluded to, that the settlement could possibly increase the costs of having their local telephone, double it or triple it.

You seem to be giving reassurances to our senior citizens and those people on fixed incomes in our society that the regulators will take care of them. That they really have no concern over this settlement. Is that basically what you are saying, Mr. Brown?

Mr. BROWN. Mr. Mottl, you are talking to the same people who managed to provide telephone service of the quality and price that it is now, and have managed to keep these rate increases down at less than half the rate of inflation over the years.

We are the ones who have been interested in this for many years and have tried hard and have succeeded in doing this. What I am saying is that these are the same people that are going to be running Ohio Bell after divestiture, and the same people are here at A.T. & T.

Our motives are not changed. Further, the rates are under the full control, and they have been all along, of State regulators. And so it is not only a motive which we have had all along, but regulations which will protect them.

Mr. MOTTL. Besides your motives of keeping costs down, you are saying that we have nothing really to be concerned about because the regulators, the FCC, and Ohio Public Utility Commission, in my State, will do a good job for the consumer, is that what you are saying?

Mr. BROWN. I cannot predict anything. What I am saying is that regulation has done the job along with the Bell Telephone people in the past. I see no reason it should not continue. Nothing about this decree changes that.

Mr. MOTTL. Heaven help us all if we had to rely upon the Ohio Pubilc Utility Commission and FCC. The history of the Ohio Public Utility Commission has been one that has never looked out for the consumer the last 20 years that I can recollect in Ohio. The record of the FCC—the administrative law judge on your long distance case just recently decided this summer—the administrative law judge recommended a rate of return of 10.85. And the FCC, which is supposed to be looking out for the consumer, came back with a rate of return of 12.75. These are the people we are going to rely

upon to make sure that our rates for residential phone use are going to be kept low?

Mr. BROWN. Mr. Mottl, there is no free lunch. When the cost of money goes up, it is necessary for the company to borrow money and pay the rates. This is what the FCC and other commissions have taken account of. They have a requirement to keep from confiscating the companies, not only telephone companies but others which they regulate.

As costs go up, prices have to go up. It is just a question of how much and how often. As you look at regulation back over the years, it has not done a bad job.

Mr. MOTTL. But, see, you are taking all the cream here. A.T. & T. is going to keep all the profitable operations. You are transferring a blue chip stock into a glamour stock in the future that is going to have a great appreciation growth if the settlement is allowed to stand and if Congress does not act to protect the consumer by making sure that we are going to have the continued subsidy of the long distance revenues for the residential use, and also for the Yellow Pages making a contribution.

Mr. BROWN. Mr. Mottl, this was not our idea. This was not our scheme of how the Bell System ought to be organized. This was imposed upon us by the Justice Department.

Mr. MOTTL. So the Justice Department imposed this ripoff of the consumer?

Mr. BROWN. I do not think it is a ripoff of the consumer.

Mr. MOTTL. Well, it is a potential ripoff. If rates double or triple in the next few years for a residential user—how many people now in the United States have access to telephones in the home?

Mr. BROWN. I think probably there are 145 million or so telephones.

Mr. MOTTL. What percentage of American homes?

Mr. BROWN. Very high, 97, 98.

Mr. MOTTL. If rates double or triple would that not go down to 50 percent?

Mr. BROWN. No, sir.

Mr. MOTTL. It would still stay at 97 or 98 percent if it doubled or tripled?

Mr. BROWN. Mr. Mottl, you cannot even buy your wife a pizza for the cost of telephone service in many States. Telephone service is a bargain. I do not really think it is fair to talk about half the people not being able to have telephones because the rates are scheduled to go up in the levels that I talked about, entirely separate from this decree, having nothing to do with the decree.

Mr. MOTTL. Do you not think it would be in the interest of most American people that we in this subcommittee, Telecommunications Subcommittee, require long distance and Yellow Pages that are being left with A.T. & T., that they be forced to continue the subsidy to local operating companies to make sure those residential rates are kept low? Do you not think that would be in their interest?

Put yourself in our place, looking out for the majority of people in this country. Give us some advice and consent on what we should do with legislation.

Mr. BROWN. I do not flatter myself that I could give you advice and consent, Mr. Mottl. But let me point out that competition has been introduced in this country by fiat of regulatory bodies. That is way down the road, it is past, it is well over the dam.

What competition tends to do is drive prices toward costs. If local telephone companies over the years have an artificial, an irrational price structure, only one thing is going to happen. And that is the technology is going to go around them. Right now for example, you see rooftop television antennas, rooftop message antennas. The Washington Post over here has an antenna right on its building, bypassing the telephone companies completely.

In the long run under a competitive environment prices have to move toward costs or technology will move around it. Every time you skim things off the local plant's revenues by virtue of going around them, the only thing that will happen is prices will rise again.

Mr. MOTTL. One last short question, Mr. Brown. It was reported in the Wall Street Journal this morning that you gave some reassurances or assurances to Senator Packwood on Yellow Pages. Can you explain what those assurances were?

Mr. BROWN. Most of the legislation which has been proposed and that which was passed in the Senate provides for phasing out of the subsidy of Yellow Pages to local service. This is a direct consequence of the attempt to separate the monopoly oriented business from the competitive business. Most legislative proposals and most regulatory proposals state that you must separate these out.

Senator Packwood's bill proposed it in a period of 4 years. All I told Senator Packwood was that I have no desire to abruptly remove this subsidy from the local companies and we would see to it, it was not abruptly removed, but it would be phased out over the same period the Senate bill proposed.

Mr. WIRTH. Thank you, Mr. Mottl. I should point out Chairman Brown has been very careful to say most legislative proposals phase this out. The bill that you introduced in the House side has Yellow Pages moving into the going concern rate. If it does move to the parent, that insures the local ratepayer receives the benefit of the full value of the Yellow Pages.

There is a variation there between the bills. I want to point that out to my colleagues as we have been discussing Yellow Pages to make clear what the difference was.

Mr. Markey at this point wanted to pass I believe. Mr. Tauke.

Mr. TAUKE. Thank you, Mr. Chairman.

Mr. Brown, a number of observers have suggested that the Bell operating companies, you refer to them as the local service companies, will be in difficulty in the 1980's. Do you believe the restrictions on the service to be offered by the local telephone companies permits, those restrictions permit them to be viable financial entities in the future?

Mr. BROWN. Yes, sir, I do. In the first place, when we were talking about shareowners a moment ago, I think it needs to be pointed out that no management, no responsible management of any company would spin off two-thirds of its assets, those assets owned by the shareowners, and mal-treat those two-thirds. Our intention is to divest these companies with full balance sheet acceptability.

In other words, we will spin them off in good balance sheet condition. So there is no reason for them to be in any financial difficulty because of their balance sheets.

Second, these companies have a wide market. It is a big revenue stream. They are almost a monopoly in their business. They are selling a vital service which is required by their customers.

Third, they have good management, they have good public acceptance, and will thrive from that standpoint.

Fourth, they are growing companies. Telephone service is growing and increasing in its usefulness and its use. Also, you must realize that these companies are the gateway to the information age. It is their facilities which will bring incoming calls, not only voice calls but data calls and all sorts of information into their customers and out from their customers.

They will have this gateway. They will have the ability to increase their revenues from all the intercity purveyors. I think it is absolutely an incorrect statement to talk at all about Penn Centrals or any other failing apparatus and apply that to a telephone company.

One more point. These companies are modern. We have poured great amounts of money into the modernization of these plants since I have been in the business. This year it will be 15 or 20 percent of $19 billion applied to modernize these companies. So they are in good shape. They have a good opportunity, given decent regulatory treatment, to stay in good shape.

Mr. TAUKE. Perhaps you can tell me what is wrong with the analysis that is being offered that suggests that these companies will be restricted in the services that they can offer to what we might commonly call the plain old telephone service, and they will be unable to move into the area of offering new services to companies or businesses or others who might want additional services, and so they cannot in a sense expand their base of operations. Yet they are somewhat like sitting ducks because A.T. & T. or other companies could come in and chip away at their local base by picking out an entity like the U.S. Congress for example, erecting an antenna up here on the office buildings and bypassing the local company for certain services that would be offered.

Is there anything in the decree that makes that analysis faulty?

Mr. BROWN. I do not think it is a good analysis, and the thought that they will be restricted from offering new exchange services is just not so. For example, a service right on the edge of being offered by these companies, will be a spectacular service, that is, cellular radio, which——

Mr. TAUKE. May I interrupt there. Are you telling me that it is the local companies that would be offering the cellular radio services?

Mr. BROWN. I would expect so, yes.

Mr. TAUKE. That would not be a service offered by let's say A.T. & T.?

Mr. BROWN. This is an exchange service.

Mr. TAUKE. So exchange service includes something like cellular radio?

Mr. BROWN. Oh, yes.

Mr. TAUKE. Thank you. Go ahead.

Mr. BROWN. That is all right.

As information services expand, the gateway facilities can be used to facilitate it and make it attractive. I have to point out that under the current Bell System organization, this bypassing of which we have both spoken is just as possible. There is no way around the economics of technology being applied to a bypass thing. So it is here anyway. It will be here under any conditions.

Mr. TAUKE. There has been considerable question raised about how exchange areas will be established. As I understand it under the decree, the local service companies will be established in the exchange areas in accordance with some criteria that have been set up.

Mr. BROWN. Yes, sir.

Mr. TAUKE. Do you think it is reasonable to expect that these exchange areas will be in areas as wide as let's say an area code basis? In Iowa we have three area codes. Might we have three exchange services in Iowa?

Mr. BROWN. No, sir, I think the basis of these exchange areas is the so-called Standard Metropolitan Statistical Area as opposed to area codes.

Mr. TAUKE. That will be true under—is the Bell operating company or local service company required to use that standard under the decree?

Mr. BROWN. Yes, sir.

Mr. TAUKE. Pardon?

Mr. BROWN. I was going to say, this is also in legislative proposals and regulatory proposals. It is not anything different. It is not a new idea.

Mr. WIRTH. Mr. Mazzoli.

Mr. MAZZOLI. Thank you very much, Mr. Chairman. I do not serve on the Telecommunications Subcommittee so I have tried to study it as best I can. I will probably ask some questions that perhaps show my lack of specific knowledge.

But one thing that I have read as a rather significant potential problem—in addition to the cost to the consumer which we all have to be very wary of—is the fact that one of the things that distinguished A.T. & T. and the Bell companies over the years has been the excellence of its staffing, the excellent people you train and draw to your company. One of the reasons that occurred was because they had the opportunity of going to New York and taking part in some of the activities for periods of time, then going back home.

Do you see the consent decree that you have engaged in with the Justice Department as intruding upon that kind of background? Would it perhaps diminish the quality of your executives and then hurt the quality of the Bell operating companies?

Mr. BROWN. I think there is one thing which is in the decree which will tend to diminish that possibility. These companies have the permission in the decree, and undoubtedly will carry out a centralized staffing arrangement. The A.T. & T. now has what we call general departments in which we do common things, common engineering principles and common methods and procedures, so the wheel does not have to be invented 22 times around the country.

This has obvious advantages of cost savings reflected into customers' prices. We will, these companies will, take advantage of this and centralize those things which should be centralized in their judgment. This of course offers a movement, an opportunity for an executive to see other companies, other geography, other conditions. It enables also the executives of these companies to see people coming in from other companies and judge them and judge their quality.

Aside from that, I guess the other safety valve is headhunting.

Mr. MAZZOLI. So it is your judgment then that this decree would not hurt that——

Mr. BROWN. No, sir, I will not say it does not hurt it. I think it does inhibit us from the personnel policies we have used in the past insofar as training executives. I do not blink that judgment.

Mr. MAZZOLI. Thank you. I think all of us agree that the thing we do not want to do is to do anything or permit anything to happen which would diminish the quality of the phone service which has been enjoyed by all Americans. I recently returned from a part of America that does not enjoy adequate and affordable, probably, and reliable phone service. That is St. Thomas in the U.S. Virgin Islands. That is run by I believe an ITT subsidiary. That phone service is I think quite terrible as I think most would agree.

I was listening to a radio show while I was there. A computer effort, who called in, said that even though the voice transmission, despite a cackling in its static, was at least enough to get the word across, it does not handle computers. They need a much finer transmission capability.

St. Thomas and all the other U.S. Virgin Islands are desperately in need of economic advantage, and that means computers. What will keep my area from being put in a position of a rate disadvantage which keeps us from going forward and having state of the art and then becoming a wasteland?

What in the consent decree prevents that from happening?

Mr. BROWN. It does not and could occur in the country today in some parts. In some areas, modernization has not been able to proceed at rates it should. That is not true in Kentucky or most States, but the regulatory treatment of States will presumably be the same in the future as it has been in the past.

I do not really see the decree has any applicability to this problem.

Mr. MAZZOLI. You say, if I followed that, that it again is up to the local adjusters, the local rate commissioners and rate commission to make these final judgments as to how much money an operating company needs in order to make these advancements and stay current with the art.

But if that regulatory body does not go along, under today's situation, right now, today, would not A. T. & T. be able to somehow help, but if the decree goes through then they could not help? Is that correct?

Mr. BROWN. We can help them over a bump, a year or two of some problems. We do not get money from any other place. There is no way we can help all the companies in the country if the regulatory bodies do not do what they are supposed to do.

Mr. MAZZOLI. I guess what I am driving at—what really worries me about the whole thing—is that I worry about the cost to the consumer very much. I represent a typical city urban area. We have many of the people my friend, Mr. Mottl has talked about. I remember vividly talking to President Sadat in 1975, the only time I met him, about the problems in his country, which are legion.

The one thing he mentioned first was the inability to communicate within Cairo and around his country. I just hope we are not doing something here or engaging in any kind of activity which is going to leave America a helter-skelter crazy quilt of operating companies on different wavelengths, so that eventually an American could not call San Francisco, a Kentuckian could not call Maine. I just hope that something can be done so that does not happen.

Mr. BROWN. Yes, sir. I can assure you services are given by people, not by anything else. Bell System people have no incentive to do anything else than give good service. I have to point out once more as I have said before, this divestiture is not our idea.

Mr. MAZZOLI. Thank you. Thank you, Mr. Chairman.

Mr. WIRTH. Mr. Edwards.

Mr. EDWARDS. Thank you, Mr. Chairman.

Mr. Brown, the Tunney Act requires complete disclosure within 10 days of all communications, oral and written, with Government employees with the exception I believe of the Attorney General, Justice Department. Are you complying with that provision of the Tunney Act?

Mr. BROWN. Yes, sir.

Mr. EDWARDS. Has that compliance already been implemented?

Mr. BROWN. I believe it will be implemented February 5, is that correct?

Mr. TRIENENS. The schedule Judge Green set out, it is 15 days after the Government publishes its decree in the Federal Register.

Mr. EDWARDS. Will this disclosure include communications, negotiations with other departments of the U.S. Government?

Mr. TRIENENS. Yes, sir, complete compliance with the Tunney Act.

Mr. EDWARDS. Including the White House?

Mr. BROWN. Yes, sir.

Mr. TRIENENS. Yes, sir.

Mr. EDWARDS. Thank you.

Mr. RODINO. Mr. Scheuer.

Mr. SCHEUER. Mr. Chairman, I do have a number of questions of the kind I alluded to in my opening remarks. In the meantime I would like to yield back to the distinguished chairman of the Judiciary Committee for any questions he may have.

Mr. RODINO. Thank you very much for yielding.

I have a few questions I would like to ask. The questions relate to the consent decree of 1956, which required that A.T. & T. make technology available on a reasonable nondiscriminatory basis. Let me ask, Mr. Brown, whether or not, first of all, you agree with the statement made by Mr. Baxter yesterday. I understand the statement to have indicated that A.T. & T. would still be obliged to license patents exising at the time the settlement was reached.

I understand, however, that in the settlement, this provision would be eliminated. How do you interpret that?

Mr. BROWN. I interpret it, sir, to mean that we will be in the same position as anybody else with respect to our patents. In other words, if we invent something, we will be in the same position as any competitor. We can either keep it, or we can negotiate with others to lease the patent, or we can negotiate patent-interchange agreements as we do now.

Mr. RODINO. That is not consistent with the 1956 consent decree provision which required licensing of a technology, is it?

Mr. BROWN. Yes, sir, that is true. We were at that time a monopoly. That was the—one of the prices we paid for the 1956 decree. It is one of the chains we have been in which have been relieved by this consent decree.

Mr. RODINO. So you do not agree with Mr. Baxter's interpretation?

Mr. BROWN. Well, I may be getting myself confused here. Mr. Trienens was sitting in the room when Mr. Baxter testified. Perhaps he can help me out of my confusion.

Mr. RODINO. Let me put the question this way. What about existing patents dealing with network. Would you continue to license them?

Mr. BROWN. We surely will remain in the contracts and compliance with the contracts that we have made with respect to existing patents, yes, sir, we will.

Mr. RODINO. Does that mean you would license them?

Mr. BROWN. We already are licensing those patents. We would not, of course, have any ability or desire to discontinue such licenses.

Mr. RODINO. Then I get it that you still believe that you would be required to license existing technology?

Mr. BROWN. Those patents which are already under cross-licensing or fee licensing, we would continue to keep that arrangement.

Mr. RODINO. If the situation arose where a new applicant would ask for a license, would you license it to that new applicant?

Mr. BROWN. You are talking about post divestiture? Or currently?

Mr. RODINO. I'm sorry?

Mr. BROWN. We are still under the restrictions of the 1956 decree and we would do that now, sir, yes.

Mr. RODINO. Let me ask this final question and I will yield back to Mr. Scheuer. Under the settlement, A.T. & T. will retain ownership of telephones and other telephone equipment on the customer's premises. Since the customers have been paying rent on this equipment for a long period of time, it seems to me they ought to have some equity in it. Should they not be given the opportunity to purchase the equipment at a favorable rate?

Mr. BROWN. Well, Mr. Chairman, as I indicated before, it is our feeling that the customers have been paying for telephone service, including the maintenance of these telephones and replacement of them. They are the property of the telephone companies.

Mr. RODINO. They are the property of whom?

Mr. BROWN. Of the telephone companies. It seems to me it is just a matter of property.

Mr. RODINO. The question is, Why does this equipment not stay in the local company as its property?

Mr. BROWN. For some time regulatory rulings have made it clear that the provision of the instrument in the home is to be divorced from the local telephone company. Second, the decree provides that. Third, most regulatory proposals provide that.

So that is not a new idea nor is it ours.

Mr. RODINO. I yield.

Mr. SCHEUER. I would like to build on the questions I brought up and those of others. We are all concerned with keeping telephone rates at an affordable level. We are all interested in senior citizens and those aged on fixed incomes and all feel a desperate need to keep rates affordable. There is also a need to maintain the integrity of the national telephone system.

Mr. Mazzoli mentioned the case of the Virgin Islands. There are other States where there is less than adequate quality of service. Can you take us to the mountaintop and give us some advice as to the kinds of questions we ought to raise as to how we maintain excellence in our national system, how can we be sure that State regulatory agencies in their keen desire to protect consumers will not go beyond the point of economic rationality as far as the local systems are concerned so the local systems cannot purchase the newest and best equipment and cannot even maintain the equipment they have?

How do we maintain a competitive economic environment for the local system so that they can remain at the top of the telecommunications art in their own systems, and how can we maintain an economic environment so that American telecommunications companies, A.T. & T., the 22 Ma Bells, Western Electric, and the others, can compete effectively in the global telecommunciations market?

Mr. BROWN. Well, sir, it is my feeling that regulation has been in effect here for some 75 years. We now do have, as you and Mr. Mazzoli point out, the best telephone service in the world. It is a combination of the incentive of telephone people to do this, the ability to combine the genius of the Bell Telephone Laboratories and the Western Electric Manufacturing to furnish technology to these companies.

This is undiminished. As far as the ability or willingness and/or unwillingness of local regulators to, as perhaps you might say, face up to the fact that inflation eats at costs and moves prices up, we have had our problems in some regulatory jurisdictions over the years. But, all in all, over these 75 years these regulators have stepped up to the problem. I think as a generality from this mountaintop you have invited me to, there really is only one thing that regulators hate worse than raising local rates, and that is having poor service.

I do not really think that their responsibility is going to be abrogated because of this consent decree.

Mr. SCHEUER. You do not see any particular need to have national uniform standards to guide State regulatory agencies?

Mr. BROWN. Well, I believe there are legal standards which do so now. Courts have ruled on this. There are certain legal standards by which these regulators operate. The job of regulating local tele-

phone companies has been with the States. And I really do feel the States have the closest touch to the telephone situation in their own communities and perhaps detailed regulation of this ought to belong with the States.

But this is a matter that is probably beyond me to be opining on.

Mr. SCHEUER. I yield back the balance of my time.

Mr. WIRTH. Thank you, Mr. Scheuer.

Mr. Hyde.

Mr. HYDE. Thank you, Mr. Chairman.

Mr. Brown, can you give me a rough idea of the value of the subsidy to the local companies that will no longer be available to them in long distance and Yellow Pages. Percentagewise or dollarwise.

Mr. BROWN. The question is: What is the amount of the subsidy which will be removed?

Mr. HYDE. Right.

Mr. BROWN. The amount of the subsidy and whether or not it is removed is in full control of the regulators. They can subsitute by the access charge principle which is included in many proposed legislative bills. They can use that apparatus to replace the so-called division of revenues apparatus which is now employed for this purpose. If they so wish they can move the whole subsidy under the new arrangement and nothing need be changed.

Mr. HYDE. In other words, local service will still have available to it, should the regulators so decide, the subsidy it now enjoys from long-distance service?

Mr. BROWN. Yes, sir.

Mr. HYDE. What about the Yellow Pages?

Mr. BROWN. Well, as I have stated before, most legislative proposals do not want to mix a competitive business such as the Yellow Pages with a so-called monopoly business for fear of cross-subsidization, one to the other. This fear of cross-subsidization does not extend to cross-subsidizing the monopoly from the competitive, and people seem anxious to retain that.

However, the decree does provide that the Yellow Pages will not be a business in which the local telephone companies will be engaged. As I have mentioned yesterday, I will, we will assure that the subsidy, if you will, will not be abruptly removed because of this. We will phase it out in accordance with a 4-year scheme.

Mr. HYDE. What I am trying to understand is your statement earlier that there would be no real impact on local service costs as a result of this decree.

Mr. BROWN. Yes.

Mr. HYDE. And any increases would occur inevitably as a result of economic changes. Yet, there is a resource now available, namely from the Yellow Pages, whether it is phased out gradually or whether it is terminated abruptly, it will be a resource not available any longer at some point to local service.

I cannot understand why that would not negatively impact on rates.

Mr. BROWN. Yes it will, sir, to a degree. The reason I am fussy about the degree to which it will affect it is that the real source is the telephone listing. The name and the telephone number, which is the base, the real fundamental base from which the Yellow Pages and all other directory competitors operate.

The telephone companies have full control of this listing. They I am sure will be selling those listing to whoever wants to use them for their directories.

Mr. HYDE. They will develop their own Yellow Pages.

Mr. BROWN. No, but they will sell the listings to others which is a source of revenue which will tend to mitigate the change in Yellow Page ownership.

Mr. HYDE. Is there anything to prevent A.T. & T. from using its regulated monopoly long lines revenues to cross subsidize its unregulated activities, including equipment manufacturing and your interest in the data processing and computer markets?

Mr. BROWN. Yes, sir. The Federal Communications Commission has addressed that very thoroughly over a long period of time. They have set up rules which prevent such cross subsidization, and they will be monitoring the long distance business to insure that no cross subsidization exists.

Second, I have to point out that the long distance is intensely competitive. And were we to keep prices artificially high in the long-distance business in order to subsidize something else, we would merely lose the long-distance business. And so the market as well as the regulators will be watching this particular problem.

We have eliminated most of this problem, this cross subsidity problem by virtue of this divestiture.

Mr. HYDE. Competition will take care of that, I would think, from what you are saying.

Mr. BROWN. Yes, sir.

Mr. HYDE. Lastly, as I understand the decree the Justice Department has to approve the form in which the divestiture of the 22 companies occurs, whether it is 4 companies or 22 companies or 44 companies. The Justice Department approval is required. Is that correct?

Mr. BROWN. That is correct.

Mr. HYDE. You do not anticipate any problem there I suppose. Reasonable people can agree. If you do not agree, I mean is this whole decree down the tubes?

Mr. TRIENENS. No, I do not anticipate any problem because the one thing that is important in the decree, which is the separation of the local exchange, local exchange access, so-called monopoly functions from everything else, that is ordered by the decree. The form of whether it is 11 or 7 or 14 operating companies, how they are organized into a general department, or national service organization, that is not the fundamental point.

The problem of whether this so-called plan conforms to the decree would be whether it does make the separation required by the decree. We are sure it will. If it does there will be no problem.

Mr. HYDE. Thank you. I yield back my time.

Mr. WIRTH. Thank you, Mr. Hyde. Just for the purpose of the record I might shed some light on the size of the subsidies which you asked about. The total amount of costs for the local loop, local telephone service companies, is approximately $40 billion; $27 billion of that comes in rates that individuals pay. About $13 billion is the subsidy we have been talking about. That subsidy is broken down in a number of ways.

About $7.5 billion of that subsidy comes from long distance and there is some ambiguity as to whether or not that subsidy will continue. About $3.5——

Mr. HYDE. Excuse me. Is there any ambiguity as to whether it will be available to the local companies under the regulatory structure?

Mr. WIRTH. There is very real ambiguity as to whether or not the FCC has the responsibility and the legal right to regulate the local carrier and charge an access charge. If the local carriers become what is called under the law 2B2 carriers, the FCC has no jurisdiction over them.

That raises the question as to whether or not we should be legislating an access charge. I happen to believe we ought to clear up that ambiguity and make sure the subsidy continues. That is about 60 percent of the total subsidy going to the local ratepayers.

Mr. HYDE. I thank the chairman.

Mr. WIRTH. About $1 billion comes from Yellow Pages and about $3.5 billion of the subsidy comes from equipment. There is a little over $1 billion of the subsidy which comes from what is called inside wiring.

Four major elements go into that subsidy. We are talking about a total pot of about $13 billion. That is what many of these questions have targeted on: how we maintain that subsidy, how it gets phased out. Everybody agrees the subsidy is there. The question is how it shall be maintained.

Mr. HYDE. The point of the legislation I take it that we are considering is to make sure the withdrawal symptoms to the local companies do not do the patient in.

Mr. WIRTH. That is one way of putting it.

Mr. HYDE. Cold turkey should be avoided at all costs.

Mr. BROWN. I would point out there is no ambiguity to the point the FCC does have the power and does exercise it along with local regulators with respect to this subsidy.

Mr. HYDE. There seems to be a controversy then between your version and what the chairman said.

Mr. TRIENENS. There may be confusion. The so-called subsidy which is allocation of this plant which the chairman mentioned, intrastate versus interstate, that is not up in the air as to where that is. That is all embraced in something called the Separations Manual. It is a book ordered by the FCC, it is in the Code of Federal Regulations, same as a statute.

Namely, there is a joint board made up of State and local regulators that recommends changes, the FCC passes on them. If it approves them they go into the code. That is where the formula divides the plant between intra- and interstate, that is where it comes from.

To illustrate that the decree has nothing to do with that, there is a pending proceeding in which all these problems of competition and degree of the so-called subsidy which is really a cost allocation problem, all before a joint board. The joint board has made a recommendation to change this formula to some degree.

That is now before the FCC. All this took place before the decree was ever announced. It had nothing to do with the decree. This

process is impacted heavily by competition, was, will be. But without regard to the decree.

Mr. WIRTH. The record will be open for discussion of the issue as to what is a 2B2 carrier; it will be open for FCC comments. There is significant disagreement, Mr. Hyde, on what the FCC can and cannot do with regards to carriers within the State only.

Mr. HYDE. I appreciate it. Thank you.

Mr. WIRTH. Now are you thoroughly confused?

Mr. HYDE. No, now I see the move toward regulation to remove any ambiguity.

Mr. WIRTH. Mr. Seiberling.

Mr. SEIBERLING. Thank you, Mr. Chairman.

Mr. Brown.

Mr. BROWN. Yes, sir.

Mr. SEIBERLING. There seems to be a defect in this communications equipment right here.

Mr. BROWN. Competition will do that every time, sir.

Mr. SEIBERLING. Mr. Brown, I get the impression from the overall impact of this decree that these local exchange companies are going to continue to be captives of A.T. & T. in fact if not in form. I would like to elaborate a little bit, but first let me ask you, what is the justification for continued A.T. & T. ownership of the Yellow Pages? How do you justify that?

Mr. BROWN. Well, sir, we own it now.

Mr. SEIBERLING. You own the companies now. But you are getting rid of the companies, yet you are retaining Yellow Pages?

Mr. BROWN. Are you suggesting we sell Yellow Pages, is that the point?

Mr. SEIBERLING. I am asking why should not the Yellow Pages become the property of the locals?

Mr. BROWN. I see. Well, the theory of the Justice Department and the theory of most of the legislative proposals is that you should not mix a monopoly situation with a competitive situation. And the concern there is for cross-subsidy between the two.

Yellow Pages are an intensely competitive situation. Thus, the urgency on both, from both the standpoint of most legislative proposals and the Justice Department is to remove them from the monopoly oriented local companies.

Mr. SEIBERLING. What is the justification for their continued ownership by A.T. & T.?

Would you continue to own the Yellow Pages?

Mr. BROWN. Yes, sir. We own them now and will continue to.

Mr. SEIBERLING. Well, you own the companies now but you are getting rid of the companies. I do not understand why you should not also dispose of the Yellow Pages.

Mr. BROWN. Why should we do that?

Mr. SEIBERLING. Why not, if you are getting out of the local telephone business?

Mr. BROWN. This is not the local——

Mr. SEIBERLING. What relevance are the Yellow Pages to the long-line business?

Mr. BROWN. It is a business we have developed over the years. It is a profitable business, and I do not see any reason in a competitive environment why we should sell it.

Mr. SEIBERLING. I suggest that is not exactly justification.

Mr. WIRTH. Would the gentleman yield?

Mr. SEIBERLING. I would be glad to yield.

Mr. WIRTH. In the gentleman's district is there more than one Yellow Pages?

Mr. SEIBERLING. No; I am merely asking the question as to why should the Yellow Pages be owned by A.T. & T.

Mr. WIRTH. The answer that I understand given was that it is an intensely competitive business. But as I understand it there is only one Yellow Pages in your district.

Mr. SEIBERLING. I do not understand how it is intensely competitive since no one else can put out a Yellow Pages that will have utility.

Mr. BROWN. I respectfully disagree that this is not an intensely competitive matter. I can give you a list of competitors. The one that comes to mind now is General Telephone which puts out——

Mr. SEIBERLING. For the companies it owns.

Mr. BROWN. No, sir; in our territories.

Mr. SEIBERLING. That is news to me. I would be interested in expanding on it.

[The following letter was received for the record:]

Charles L. Brown
Chairman of the Board

AT&T
American Telephone and
Telegraph Company
195 Broadway
New York, N.Y. 10007
Phone (212) 393-1000

February 17, 1982

Dear Mr. Seiberling,

During my January 26 appearance before the Judiciary Committee a question was raised concerning the competitiveness of Yellow Pages

Bell System Yellow Pages advertising has experienced growing competition over the years from a number of sources. Competitors sell advertising and distribute directories in Bell operating company areas. In addition, competitors distribute directories in non-Bell areas which include advertising sold to businesses in both Bell and non-Bell areas. Independent publishers -- those not affiliated with the Bell System -- have grown from 20 in 1975 to more than 100 today. Some of the larger publishers include:

General Telephone Directory Company
L. M. Berry
R. H. Donnelley
Leland Mast Directory Company -
(Continental Telephone)
Gronseth Directory Services
White Directory Publishers

The extent of competition varies widely. For example, in Ohio, while there are no competitive directories in the Akron SMSA, in the Dayton SMSA there are six Ohio Bell directories and fifteen competitive directories.

Yellow Pages, of course, is only one of many media available to business advertisers. According to McCann-Erikson Advertising Age, U. S. Business Advertising in all media totalled $54.8 billion with all Yellow Pages making up $2.7 billion of the total.

I trust this information will give you a better understanding of the extent of Yellow Pages competition and their place in the overall market which serves business advertisers.

Sincerely,

Mr. SEIBERLING. What is the justification for A.T. & T. being allowed to retain Western Electric?

Mr. BROWN. In the first place, one of the objectives of most legislative proposals, one of the objectives surely of the Commerce Department and the country as a whole, is to retain this country's ability to bring technology to the United States and to maintain its competitiveness in the world. The combination of the Western Electric Co. and the Bell Telephone Laboratories is the prime competitor in the world in telecommunications techniques and telecommunications development.

To break up this and make it unavailable to the American people has not made sense to most people, including the Justice Department who agrees that this vertical integration should remain intact.

Mr. SEIBERLING. If that rationale is appropriate for A.T. & T., then what is the justification for the local exchange companies being prohibited from owning manufacturing facilities while A.T. & T. is allowed to continue to do so?

Mr. BROWN. Only the justification which is the same one as the Yellow Pages. That the local companies are a monopoly. It is not desired, from a Justice Department standpoint, or from a regulatory standpoint, and from most legislative standpoints, to mix monopoly with unregulated businesses. That is the basic reason for these companies not being in manufacturing.

Mr. SEIBERLING. Well, it would not be a monopoly because A.T. & T. would have laboratories, manufacturing facilities, and so would the local companies if they were permitted to do so.

Mr. BROWN. Yes, sir; but manufacturing presumably would be an unregulated business. The mixture there is what is trying to be avoided.

Mr. SEIBERLING. I see. Well, would not the LEC's then be forced to continue their reliance on A.T. & T.?

Mr. BROWN. No, sir; the matter of procurement is now at the decision of the local operation companies. Surely with divested operating companies they can buy wherever they want to buy.

Mr. SEIBERLING. In other words, the fact that A.T. & T. will continue to own the equipment in the home does not prohibit the local exchange companies from going ahead and getting another supplier of equipment?

Mr. BROWN. No, sir; they would not be in the telephone business, telephone instrument business. But they will go to any supplier they choose to go to in order to buy cable, in order to buy switching equipment, in order to buy carrier equipment within the exchange.

Mr. SEIBERLING. What about the telephones themselves?

Mr. BROWN. Well, sir, they are not in that business. They do not own the telephone.

Mr. SEIBERLING. Can they buy their telephones from someone else?

Mr. BROWN. I am sorry, sir. They are not in the telephone instrument business. They are not allowed to buy telephones.

Mr. SEIBERLING. That is my question. What is the justification?

Mr. BROWN. Well, this is not my idea.

Mr. SEIBERLING. I am not asking whose idea it was. What is the reason?

Mr. BROWN. The reason is that you can buy a telephone at Sears, Roebuck, or Montgomery Wards, or your local drugstore, many department stores, many specialty stores. And the desire is to separate that competitive business from the monopoly business.

Mr. SEIBERLING. In effect it is not a prohibition on someone else supplying that equipment, merely that the local company cannot own it.

Mr. BROWN. That is correct, sir.

Mr. SEIBERLING. Is there any guarantee in the decrees that the local exchange companies will have access to Bell's long-distance services, or is there simply the assumption competition will take care of that?

Mr. BROWN. It is certainly in the interest of A.T. & T. and every other long distance competitor to furnish long distance service to these companies. They will have wide choices, as they do now.

Mr. SEIBERLING. Finally, Mr. Rodino asked a question about making available patents and technology on a reasonable and nondiscriminatory basis. You indicated you would carry out your existing commitments. But his question was: Will the requirements of the decree as to all existing technology continue to be in effect, so that if someone in the future, who does not now have a license, wants to get one on your preexisting technology, they can get one?

Mr. BROWN. Future patents——

Mr. SEIBERLING. Not future patents. Past patents is my question.

Mr. BROWN. Past patents——

Mr. SEIBERLING. Which are not now licensed to a person if he wants a license, will the decree require you to give it to him?

Mr. BROWN. After the decree is in effect, no.

Mr. SEIBERLING. So all you are talking about is the existing license agreements remaining in effect, but you will no longer have a commitment to license others?

Mr. BROWN. I would point out also that anybody now can come to us under this 1956 decree and negotiate for patents. And we have to provide them on a reasonable basis.

Mr. SEIBERLING. Once the consent decree is entered into, they cannot do that.

Mr. BROWN. We will be in the same position as anybody else at that time.

Mr. SEIBERLING. In other words, the anwer is yes, they will no longer have that option?

Mr. BROWN. Yes, that is right.

Mr. SEIBERLING. Thank you.

Mr. WIRTH. Thank you, Mr. Seiberling.

Mr. Luken.

Mr. LUKEN. Mr. Brown, following up some of the other previous questions, there was discussion, question as to the amount of the subsidy. It was not answered from your end, then later it was answered by the chairman.

Do you agree with those figures?

Mr. BROWN. The chairman's figures are in the ball park, yes, sir. I would not argue with them. As far as the amount of the subsidy goes.

Mr. LUKEN. About the Yellow Pages subsidy. It is somewhere in the neighborhood of $1 billion, a little less, right?

Mr. BROWN. It is less than that, sir.

Mr. LUKEN. Close to it?

Mr. BROWN. Well, I have to be fussy about that because I am not really sure. It is mixed up with this business of charging for listings. It is not at all—it is not easy to state it because it has different situtions in different jurisdictions.

[The following letter was received for the record:]

AMERICAN TELEPHONE AND TELEGRAPH COMPANY

1120 20TH STREET, NORTHWEST

WASHINGTON, D. C. 20036

(202) 457-3840

R. L. MICKEY McGUIRE
ASSISTANT VICE PRESIDENT AND ATTORNEY

March 3, 1982

The Honorable Thomas A. Luken
Subcommittee on Telecommunications,
Consumer Protection and Finance
United States House of Representatives
240 Cannon House Office Building
Washington, D. C. 20515

Dear Mr. Luken:

During Mr. Brown's January 26 appearance before a joint hearing of subcommittees of the Energy and Commerce and Judiciary Committees, you raised a question on the amount of the Yellow Pages "subsidy" (transcript page 81).

According to a report prepared by the National Association of Regulatory Utilities Commissioners (NARUC), and printed in the Congressional Record, S11139 and S11140, October 6, 1981, the net revenue derived from Bell System directory advertising and applied in ratemaking was approximately $400M for the most recent fiscal periods for which data is available. Because of differences among the various jurisdictions, data was available for fiscal years ending June 30, 1980 through August 31, 1981. A copy of the NARUC report is attached.

The NARUC figure of $400M is comparable to our estimate of net income from directory advertising of $500M for 1980. Our figures are of necessity an estimate since neither AT&T nor the BOCs do cost accounting for directory advertising and publishing as a separate line-of-business. The estimated contribution (pre-tax) of $500M is arrived at by deducting direct expenses associated with production of both White Pages and Yellow Pages from net collected directory revenues to arrive at a gross margin of revenues over direct expenses. Both revenues and direct expenses are accounting entries in the Uniform System of Accounts.

To arrive at the net contribution available for ratemaking purposes, overheads associated with direct expenses, e.g., Social Security, pensions, and other benefits must be subtracted as well as other overheads such as motor vehicle expenses, administrative services expenses, business office expenses, etc. The net result after all directory and overhead expenses are subtracted is the figure of approximately $500M for 1980.

I trust this answers your question on the Yellow Pages subsidy.

A copy of this letter is being forwarded to Chairman Wirth for entry into the record of the January 26 hearing at page 82, line 1932.

Sincerely,

Mickey McGuire

USE OF TELEPHONE DIRECTORY ADVERTISING REVENUES IN STATE RATEMAKING

[Prepared by National Association of Regulatory Utility Commissioners]

Name of agency	Considers directory advertising revenue for ratemaking	Net revenue derived from directory advertising and applied to ratemaking		Gross revenue necessary to replace loss of directory advertising revenue for ratemaking	Increase in subscriber's monthly bill if directory advertising revenue not applied in ratemaking	Fiscal year ended
		Bell System	Other telephone companies			
Alabama PSC						
Alaska PUC	Yes			[1] 4,000,000	5.50	Dec. 31, 1980.
Arizona CC	Yes					
Arkansas PSC						
California PUC	Yes	121,600,000	[2] 41,400,000		1.25	
Colorado PUC	Yes	12,175,000		[3] 23,658,000	1.59	Do.
Connecticut PUCA						
Delaware PSC	Yes	1,800,000		3,800,000	1.38	Do.
District of Columbia PSC	Yes	2,600,000		5,500,000	.71	Do.
Florida PSC	Yes	35,300,000	13,700,000	53,000,000	1.81	Do.
Georgia PSC						
Guam PUC						
Hawaii PUC	Yes		4,657,821	8,969,700	1.85	Do.
Idaho PSC	No					
Illinois CC	Yes	57,293,559			1.08	Do.
Indiana PSC	Yes	12,127,320			1.51	Do.
Iowa SCC	Yes	11,556,261		[4] 23,231,501	2.04	Do.
Kansas SCC	Yes	9,656,600	157,000	[4] 20,135,000	2.01	June 30, 1981.
Kentucky PSC	Yes	4,329,447	1,620,922	11,843,756	.75	Dec. 31, 1980.
Louisiana PSC						
Maine PUC						
Maryland PSC	Yes	14,250,755		33,713,642	1.46	Do.
Massachusetts DPU						
Michigan PSC	Yes	37,528,927	2,431,845	74,031,430	1.73	Do.
Minnesota PUC						
Mississippi PSC						
Missouri PSC	Yes			63,938,518	2.53	Dec. 12, 1980.
Montana PSC	Yes	1,453,000		2,960,000	.92	June 30, 1982.
Nebraska PSC	Yes					
Nevada PSC	Yes			21,015,746		Dec. 31, 1980.
New Hampshire PUC						
New Jersey BPU						
New Mexico SCC	No[5]					
New York PSC						
North Carolina UC	Yes	7,826,745	7,520,009	31,000,000	1.14	May 31, 1981.
North Dakota PSC	Yes	2,719,124	506,812	6,351,650	1.93	Dec. 31, 1980.
Ohio PUC	No					
Oklahoma CC						
Oregon PUC	Yes	20,574,000	4,859,000	38,041,000	2.81	Do.
Pennsylvania PUC	Yes					
Puerto Rico PSC						
Rhode Island PUC	Yes					
South Carolina PSC	Yes	5,756,792		[6] 7,473,564	.77	Do.
South Dakota PUC						
Tennessee PSC	Yes			21,057,476	1.68	Do.
Texas PUC	Yes					
Utah PSC						
Vermont PSB						
Virgin Islands PSC	No					
Virginia SCC	Yes	10,125,000		[4] 19,483,000	1.00	Aug. 31, 1981.
Washington UTC	Yes	18,855,000	3,653,000	43,638,000	2.06	Dec. 31, 1980.
West Virginia PSC						
Wisconsin PSC	Yes	11,200,000	5,200,000	37,550,000	1.56	
Wyoming PSC	Yes					Do.

[1] Anchorage Telephone Utility (municipal) represents at least 50 percent of all gross revenues.
[2] General Telephone of California only.
[3] Applies only to Mountain Bell intrastate.
[4] Bell System only.
[5] Figures derived from rate cases of Southwestern Bell Telephone Co. and United Telephone Co. of Kansas which supplies approximately 20 percent of independent main stations.
[6] However, New Mexico SCC is seeking constitutional amendment to permit consideration of directory advertising revenue for ratemaking purposes. The net revenue derived from directory advertising by Mountain Bell is $7 029 000 and the net revenue derived from such advertising by the 3 largest independents (Continental, General Tel. of S.W. and Navajo) is $791,718.

Mr. LUKEN. When we got to that point you said that in reference to that subsidy, that A.T. & T. did not intend to abruptly cut that subsidy.

Mr. BROWN. Yes, sir.

Mr. LUKEN. So there would be a transition period. I assume from your comment there that under the terms of the settlement this would be within A.T. & T.'s discretion?

Mr. BROWN. Yes, sir.

Mr. LUKEN. Then that would not be regulated in any way, is that correct?

Mr. BROWN. That is right, sir.

Mr. LUKEN. Then that would appear to be an argument, as has been made here, for legislation going ahead, and not leave it up to A.T. & T., its discretion.

Mr. BROWN. Well, sir, if this is to be a competitive world as I understand it to be, it does not seem reasonable, and most legislative proposals agree, it does not seem reasonable to be subsidizing a regulated business from an unregulated one.

Mr. LUKEN. I am just going on the premise, which I think your comment was made on that premise, that we do not want to provide an abrupt decrease.

Mr. BROWN. Yes, sir; I do not propose to make it abrupt. To phase it down as some legislation has proposed.

Mr. LUKEN. So as the comments are going here about the question of moving with legislation, immediately, I am just wondering about another aspect of that question. Can we really make a determination of what this decree will mean in your opinion to the local ratepayer without knowledge of certain things such as the plan to spin off the operating companies and the plan to value and separate the assets, evaluate and separate the assets of A.T. & T.?

Are we not going to be learning these things as we go along in the ensuing months?

Mr. BROWN. No, sir; I think the decree is quite clear. We spin off the operating companies, and they are separate ownership. I do not see the ambiguity there.

Mr. LUKEN. A number of articles have been published in newspapers on the effect the divestiture will have on the BOC's and bond market for example. Do you share that concern?

Mr. BROWN. No, sir.

Mr. LUKEN. Will there be a change in the bond ratings that affect local rates?

Mr. BROWN. I hope not and do not expect so. These companies' bond ratings are based on their own financial condition now.

A.T. & T. does not stand behind operating company bonds. The bonds of the Ohio Bell, bonds of the Cincinnati company, are all——

Mr. LUKEN. Aren't they tied to A.T. & T.?

Mr. BROWN. Not from the standpoint of their bonds, no. They issue their own bonds. Their bonds are based on their own credit rating.

The rating agencies take a look at their interest coverage, their debt ratio, and decide whether it is a AAA rating or whether it isn't.

Mr. LUKEN. These companies are now subsidized by the long lines and the Yellow Pages, are they not? Wouldn't that affect those rates because it affects their well-being.

Mr. BROWN. Well, yes, sir, it would. I think that it is going to take us a little while for all this to shake out to find out precisely what the situation is going to be.

Mr. LUKEN. I think that is what I said a moment ago. No; I am not suggesting it is all that simple.

Mr. BROWN. It is kind of a Rubic's Cube of problems I face, I am afraid.

Mr. LUKEN. Moving right along, in analyzing your testimony, your opinions here, do you think that because of the consent decree, and with the revenue problems that LEC's, or new operating companies are going to be having or we anticipate they are going to be having, that we will be witnessing a general deterioration of nationwide, the nationwide network?

Mr. BROWN. No, sir, I don't think so. We certainly do not intend that to happen.

As I mentioned before, it is our stockholders' investment that we are talking about here. We surely intend to do the right thing by people who own the business and who invested their money in it over the years.

We will surely keep the Congress informed as to what is going on and what is happening with respect to the divestiture plans. I am sure the Congress will and should act in the event that there is some difficulty anticipated.

But you know, there are a lot of things that are unanswered at this point.

Mr. LUKEN. I believe you made an observation when we were discussing that before, that if the State utility commissions give proper treatment to the local companies, that that in effect would be necessary in order to avoid financial problems with those local companies.

Mr. BROWN. Yes.

Mr. LUKEN. So they can operate and operate effectively to avoid the deterioration.

Mr. BROWN. Yes, sir. This has happened over the years and I would expect it to continue to happen.

Mr. LUKEN. Well, sir, I think we were talking about the effects of the settlement at the particular time. That is what we are talking about now.

It seems to me I would conclude from your statement that the result of the settlement would be that appropriate or proper treatment be given by the utility commissions back home and in the various States, and that would inevitably mean higher rates, of course.

Mr. BROWN. Perhaps I was not making myself clear. I don't think that the obligation and the intention of regulatory bodies to deal with the local operating companies is going to be any different under divestiture than it is now. That was what I intended to say.

Mr. SEIBERLING. Would the gentleman yield?

Mr. LUKEN. I would gladly yield to the gentleman from Ohio.

Mr. SEIBERLING. Thanks. I think the gentleman has opened up a very important question here. I would like to just ask a follow-on question

Mr. BROWN. Yes, sir.

Mr. SEIBERLING. From the standpoint of the stockholders of A.T. & T., who want the divestiture to take place and who will also become stockholders of the local exchange companies, what difference does it make to them whether the Yellow Pages, terminal equipment, et cetera, are owned by A.T. & T., or by the local exchange company since they are going to still end up owning the whole package?

Mr. BROWN. No difference.

Mr. SEIBERLING. Well, then, why is it important to A.T. & T. to retain all these advantages and not have them given to the local exchanges?

Mr. BROWN. It is not my idea that the operating telephone companies give up the Yellow Pages or the telephones. It is an idea promulgated by regulatory bodies and by the Justice Department.

Mr. SEIBERLING. Thank you.

Mr. BROWN. The theory is that you should not mix regulated monopoly-type business with unregulated business.

Mr. SEIBERLING. So as far as you are concerned, it could go either way, as far as the stockholders are concerned?

Mr. BROWN. Yes, sir.

Mr. SEIBERLING. Thank you.

Mr. LUKEN. You are not saying A.T. & T. would be willing to alter the terms of the settlement agreement to that effect; are you?

Mr. BROWN. No, sir. You know, this has been a traumatic enough situation now. I really don't think I want to get involved in trying to change it now.

Mr. LUKEN. Obviously, I guess Congress might consider that alternative. I want to pursue one easier question perhaps.

Are you familiar with the term POTS, plain old telephone service?

Mr. BROWN. Yes, sir.

Mr. LUKEN. A.T. & T. currently offers a hybrid of services, including terminal equipment, local exchange, and long-line service; right? With the LEC's prohibited from offering anything other than POTS, that is what they are going to be offering; right?

Mr. BROWN. No, sir; they are not confined to that. This is one part of their business. The other part of their business is access to and from the long-distance networks offered by us and competitors.

Mr. LUKEN. Access.

Mr. BROWN. Access. They will be in this cellular business, in other words, the mobile telephone business, with new cellular technology.

Mr. LUKEN. What I am getting at is, and I only have a moment so if you will pardon me interrupting a little bit, as far as the users are concerned, do you see they may have a problem? That they are either going to be dealing with separate entities and, therefore, a confusing situation to them, or, in effect, it is going to be the same old thing.

A.T. & T. is going to be running the show and that would violate the terms of the agreement.

Mr. BROWN. No, sir; A.T. & T. is not going to be running the show. But it is the intention of all telephone people, who have common stockholders, to make this transition which is going on anyway, regardless of this consent decree, to make this transition as transparent to the customers as we can possibly make it.

It is not to our advantage to have confused customers. We are going to try to avoid it. I guess we just have to wait a little bit to see whether we are successful in this. I think we will be.

Mr. LUKEN. Thank you for helping with a confusing situation. I yield the balance of my time.

Mr. WIRTH. Thank you, Mr. Luken.

Mr. Bliley.

Mr. BLILEY. Thank you, Mr. Chairman.

Mr. Brown, at some point, A.T. & T. and operating companies will begin to have separate interests as you go down the road of divestiture.

Yet you will be ultimately making the decisions about the divisions between A.T. & T. and operating companies. Is there any way you can provide independent voice from the operating companies early in the process?

Mr. BROWN. Yes, sir; we have monthly or more frequent meetings between our operating company presidents and ourselves. I have assured and clearly intend that they have full input to what goes on here with respect to the form of divestiture.

Mr. BLILEY. I see. A.T. & T. now has a great mix of high costs and low-cost debt, as well as improved investment tax and accelerated depreciation credit.

What principles will you use to divide these assets between A.T. & T. and the operating companies?

Mr. BROWN. We will surely not be putting A.T. & T. parent debt on the operating telephone companies. In fact, it probably will be in the reverse. We will insure also that the interest rate situation is equitable. And we do not make it inequitable with respect to the interest rates.

Mr. BLILEY. Thank you. Following up on an earlier question, line of questioning put to you by Mr. Rodino, the inside wiring in the customer's home, will that be handled by the operating company or local companies?

Mr. BROWN. The local companies.

Mr. BLILEY. The local companies?

Mr. BROWN. Yes, sir.

Mr. BLILEY. Finally on this matter of Yellow Pages, customers currently, themselves, individuals, receive a directory every year from the company at no direct charge. Will A.T. & T. supply directories for local listings in each locality now, since you are going to have the Yellow Pages which pay for this, or will the local companies have to issue directories themselves, and how will they finance them if that is the case?

Mr. BROWN. The issuance of local directories will be the responsibility, these are the white pages we are speaking of, they will be the responsibility of the local company. The combination or no combination of the Yellow Pages in connection with this will be a matter of negotiations between ourselves and the companies.

They will be compensated for any costs that are involved in this.

Mr. BLILEY. How about the customer? Will he then have to buy the directory?

Mr. BROWN. I see no change in that, sir. There is no reason I can see that that would change at all.

Mr. BLILEY. Then it will be an expense item on the part of the local operating company with no offsetting revenue as I see it, because Yellow Pages today pays the freight for providing the listings in addition to that, a subsidy.

Mr. BROWN. The operating companies will be able to charge what the market will bear with respect to the basic ingredient of Yellow Page directories, that is the listing.

They control those listings and they can charge whatever the market will bear with respect to the use of those listings.

Mr. BLILEY. Thank you, Mr. Chairman. I yield the balance of my time.

Mr. WIRTH. Thank you very much, Mr. Bliley.

Mr. SWIFT.

Mr. SWIFT. Thank you, Mr. Chairman.

Mr. Brown, from your understanding of the settlement, who sets the access fee?

Mr. BROWN. The regulators.

Mr. SWIFT. Which regulators?

Mr. BROWN. In the case of interstate service, I would assume it is the Federal Communications Commission. In the case of intrastate matters, it is the State commissions, I would assume, unless there is some change in jurisdiction about which I don't know.

Mr. SWIFT. One of the reasons I raised it is that there seems to be very little that is clear and certain about that.

You indicate the assumption on your part in your testimony. Before the Senate, other parties also assumed it was going to be one way or another. Justice has told us that the agreement is neutral on this question: It seems to me there is room for a lot of mischief there, for disagreements between the FCC and PUC's.

Mr. BROWN. I don't see any ambiguity. FCC is charged by law with regulation of interstate service and they clearly have jurisdiction over regulation of the interstate businesss.

As a matter of fact, they have a docket on that now.

Mr. SWIFT. So you are saying that the access fee that would be charged by a local exchange would be set by whom?

Mr. BROWN. For access to interstate service, the final determination would be in the jurisdiction of the Federal Communications Commission. They arrive at these decisions frequently by the use of a joint board. But it is their jurisdiction.

Mr. SWIFT. Currently in Federal law, there is no such thing as an access fee, right?

Mr. BROWN. Well, the——

Mr. SWIFT. You have had a separations and settlements process that has been used in the past.

Mr. BROWN. Yes; but they are in charge of that separations process. It is their separations manual which determines the cost and basis of the subsidy Chairman Wirth spoke of awhile ago.

This same separations manual can and probably will be used for access charge determination.

Mr. SWIFT. Again, you say can and probably will. You assume. Bernie Wonder said in the Senate that he assumed. The fact that that word comes up, and one says we think it is going to work out this way, doesn't trouble you in terms of the certainty of being able to carry out this agreement without resorting to further court cases?

Mr. BROWN. No, sir; I think those words are used because it is hard to know what is going to happen among regulatory bodies in the future or with legislation. But there is no question as to what the authority of the FCC is in this regard.

Mr. SWIFT. But it is hard to know what—you just said it is hard to know what future regulatory bodies are going to do, but it is clear that the FCC has the authority.

What is unclear about what regulatory authorities might do in the future if it is clear that the FCC has the jurisdiction?

Mr. BROWN. Well, there is a problem here which probably causes this to happen, this ambiguity to occur. That is the jurisdiction for intrastate, long-distance business. That is clearly under the jurisdiction of the State public service commissions.

There are proposals and there are discussions about the FCC's authority with respect to that. The statement being made that it is possible to have one access charge for intrastate long distance and another access charge for interstate, and this would be rather peculiar, to say the least.

I think that is where this ambiguity and assumption occurs. But right now, it is clear. The FCC has the authority for interstate, States have the authority for intrastate. That is clear.

Mr. SWIFT. In trying to determine, aside from what may be the current status, the situation or what the settlement would do, one has been forced to really kind of try to make some evaluations of what good policy would be in this regard.

I must admit I am confused because I think you built a good case in terms of local ratepayers to have it done at the State level. You can also see all kinds of problems that grow out of that, not the least of which that in an effort to be kind to local ratepayers, they could set access fees so high that, in effect, it would drive some big users off the system, to the detriment of the local ratepayers.

Nevertheless, it seems that is an issue that will be argued in a great variety of ways and a greater certainty in who is doing what would be something that would ultimately be to everybody's benefit, the consumers of all kinds, and to telephone companies and so forth.

You still maintain, however, that, as of now, that is clear in your judgment, that the FCC has the authority to set access fees on interstate calls.

The uncertainty, as I understand it, comes from not knowing what is going to come in the future in the way of the intrastate system and whether 50 PUC's are going to decide that in a crazy quilt.

Is that what you are saying?

Mr. BROWN. That is where the problem might occur, yes.

Mr. SWIFT. Is there mention of the access fee in the decree at all?

Mr. BROWN. Yes, sir.

Mr. SWIFT. What does it say? Or is that an unfair question?

Mr. BROWN. I can read it to you. I guess it is fair to summarize it by saying that the access fee scheme, as outlined in the decree, follows essentially what the FCC has set out in their tentative access plan docket.

It follows, also, some legislative proposals almost word for word.

Mr. TRIENENS. I should add technically that the decree orders A.T. & T. to file access tariffs, carrier-initiated tariffs. As you advise, the decree has to be neutral on the question of what the jurisdiction of the FCC is and what the action of the FCC is on those filed tariff applications.

Mr. SWIFT. Thank you, Mr. Chairman.

Mr. WIRTH. Thank you.

Mr. Tauzin.

Mr. TAUZIN. Thank you, Mr. Chairman.

First, Mr. Brown, let me ask you a question a constituent asked me to ask you. In reference to the settlement agreement, who will own the link between the class 4 toll centers and class 5 local exchange?

Mr. BROWN. Who will own the link between the class 4 and class 5? The operating telephone companies will own them.

Mr. TAUZIN. That is, one of the 22 companies will own those links?

Mr. BROWN. Yes, sir.

Mr. TAUZIN. Next, let me preface my questions by telling you that I have been trying to read a lot about the settlement agreement.

Mr. BROWN. It is hard to avoid it, isn't it?

Mr. TAUZIN. Very hard today. One of the advantages I have, being a young member of the committee, is that I have the advantage of hearing a lot of my colleagues ask you questions. Also, I promised the folks back home I would try to approach these issues with a little commonsense. So let me try to distill some things and get some things straight in my own mind.

First of all, operating from memory, the A.T. & T. system has approximately $119 billion in assets, something in that range?

Mr. BROWN. It is $135 billion, roughly.

Mr. TAUZIN. Bigger than. You are spinning off about $80 billion of assets, right?

Mr. BROWN. Yes, sir.

Mr. TAUZIN. The assets you are keeping, Bell Labs, Western Electric and the longlines, basically are more lucrative. That is, they produce more income for dollar of assets than do the $80 billion you are spinning off, is that correct?

Mr. BROWN. That is why the subsidy is in there, yes, sir.

Mr. TAUZIN. Is it also correct that the same stockholders are going to own the companies spun off, as well as what remains of A.T. & T., as one of my colleagues mentioned?

Mr. BROWN. Yes, sir, immediately.

Mr. TAUZIN. So the stockholders will then, owning the 22 companies, have a great interest in seeing to it that the 22 companies become more lucrative than they have been in the past, is that correct?

Mr. BROWN. I am sure shareholders are always glad to see a company thrive, yes.

Mr. TAUZIN. Yes, and they wouldn't want the 22 companies to profit at the expense of what remains of A.T. & T. since they also own stock in A.T. & T., correct?

Mr. BROWN. I would say that, yes, sir.

Mr. TAUZIN. That leads me to the conclusion that your desire that the local rate regulators live up to their responsibilities and choose higher rates over poorer service, that that desire would probably be fulfilled in the settlement agreement because those people who own the operating companies will, of course, be, as much as possible, setting up a scenario where they can get their costs and profits covered by consumers rather than by A.T. & T. subsidies, is that not correct?

Mr. BROWN. There is no difference between that and the situation today.

Mr. TAUZIN. Well, no difference except they may now have some chances of doing that they don't have today. That is if, in fact, there is no longer the Yellow Page subsidy or perhaps inside-wiring subsidy, or if there is ambiguity on the longline subsidy they can be resolved in favor of the local 22 companies not having to rely upon Bell, but rather to put pressure on the local PUC's that that would be the option chosen, I suppose, by the local ownership and management of the 22 companies, would it not be?

Mr. BROWN. I am very sorry. I lost the train of what you were saying. I am very sorry. Do I understand you to be saying that the local companies will be trying to make their business more profitable, and therefore will be putting pressure on the PUC's?

Mr. TAUZIN. What I am saying is if there is a mechanism by which the local company need not rely upon A.T. & T. for subsidy, if there is an ambiguity, the local companies would probably want to settle that ambiguity in favor of relying upon the customers to make up that difference rather than relying upon A.T. & T., which would hurt their profits on the other stock they hold.

Mr. BROWN. No, sir, I don't believe that would be the case. I say that for this reason. The subsidy of which we keep talking comes not only from A.T. & T., but from other long-distance providers who come into this territory to the local telephone companies.

Mr. TAUZIN. That is a good point.

Mr. BROWN. They will be charging access charges, both to A.T. & T., and other providers who come in. And so there is no reason for them to, aside from the bypass thing about which we talked, to make one end of the business any more rational than the other.

Mr. TAUZIN. Why is it then that you cite history of local rates rising at about one-third the rise in inflation, 4 percent as compared to 12 percent?

Mr. BROWN. Yes.

Mr. TAUZIN. Which has been recent history, and then you make a prediction that local rates are going to rise at rates in excess of the rate of current inflation, the 8.9 rate recently released.

You say they are going to rise at 8 to 10 percent now. You said the next few years. Why is it then suddenly you predict local rates are going to rise at three times the current rate in relation to inflation?

Mr. BROWN. I don't predict three times the current rate.

Mr. TAUZIN. One-third the inflationary rate next year. You predict now it is going to equal or better the inflationary rate. That is three times.

Mr. BROWN. I talked about 8 or 10 percent as opposed to 4 percent. That was my confusion.

Mr. TAUZIN. Yes.

Mr. BROWN. As I mentioned in my opening remarks, there are several reasons for local rates to go up. One of them is inflation, as we have talked about.

The other is the introduction of new technology and competition which operates on depreciation rates by virtue of shorter lives for equipment.

Equipment turns over quicker under——

Mr. TAUZIN. Hasn't that been the case in the last several years?

Mr. BROWN. Not to the extent that it is prospectively. And it has been the case in the last several years to a degree. You will notice the FCC issued an order last week directly pertaining to this point.

So it is not a matter solely of inflation. It is these other factors I mentioned in my opening statement which also have a bearing on this.

Mr. TAUZIN. Of grave concern also in this consent decree to many folks who view the enormous strength of A.T. & T. in the marketplace, and who are going to be consigned to open competition now, is the fact that A.T. & T. has retained, indeed, its most lucrative assets.

And having been relieved of the 1956 decree limitations upon its ability to compete, that now A.T. & T. has a much greater capacity, in fact, to enter other competitive markets and to drive out the competition.

That fear is expressed to me very often. What are your comments with regard to that?

Mr. BROWN. I am sure competitors are not anxious to have more competition. It makes very little sense to me to restrain a competi- about people who would like to chain the A.T. & T. so it cannot compete.

This is a normal expectation, and we have seen it in recent years and will continue to see it.

The whole point is, however, that what has been decreed here is competition. It makes very little sense to me to restrain a competitor by worrying about other competitors.

Allocation of the market on the part of Congress is not exactly something that corresponds with competition.

Mr. TAUZIN. Well, of course, their argument is that because A.T. & T. had, in effect, a monopoly operation and was protected in developing its Bell labs and its Western Electric manufacturing assets, in other words, it built itself up on the back of a monopoly, that turning it loose on the rest of the field of telecommunications competitors does some violence to the theory of fair competition.

Would you comment?

Mr. BROWN. We have divested two-thirds of our assets.

Mr. TAUZIN. Well, the less lucrative two-thirds.

Mr. BROWN. If you will let me finish, let me tell you what we are facing in competition with the remaining A.T. & T. business.

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First of all, the Western Electric Co. is part of that business. I am sure manufacturers will complain that we have an unfair advantage because we have Western Electric Co.

What is Western Electric's market? It is these very operating companies and other operating telephone companies throughout the world. They will be selling directly in competition with everybody.

Mr. TAUZIN. Excuse me, if I might stop there. You made that argument earlier. The same stockholders are going to own both companies. You tell me the stockholders of the operating companies are not going to want to buy from the same company in which they also own stock?

Mr. BROWN. Well, sir, the stockholders are not the ones who have control of who buys from what. The decree specifically charges these operating companies to deal in an evenhanded way among all suppliers.

Mr. TAUZIN. I understand that, but I am saying again the realistic world where I am working for stockholders who also own another company, aren't I going to be more interested in buying from another company, all other things being equal?

Mr. BROWN. Not unless you want to get arrested for violating the decree.

Mr. TAUZIN. I just bring it to your attention because it is of some concern. When you have the same stockholders operating in both companies. Without violating any decree, isn't it going to be natural for the companies to want to support each other?

Mr. BROWN. Although the shareowners will be the same at the day of divestiture, these shares will trade on the market, and soon there will be an entirely different set of shareholders owning one company versus the other.

Mr. TAUZIN. Thank you, Mr. Brown.

Thank you, Mr. Chairman.

Mr. WIRTH. Mr. Markey.

Mr. MARKEY. Thank you. I would like to just piggyback now on what Mr. Tauzin was just discussing with you, if I may.

And that is the posture now in which we have placed the competitors to Western Electric, the Wangs, the Digitals, Honeywells, people from my district, people from these companies who have counterparts all across the country.

My concern goes to the subsidy which still flows to Western Electric.

Mr. BROWN. No, sir, there is no subsidy to Western Electric.

Mr. MARKEY. You still have the longlines. You still have, for all intents and purposes, the monopoly long-line service.

If I understand this correctly, the long line service generates more revenues than did the cumulative total of the 22 operating companies, is that not correct?

Mr. BROWN. No, that is not correct.

Mr. MARKEY. That is not correct. Could you break it down for us in billions of dollars, how much revenue long lines generates for A.T. & T., and how much the Bell operating companies did?

Mr. BROWN. I think I better not try to guess at that one. I will be glad to give it to you after I consider it a little bit. But I don't want to try to guess it now.

Also, one of the reasons I don't want to try to guess it, because it will change so drastically with respect to the reforming of district lines or exchange lines in connection with this divestiture.

The question of whether or not Western Electric has a monopoly is one I would like to address, however. The major market of the Western Electric Co. is the operating telephone companies.

The new technology in this world today for long distance is, the important new technology has to do with microwave and has to do with satellites. Western Electric manufactures about 25 percent of the microwave in this country, sold in this country. They manufacture none of the satellites.

Western Electric is far behind a good many manufacturers in the world as far as size is concerned.

[The following letter was received for the record:]

Mr. MARKEY. What size of long-distance service do you now have?

Mr. BROWN. What percentage do we now have? It is high. It is in the 90's.

Mr. MARKEY. Close to 97 percent. You have had competition for 10 years. My understanding of the classic definition of monopoly is an entity that can raise their rates and not see any significant diversion of business from that entity.

Now this past year, you raised your rates 16 percent. That was your request. That was what you were granted, 16 percent long distance increase.

What kind of diversion of business have you suffered in the past year?

Mr. BROWN. This rate increase was after 4 years. I think if you compare that with any other things that have happened in this country in that 4 years, you will think 16 percent was rather low.

Mr. MARKEY. How much of your business was diverted, though, that is the question? You raised the rate 16 percent. Did you lose any business?

Mr. BROWN. Yes, we did.

Mr. MARKEY. How much?

Mr. BROWN. Well, it is hard for me to tell, Mr. Markey. How do I know whether the recession has something to do with the loss of business or whether the prices have something to do with the loss of business? The competitors have been growing at the rate of 40 to 50 to 60 percent a year, and the predictions are 100 percent a year.

Mr. MARKEY. One hundred percent of one percent is still only another one-tenth of 1 percentile. MCI, your major competitor, is still under 1 percent of the total market, so you are really not talking about that kind of significant effect on the monopoly service you now own.

That is my concern, if I can get back to that. This tremendous amount of revenues which Western Electric still has access to long lines to help subsidize their competition in the computer and data processing business as they now get out there and begin to compete.

The same kind of subsidy that exists for Western Electric in being able to extract a premium price from long lines for the equipment which it sells to it.

The company doesn't have any real incentive not to build that price increase in since it goes right into the rate base.

Mr. BROWN. Mr. Markey, you must understand that the regulators watch closely the prices Western Electric charges to operating Bell companies and long lines.

Second, the market will stop that. If there was any such subsidy, long lines prices would be higher and the market would go faster. There is no subsidy and there is no incentive for subsidy to Western Electric.

Mr. MARKEY. We had the chief of the Common Carrier Bureau in from the FCC last year. He told us that it was impossible for the FCC to be able to keep track of your costs of service, all of the charges within the system and basically they just took a rough cut, is what he said to us, at what goes on.

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It was impossible for them to really keep track, since the new uniform system of accounts is not yet in place, they have no ability to be able to monitor——

Mr. BROWN. I cannot believe anyone said there was no uniform system of accounts, Mr. Markey. How can that possibly be? This is a system of accounts that regulates all telephone companies in this system. How can anybody say that?

Mr. MARKEY. I think they were probably indicating not that the system is not there, but there hasn't been any compliance.

Mr. BROWN. We are not complying with the uniform system of accounts? Mr. Markey, we would go to jail.

Mr. MARKEY. We would have trouble finding a jail big enough. As a result, we just deal again in the regulatory process with the only telephone company we have got.

Again, I want to, for my own purposes, just understand, again, following up on Mr. Tauzin's point, on what the relationship will be between the Bell operating companies and Western Electric as far as the procurement.

You say there will be competition. But isn't there a provision in the consent decree that special preferential treatment should be given to the Bell operating companies by Western Electric over the next 5 years?

Mr. BROWN. Yes, sir, there is an obligation on the part of the Bell labs and the Western Electric companies to supply these companies with certain technology which will permit them to apply—to comply with the provisions of the decree.

But this is a very small part of the procurement matter. It is the provision of changing central offices to permit access to be comparable among incoming and outgoing other common carriers.

It is not a preference to Western Electric over that period of time. It is a demand that the technology be furnished to these companies.

Mr. MARKEY. Could you just expand on that?

Mr. BROWN. It is an obligation of the A.T. & T., through Western Electric and Bell labs, to make sure that these companies have the technology which will permit them to comply with the decree, especially in those parts of the decree which deal with equal access of other common carriers to the local plant.

Mr. MARKEY. You are saying that preference will not go to price, then, at all?

Mr. BROWN. No, sir. I am sorry. I didn't understand. It is not a price preference at all. It is a priority which the Western Electric and Bell labs is required to give to that provision.

Mr. MARKEY. Thank you, Mr. Chairman, for your indulgence. My real concern here is that the Digitals and the Wangs and Honeywells, are not still put in the situation which Mr. Tauzin has so well put, is that a company has been able to divest itself of two-thirds of the assets while still retaining two-thirds of the revenues and not be able to use those revenues, and this was one of the primary bases for the antitrust suit in the first place, to cross-subsidize in their competition with data processing and computer companies that are out there. If Bell is going to be allowed——

Mr. BROWN. No, sir, that was not the basis of the antitrust suit.

Mr. MARKEY. All right, the basis of legislation that we have been discussing here in Congress over the past several years has been to try to minimize whatever cross-subsidies would go——

Mr. BROWN. Yes, sir.

Mr. MARKEY. From the mother company to Western Electric in its competition with computer companies.

Mr. BROWN. We have eliminated that by divestiture of the operating companies.

Mr. MARKEY. But you still have the long-line potential subsidy from the premium changed from the captive long-lines market that Western Electric still retains.

Mr. BROWN. This is not a monopoly.

Mr. MARKEY. I think at 97 percent you would have a hard time convincing most people it is not a monopoly service.

Mr. BROWN. The antitrust expert in this field is apparently Mr. Baxter. If you read his comments he points out that in this kind of a situation there is little connection between market share and market power.

Mr. WIRTH. The gentleman's time has expired. Thank you, Mr. Markey.

Mr. Collins.

Mr. COLLINS. Mr. Brown.

Mr. BROWN. Yes, sir.

Mr. COLLINS. All of us in Congress when we go home, are hearing more and more about this matter of local rates, particularly the residential rate, the homeowner rate. This has come about I think because the press has told the public, in view of these court decisions and trends, that A.T. & T. is going to provide a smaller subsidy out of long distance to pass on to benefit local rates. Was it the policy of the telephone company to give preference to homeowners in the past by charging a little more for long distance?

Mr. BROWN. Yes, sir, long-distance rates were higher than they needed to be in order to furnish the subsidy to homeowners among others.

Mr. COLLINS. If you did that, and if the courts order it to become more and more competitive, I am worried about the fact that local rates are going to go up and up. How do they stand with respect to electricity and water rates? Have you been raising them faster than these other utility rates?

Mr. BROWN. No, sir. I think any comparison between telephone rates and electric rates will indicate very quickly that telephone rates have gone up far slower, far slower than electric rates almost anywhere.

Mr. COLLINS. Someone told me the other day and I do not know whether it is right or not, that your rate of increase has been only half that of other utilities. Is that about right or do you know?

Mr. BROWN. I think that is at least so. Other utilities, it is a little hard for me to make that statement without some look, but I think it is perfectly safe for me to say that the rate of increase of telephone rates has been lower than most anything in this country. Utility or otherwise.

Mr. COLLINS. And divestiture, I don't see how that is going to have any effect on local rates one way or another, will it?

Mr. BROWN. No, sir.

Mr. COLLINS. Whether you divest it or not, if you can no longer subsidize out of long-distance rates, it is going to mean that local rates must go up. Is that the inevitable conclusion?

Mr. BROWN. Well, the subsidy can still be there at the option of the regulators, but the competitive environment and the effects of inflation and depreciation matters about which you are very familiar are going to cause local rates to go up regardless of divestiture.

Mr. COLLINS. If you have divestiture, long lines is still under regulation?

Mr. BROWN. Yes, sir.

Mr. COLLINS. So this wouldn't have any impact one way or another.

Mr. BROWN. No, sir.

Mr. COLLINS. You are regulated, whether you are or are not.

Mr. BROWN. Absolutely.

Mr. COLLINS. I have never understood how these local regulators go about doing the regulating. I went over here and I had to make a pay call this morning. And I paid 15 cents. At home I pay a quarter. It seems to me more logical to charge more on pay phones. Why is it in Washington, D.C. they don't charge these visitors a quarter instead of like they do at home?

Mr. BROWN. Not to give you a smart answer, it is the same reason you pay only a dime in New York.

Mr. COLLINS. Is that all you pay in New York? No wonder that city is busted.

Mr. SCHEUER. I would like to protest this line of questioning.

Mr. BROWN. Well, the facts are, Mr. Collins, that what happens in the various jurisdictions is that the regulatory bodies decide how rates will be spread. Some of them feel, as you perhaps do, that the user of a coin telephone ought to pay an appropriate amount for the use of that. Others take the position that coin telephones are useful to poor people who don't have their own telephone and that that rate ought to be kept low. So, it is a difference in regulatory philosophy that applies.

Where those rates are kept low, of course residential rates and business rates have to be higher in order to again subsidize the coin rate.

Mr. COLLINS. Thank you very much.

Mr. BROWN. Yes, sir.

Mr. WIRTH. Mr. Rinaldo.

Mr. RINALDO. Thank you very much, Mr. Chairman.

First of all, I certainly want to welcome Mr. Brown and congratulate Chairman Rodino and Chairman Wirth for holding this very important hearing. Despite the consent decree, and I have heard your understanding of it, and all that has been accomplished and will be under it once it is signed and put into effect, I feel much still remains to be done legislatively.

What I would like to do is give you a few areas where I think legislation is necessary, and ask you to comment on my statement, and also on a question that I will ask at the conclusion concerning the overall scope of the legislation.

Mr. BROWN. Yes, sir.

Mr. RINALDO. First and foremost, in my opinion, we need legislation to set up a mechanism to guarantee the continued availability

of high-quality local telephone service at reasonable rates. Now, the bill that was before our committee, H.R. 5158, which I am sure you are familiar with, provides a very detailed and ingenious mechanism for computing access charges and access surcharges. This, in my opinion, will go a long way toward keeping the cost of local telephone service down. I am also encouraged, Mr. Brown, by your letter of yesterday evening to Senator Packwood in which you stated that A.T. & T. will continue to provide support to the divested local telephone companies for 4 years by attributing Yellow Pages revenues to them. This is, in my view, additional assurance that local rates will not rise as high as we have been reading as a result of the settlement.

Mr. Chairman, at this point I would like to ask unanimous consent that Mr. Brown's letter to Senator Packwood be made part of the record.

Mr. WIRTH. Without objection.

[The letter of Charles Brown follows:]

AT&T

Charles L. Brown
Chairman of the Board

American Telephone and
Telegraph Company
195 Broadway
New York, N.Y. 10007
212 393-1000

January 25, 1982

Dear Senator Packwood:

In reference to our discussion in the hearings this morning on Yellow Pages, I am prepared to make the commitment of which you spoke.

We will not abruptly discontinue the support for local rates from the Yellow Page source. S.898 provides for a four-year phase down of this support. Unless future legislation affects this matter, we will see to it that the support is not phased out until four years from now. This may be affected, of course, by any changes which may occur in charges by the local telephone companies for the prompt provision of telephone number listings to anyone who sells yellow page type advertising.

I'll be glad to discuss this matter with you or your Staff at your convenience.

Sincerely,

C L Brown

The Honorable Robert W. Packwood
United States Senate
145 Russell Senate Office Building
Washington, D. C. 20510

Mr. RINALDO. In addition, we would need legislation so that the FCC can reduce or eliminate regulation of the telecommunication services as competition develops. A reduction and elimination of regulation is not provided or permitted by the present Communications Act.

In fact, quite the contrary, my reading of the act requires that the act itself continues regulation even where, for example, it may be totally or completely unnecessary. In my view this results in a preposterous waste of Government resources and imposes needless burdens on carriers as well. As far as regulations go I hope we agree with what the current administration is doing.

Where regulation is unnecessary the Government should step aside. I would hope that our legislation would accomplish this objective. Another problem that must be taken care of in legislation is the protection of rights of A.T. & T. employees who are transferred. Now, I understand they are going to be transferred either to divested companies or to another entity within the restructured A.T. & T. organization. And my further understanding is that several hundred thousand employees will be transferred as a result of settlement, and certainly we should make sure that their careers are not adversely affected by the consent decree.

So, in light of these changes, in light of all that has been said this morning, the testimony that you have given and the questions that have been propounded, A.T. & T. now finds itself in a different set of circumstances. How do you now view the need for legislation such as H.R. 5158 or S. 898? How would you respond to the comments that I have made? What form do you feel, and this is, I know, a question with many components, what form do you feel such legislation should take, and what changes in the present legislation, primarily S. 898 and H.R. 5158, would you recommend? If you want I can go through that entire scheme again but I think you understood the general tenor of the question.

Mr. BROWN. Perhaps to speak to Mr. Scheuer's remark about the mountaintop, I could respond to this in, first, by saying I have said and I repeat that legislation in the area of telecommunications is a desirable thing. We are dealing with a 1934 act. Aside from its antiquity, it has the regulation principles, instead of the competition principles.

In other words, it is upside down. Clearly there are things that are occurring in 1982 which have no connection to 1934, and a careful study of what is needed should produce legislation which could perhaps clear those defects.

I would add to that however, that this consent decree has made a massive change in the telecommunications situation in this country. And I would think that the Congress would like to take a look at bills which have been crafted under the present situation to solve problems which were detected and assumed under that situation.

Look carefully at what the situation will be under a completely divested operating, local operating company situation in serving about 80 percent of the telephones. This situation I cannot emphasize too much is a massive change. I do not think any of us know where it will have an effect or what effects it might cause in telecommunications policy under the existing act. And, so, I would just

suggest very sincerely that the matter not be rushed into legislation, but be looked at very carefully with an understanding of what is now happening.

Insofar as employee rights are concerned, employee rights are not affected by this. Most all of the bargained-for workers are under contracts which will be maintained or are valid. They now exist with the operating telephone companies and will continue to exist so. Pension plans are sound and will not be affected. I do not feel employee rights, the employee-rights problem is of any significance and needs legislation at this time.

The Congress may decide otherwise, but you have asked my opinion. I do not feel it is of any real significance. Insofar as the FCC being given the power to forbear regulation, I believe they want this. I think it is in accord with the philosophy of today's deregulatory principles.

I would caution, however, that to put a government agency, any government agency in a position of allocating the market by judging what is competitive and what isn't, is a matter I would hope the Congress would not do. I don't believe the American people are interested in a government-managed cartel with respect to long-distance communication, and I would hope that would not occur. As far as mechanisms to assure high-quality service at low cost, I certainly believe this should be the principles of any legislation. It ought to be studied out carefully because the mechanism is currently there today and can be used, is being used by the regulators. I do not see an immediate need to establish different kinds of regulatory schemes.

Mr. RINALDO. Do you agree with the provision that is currently in the legislation in that regard?

Mr. BROWN. Which legislation?

Mr. RINALDO. H.R. 5158 regarding access charges and access surcharges.

Mr. BROWN. I am sorry, sir. I came here to answer questions on the consent decree. I am no poet on this legislation. I would rather not try to answer that.

Mr. RINALDO. I understand. I would appreciate it, Mr. Chairman, if we would give Mr. Brown and his counsel the opportunity to review that provision and give us the benefit of their thinking on it because I feel it is an integral part of this entire matter.

Mr. WIRTH. We would appreciate it if you would, Mr. Brown. I might add that we will leave the record open for further comments by you or Mr. Trienens or by Members, and also for questions that I know a number of Members would like to submit for the record for you to answer.

Mr. BROWN. Fine, sir.

Mr. RINALDO. I just want to conclude with one further question that ties right into this rate question.

Do you agree or disagree with a statement attributed to your president which received quite a bit of publicity, and I have a reputable newspaper, the Christian Science Monitor, in front of me in which William Ellinghouse told reporters that local phone rates would possibly double or triple as the phone company spins off its local operating companies. This has caused a tremendous amount

of consternation with my constituents and I am sure the constituents of other people on this panel.

I would appreciate your view as to whether or not this is an accurate statement, or an off-the-cuff statement that you are ready to discredit.

Mr. BROWN. I am not in the business of discrediting my chief operating officer. But, I do have to say that there has been a good deal of confusion. He may have been talking about one jurisdiction in which the rates are low, and these factors of which I talked might involve this kind of an increase. He surely was not tying this kind of an increase to the decree.

Mr. RINALDO. What do you think the increase will be on the average?

Mr. BROWN. It has been going up at the rate of about 4 percent. Due to the factors I talked about earlier in my statement it will go up in the future not because of the divestiture decree at all, but because of other reasons of which I spoke, in the order of 8 to 10 percent.

Mr. RINALDO. Thank you.

Mr. WIRTH. Mr. Brown, you will be happy to know the final questioning will come from the gentleman from California, Mr. Moorhead.

Mr. BROWN. Mr. Moorhead, how are you, sir?

Mr. MOORHEAD. Very good. The settlement provides that A.T. & T. shall submit a reorganization plan to the Justice Department within 6 months to complete the reorganization 1 year later. Do you believe this is a realistic timetable?

Mr. BROWN. Yes, sir, I believe we can do this.

Mr. MOORHEAD. Most of the legislation being prepared would have given you a longer period of time?

Mr. BROWN. I would like to point out in that connection that it is not in our advantage to delay this at all, primarily because of the financing matter. We must finance these companies. We have a very large construction program. As long as there is a question in the market, we have problems.

Mr. MOORHEAD. One question that has come up several times in this discussion period relates to the employees. I would agree with you that legislation is probably not necessary there. But I know that out there in the field where a lot of the employees of the telephone company are concerned, I think the sooner they can be told where they stand, what their rights and benefits will be, the better off everyone will be.

For one thing, of course, the people on the coast, many of them have had stock options with A.T. & T. Many are owners of stock in A.T. & T. What their rights would be there is something else.

Mr. BROWN. No, sir, we don't have any stock options. Many of them are shareowners of A.T. & T. That is correct.

Mr. MOORHEAD. Some of them got stock through the years on a reduced basis, have they not?

Mr. BROWN. They have bought stock over the years, yes.

Mr. MOORHEAD. Yes. I know they are concerned their rights would continue on the same basis if possible, or higher level, and they are concerned with that. I think it would be a good idea that, as soon as it can be done, they find out about that.

Mr. BROWN. Mr. Moorhead, I really do agree with you. I understand the turmoil that this, as I say draconian change has induced in Bell system people. I am anxious to move it along as quickly as I can.

Mr. MOORHEAD. Was there consultation with the Department of Defense about the settlement?

Mr. BROWN. No, sir, not about this settlement. I told the Department of Defense about it but we did not consult with them in regard to this particular settlement.

Mr. MOORHEAD. Is it your understanding that this agreement addresses national security and emergency preparedness concerns?

Mr. BROWN. Yes, sir, there are clauses in the agreement which address this specifically.

Mr. MOORHEAD. Is the DOD then going to be brought in on a consultation basis?

Mr. BROWN. Yes, sir, we are already in consultation with the DOD people. And we have assured them that to the very best of our ability we will respond to defense needs. I believe we can do so.

Mr. MOORHEAD. They will have a voice at least in whatever is arranged?

Mr. BROWN. Yes, sir, in the arrangements that are set up, we are talking with them now about that.

Mr. MOORHEAD. Under H.R. 5158 the bill requires that A.T. & T. form a separate subsidiary, that it engage in competitive activity only through this separate subsidiary. Moreover, the separate subsidiary is required to have very substantial outside investors. How do you believe the decree will affect this provision?

Mr. BROWN. The decree does not deal with that, sir.

Mr. MOORHEAD. You don't think it would have any effect on it?

Mr. BROWN. As you may know, sir, we object strenuously to a provision in law which would require minority, that is, non-Bell ownership of its own subsidiary. As time goes on and the subsidiary is required to raise money, it gives a very difficult problem and really amounts to divestiture of the subsidiary on a slow basis.

Mr. MOORHEAD. There is one provision of the agreement I do not know how anyone will ever enforce. I am sorry, H.R. 5158. It prohibits employees who work for the separate subsidiary from communicating with A.T. & T. employees. How would you ever keep people, many of whom are friends, from communicating?

Mr. BROWN. I don't see how this is an enforceable procedure, sir. It does not seem practical nor does it seem to me to have any necessity. We do intend, regardless of legislation, regardless of the decree, we do intend to set up a separate subsidiary in order to conduct our deregulated or nonregulated businesses.

We intend to assure the regulators and anybody else who wants to know that we do have a clear line between the regulated business and those which are not regulated. I do not think such provisions as you cite are necessary.

Mr. MOORHEAD. There is one final question I wanted to ask you.

You know, many of us feel we have had the best possible telephone system in the world, with A.T. & T. perhaps having the vast majority of it, although there are smaller companies involved. Is there any way you can break up this system that we are doing now, as many of the bills would do, and still be able to maintain

the same potential, the same high quality of service that we have had and expect in this country?

Mr. BROWN. Mr. Moorhead, as I said earlier in this hearing, this whole thing was not our idea.

Mr. MOORHEAD. No; I understand that. But I am just asking you in spite of whose idea it may be.

Mr. BROWN. And further, I do believe that the efficiencies of horizontal integration as well as vertical integration are beneficial to the telephone system in this country and have been beneficial in the past. We are now entering an arena of competitive environment where the kind of things which worked in a purer monopoly environment will just not work under the new national policy. We have a series of alternatives, and this was the alternative we thought was best for our shareowners and for the public, and it is our job, and I am sure the telephone company people will do this, it is our job to make this change as transparent to the public as is humanly possible. It is to our advantage to do so, and we will surely try.

Mr. MOORHEAD. As a result of this change, regardless of whether it is done by this decree or legislation, will the total telephone bill be going up?

Mr. BROWN. Will the total telephone bill go up?

Mr. MOORHEAD. Is it going up because of what we are doing? I know it is going to go up in the future anyway. Everything is going up. But are we embarking, either legislatively or by decree or whatever we do, on a road that will give the American people a higher telephone bill?

Mr. BROWN. I think over a period of time the long-distance rates will go down relatively, of course, depending on the inflation factor. And as I have talked here today the local rates will go up to a degree. Local rates will still be a bargain. Long-distance rates will be more of a bargain. I think this will balance out.

Mr. MOORHEAD. Thank you very much, Mr. Brown.

Thank you, Mr. Chairman.

Mr. WIRTH. Congressman Marks was unexpectedly and unavoidably delayed this morning for treatment of a very bad back. He regretted that he was not able to be with you this morning, Mr. Brown, and asked that his opening statement be included in the record after the other opening statements. Without objection it will be included in the record at that point.

I think we all, Mr. Brown, feel that this was an enormously helpful morning. The issues you addressed in your written testimony and comments today related to local rates, access charges, and equipment issues that have been discussed earlier. Second, the integrity and quality of the local service and the Bell operating companies, local operating companies. Third, the cross-subsidy issue, the clear line that you were talking about here. Those three I think you addressed this morning and remain of great concern to members of both subcommittees as you heard this morning.

Another issue that came up this morning that has always been of concern to members of the subcommittee I chair, and also of members of Mr. Rodino's subcommittee, is the issue of employee rights. There are provisions in the bill I drafted and in the Senate bill on this issue which must be addressed.

The patent issue on which we have been working with the Judiciary Committee has to be addressed. Finally, all of us agree with the need for regulatory reform giving the FCC the ability to forbear from regulating in certain areas. Those are the six fundamental issues that I think most of us believe must be addressed with legislation and must be addressed very quickly. I hope we can look forward to working with you and your very able staff in the development of that legislation.

Our next hearing will be this coming Thursday morning in the Judiciary Committee room under the chairmanship of Mr. Rodino; 2141 Rayburn House Office Building at 9:30 a.m., day after tomorrow.

Mr. Brown, Mr. Trienens, thank you very much for being with us and, my colleagues, thank you for your very good questioning and a very good morning.

Thank you, Mr. Brown.

Mr. BROWN. Thank you, sir.

[Whereupon at 12:40 p.m., the hearing was adjourned to reconvene at 9:30 a.m. Thursday next.]

PROPOSED ANTITRUST SETTLEMENT OF UNITED STATES VERSUS A.T. & T.

THURSDAY, JANUARY 28, 1982

HOUSE OF REPRESENTATIVES, SUBCOMMITTEE ON TELECOMMUNICATIONS, CONSUMER PROTECTION, AND FINANCE, COMMITTEE ON ENERGY AND COMMERCE, AND SUBCOMMITTEE ON MONOPOLIES AND COMMERCIAL LAW, COMMITTEE ON THE JUDICIARY,

Washington, D.C.

The subcommittees met, pursuant to notice at 9:10 a.m., in room 2141 of the Rayburn House Office Building, Hon. Peter Rodino (chairman of the full Judiciary Committee) presiding.

Mr. RODINO. The committee will come to order. This morning I would like to welcome the members of the Subcommittee on Telecommunications, Consumer Protection, and Finance to the second day of our joint hearings on the A.T. & T. settlement. Because we have a recess before 11 a.m. to attend a joint session honoring President Franklin Roosevelt, I am going to dispense with any opening remarks so we can get right into the testimony.

Before doing so, however, I would like to ask Chairman Wirth of the Subcommittee on Telecommunications if he would like to make any opening remarks.

Mr. WIRTH. Just very briefly. Thank you, Mr. Chairman, and members of the subcommittee for hosting us in the Judiciary Committee. I expect that this morning's session with Assistant Attorney General Baxter will be as fruitful as Tuesday's session with Chairman Brown.

The modification of the 1956 consent decree agreed to by A.T. & T. and the Government will clearly have a far-reaching impact not only on the Bell System but on the entire telecommunications industry. Still, I think it is very important for us to remember and to keep clearly in mind that the settlement does not deal with many issues that directly affect rates for local telephone service. It does not insure maintenance and improvement of our telephone system's high quality, particularly at the local level. It leaves unresolved issues that affect the development of full and fair competition in the telecommunications industry. The proposed settlement blurs the line between Federal and State regulatory jurisdictions. It does not, and it cannot, overhaul the FCC's machinery to enable the Commission to deregulate competitive markets.

These are some of the issues that must be dealt with in legislation. They are not diminished. As I suggested last week, and on

Tuesday, these are issues that we must deal with in the legislative framework, for they cannot be resolved in the settlement.

The settlement didn't create these issues, but it has brought them into starker relief. As I have said on many occasions, and as our hearing on Tuesday reflected, we all feel a sense of urgency to pass legislation very expeditiously to supplement, to reconcile and make workable the settlement agreed upon last month. Thank you very much, Mr. Chairman.

Mr. RODINO. Mr. McClory.

Mr. MCCLORY. Mr. Chairman, thank you. I am aware also of the time constraints, and I want to just extend a brief welcome to Assistant Attorney General Baxter. I note that this is his sixth appearance before our committee, so he has been making himself very available to us and I appreciate it, as I'm sure my colleagues do.

The only other thing I would like to say is, I would want to commend him on moving rapidly and decisively toward terminating the two drawn-out antitrust cases that he found when he entered the Department. I commend him on that and hope that we can cooperate legislatively to bring these cases to a final termination to the extent that any legislation is needed.

I look forward to your testimony. Thank you, Mr. Chairman.

Mr. RODINO. Our witness this morning is the Assistant Attorney General, William F. Baxter, in charge of the Antitrust Division.

We welcome him this morning. He has prepared testimony on both the A.T. & T. matter and the IBM settlement. However, in order that we may accommodate the members of the Subcommittee of Telecommunications who are interested in the A.T. & T. settlement, we will first dispose of those matters relating to A.T. & T. and then proceed with the testimony and questions relative to IBM.

Mr. Baxter, please go forward with your prepared testimony.

STATEMENT OF WILLIAM F. BAXTER, ASSISTANT ATTORNEY GENERAL, ANTITRUST DIVISION, DEPARTMENT OF JUSTICE

Mr. BAXTER. Thank you, Mr. Chairman. I welcome the opportunity to come today and talk about the disposition of these two very important cases. Their disposition represents the most important thing I have done, I think, since my assuming this role. And I fully understand the interest of the committees in discussion of them both.

As you said, Mr. Chairman, I have prepared testimony on both cases, and I have submitted that to the committee, and understand that it will be included in the record. Realizing from your own abbreviation of your own introductory remarks the time pressures the committee is under, I think perhaps it would be best for me, too, to be quite brief in any opening statement I make, and give the committee a maximum opportunity to ask such questions as it wishes.

Confining myself as you have indicated that you would prefer for the moment to the A.T. & T. case, I will simply say that when I took office last February, I made that my No. 1 item of business. I spent most of the months of February and March studying the

case—its pleadings, and the stipulation packages that had been prepared. I satisfied myself relatively easily of two things. One was that the theory of the case was sound. The second was that evidence of the conduct that we claimed had occurred was persuasive, readily available to be proved and included in the record. And, as I said at a press conference in April which received rather more attention than I had hoped or expected, I intended to go forward with the case vigorously.

The original relief requested in the case seemed to me a little diffuse. I was anxious to have the relief proposals clarified and sharpened last spring to focus on what I believed the structural problem to be; namely, the combination in one enormous enterprise of natural monopoly, regulated functions, and functions which could not be so described. And relief contentions in the case and my own statements over the intervening period indicate quite clearly the relief we were seeking—again, precisely, the separation of the regulated natural monopoly functions from the potentially competitive activities of the company.

In the early days the A.T. & T. Co., exhibited no particular interest in that approach to relief as a basis for settlement discussions. Of course, as a consequence, the litigation went on. In December, it became clear that the company was willing to think about that kind of structural change as a basis for settlement. And, from that point forward, things moved fairly rapidly.

We have negotiated a consent decree which, in my view, will achieve precisely the objectives of the lawsuit, and which I would have to say in my view represents the most significant victory, not just for the Antitrust Division, but far more importantly, the American people, in the field of antitrust at least since 1911, and, I would say, since the passage of the Sherman Act in 1890, as the relief granted in the Standard Oil case of 1911 was not particularly sound from a structural standpoint.

I know you are interested in the substantive content of the proposed modification of the 1956 decree. Let me take only a moment and say a few words about the procedural setting as of the end of the year and why we went about wrapping the thing up as we did.

If you will recall the procedural setting immediately antecedent to the steps we took on January 8, you will recall that we had litigation with A.T. & T. proceeding on a number of fronts. First of all, the decision of the FCC in computer II had been appealed and was pending before the Court of Appeals for the District of Columbia. After the FCC's decision had been issued, the A.T. & T. Co. sought an order of interpretation from Judge Biunno in New Jersey, a request which Judge Biunno had granted. And we had appealed that order of Judge Biunno to the Court of Appeals for the Third Circuit, so there too, we had an open litigation front with A.T. & T. And, of course, there was the 1974 antitrust case pending here in the District of Columbia.

Any settlement that was satisfactory in my view had to bring to a close as many of those controversies as was possible. In particular, it was operationally impossible to settle the 1974 litigation along any such lines as we had in mind without simultaneously disposing of the 1956 decree, which was not only in a different circuit, but in some technical senses was not even before the judge be-

cause of the outstanding appeal from the 1956 clarification or interpretive order.

We had to get those two cases together somewhere. I was determined that the place was here, and the judge was Judge Greene. And so, the effort was essentially to get the 1956 case down here. To that end we did a number of things. First of all, we dismissed the appeal from Judge Biunno's order so as to reinvest him with jurisdiction over the earlier case. We thereupon filed a joint motion to have the case transferred down to the District Court in Washington. We filed the agreement we had reached as a modification of the 1956 decree so that as a procedural matter we would have only one case going, rather than two when it did get transferred down to Judge Greene.

And having done all those things, we dismissed the 1974 case that was pending here in Washington. At this time the case is in precisely the procedural posture that I contemplated when we did all these things. There is one case technically, a case commenced in 1949 and which resulted in the 1956 decree, with a proposal to modify that decree. It is pending in Judge Greene's court here in Washington, the judge who by all measures is most familiar with the current state of the industry and the history of conduct with which we have been involved.

It is our view that the Tunney Act does not by its terms apply to modifications of decrees. A very large fraction of modifications of decrees are utterly trivial in their import. To suppose that the Tunney Act applied to them all, with the consequent obligations to publish in the Federal Register the sometimes voluminous papers which are involved, papers whose length bear no necessary correlation to the importance of the modification which is under consideration, would seem to me a serious misinterpretation.

Nevertheless, because this matter was of considerable importance, although many modifications are not, we also jointly urged that the judge hold the hearings, and indicated that we would in this case make the publication in the Federal Register.

In short, we proposed to proceed on a discretionary basis, just as if the Tunney Act did apply. And it would be our intention in general to follow Tunney Act-like procedures in situations where modifications of significance were involved, although, as I say, as a matter of statutory interpretation we do not think the Tunney Act by its own terms does apply.

Mr. RODINO. Mr. Baxter, right at that point, I don't usually interrupt. But, I think that this is an important point that you are making. I would like to address this question to you.

What will happen if Judge Greene determines that the proposed settlement is not in the public interest? Then what happens insofar as the Tunney Act and its provisions are concerned? Would the judge still have the power to continue the 1974 proceeding as envisioned by the Tunney Act?

Mr. BAXTER. We have the power to continue that proceeding, yes. We were very careful to dismiss the 1974 case without prejudice. And we are free to resume that litigation.

Mr. RODINO. What about Judge Greene? I mean, you are saying you have the power. What about Judge Greene?

Mr. BAXTER. Judge Greene does not, himself, have the power to resume the litigation. But of course, as a practical matter, a judge never has the power to resume litigation.

If the plaintiff does not show up in court, there is not much a judge can do to continue litigation in any set of circumstances. So, they do not view——

Mr. RODINO. What if he determines that you are not complying with the spirit of the Tunney Act, and he feels that that settlement is not in the public interest? What does he do then?

Mr. BAXTER. Of course, he can reject the settlement, just as he could reject the settlement under the terms of the Tunney Act, and ask us to proceed, at which point we would resume litigation of the 1974 case. I do not see Judge Greene's posture is different in one iota under the procedures that we have suggested than his posture would be if the Tunney Act actually by its terms did apply.

Mr. RODINO. Then why was this done?

Mr. BAXTER. Why was what done?

Mr. RODINO. The fact that you are now proceeding with this kind of settlement, and, yet, feel that you are technically not bound by the Tunney Act, and insist on making this distinction.

Mr. BAXTER. As I explained, we had to get the two cases together, or the whole of the set of the controversies together before one judge. And I wanted them before Judge Greene. We could have filed a consent decree in the 1974 case and then gone up and tried to transfer the 1956 decree down here. And then we would have had to make a motion to vacate the 1956 case as part of the proceedings down here.

One could imagine alternative procedural ways for going about all that. The simplest, cleanest way was the way we did it, in my judgment. And I must confess that I see no difference whatsoever between Judge Greene's posture as we have created the situation, and what his posture would have been under the Tunney Act.

The applicability or nonapplicability of the Tunney Act, since I intended to urge that its procedures be followed, simply was not a significant consideration in my decision to do it one way, rather than another.

Mr. RODINO. I understand that. Mr. Baxter, since there has been so much made about whether you are bound by the Tunney Act, or whether or not you will comply with it, I guess the bottom line—and I believe that you have set my mind at rest—is that you do intend to comply with it nonetheless.

Mr. MCCLORY. Would the Chairman yield?

Mr. RODINO. Would you let Mr. Baxter respond?

Mr. BAXTER. We certainly do. I have always intended to parallel the procedures contemplated by the act. On the other hand, I do feel very strongly, Mr. Chairman, that we do not want to be forced into the position of publishing reams of material in the Federal Register—the publication costs necessary to comply with the Tunney Act in some cases have run to hundreds of thousands of dollars. If there is nothing of public moment involved in a modification, I would very much resist being faced with an interpretation that says the Tunney Act applies in general——

Mr. RODINO. I agree with you wholeheartedly. I am talking about substance. I am talking about the public interest being served ulti-

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mately. That is all. I am sure that what you have stated has set my mind at rest. I am not asking that you justify some kind of procedure that maybe we could quibble over. That is not my concern.

Mr. BAXTER. No. I am sure you will be satisfied with the way this particular matter is handled in that respect, Mr. Chairman.

Mr. RODINO. Thank you very much.

Mr. MCCLORY. I just want to ask this one question for my clarification.

Is there anything, any authority in the Tunney Act which the judge himself is not free to exercise?

Mr. BAXTER. I think that a judge has discretion to do without enabling legislation substantially everything that the Tunney Act contemplates. Even if, contrary to fact, the Justice Department had not affirmatively suggested and affirmatively intended to do this, or if in some other case it did not, the judge himself would always have discretion to follow a procedure paralleling that contemplated by the Tunney Act.

Mr. MCCLORY. Thank you.

Mr. RODINO. Please proceed, Mr. Baxter.

Mr. BAXTER. I am not really sure there is much more that I wish to say, Mr. Chairman. I have explained the procedure that produces the present posture of the matter. I would say only that we are by no means through here. The reorganization remains to be fleshed out. Needless to say, we will be watching that process with great care. My understanding is that the company intends to stay in close contact with us as they work on that problem so that they don't eventually submit something to us at which point we say, "Oh, well, that is totally unsatisfactory." If there are to be disagreements about this, we would like them to be surfaced as early as possible, so that I think we will be deeply involved in working on the reorganization, although the proposed modification, of course, makes that an initial responsibility of the company subject only to approval of the Department of Justice.

We have a lot of work ahead of us, and some potential problems down the road. I can readily imagine reorganizations which I would not find at all acceptable and others that I would find highly acceptable. So, the case is by no means over, but I think we have it in a very promising posture. I think the A.T. & T. Co. is committed to a strong and viable set of operating companies.

Indeed, anything other than that would not be in the interest of their own shareholders, who are going to be the shareholders of those companies. And I am afraid I must immodestly tell you at this point I am quite pleased with the job we have done with the case.

[Testimony resumes on p. 96.]

[Mr. Baxter's prepared statement follows:]

PREPARED STATEMENT OF WILLIAM F. BAXTER, ASSISTANT ATTORNEY GENERAL, ANTITRUST DIVISION

I am happy to be here today to discuss the recent actions of the Department of Justice regarding the AT&T and IBM cases. As you know, on January 8, 1982, the Department and AT&T filed an agreed-upon modification of the 1956 Consent Decree in United States v. Western Electric and AT&T, and stipulated to dismissal of the Government's monopolization case filed against AT&T in the District of Columbia in 1974. Also on that day, the Department stipulated to dismissal of the Government's monopolization case against IBM, a case that was filed in 1969, and that had been pending for some 13 years. The decisions to take these actions were clearly the most important that I have made as Assistant Attorney General. The dispositions of these cases are most significant. I appreciate fully the interest of the Subcommittees in them.

The way in which we have moved to resolve our antitrust controversies with AT&T is one that I hope will be widely recognized as promoting competition in the dynamic telecommunications industry and as doing so in the most efficient way. While the modified Decree does not, and is not intended to, resolve all of the regulatory or legislative issues that may exist in telecommunications now or in the future, it does do what an antitrust decree should in these circumstances--eliminate the key structural barriers to the emergence of effective competition in the industry.

We had two litigation fronts open with AT&T, one involving a 25-year old decree that recently had been interpreted in a

way that had substantial competitive ramifications, the other involving a monopolization case brought by the Government seven years ago, the trial of which was nearing completion. The restructuring of AT&T to which we have agreed, and the accompanying injunctions, resolve both of these controversies.

The 1956 Consent Decree was entered in settlement of an antitrust case filed in 1949 in New Jersey by the Department of Justice. That case charged AT&T with monopolizing the manufacture and distribution of telephone equipment in violation of the Sherman Act. Although the complaint in the 1949 case sought, among other things, the divestiture of Western Electric, the 1956 Decree did not require that divestiture. Instead, the 1956 Decree contained various restrictions on AT&T's activities, including limiting AT&T to providing "common carrier communications services," the rates for which are subject to governmental regulation. The premise underlying that restriction, I think, has been that absent such structural relief as would effectively eliminate AT&T's incentives and abilities to monopolize, confining AT&T to its traditional regulated common carrier communication businesses would ensure against AT&T subsidizing the provision of unregulated services and equipment with revenues derived from its regulated monopoly activities.

In September 1981, the U.S. District Court in New Jersey interpreted the 1956 Decree as permitting AT&T to offer certain equipment and services even though the rates for such equipment and services would not be subject to regulation. AT&T sought this

interpretation after the FCC, in its 1980 Computer II decision, allowed AT&T to offer such equipment and services through fully separated subsidiaries. The Department appealed the district court's interpretation, but in conjunction with its agreement with AT&T on modification of the Decree moved to have the appeal dismissed.

Under the modified Decree, all of the provisions of the 1956 Decree would be eliminated and replaced by provisions requiring AT&T to undertake an 18-month reorganization, after which the Bell operating companies providing local exchange telephone services will be divested by AT&T into one or more companies. AT&T will continue to own a nationwide intercity network composed of its Long Lines Department and the intercity facilities of the Bell operating companies, and will retain ownership of Bell Telephone Laboratories and Western Electric. AT&T will also provide customer premises equipment, including that now furnished by the local Bell companies. AT&T's plan for the required reorganization is to be submitted to the Department of Justice for approval within six months of the effective date of the modified Decree.

The modified Decree also requires the to-be-divested operating companies to provide, on a phased-in basis, exchange access to all intercity carriers equal to that provided to AT&T, and forbids the operating companies from discriminating against AT&T's competitors with respect to procurement, interconnection of equipment or services, the establishment and disclosure of

technical specifications, and the planning of new facilities and services.

Let me explain the reasons for our seeking this modification. Any successful effort to establish a truly competitive telecommunications industry must prevent a dominant regulated carrier such as AT&T from frustrating the emergence of competition, particularly in telecommunications equipment, intercity services, and related information markets. AT&T's control of regulated local monopolies has enabled it to dominate intercity service and telecommunications equipment markets. Through its ownership of exchange monopolies serving 80 percent of the nation's telephones, AT&T has controlled facilities essential to any firm attempting to challenge Long Lines or Western Electric.

The most straightforward and effective way to eliminate AT&T's incentives and abilities to exclude competition from potentially competitive telecommunications markets is to require the divestiture of its regulated local exchange monopolies from those portions of AT&T that engage in competitive and potentially competitive activities. That is precisely what the reorganization required by the modification does. Divesting ownership of local exchange facilities from intercity facilities will eliminate the incentive and ability of a joint provider of local and intercity services to discriminate against other providers of intercity services when such services must rely at some point upon the local distribution network. Similarly, the divested regulated operating companies would not have incentives to discriminate in

favor of Western Electric and against other suppliers of telecommunications equipment. Because the divested operating companies may, for a period of time, retain some institutional loyalty and as a result of inertia continue to favor prior affiliates, the modified Decree establishes basic equal access and non-discrimination requirements to backstop the reorganization in promoting competition in intercity service and equipment markets.

The divestiture of AT&T's regulated local exchange monopolies that is accomplished by the modified Decree obviates the need for the restrictions that the 1956 Decree placed on AT&T. Without its base of regulated local exchange monopolies, there is no longer the same need to worry over the long run about cross-subsidized forays into unregulated markets and, therefore, no reason to restrain AT&T from entering such markets. To the contrary, enabling an enterprise with tremendous skills and resources to enter unregulated markets should increase competition and the pace of innovation in those markets.

We also believe that the modified Decree provides a framework for satisfaction of the concerns of the Department of Defense. Since early spring of last year when Secretary Weinberger, appearing before the Senate Armed Services Committee, indicated his concerns over the relief sought in the 1974 AT&T suit, we have had numerous meetings and discussions with DOD officials to discuss the specifics of our proposals and for us to learn their specific national security concerns. Under the modified Decree, national defense

benefits from an integrated Long Lines, Western Electric, and Bell Labs will continue. In addition, the modification contains specific provisions to ensure continued centralized coordination among local Bell operating companies to meet national security and emergency preparedness needs.

Many have speculated that the restructuring required by the modified Decree will necessarily lead to sharply higher rates for local telephone service as subsidies from long distance revenues are removed. In fact, the Decree itself will have no such effect. The current subsidy system would have been subject to some pressure from competition in long distance service in any event. Moreover, there is nothing in the modified Decree that would prevent federal or local authorities from generating a local service subsidy through local exchange access regulation. Indeed, the issue of whether to continue such subsidies is presently being reviewed by a joint federal-state board under the auspices of the FCC.

Agreement upon the modified Decree made it unnecessary to continue litigating the Government's 1974 monopolization case against AT&T. That case alleged that AT&T had monopolized certain telecommunications services and equipment markets. Trial began in early 1981 and was scheduled to resume on January 12 and be concluded in February. The reorganization achieved by the modification of the 1956 Decree is nearly identical to the relief that had been sought by the Department of Justice in the 1974 litigation, and, together with the injunctive provisions in the modification, substantially achieves the purpose of the 1974

case. Accordingly, the Government and AT&T stipulated to dismissal of the 1974 case without prejudice.

Concern has been expressed about the procedures to be followed in connection with the entry of the modified Decree. It is and always has been the intention of the Department, and AT&T, to follow the procedures of the Tunney Act in this matter, in order to allow opportunity for comment by others and a complete exposition of the modification's merits. The Decree will require a basic restructuring of the telecommunications industry, and thus necessarily affects vital public concerns. While we believe that the Tunney Act does not by its terms apply to modification of existing decrees, most of which involve minor adjustments of concern only to the immediate parties, the Act's procedures and standards can help facilitate thorough review of major decree modifications. Accordingly, we have followed comparable procedures in connection with major decree modifications in the past.

It has also always been our intention to follow the Tunney Act procedures here in the District of Columbia. We believe that Judge Greene, who as a result of the trial of United States v. AT&T has substantial expertise in the telecommunications industry and the effects of restructuring, is uniquely qualified to make the determination that the modified Decree is consistent with the public interest. Therefore, upon filing the proposed modification in the U.S. District Court in New Jersey, the Government and AT&T moved to have jurisdiction over the 1956 Decree, and any proceedings relating to its modification, transferred to the District Court in Washington.

As the Committee knows, the District Court in New Jersey unexpectedly entered the modified Decree on January 11. While we appreciated that Court's view of the merits of the modification, we remained committed to thorough review in the District of Columbia using Tunney Act procedures. On January 14, 1982, Judge Biunno entered an order transferring the matter here. On January 21, 1982, Judge Greene, to whom the matter has been assigned, vacated the order entering the Decree and set out the procedures--identical to those of the Tunney Act--that he intends to follow. We intend promptly to take the steps required by Judge Greene's order. In short, we are following the Tunney Act path that we have intended to follow all along.

Finally, it is obvious that the changes in industry structure to be brought about by the Decree will have to be taken into account in assessing the need for and content of pending or future telecommunications regulation or legislation. Complex regulatory provisions designed to guard against anticompetitive cross-subsidization by AT&T are probably no longer necessary. There may be other issues not so directly related to competition that deserve regulatory or legislative attention--for example, the question of whether or how to subsidize local telephone service in a competitive environment--but I would defer comment on such matters at this time.

I would like to turn now to my decision to dismiss the Government's case against the International Business Machines Corporation. When I came to the Department in early 1981, I was only generally familiar with the case. I knew, however, of the

public controversy as to its merits, and that it had consumed tremendous governmental, judicial, and private resources. I determined to make a decision about how to proceed with the case as soon as possible.

Some substantial efforts to review the case had been made not long before my arrival. In 1979, during the appeal of IBM's effort to remove the District Court judge from the case, the Second Circuit suggested that settlement would be in the best interest of all concerned. Not long thereafter, in November of 1979, the Antitrust Division assembled an internal task force of lawyers and economists to review the merits of the case with a view toward exploring different approaches to settlement. By the summer of 1980, this task force, aided by economic and technical consultants, completed its review of the merits of the case and various relief options. During the summer and fall of 1980, my predecessor, Sanford Litvack, met with the trial staff and with IBM counsel to discuss settlement possibilities. Nothing came of these discussions, however.

Upon my arrival in the spring of 1981, I reviewed the work that had been done on the case thus far. Between September and December of 1981, I held several meetings with the trial staff, alone and with counsel for IBM. I also reviewed materials submitted to me by the trial staff, the reports of the earlier task force, and met with senior Division attorneys and economists familiar with the case. I concluded that, in light of the state of the record and the state of the computer industry today, the

case presented very substantial problems. There were problems with market definition, with evidence of bad conduct, and with relief.

In order to prove a violation of Section 2 of the Sherman Act, the Government has to define and prove the market that the defendant is alleged to have monopolized. This task was made particularly difficult in the IBM case because the market continued to evolve as the case proceeded. The Government defined the market as that for large general purpose computer systems optimized for business use. This definition had become increasingly troublesome as computer systems became more powerful and were adapted to a greater variety of uses throughout the 1970s. The advent of distributed processing and the introduction of minicomputers with computing power comparable to that of the largest systems of earlier years created a definite litigation problem. The market we had defined had begun to seem either outdated or amorphous.

There were also theoretical and factual problems with our evidence of monopolizing conduct, or "bad acts." The theoretical problems of the case had been accentuated by recent judicial decisions that addressed the nature of the conduct that must be proved to establish monopolization. Briefly, the courts have shown a heightened awareness of the social benefits of aggressive competition, even by firms with large market shares, and an appropriate reluctance to equate such competition with the type of predatory practices condemned by Section 2. These courts,

and I include the Second Circuit as evidenced by its decision in Berkey Photo */ in this category, rightly have begun to consider the consumer benefits of conduct that is alleged to have excluded competitors. At least by today's legal standards, the theoretical underpinnings of the IBM case were uncertain.

There were also factual problems with our evidence of bad acts. For example, perhaps the strongest evidence of predatory conduct concerned the prices IBM set for its System 360 Model 90 computer in 1964. Evidence introduced tended to support the conclusion that IBM set prices for this computer system at such a low level that the company did not realistically expect its sales revenues to cover the costs of developing and manufacturing the machine. However, there were problems even with this episode. First, the 360/90 was not offered in the market we alleged to have been monopolized, that for general purpose computer systems optimized for business use. The 360/90 was a very powerful computer offered in the scientific market, a "number cruncher." Thus, the nexus between this pricing conduct and the maintenance of the monopoly we set out to prove is problematic. Also, there was relatively little evidence that IBM's pricing of the 360/90 was effective in maintaining monopoly power. It was offered in competition with Control Data Corporation's largest computer,

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*/ Berkey Photo, Inc. v. Eastman Kodak Co., 603 F.2d 263 (2d Cir. 1979).

the 6600; Control Data manufactured far more of these systems than did IBM.

By way of further example, there was also evidence that for competitive reasons IBM rushed to market its System 360 Model 67 computer system, its first model designed to offer time-sharing, and did so with an awareness that it might not be profitable. Here, however, the evidence of predatory intent was much more ambiguous than was the case for the Model 90. IBM believed it was very important to develop a time-sharing system, which was perceived as the wave of the future. Many of the problems IBM encountered with the Model 67 were unforeseen and were also experienced by its rivals. There was little evidence that IBM's conduct in this episode had the effect of maintaining its power in the market for general purpose computer systems.

Finally, there were allegations in the case that IBM changed the interfaces on its computer systems--the ways in which the various components in the systems were connected--in a manner intended to harm emerging competitors that offered peripheral computer devices designed to be used with IBM systems. The problems with this allegation arise from the difficulties in asserting that design changes in computer systems can amount to Section 2 violations when they at least arguably represent improvements in the design of the systems. The fact that four of the peripheral manufacturers themselves sued IBM on the basis of this evidence and that IBM won all four suits certainly dampened whatever confidence the Division once had about prevailing on these episodes.

Thus, it was far from clear that we would win this case. Unfortunately, what relief we would seek if we were to win it was equally unclear. In a civil Section 2 case, there are two general types of relief that can be sought: injunctive and structural. Injunctive relief involves framing rules for the defendant to follow that are designed to prevent the illegal acts of the past and open the way to unfettered competition. The challenge in framing injunctions is to make them general enough to prevent easy evasion yet specific enough to amount to more than a simple restatement of the antitrust laws. Specific, detailed injunctions are particularly difficult to draw up in such an innovative and rapidly-changing field as computers. Such injunctions require continued monitoring and there is always a danger that regulatory-type injunctions may inject an artificial restraint that interferes with procompetitive responses to market forces. In the long history of the IBM case, no one to my knowledge ever proposed injunctions that would be both responsive to the evidence in the case and likely to improve performance in the industry.

The problems with possible structural relief in the IBM case were even more substantial. Structural relief involves realigning the structure of the defendant, most commonly, as in the AT&T modification, through the divestiture of assets. Structural relief in IBM likely would have involved splitting the firm up into two or more entities. The first problem with such an approach was that it seemed far out of proportion to any violation that

we possibly could have shown. Also, in stark contrast with the AT&T situation, there was no obvious way to restructure the firm and thereby guarantee a procompetitive result. Splitting up an integrated firm of IBM's size, scope, and complexity would present mammoth practical problems. There is no assurance that a restructured IBM would perform more efficiently than it now does and there is a substantial possibility that it would perform considerably worse. Structural relief in the IBM case seemed to me wholly inappropriate.

I thus was presented with a case that had dragged on for 13 years and was likely to continue for years more if the Government were to prevail, that was costing the Government millions of dollars, that was not proceeding in our favor, and that posed very substantial relief problems in any event. Had there been substantial factual and legal merit in the case, I would have ordered its continuation, notwithstanding its expensive history. While I believe that efforts to streamline such cases are important and should continue, I do not believe that the Government should shy away from meritorious cases because they may be complex, expensive, and time-consuming. I think the AT&T case shows that the Antitrust Division will continue to litigate aggressively when we are convinced of the merits of our cause, regardless of its complexity. In IBM, I was not so convinced.

It might have been possible in these circumstances to seek a cosmetic settlement with IBM, more as a face-saving gesture

than anything else. However, I did not think that such a settlement would speak well for the integrity of the Department or serve the public interest. I therefore decided to dismiss the case. It was not an easy decision, but it was a decision on which I will stand.

Before closing, I would like to say a few words about the many Division attorneys and other professionals who worked on this case for the past 13 years. I realize that in many ways this was a thankless task. The trial staff was located in New York, away from day-to-day contact with and support from the rest of the Division. They were litigating against aggressive attorneys, with far better resources and staff support. Nonetheless, the members of the trial staff did their best, against considerable and growing odds, to win the case to which they had been assigned. Their work on the case has clearly reflected their effort and dedication.

Mr. Chairman, this concludes my prepared remarks. I will be glad to address any questions you may have.

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Mr. RODINO. Mr. Wirth.

Mr. WIRTH. Thank you very much, Mr. Chairman.

Again, Mr. Baxter, we are glad to have you here. You have conducted yourself with distinction at the Justice Department.

Under the definitions in the settlement, are Yellow Pages considered to be information services —which go to the parent—or directory services—which stay with the local company?

Mr. BAXTER. The decree does not make any reference to Yellow Pages, as you have indicated. The situation with the Yellow Pages is that one must think about the Yellow Pages in a less aggregated way than the use of the term "yellow pages" initially brings to mind.

Mr. WIRTH. Let me ask you this. Are Yellow Pages transferred to the parent company in that 18-month period of time?

Mr. BAXTER. Yes; in the following sense. In order to prepare Yellow Pages, one needs to take a lot of functional steps. One has to solicit display advertising. One has to make printing matter, one has——

Mr. WIRTH. With the limited period of time, let me ask you, if Yellow Pages is transferred under your understanding of the settlement in 18 months, why did Mr. Brown's letter of January 25 to Senator Packwood say that they would phase the Yellow Pages out of the local companies over 4 years?

Mr. BAXTER. Well, there are two confusions involved there. There is no relationship whatsoever between what I am talking about and Mr. Brown's commitment, which is totally collateral to that. What I am doing is resisting the word "it" in your statement. "Does 'it' get transferred to A.T. & T." because it is not an "it," it is a "they." The potentially competitive activities of soliciting advertising, printing, distributing the Yellow Pages goes to A.T. & T. But it is not in any of those functions that the very, very substantial profitability of the Yellow Pages is inherent. What makes the Yellow Pages, or has made them very, very profitable for the A.T. & T. Co. is that the A.T. & T. Co. has monopoly power over a machine-readable listing of local business telephone numbers. You must have that listing in order to be able to prepare Yellow Pages.

Mr. WIRTH. Does A.T. & T. have the same kind of flexibility in deciding when to transfer terminal equipment under your understanding of the settlement?

Mr. BAXTER. I will have to come back and think about terminal equipment separately. My point is that although the competitive activities with respect to the Yellow Pages go to the parent company, it inherently continues to be the case that the local operating companies have exclusive possession of the computerized listing of local businesses. And they will be in a position to auction it off to the highest bidder, which may or may not be the A.T. & T. Co.

So, the basic operating companies will continue to be in a position to gather all the supracompetitive profits that have ever been associated with the Yellow Pages because of their exclusive possession of the computerized listing.

One must say, yes, the Yellow Pages in a sense go to A.T. & T. One must not lose sight of the fact that all the supracompetitive profits remain with the operating companies. Mr. Brown's promise the other day was in the nature of a guarantee expressed to Mr.

Packwood that they would protect the income position of the local operating companies should that become necessary by remitting profits from Yellow Pages——

Mr. WIRTH. So, there are a lot of ambiguities surrounding Yellow Pages. Let's move on.

It is my understanding at this point that Bell Labs has a very significant patent portfolio that touches just about every part of the telecommunications industry.

Last Monday you told the Senate committee that patents developed before divestiture remain subject to the licensing provisions of the 1956 decree. On Tuesday, in response to a question asked by Chairman Rodino, Mr. Brown said the new applicants would not have guaranteed access to Bell's patent portfolio. Who is right on the patent issue?

Mr. BAXTER. The 1956 provisions will disappear if the modification is accepted. It contains no provision for continued licensing. The patent portfolio of the Bell Laboratories has been subject to mandatory licensing under the 1956 decree for a period of many years. And there are a very, very large number of licenses outstanding at the present time.

Those licenses would of course continue in effect. So far as I have been able to find out, all those licenses run for the full life of the patent. There is at present access by a large number of competitors to the technologies covered by that patent portfolio, and that will continue to be the case. Mr. Brown's answer had to do with new applicants, people who have not heretofore taken advantage of the opportunity to apply for licenses under the 1956 decree, or more accurately yet, people who do not make such applications between now and such time as the 1956 decree disappears. The 1956 decree, today and tomorrow, of course, is still in place, and people can still make applications. But Mr. Brown is quite right. Once the 1956 decree is displaced by the modification we have proposed, then, of course as to newly invented and newly patented inventions, but also, as Mr. Brown said, as to the existing patent portfolio, one who has not by that time made application for his license under the terms of the 1956 decree would no longer be entitled mandatorily, to a license under it. He could of course negotiate——

Mr. WIRTH. To finish off, how does the ratepayer get compensated for those patents which that ratepayer has paid for over a period of time after divestiture occurs? Or does your plan fail to provide for the ratepayers to be compensated for patents they have financed?

Mr. BAXTER. By continuing to collect—oh, the rate—no. As a practical matter the ratepayer will cease to be compensated as of the time the 1956 decree disappears, except to the extent that funds are put into the operating companies that correspond to revenues that have been collected over the years.

Mr. WIRTH. Thank you very much.

Thank you, Mr. Chairman.

Mr. RODINO. Mr. McClory.

Mr. MCCLORY. Thank you, Mr. Chairman.

My question is this: We lift the ban on A.T. & T. acquisition of independent companies by vacating the 1956 decree. Now, on page 5 of your testimony today you appear to justify that by stating that

the need to worry over the long run about cross-subsidized forays into unregulated markets will disappear. Aren't you worried at all about subsidies from regulated long lines flowing into the unregulated markets? It is my understanding that intrastate, at least, there are long lines which I guess A.T. & T. will take over, even though they are going to be operated by and serve the local operating companies.

Mr. BAXTER. No; they won't be. They will be operated and served by A.T. & T. Co., notwithstanding that they are intrastate.

Mr. MCCLORY. When you talk about the long run, over which these unregulated markets will sort of take care of themselves, what do you mean.

Mr. BAXTER. By and large what I mean by long run is that period of time over which there is opportunity for a substantial amount of entry into performance of a long-distance function. And that is not some clean time period. It will not be the case that nothing happens for 5 years, and then all of a sudden there is a lot of entry. There are firms already competing in those markets.

I expect them to expand their capacity. I expect other firms to enter, so that it will be a gradual process of erosion. Now, one might say, well, by gradual, do I mean 2 years, or do I mean 5 years, or do I mean 7? Any of those would be tolerable answers to the question. Certainly, within the next decade, in my view, well within that decade, there will be very substantial entry and a great intensification of competition in long-haul communication services. In this respect, I do not regard long lines, although it is regulated, as being in the same category at all as the local operating companies. That is the significance of my use of the term "regulated natural monopoly services" in the statement I made this morning.

So, I do not see long lines, notwithstanding that it has a very large market share, as having significant market power. I believe that market share will be eroded quite rapidly, and it would be eroded even more rapidly if Bell tried to use it as a source of cross-subsidization.

Mr. MCCLORY. In the 1956 decree, too, there was a prohibition against A.T. & T. acquiring independent equipment manufacturers. That has been lifted as a result of the vacating of that decree.

How do you feel about that? Isn't that going to provide for further utilization of A.T. & T. assets to get into unfair competition against other competitors?

Mr. BAXTER. I am not sure what kind of a transaction you contemplate, what kind of transaction A.T. & T. might engage in. Acquisition of an equipment manufacturer by a company which held Western Electric among its subsidiaries would obviously pose very serious problems under section 7 of the Clayton Act. A.T. & T. in the time frame you are talking about will be an unregulated company that is a very major competitor in telecommunications equipment. But you are quite right. They would simply be remitted to the tender mercies of the antitrust laws with respect to any such acquisition.

Mr. MCCLORY. There are 2 companies in addition to the 22 being spun off in which A.T. & T. has rather substantial ownership. Although less than 50 percent; what about the threat of cross-subsidi-

zation by Cincinnati Bell and Southern New England Telephone Companies?

Mr. BAXTER. In the first place, because they do have less than 50-percent control, any attempt to use those companies, with their very substantial outside ownership, as a means of cross-subsidization would be resisted by the boards of directors and outside shareholders of those companies.

Second, with the vast majority of the operating companies out there in an independent relationship, we will have an opportunity which we have never had before to see what kind of arrangement independent operating companies are likely to reach, and what kind of prices emerge across an adversary bargaining interface.

Those newly independent companies will soon afford us a kind of a bellwether effect, and we will be far better able than we have ever been before to examine the relationship between A.T. & T. and the companies you are now talking about.

Mr. MCCLORY. We may want to take further action.

Mr. BAXTER. Possibly so.

Mr. MCCLORY. Thank you very much.

Mr. RODINO. Mr. Scheuer.

Mr. SCHEUER. Thank you, Mr. Chairman.

Mr. Chairman, I have asked unanimous consent that I may file a brief statement.

Mr. RODINO. Without objection.

Mr. SCHEUER. I would also ask unanimous consent since the time is so short today that members with additional questions may submit them in writing to you.

Mr. RODINO. Without objection it is so ordered.

Mr. SCHEUER. It is a great pleasure to have you here. You and I have spoken before about the need to have an economic environment in our country that enables our major industrial enterprises to compete effectively in global competition.

Let me shift the focus a little bit this morning from some of the questions that you have been asked. In your opinion is there anything in this consent decree that would unnecessarily cripple or hobble A.T. & T., Bell Labs, Western Electric, or any other element of our telecommunications industry from competing in the global competition for telecommunications business of all kinds of services, equipment, systems, the like?

Mr. BAXTER. No. On the contrary, Mr. Scheuer, it seems to me that by separating itself from the operating companies, and thereby at least potentially deregulating itself in a very significant sense, both from the local public utility-type regulation, which quite appropriately is imposed on natural monopoly, basic operating companies, and also I would hope over some reaonable period of time, eliminating regulation at the long-distance level, which should quite rapidly become a competitive activity, and simultaneously, by freeing itself from the restrictions of the 1956 consent decree, the surviving A.T. & T. Company has positioned itself to be a vigorous unregulated competitor, all of which should enhance, significantly, I think, its freedom of action to compete vigorously in world markets.

Mr. SCHEUER. Can you give us any suggestion as to actions Congress should take legislatively, or actions that we should request

the FCC to take administratively, that would eliminate any roadblocks or improve the competitive position of American companies to engage in global competition? And that means aggregating the capital that has been very difficult in the past.

As you know, companies around the world have banking arrangements, some from government, some from the pirvate sector, that give the financing without the need to show profits on a quarterly basis. The long-term view that some of the major foreign competitors in the telecommunications industry take of their requirements, and willingness to go along with long-term financing without any need for short-term profits, has been one of the keys to the success of the Japanese, the Germans, the Swedes and others in closing the technological advantage we have had.

Can you think of anything either Congress ought to do itself, or that we should ask the FCC to do further to enable our American corporations to compete effectively?

Mr. BAXTER. At this time I do not think I can. I would adopt a wait and see attitude there. As Congressman Wirth has already suggested, this is going to represent a very major change in the industry. I think we should wait and see if problems which would yield to legislation emerge.

It is not clear to me that they will. We are not after all creating a 98-pound weakling here. The surviving A.T. & T. Co. will be a company with something approaching $60 billion in assets, and will continue to be one of the world's largest industrial enterprises. It has well-established connections with the investment banking community and capital markets. The notion that its credit is likely to be cut off seems to me quite unlikely. I do not foresee that it will need, or, in my view, should have any special Government assistance. I think it will do a very credible job as any competitive enterprise of that size is likely to do.

Mr. SCHEUER. One last question. Telephone service is convenient and attractive and desirable for everybody. It is essential, vitally essential for the elderly. It is their link to the outside world in the event of an accident, a fall, a sickness. Many elderly people have frozen to death in the last 30 or 40 days as a result of heat failure. It is unthinkable that we would deny the elderly their lifeline to the outside world due to rapidly rising local phone rates that have been predicted with various degrees of certainty. What do you see as the public policy options that the Congress has in making sure that the lifeline for the elderly is maintained? Is some kind of subsidy needed to cap the possible future increases in costs to the elderly? What are the alternatives? The access charge is one of them. Perhaps the Yellow Pages profits might go to subsidize increases in tolls for the elderly. There are other public policy options.

Can you give us some guidance or suggestion on how we can protect the absolutely quintessential importance of maintaining affordable phone service for our elderly?

Mr. BAXTER. Well, first of all, let me say that I think it is very unclear whether at the present time there really is any subsidy that is flowing to hold down local rates. It is true that in the process of allocating the costs of the so-called nontraffic-sensitive plant, A.T. & T. has historically been quite generous to the local companies. And this is where the subsidy is supposed to flow. But at the

very same time, those local companies in the past have had to pay the license contract fee, which they will no longer have to pay. They will be able to buy their equipment competitively, which has not been the case in the past. How those things will net out I do not think is clear.

Nevertheless, we built a mechanism into the decree, the exchange access tariff mechanism, which is available for the regulators to achieve almost any level of subsidy they wish to achieve. If it is their regulatory choice to impose an excise tax on users of long-distance service in order to subsidize local service, the mechanism with which they can do that is there.

Congress, of course, has an even wider range of choices. The subsidy to local service is a subsidy that runs to the affluent, the old, the young, the healthy, all without any differentiation. If the concern is really holding down the lifeline telephone function for the elderly, why, I would think it would be preferable to do that in a much more direct way than a blunderbuss subsidy to local rates. And that could be done, as you can well imagine, with income tax credits or a variety of voucher techniques.

The possibilities are virtually limitless. But I am sure you are more familiar with them than I am.

Mr. SCHEUER. Thank you, Mr. Chairman.

Mr. RODINO. Thank you.

Mr. WIRTH. Mr. Chairman, just a unanimous consent request, if I might. Congressman Marks was unable to attend the hearing this morning. He is continuing to be troubled with a very bad back problem and asks the record be left open for the opportunity to enter questions.

Mr. RODINO. Without objection.

Mr. RODINO. Mr. Bliley.

Mr. BLILEY. Thank you Mr. Chairman.

Mr. Baxter, under your understanding of the settlement proposal, would A.T. & T. or the operating companies provide cellular service?

Mr. BAXTER. That I think is open to some question. I believe the operating companies would.

Mr. BLILEY. I see.

Mr. BAXTER. I do not think that is clear.

Mr. BLILEY. Excuse me?

Mr. BAXTER. I say, I do not think the answer to that question is clear.

Mr. BLILEY. I see.

Mr. BAXTER. I do not think the decree necessarily implies one or the other, the proposed modification.

Mr. BLILEY. Following up on that, your previous testimony, you said the reason we transfer the yellow pages to the parent was because it is a nonregulated function. Cellular is nonregulated, too.

Mr. BAXTER. I think that is right. And I myself think they would take the position that, until the signal enters the local exchange wire network, it was a competitive function for which exchange access of a slightly different kind, to be sure, to the local system was necessary, and that the mobile and radio portions of the serv-

ice ought to be regarded as a competitive service, and that equal access for all providers of that service should be provided through tariffs to the local operating system.

Mr. BLILEY. Can you explain why the installed terminal equipment is transferred to A.T. & T. immediately, rather than left to the operating companies until it is fully depreciated?

Mr. BAXTER. I can. The provision of customer premises equipment is perhaps the most obviously competitive of all services. In accordance with the basic philosophy of separating the natural monopoly functions from other functions, customer premises equipment it seems to me quite clearly should be in the competitive sector. One can imagine a phaseout that would involve leaving existing customer premises equipment where it is, but I see nothing to recommend such a phaseout. It would cause a certain amount of confusion on the part of customers who would have some equipment in their house, both Bell equipment for which they had to call the local telephone company in the event of problems, and other equipment for which they had to call A.T. & T. in the event of problems.

It would seem to me much more desirable to have a single source of that equipment than simply to transfer it.

Mr. BLILEY. Following up on that, how do you regard inside wiring?

Mr. BAXTER. I do not regard inside wiring as customer equipment. I regard it as staying with the local exchange function. There are problems there about the independence of the property owner to make changes in that wiring, and so on and so forth, that remain to be resolved, to be sure. But, we have not contemplated, and would not, I think, contemplate any transfer of the local wiring away from the base company.

Mr. BLILEY. But if a customer has a problem, then, wouldn't he have to call both A.T. & T. under your scenario and the local operating company as well to determine whether the problem is within the terminal equipment, or whether it is in the wiring?

Mr. BAXTER. He may have to do that. The function of the basic operating company is essentially to produce a dial tone at the plug in the wall. If he is getting a dial tone the basic operating company has done its job, so that, sure, there is always the possibility of having to call two different suppliers. The only way one could avoid that would be to have instrument-to-instrument monopolization of the basic operating company local exchange function, the long lines function, the equipment manufacturer and everything else.

That in my view would be a prohibitively high cost to pay in order to avoid a second phone call.

Mr. BLILEY. Thank you, Mr. Chairman.

Mr. RODINO. Mr. Swift.

Mr. SWIFT. Thank you very much, Mr. Chairman.

I would like to explore a couple of clarifying questions in which there may be some ambiguity that you can clear up. Two days ago, Mr. Brown said with regard to access charges that he didn't see any ambiguity. But his testimony was riddled with "I would assume." "I would assume unless." "Probably." "It is hard to know what will happen with regulatory matters in the future." Essen-

tially what he said was the FCC would have charge over interstate matters and the PUC's over intrastate. I am troubled with the 2(B)(2)'s, in which the 1934 act says very clearly that the FCC does not have jurisdiction over them. What happens, in your understanding of this agreement, when a 2(B)(2) company wants to file an access charge tariff with somebody that is in interstate, is an interstate carrier?

Mr. BAXTER. Well, I guess my not very confident answer to that question, which may deserve some more thought and research and a written answer, Mr. Swift, is that interexchange carriers, will be a competitive set of carriers. And the 2(B)(2)'er would simply go from one to another until he made a satisfactory arrangement with one or the other.

It is not clear to me that they need any regulatory intervention at all.

Mr. SWIFT. So, you don't know whether either the State PUC's or FCC would have jurisdiction in that regard as to the access charge charged to the 2(B)(2)'er?

Mr. BAXTER. To the 2(B)(2)'er.

Mr. SWIFT. OK.

Mr. BAXTER. Yes. I don't see that anything other than freely negotiated contractual arrangements are necessary in that context.

Mr. SWIFT. Perhaps I am asking too technical a question to expect you to answer it off the top of your head. But, it seems to me if these types of questions aren't tied down, that we are going to end up in court. I can see where, if certain things were done, a 2(B)(2)'er might go to court. I can see where PUC's could go to court. If there should be some way of resolving these ambiguities in the agreement or with subsequent legislation. Because I think there is also a policy issue on access charges as well, then it should be done. I was just not as confident as Mr. Brown was that this was so clear in the agreement. I would appreciate any additional light you might be able to shed on that in writing.

Mr. BAXTER. Surely. I am certain there is going to be additional legislation. The 1934 Communications Act really needs to be revised and updated in any event. But it does seem to me with this very, very substantial change soon to happen that a little waiting and watching would be well-advised. The regulatory agencies, after all, are still there to answer questions such as this, and going to court is not the end of the world either.

There is always litigation. Usually there is more litigation over a new statute than there is an old one.

Mr. SWIFT. It is my special bias that we normally get into trouble when courts start making policy that probably ought to be done through legislation in the first place. If in fact it is unclear what regulatory agency has the authority, as I think may be the case here with access charges and 2(B)(2)'ers, then that should be clarified, because the regulatory agency then is not the place where it gets resolved. It wanders off into court for Lord knows how long.

I also think that watching and waiting how things develop when you don't know what the problems are makes sense. But when you spot the problems at the outset, it seems waiting for that problem to prove you right doesn't make a lot of sense.

One other different issue which you could clarify for me. You indicate in the settlement agreement paragraph that calls for divestiture that transfer of ownership, that is the term you used, will be done. On page 6 of the same document, referring only to a different paragraph, it defines ownership as 50 percent or more ownership of the company. It clearly does not refer back to the transfer of ownership. But there is no definition of what transfer of ownership means in that earlier paragraph.

I would appreciate knowing your understanding, whether Bell has to transfer 100 percent of its ownership of the BOC's or whether there is some fraction thereof that would be satisfactory for divestiture.

Mr. BAXTER. No; complete divestiture was contemplated.

Mr. SWIFT. One hundred percent?

Mr. BAXTER. One hundred percent.

Mr. SWIFT. Thank you very much.

Thank you, Mr. Chairman.

Mr. RODINO. Mr. Luken.

Mr. LUKEN. Mr. Baxter, let's get back to the Yellow Pages for a moment.

When Mr. Brown was here he talked about the commitment, or suggestion that A.T. & T. would, for a period of time, provide a concession, call it, in order to phase in and to cushion the shock to the individual user. Now, I take it from your testimony here this morning from what you have said before that the valuable asset of Yellow Pages in your opinion is with the BOC. So, that Mr. Brown's magnanimous gesture was not so magnanimous.

Mr. BAXTER. I wouldn't put it that way, Mr. Luken.

Mr. LUKEN. Well, I think these are the facts. If he didn't have anything to give, why did he talk about giving it?

Mr. BAXTER. Well, I think first of all, there is no misunderstanding or disagreement between the Department of Justice and A.T. & T. whatsoever.

Mr. LUKEN. Bring us in on it.

Mr. BAXTER. The situation is understood by them and by Mr. Brown, as well as by ourselves, to be what I described. The thing that is really of value is this computerized listing, and that goes to the BOC's. Mr. Brown was confronted by repeated expressions of opinion by Members of the Congress that there would be a shock attributable to the transfer of the Yellow Pages.

Essentially, I understood him to be saying, "Look, we don't think there is going to be a shock. But if there is a shock, we will take care of it. Do not worry about it. We are perfectly willing to underwrite that income stream for some period of time." I do not see——

Mr. LUKEN. If I may get back to it, Mr. Brown admitted, and I do not think you are challenging that, that there is income, a profit of almost $1 billion from Yellow Pages.

Mr. BAXTER. No question about that.

Mr. LUKEN. His testimony, and I think everyone acknowledges it that heard it on the subject, that that $1 billion, approximately, was being used to defray part of the local user costs.

Mr. BAXTER. No question about that.

Mr. LUKEN. Well, we are talking about, therefore, what is going to happen to that $1 billion. And he talked about it very clearly, I

was here. He talked about it very clearly, that this was to be the property of A.T. & T., and that they were going to, and I found no fault with that at the time, my problem is that we are getting a different set of facts here today, that he was going to work it out, that A.T. & T. would work it out so that that would be available, at least over a period of time, to continue to cushion or defray part of those charges.

Now, you are saying that he can't do that because A.T. & T. is not going to have the valuable asset.

Mr. BAXTER. That is what I am saying. I was not here, so I am hesitant to argue with you. What I understood Mr. Brown to be saying was that, yes, the Yellow Pages went to A.T. & T. How explicitly he made the point that this critical element remained with the local operating companies I do not know.

Mr. LUKEN. It becomes important to us because we are considering the possibility of the need for legislation. Under Mr. Brown's testimony we might need to legislate to protect the local user. Under your interpretation there wouldn't be any need because the BOC's are going to have it anyway.

Mr. BAXTER. Yes. In my view the BOC's will retain the only asset which is capable of earning more than a competitive rate of return, and therefore, has any utility for the purposes of cross subsidization.

I assure you that A.T. & T.'s view of the matter is the same. I will not try to speak to the actual words used by Mr. Brown here last Tuesday.

Mr. LUKEN. I have just been handed, and I think this is important and therefore I will read this letter which I haven't read before. I will take a chance on reading something I haven't read before. In reference to Senator Packwood, a letter from Mr. Brown, in reference to our discussion in the hearings this morning on yellow pages I am prepared to make the commitment of which you spoke.

> We will not abruptly discontinue the support for local rates from the yellow page source. S. 898 provides for a 4-year phase-down of this support, unless future legislation affects this matter we will see to it that the support is not phased out until 4 years from now. This may be affected of course by any changes which may occur in charges by the local telephone companies for the prompt provision of telephone number listings to anyone who sells yellow pages type advertising.

That is the end of his letter.

Mr. BAXTER. That is completely consistent with what I have been saying. Mr. Brown is saying, "Do not worry about Yellow Page income. To the extent there is any diminution in Yellow Page income, we will protect the basic operating companies for at least 4 years."

He is saying that in part because, I believe, he realizes that what is really valuable about the entity that we have heretofore called the Yellow Pages is the exclusive local computerized telephone listing, and that is not being transfered to A.T. & T.

Mr. LUKEN. I don't read it as being that simple. As I read it, the latter part may bring in the element you are speaking of. But it seems to me he is saying the same thing which we all heard interpreted.

That they have a proprietary interest or holding here, and that they are going to continue to provide it, even though they may not be required to. In any event, it brings up an ambiguity which I am not at ease about right now. I don't know whether we need to go ahead and even consider legislation to protect the local user because of this change.

Do you think we should?

Mr. BAXTER. Mr. Luken, let me say this: Changing telephone rates is a long, slow process. Proposed new tariffs have to be filed with the Public Utility Commission. There have to be hearings and cost studies and so on and so forth. Congress will have a long period of time during which it can see whether some of these problems about which there is concern actually develop, turn out to be real problems, or whether they do not.

I am perfectly——

Mr. LUKEN. You mean after the rates go up, then we should consider it?

Mr. BAXTER. If there are waves of rate filings, and part of the explanation is the Yellow Page income has disappeared and so on and so forth, these problems, and the 2B2 problem that Mr. Swift mentioned, are going to turn out to have relationships with one another.

I would think that at some point in time, undoubtedly in the next Congress, we will want to pass one comprehensive piece of legislation that updates the 1934 act and addresses such problems as have emerged.

However, as for the particular Yellow Page problem you are now talking about, I am completely satisfied that there is not a problem there.

Mr. LUKEN. Well, I am not. And I think our committee should consider legislation which would enable at least some of the revenues from Yellow Pages to go to the BOC's. I think there is enough of an ambiguity here that, if it isn't clear, that Mr. Brown's statement and interpretation which we have all put on it up until now, I think in protecting the consumer, I think we would have to assume his interpretation is correct.

Mr. BAXTER. I would hope you would at least ask Mr. Brown one more time explicitly the extent to which he thinks the value of the Yellow Pages inheres in the exclusive computerized local telephone listings.

Mr. LUKEN. Perhaps we should. Thank you, Mr. Chairman.

Mr. RODINO. Mr. Mazzoli.

Mr. MAZZOLI. Thank you, Mr. Chairman.

Mr. Baxter, welcome. A moment ago, in a question by Mr. Bliley dealing with cellular services, your answer—was in a sense—that it was not clear from the terms of the agreement. I am just wondering, how can something as profoundly important to the future of this country as is this proposed agreement not be absolutely clear in all its parts?

Mr. BAXTER. Well, the only thing I can say to that is the telecommunications industry is an enormously complicated and very dynamic industry. If we had attempted to write a document that was absolutely clear on every question that anyone might conceivably raise over the next year, let alone the next 5 years, we would have

consumed all the trees in the United States in the paper it took to write it down on.

This is a very short agreement in principle that does not explicitly resolve a very, very large number of questions. But it is very clear about the principles. As these questions come up, you simply have to say, well, what are the implications of the clearly agreed principles for this particular problem?

The proposed modification makes no reference to cellular radio, and so one has to ask to what extent is cellular radio part of the local natural monopoly phenomenon, and to what extent is it potentially competitive?

As I suggested to Mr. Bliley a moment ago, it seems to me that one probably has to disaggregate cellular radio into two different phases of the service, one of which takes place in the local loop wires, the other of which takes place largely by radio and transponder switching.

Mr. MAZZOLI. I think, if you can excuse me, of course, this is where we get into technical stuff. In other words, if the proposed agreement had said we can't anticipate the future, technology will outstrip any agreement, but cellular radio, cellular services will be controlled by the local, I think you call it BOC's, be done with it. That is it. Why didn't the agreement which has now been festering for 8 or 9 or 10 years and could affect the future of the Nation's ability to compete because of computers and everything else, why wasn't it at least that explicit?

Mr. BAXTER. One can focus on a very large number of things other than cellular radio and ask the same question.

Mr. MAZZOLI. Then let me ask you this generic question. What sort of agreement is it when it is an agreement to agree or disagree later?

Mr. BAXTER. It is not an agreement to agree or disagree later. It is an agreement that the BOC's will be fashioned so that they embrace all of the natural monopoly local services, and nothing else. And that is a standard that is susceptible of being applied with a substantial degree of clarity, but not always perfect clarity, to each of the many questions of this type that can be raised.

Mr. MAZZOLI. Of course, I think if I were in the industry, either actively in management or a lawyer working on this case, or perhaps yourself working with it all these years, maybe I would have a little more appreciation for the fact that these things will all sort of divide and kind of arrange themselves in the future, not at the jeopardy of the payer of the bills, the people at the end of the line, the people my friend Mr. Scheuer talks about, the older people.

But I am a little uncertain about that. But let me proceed to another area.

I understand that Judge Greene will have to determine under, I think you call it the Tunney Act, or something, whether or not this agreement is in the public interest. Is that essentially a correct statement?

Mr. BAXTER. Judge Greene will have to make a determination whether this agreement is in the public interest.

Mr. MAZZOLI. Is "in the public interest" defined anywhere in the books?

Mr. BAXTER. No, it really is not.

Mr. MAZZOLI. Do you have some idea in your own mind what constitutes in the public interest?

Mr. BAXTER. Yes, I do.

Mr. MAZZOLI. And this agreement constitutes in the public interest in your judgment?

Mr. BAXTER. Yes.

Mr. MAZZOLI. Does it do so, even though you are spinning off or requiring to be broken out as many as possibly 22 companies or some array of those 22 companies? I asked this question when Mr. Brown was in the chair in the other room the other day. I am very much concerned about the quality of the service in this Nation.

I think our future, and I used two specific examples in my questions the other day, where the ability to communicate accurately and reliably is absolutely vital. I ask you, in your judgment, is the public interest served by requiring these operating companies to go hither and yon?

Mr. BAXTER. Nothing requires the operating companies to go hither and yon. Their divestiture from the A.T. & T. Co. is required. Whether there will be 3 operating companies, or 10, is not determined. I am reasonably confident that the company does not contemplate either creating a single operating company, or creating 49.

Mr. MAZZOLI. Is it up to A.T. & T. to decide that?

Mr. BAXTER. The reorganization plan is submitted for approval, so we certainly will have an opportunity to look at that.

Mr. MAZZOLI. Is one of the things you look at whether somebody from Kentucky could call somebody in Maine or Hawaii, and do it quickly and with a quality you could hear, where you wouldn't have static in the background or have to pay separate charges? Is that one of the things you will look at?

Mr. BAXTER. Of course. It is inconceivable from the standpoint of corporate self-interest that they would contemplate any organization that did not permit people in Kentucky to call people in Maine.

That is precisely the product that they sell.

Mr. MAZZOLI. There is going to be, as I understand the thing, I know my time has expired, but I mean there is a lot of competition now out in these operating companies. I returned just recently from St. Thomas where it is very nearly impossible to make adequate phone calls back and forth.

This gentleman who was on a radio call-in show said he can't get his computers to work because the quality of the ITT subsidiary, Itelco, is so bad that the computers don't work.

Is that a possibility of the outcome of all that we are doing?

Mr. BAXTER. Well, of course there will be no equipment changes as a consequence of this reorganization. The switches that are there today will be there the moment after the reorganization.

Mr. MAZZOLI. What happens if they don't have the money, sir, to repair those or to continually update them and modernize them? That is my worry.

Mr. BAXTER. Who is the "they?"

Mr. MAZZOLI. What you call the BOC, I presume.

Mr. BAXTER. The basic operating companies confront a demand curve that is so high and so inelastic in comparison with their costs

that they could make incredible sums of money, and indeed would make incredible sums of money if it were not for the fact that they were regulated.

Indeed, that enormous potential for profit is precisely why they are regulated. If the BOC's are financially unable to maintain a quality system, it will be a consequence of bad regulation.

Mr. MAZZOLI. I thank you very much. My time has expired. My last statement is, I do hope that you, as long as you are head of the Antitrust Division, I hope that the public interest of being able to have a system which is the best in the world, and upon which our industrial base is founded, remains for the future.

I thank you, Mr. Chairman.

Mr. RODINO. Mr. Railsback.

Mr. RAILSBACK. Mr. Baxter, what do you envision to be the role of the Justice Department in evaluating the assets that are permitted to go with the local companies that are going to be spun off?

In other words, are you going to have any role in determining the assignment of debt for instance, that may be part of the transfer from the parent to the spun-off subsidiary?

And also, I am wondering about the process of evaluating the assets and how they will be determined or allocated.

Mr. BAXTER. Well, let me answer, Mr. Railsback, in the following way.

The proposed modification gives us a very broad approval authority. As for your particular question, yes, I would certainly intend to look at the debt in certain respects. I don't mean to suggest for a moment that the company might try to do this if we weren't very alert. But just as an example, if the company were to assign a lot of debt to the operating companies that was recently issued and carried very high interest rates, and were to keep for itself a lot of older debt that carried very low interest rates, I would find that unsatisfactory.

I would be inclined to insist that the cost of imbedded debt to the basic operating companies not significantly exceed, perhaps not exceed at all, the cost of imbedded debt to the parent company.

Mr. RAILSBACK. Then under the arrangement or agreement, what are your options in the event that you do decide that what they are doing is unsatisfactory?

Mr. BAXTER. Simply not to approve it. It doesn't go into effect.

Mr. RAILSBACK. Is it possible in the spin-off of the 22 companies that two companies will result. I believe this could happen under the agreement?

In other words, am I correct in saying that there is nothing that requires that there be 22 independent companies?

Mr. BAXTER. Certainly not.

Mr. RAILSBACK. What is your feeling about that?

Mr. BAXTER. If there were two?

Mr. RAILSBACK. Yes, are you concerned that that might give them a certain economic leverage that could pose a problem under the antitrust laws?

Mr. BAXTER. No; I don't think so, not unless there were some aggravating circumstance that you haven't included in your question. But I would like to give you a rather fuller answer to your former

question if I could, Mr. Railsback, because I think there is an important distinction there.

Mr. RAILSBACK. Yes.

Mr. BAXTER. Certainly we will look at the assets that are put in the basic operating companies. I gave you one example of one kind of thing I would like to look at. Certainly, we are going to be looking at the assets to assure that everything has been transferred that is necessary to perform the local service function, and to effect exchange access for originating and inbound traffic and so on and so forth.

But your question was in large part focused on valuation. There, my answer is quite different. No, we do not intend to get involved in the question, "what is the financial value of these assets that have been transfered?"

I see that as being part of the job of the local public utility commission. The local PUC will have to make a rate base determination after these transfers are completed of what the new rate base of the regulated company is.

And, of course, rates will be based on the new rate base in the sense that rates are usually connected with the rate base—in the sense that that is the amount of capital committed to the enterprise with respect to which the company is permitted a cost of capital rate of return.

I want to make a distinction between the process of valuation, which you seem to be referring to in certain portions of your question, and certain other kinds of functional checks that we do certainly intend to perform.

Mr. RAILSBACK. Can A.T. & T. walk away from this settlement if Judge Greene orders a modification which he believes to be in the public interest?

Mr. BAXTER. Yes.

Mr. RAILSBACK. I think that is all, Mr. Chairman.

Mr. RODINO. Thank you very much. Mr. Baxter, coming back to the question of the local telephone user, the ratepayer, I guess you would agree that, when it comes to Bell Labs, which has been the research arm, principally, of A.T. & T., that they have a storehouse of patents and technology. I guess all of this, you might say, is a very valuable asset which in great measure is the result of the payments made by the local ratepayers. Isn't that correct?

Mr. BAXTER. I agree with all that. I would only make this note about it. That patent pool has been subject to compulsory licensing for a period of 25 years now. Consequently, there are a large number of licensees under most of that patent portfolio, more than one. So exclusive positions with respect to that patent portfolio have been largely destroyed by the 1956 consent decree.

Since nobody has an exclusive position to any portion of that technology which is of any importance, it also follows that nobody has anything that is particularly of value, except the right to compete using that technology. And that will not change.

Mr. RODINO. I must conclude from what you say, that you don't believe that there was any inherent unfairness in turning over Bell Labs to A.T. & T., even though this provision makes no allowance to the local operating companies for these various assets which were there.

Mr. BAXTER. Yes. No; I do not, except in one very, very limited sense, which I think is different from the point you have in mind. One could get somewhat more sophisticated and say, well, wait a minute. This is a three-part phenomenon we are looking at, not a two-part phenomenon. I referred to patents granted before and after the reorganization.

One could say, well, there are a whole lot of patents that are granted before the reorganization. But as of the moment of the reorganization, there will be lots of research going on that has already occurred in recent months, but has not yet yielded patents. And the patents that they will get out of the Patent Office over the next couple of years will mostly be attributable to research that was done before the reorganization.

And then you have a third phase where the research that leads to the patent will be financed by the equipment sales of Western Electric and the other activities of the reorganized company, and those quite obviously are appropriately the property of the reorganized company.

Thus, there is a transition problem there with which one could concern himself if he wished. It did not seem to me to be one of more than a couple of years' duration. And it seemed to me the difficulties of dealing with it in any reasonable way were so great that it did not justify the effort to do so.

Mr. RODINO. How would you address the research that is in progress? This is being paid for by the local ratepayers?

Mr. BAXTER. That is exactly what I am talking about. Research currently being paid for by the local ratepayers will yield patents issued after the reorganization. That is the transitional problem to which I refer. It is a transitional problem perhaps of 2 years' duration.

Mr. RODINO. When you say transitional problem, are you suggesting perhaps that that is an area that Congress might examine, and see whether or not there ought to be some kind of compensation?

Mr. BAXTER. Oh, that is a possibility. I hadn't really meant to suggest that. I think the problem will come and go before legislation is likely——

Mr. RODINO. Do you see that as a possibility?

Mr. BAXTER. Yes, I do. I think it is the kind of thing that would be better taken account of in the reorganization itself by Bell saying, "Well, we will give the BOCs some extra working capital in view of this problem. But this is a problem that is going to begin and end within a period of a couple of years.

Mr. RODINO. Do you think that is a problem Congress ought to take under consideration, recognizing that this may not be dealt with?

Mr. BAXTER. I do not at the moment have any solution in mind, legislative or otherwise. And I would not counsel the Congress to address itself to a problem until I had decided that I could identify a coherent legislative solution. Not being able to do that, I would not say that I was making a recommendation of any sort.

Mr. RODINO. Mr. Baxter, let me say, and this is going to conclude the phase of this hearing that relates to A.T. & T., that I appreciate—before I conclude, Mr. Wirth.

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Mr. WIRTH. I have several comments and one question, Mr. Baxter. Going back to Mr. Railsback's question on the transfer of assets, and the division of their value between the two companies. And these decisions will be made by A.T. & T., is that right?

Mr. BAXTER. Yes.

Mr. WIRTH. Will they come back to you what recommendations that you can approve or disapprove.

Mr. BAXTER. They will propose a reorganization.

Mr. WIRTH. What role will the State Public Utility Commissions or FCC play in that?

Mr. BAXTER. Initially none at all. But of course they will have to deal with them.

Mr. WIRTH. After the fact?

Mr. BAXTER. After the fact.

Mr. WIRTH. There are a number of billion dollar issues in this process: The valuation of assets, the distribution of debt, the allocation of joint switches, the transfer of patents (about which Mr. Rodino spoke) and the valuation of terminal equipment. A.T. & T. will do all that?

Mr. BAXTER. Of course—you went very quickly over a number of different items.

Mr. WIRTH. There are indeed a number of concerns.

Mr. BAXTER. There are, indeed. But the answers are different.

Mr. WIRTH. There will be no role in the valuation for the Public Utility Commissions and FCC?

Mr. BAXTER. No; no one will perform a valuation role except the PUCs and FCC. That is precisely the role they will perform. They will then have in that 6-month period of time—the PUCs and FCC will have a role.

Mr. BAXTER. No. The valuation will be performed after the reorganization when the regulatory analyses of necessity address themselves to the question, what is the rate base on which——

Mr. WIRTH. Perhaps we are misunderstanding each other. Who determines what values end up in the local operating company and what values end up in the parent company? The question is, will the PUC's and FCC have a role?

Mr. BAXTER. Mr. Wirth, I think of functional properties as being one thing, and the accounting value that is attached to them as being something else. In the reorganization, the Department of Justice will oversee the physical distribution of functional assets, including some financial assets like bonds.

We will decide who owns this switch, to take an example.

Mr. WIRTH. You and A. T. & T. will decide that?

Mr. BAXTER. That is right.

Mr. WIRTH. There will be no role from the PUCs or the FCC in determining the values of those assets. Is that correct?

Mr. BAXTER. No. Determining which functional assets go where. After we have gotten through putting the functional assets in two different piles——

Mr. WIRTH. Let me give you an example. You have said that terminal equipment is competitive and will move right away on the parent company.

Someone could value that terminal equipment at a dollar a piece and move it to the parent company. That would have a very, very dramatic impact on the local rate base.

Mr. BAXTER. Yes.

Mr. WIRTH. PUCs have been grappling with this question of valuation of equipment for a long time and are very expert in that area. Let me ask you again, will they have any role in this process? Or will that all be done by the A. T. & T. and approved by you?

Mr. BAXTER. Only the Public Utility Commissions will be involved in any question of valuation.

Mr. WIRTH. So they will be involved in evaluating that equipment ?

Mr. BAXTER. Yes; indeed they will.

Mr. WIRTH. That is different from what you have stated.

Mr. BAXTER. No; it is not. It is the same.

Mr. WIRTH. We are, as you know, Mr. Baxter, very interested in getting your expertise, the expertise of your staff and the Department on the impact on the issues we have to address both from the perspective of the subcommittee they chair, and the full Judiciary Committee.

Chairman Rodino and I have sent you a letter requesting that assistance. Our staffs met together last Saturday to discuss this matter. There now appears some confusion as to how forthcoming the Justice Department will be in helping us exercise our respective jurisdictions over these issues.

At this point I ask you to look into this matter carefully. We would very much like to work with you and with your staff.

Finally, I would note that over the years I have consistently defended the role of the Justice Department.

It is your job, and was your predecessor's job, to enforce the antitrust laws.

At the same time, I have also consistently stated (and I think most other people have agreed) that it is the job of the Congress to set national telecommunications policy. It seems to me that the need for doing that is right now, as I have said, not to wait for a number of other happenings that it seems to me will further complicate the process and make it very difficult for us to do anything.

There are a number of issues that we must address now. We must mandate regulatory reform within the FCC. We have to, for example, give the FCC, where appropriate, the authority not to regulate, which they do not now have. There is also the question Mr. McClory discussed, the need to insure that there will be no cross-subsidies running from the regulated long lines to Western Electric.

We must look at the question of the transitional rates, what is going to happen to the Yellow Pages, imbedded terminal equipment, how the access charge works.

I hope you have heard us very clearly this morning on the variety of additional issues.

Mr. Mazzoli and Mr. Railsback have raised questions of integrity in the cost recovery of the Bell operating companies to make them viable and continuing to have incentives to upgrade themselves.

The employee protection issue which was discussed the day before yesterday. The patent issue which Mr. Rodino just talked

about and the very broad cluster of issues regarding international trade have been of great concern to Mr. Brock.

It is certainly my feeling that a strong legislation will go far to supplementing and strengthening the settlement that you have been so aggressive in pursuing.

I, for one, thank you very much for being here. I know that Mr. Rodino and his committee have a number of other issues related to IBM. Thank you very much, Mr. Baxter.

Mr. RAILSBACK. Mr. Chairman, could I just ask one follow-up question?

Mr. RODINO. We are going to conclude in 5 minutes. And the Chair has a concluding statement to make, so I would make the question very, very brief.

Mr. RAILSBACK. I will make it very brief. I know that as far as the discrimination provisions relative to the BOC's, that the procedures must be submitted to the Department of Justice. Section 2C, prohibits discrimination by the operating companies, between A.T. & T. and other persons. I can find no provision for a signoff by the Department of Justice, or an actual approval by the Department of Justice. Do you know what I mean?

In other words, they have to submit their procedures, but there is no requirement that Justice must approve.

Mr. BAXTER. Well, effectively, there is a requirement that they be submitted for approval——

Mr. RAILSBACK. I see.

Mr. BAXTER. Which contemplates an approval function. It is perfectly true that it is not stated. It is simply contemplated that if we find that the procedures are inadequate, we will go before the court to obtain an order requiring necessary improvements.

Mr. RAILSBACK. Thank you.

Mr. MCCLORY. Mr. Chairman?

Mr. RODINO. Mr. McClory.

Mr. MCCLORY. Thank you, Mr. Chairman.

In my opening statement on Tuesday, I said that what we have here is an agreement to agree. And I assume that after you have reached an agreement on substantially all or all of the problems which are going to then be embodied in the decree of the district court, that some time contemporaneously or just before or just after we will have another hearing in which you can report to this committee with respect to the implementation.

Mr. BAXTER. That sounds very reasonable, Mr. McClory. I haven't thought through the exact procedures at that point.

Mr. MCCLORY. What if there is something that A.T. & T. proposes and you disapprove of it? Are you able to revive the case then? Are you able to effectively resume the dismissed case?

Mr. BAXTER. Yes.

Mr. MCCLORY. Then do we start off right where we were? We wouldn't start over again, would we?

Mr. BAXTER. We wouldn't have to start over again, no.

Mr. MCCLORY. Thank you very much.

Mr. RODINO. Mr. Baxter, maybe you might not want to answer this question or haven't formed an opinion on it. But you are aware of the fact that Chairman Wirth has introduced legislation on this subject. I don't know the exact provision, but I do believe

that Mr. Wirth has a provision in his bill which would allow for compensation to the operating companies for some of the research which he considers valuable.

And I am wondering whether or not you have an opinion as to whether or not you could support that?

Mr. BAXTER. I do not at this time, Mr. Chairman.

Mr. RODINO. Mr. Baxter, let me say for the committees that we appreciate your coming here and testifying on a matter which I know you have long wrestled with. As you recall on a number of other occasions I, in discussing this matter with you when you appeared before this committee, hoped that the day might come when we might come to a resolution of this very important and yet so complex problem. I urged from time to time that the parties might find a solution that could ultimately result in some kind of a settlement without all the protracted litigation.

There are areas of concern. You yourself stated that we are going to be following this, that the problem has not yet been firmly and finely resolved. We hope you will continue, of course, to keep us informed and that we intend to exercise our responsibility in this area.

But nonetheless, I wanted to state, as I did in my opening remarks—you were not present there—opening remarks when Mr. Brown and Mr. Trienens were there. I commended them for the part that they played in this.

And I want to commend you for the part that you played in this settlement. I do hope that you will continue to pursue this, though, because some of the areas we have expressed concern about have really not, in our minds, been satisfactorily addressed.

Of course, we know that no agreement is going to be satisfactory to all parties. With that, we thank you very much.

Mr. BAXTER. Thank you, Mr. Chairman.

Mr. RODINO. I understand, Mr. Baxter, you will be returning at 2 when we will be undertaking the IBM portion of this hearing.

Mr. BAXTER. That is my understanding.

[Whereupon, at 10:48 a.m., the subcommittee recessed, to reconvene at 2:10 p.m., the same day.]

AFTER RECESS

[The subcommittees reconvened at 2:10 p.m., Hon. Peter W. Rodino, presiding.]

Mr. RODINO. The committee will come to order.

The major part of this afternoon's hearing will deal with IBM. There are some members, however, who have requested that, when they do appear, they may be permitted, Mr. Baxter, to ask some questions relative to A.T. & T.

They did not have that opportunity this morning. I hope you won't mind us going back and forth at some point. However, I believe that in the interest of saving time, we will just have you pro-

ceed with that portion of your statement, and please feel free to summarize it, as it relates to the IBM matter.

STATEMENT OF HON. WILLIAM F. BAXTER—Resumed

Mr. BAXTER. I think I will proceed more or less as I did this morning, having submitted a formal statement to the committee and summarize very, very briefly the historic developments, if I may use that term, for a span of time that included only 8 or 9 months.

As I indicated this morning, I sort of specialized in getting to know the A.T. & T. case for the first few months I was in office, and with the other challenges of a job with which I was not familiar, it was early summer before I felt able to turn my attention largely to the IBM case.

We then asked for an extension of time within which to file proposed findings and briefs to the court. I wanted to conduct a review not only in the sense of reading the written studies, but also of having intensive seminars with my staff, and they were busy drafting findings over the summer, and I had no inclination to interfere with that process. We did, then, divert them from that process of writing findings, starting in September, and through the months of late September, October, November, and early December, we had a series of seminars on major issues in the case.

Written material was submitted to me by my own staff, and also by IBM counsel. And then we would meet essentially for the whole of the day Friday, and go over the contents of the record on the major issues. That process concluded as I recall about the end of the first week in December. I spent a good part of the month of December going back over points that had been troublesome to me or unclear, and asked for at least one supplementary submission by the trial staff. And by the end of the Christmas vacation—I reveal my academic background by that statement—near the end of the Christmas holidays somewhere, I had reached the conclusion that the only appropriate recourse in the IBM case was simply to dismiss it.

At that point, I was scheduled to be out of the city on a short vacation over the New Year's weekend, then to give a talk as part of a seminar mid-week in Salt Lake. I was returning to the city late at night on January 7. And because of a variety of particular considerations having to do, among other things, with the necessity to stop trading and avoid the possibility of insider trading on the basis of inside information, we scheduled a dismissal for Friday, January the 8. It had to be done on Friday because I was leaving again for a week at the OECD meetings in Europe the following weekend. That was the only full day which my schedule called for me to be in Washington for a period of several weeks in early 1982.

We got the papers ready. We contacted counsel for IBM who learned of my intentions for the first time late in the day. I shouldn't say late in the day—sometime during the day of Wednesday January 6.

After some initial shock they found their way clear to sign the papers, and they were filed on Friday, January 8. That was the time at which I made the announcement. I think because I am not

sure exactly where the committee's questions may be focused that I will stop with that very brief statement and respond to such questions as the committee may have.

Mr. RODINO. Thank you very much, Mr. Baxter.

Mr. Baxter, so that we put this hearing in focus, I am going to draw attention to a letter that was directed by me to the Justice Department, to your attention, on January 15, requesting certain information in order to prepare for these hearings, and particularly with reference to the IBM matter. I recognize that you have been most cautious in protecting the deliberative process of your division. We believe that the requests that we made for information have been reasonable, and it becomes rather difficult for us to understand the Department's response, in the light of circumstances that are present in this case, a case of this enormous magnitude which went on for many years, involving the outlay of a great deal of time, money and effort and manpower on the part of the Department and IBM. We felt that the information that we sought would provide us a better basis for understanding the causes of the long delay so that we might focus our questioning during the course of the hearing itself.

And very frankly, while I recognize that there may have been some reason that motivated you to not provide us with this information—and I realize that you did designate your deputy, Mr. Lipsky, to provide a briefing to the subcommittee staff which was helpful—we still feel that the kind of information that we sought of you is necessary, is essential, and important.

I am stating to you at this time that this material should be supplied to the committee unless there is some all-compelling reason why you can't supply it. Of course we know that, and you have stated publicly, or at least it has been announced publicly, that your trial staff did not agree with the decision that you made. This leaves us in what I believe to be a difficult dilemma—we are unable to confirm this disagreement, or even find out what the staff's views are. I think that is a proper statement, is that not?

Mr. BAXTER. I believe I said, and would say again, that I was virtually certain that some number of the trial staff would not agree with my action. I did not poll the trial staff. I did not ask what their views were on that matter. I mean they had a period before me for a number of months essentially arguing the case from their standpoint.

Of course I deliberately cast them into the role of advocates. It is conceivable that they were merely advocating a position, as a good lawyer should. But, nevertheless, it was my perception that they believed that the arguments they were making were not only the best arguments available, but were sound arguments. And from that, I infer that some unknown but substantial number would not agree with the action I took.

Mr. RODINO. Well, that leads me to say, too, that the failure of the Department to make available to us through interviews with your staff this kind of information creates a more troublesome kind of a climate in that there is a question as to whether or not the division has been forthcoming.

I would like to emphasize the importance of this request. While I naturally respect the decisions you made—I am sure you believe

them to be correct—nonetheless, I hope you realize that this legislative oversight responsibility which we have is fundamental to the proper function of our constitutionally balanced system of government.

I would hope that, in the light of that, you reexamine some of the requests that we have made.

Mr. BAXTER. I certainly will, Mr. Chairman. Let me reply for the moment in the following way. I would wish to make a distinction between information that you would like to have—there is no information that you could possibly wish to have which we are unwilling to furnish.

If you would like a poll of the trial staff to find out how many agreed and how many disagreed, I will conduct a poll of the trial staff. If you would like information on any issue of the case we will prepare it or have it presented to the staff. In short, I draw a distinction between information of any kind, which we are entirely willing to furnish, and the procedure by which that information is obtained.

I certainly agree and agree most emphatically that the oversight role of the committee is an important one that must be given a great deal of weight. I feel with equal emphaticness that the consultative process within the division must also be respected. I regard it as extremely important that career civil servants, giving advice orally or in writing to the Attorney General or the deputy or the head of the Antitrust Division or whoever it may be, should be able to do so without having their mind focused on the question, "How will this reflect on me on that eventual day when this document I am writing or these statements I am uttering will appear in the Congressional Record and in the press?"

So, I draw a very, very sharp distinction between turning over the very documents that were written by way of advice to me, or interviews with the people who were advising me on the one hand, and other presentations of such information you might wish to have on the other. In that conjunction, I think our staffs have agreed that at least on some issues, they will have sessions with Mr. Lipsky at which they will present whatever questions they wish to ask.

Mr. Lipsky will assemble knowledgeable people within the Division who have that information to assist him in responding to those questions, but the interview will be of Mr. Lipsky, a noncareer official of the Department, and a politically responsible official of the Department who, with the assistance of other lawyers in the Division, will respond to whatever questions may arise.

Mr. RODINO. Well, will there be any caveat placed on your staff people in their discussions with us as to providing us with information that is substantive? Are they going to be free to discuss all aspects of this matter, the legal analysis which you may have had as to whether or not you were or were not in compliance with the Tunney Act, or whatever methods you might have used in reviewing this matter?

Mr. BAXTER. I am uncertain that I understand the import of the question. There are no restrictions whatsoever on Mr. Lipsky, if that is what the question means, and indeed, certainly none on myself. Whatever questions you wish to ask, we will answer. To the

extent it is necessary to draw upon the career staff in order to provide those answers, we will draw on the career staff. If you are asking a question about direct interviews of the career staff, the answer is that that process, or the surrender of documents which constitute advice to me within the Antitrust Division would not be consistent with departmental policy, and in my view would constitute a violation of the separation of powers of a different kind than the one to which you alluded.

Mr. RODINO. Let me ask one final question at this point.

Will the members of the trial team, or trial staff, be available for our staff to interview?

Mr. BAXTER. The members of the trial staff will be available to the extent that Mr. Lipsky or I find it necessary to obtain information from them or of them—available to help us answer questions, depending on what questions it is you may wish to have answered.

Mr. RODINO. Mr. McClory.

Mr. MCCLORY. Thank you, Mr. Chairman.

Let me say I agree with the position which you are taking. I think that it would be most unfortunate if this committee, in the exercise of its oversight, would undertake to require turning over in-house confidential files with regard to litigation, pending litigation, or litigation, that may have been disposed of. It seems to me that that would be an offense to the confidentiality which exists between the Government, your client, and the attorney. And likewise, I can't see that it is justified on the basis of our oversight authority which should and does relate to legislation or prospective legislation because I do not think there is any nexus involved as far as the subject of your present inquiry is concerned.

The questions I have are of a slightly different nature. For one thing, I am concerned that we consume the time and the energy of dozens, I do not know how many attorneys, with regard to a case over a period of 13 years, and likewise, subject a large defendant company to all of the expense of the pending litigation over this long period of time, and then come to the conclusion that we don't have a case and to dismiss the case.

It seems to me that delay is something we should concern ourselves with as far as the administration of justice is concerned. I understand the attorneys for the defendant state quite forthrightly that the only way they are able to get the delays is either through the cooperation of the court or through the cooperation of the Attorney General.

Now has there been, in your view, cooperation, willingness on the part of the Attorney General to let this thing drag along? Or is it the fault of the court, or are the defendants so smart that they are able to hoodwink the Attorney General and the court to get these long delays, and then finally they are off scott free?

Mr. BAXTER. Well, I do not think the delays really have anything to do with the ultimate outcome, Mr. McClory.

Mr. MCCLORY. They have something to do with the expense involved to our Government and to the private sector, including an estimated $250 million in costs to IBM.

Mr. BAXTER. I assume that is correct. Addressing myself to the question of delay, I would say first of all that I would ask you to remember that my institutional memory goes back only a year.

What I know about the causes of delay I know secondhand and by hearsay from talking to people about what caused the delay. That I must also confess was of secondary interest to me over this most recent period which was really spent focusing on the merits of the case and being anxious to get it disposed of.

I am very clear in my own mind that we should go back and take a much more careful look than we have so far about what mistakes were made that permitted the case to drag on as it did drag on.

Mr. MCCLORY. You really don't have any analysis or conclusion to draw with regard to the reason for the delay?

Mr. BAXTER. No. I do have one point I would make. I would attribute a large fraction of the delay to this point. That is that, unlike A.T. & T., where the case was really handled with great dispatch, the complaint in the IBM case was drawn with vagueness.

I am not sure whether it was considered vagueness, because the Department wished to pursue simultaneously several different theories of section 2 without, frankly, recognizing and facing up to the fact that they were pursuing different theories, some of which were not really justified by the existing precedents, or whether it was mere oversight and lack of careful thought that led to drafting of a pleading in this way.

Nevertheless, it is the case that the original complaint was drawn with considerable vagueness about the theory of section 2 liability that was being invoked. And when a complaint is drafted in that way, if the theory that underlies the complaint is not clear, then it is exceedingly difficult for anyone to say with any confidence what is relevant to proving these charges, since the charges themselves are rather vague.

I think that enormous amorphousness about the complaint and constant uncertainty about what was relevant, therefore what the scope should be, what factual issues should be pursued, was a very major factor in making this case so cumbersome and difficult to try.

Mr. MCCLORY. I can see one reason for the delay being the built-in interest of the Government lawyers. Being on the Government payroll working in the Antitrust Division, some would say they couldn't care less whether the case ultimately gets disposed of.

Would it not be a good action on our part to contract out or to hire out legal talent in a case like this, instead of having Government employees in the division handling this kind of a case?

Mr. BAXTER. It has——

Mr. MCCLORY. The lawyers are up in New York, I understand anyway. They are not even down here with you.

Mr. BAXTER. That is correct. Of course, we do have a New York field office with whom they work in some degree of conjunction. It has often occurred to me that there is a certain amount to be said in contracting out what I would call the lead trial role to some very, very experienced and skillful private sector litigator.

I must confess I have never even considered the possibility of contracting out the whole trial function. I would have to give that some more thought. I don't, myself, believe that a sort of self-interested featherbedding mind set on the part of the Government lawyers is a credible explanation for the delay in this case.

If you were to suggest that they might have been more competent than they were, that would seem to me a plausible possibility. But after all, they do have fairly well-protected jobs in the Department of Justice. If this case were to go away, there would be some other case for them to do. I can see no sense in delaying. I really don't think that is the explanation.

Mr. MCCLORY. Thank you, Mr. Chairman.

Mr. RODINO. Mr. Hyde.

Mr. HYDE. Thank you, Mr. Chairman. I think parenthetically it is interesting to note this happens occasionally, what has happened here. Many a private firm would go bankrupt if they settled a couple of estates that they have had around for a long time. I do not think the Government has that problem, but I know from some law firms that have subsisted upon a few fat estates that controversy can be generated.

There was a dye and film company case, they are now the GAF company, I believe, that had hung around the Department for about 15 years. A man named Robert Kennedy came in and settled it in 1 day. I dare say there was a lot of chagrin about that but probably not an inquiry into the staff feelings and motives.

But let me just say this. I am distressed as a bystander, really, by the personal attacks that seem to have been lodged against you, Mr. Baxter, by the trial judge. I like to think of judges on Mount Olympus, sort of detached from the political swamps and from ad hominum attacks on people.

But this judge, if the Wall Street Journal's issue of January 26 is an accurate account of what he said, he seems to be really distressed that this case was settled, and makes some serious personal attacks that I do not think are appropriate for a Federal judge.

I just wanted to avail myself of this opportunity to question the propriety of his remarks. That is all I have to say. It does not call for a response, unless you want to make one.

Mr. BAXTER. Thank you, Mr. Hyde.

Mr. RODINO. Is that all, Mr. Hyde?

Mr. HYDE. No; but this may not be the appropriate forum. I still never found out why Justice never prosecuted Dr. Pete Bourne. I wish I had polled the lawyers then. I didn't think of it, Mr. Chairman. Thank you.

Mr. RODINO. Mr. Scheuer.

Mr. SCHEUER. Thank you very much, Mr. Chairman.

I would like to ask your indulgence, Mr. Attorney General, in reverting to the A.T. & T. case for just a couple of questions.

The first question that comes to mind is sort of a follow to the very interesting colloquy that you had this morning with Congressman Mazzoli when he mentioned the deterioration of service in the Virgin Islands. I don't want to put words in his mouth, but this was more or less the import of his question. He asked you that, in the event that there was tremendous local pressure to keep down telephone rates, and in the event that rates were capped at a level which did not provide adequate cash flow to the local phone company to maintain its services and purchase new technology according to the highest state of the art, what would be the remedy for the situation.

And you said, well, if the company were so capped on its phone rates that it couldn't adequately maintain and improve its system, that would be the result of bad regulation.

You recall saying that?

Mr. BAXTER. Yes; I do.

Mr. SCHEUER. Now, my answer is, that is a real and present danger, because there is a strong feeling around the country that we have to cap these rates, have to limit the increases. You know there have been predictions of 200 and 300 percent increases, trebling of rates. We hope that won't happen, but we don't know. But in the event a particular local system under the political pressures on the State regulatory agencies is kept at such a rate of inadequate cash flow that it really can't invest properly in new maintenance and systems, that would be a rip in our national telecommunications net.

There would be a national interest in that not happening. In the event the "bad regulation," the consequences of bad regulation that you referred to would lead to that, do you think there would be an interest in the Congress facing that challenge and taking steps to prevent that from happening? Do you think, for example, that we would be justified here in the Congress in establishing some kind of uniform national standards to guide local regulatory agencies to make it clear that, while we sympathize with the goal of keeping down—to keeping increases in phone rates to the lowest feasible level, and while we sympathize with the concept of some kind of subsidy, we don't expect the cap to be kept at such a low rate that the integrity of the service and quality of the service is seriously diminished.

Would you favor our setting some form of uniform national standards to guide State regulatory agencies?

Mr. BAXTER. Let me answer in several ways, Mr. Scheuer. First of all, and I realize to some extent it is arguing with your question rather than answering it, I would emphasize that we have created in the proposed modification a system of access tariffs so that the present level of subsidies, or perhaps a somewhat higher level, if one takes into account the other fund flows that I mentioned this morning, the same level of subsidies as presently exist can be captured from the several interexchange carriers simply by the process of cost allocation in the construction of those access tariffs. But that simply is a reason why the hypothetical question you asked me would not come about. It does not answer the question, well, what if it did come about.

Mr. SCHEUER. Thank you, Mr. Attorney General. I have one more question to ask you in our limited time.

On Tuesday, when Mr. Brown appeared before us, there was some consideration of future patent policy of A.T. & T. I understand that under the new agreement the current patent situation will be changed. I recall that some years ago, under the 1956 consent decree, A.T. & T. was required to license for a nominal fee its transistor patent. And a little mom and pop Japanese corporation, for a nominal fee picked that up. Today that corporation is Sony Corp., is engaged in a lively clobbering job on its American competitors around the world that has cost us billions of dollars.

Is it contemplated under the consent decree that IBM, and perhaps other American corporations, will be required to place their patents in the public domain? Perhaps you could consider the rationality of this kind of vast giveaway of the highest state of the art of American technology. And is that in our national interest?

Mr. BAXTER. Mr. Scheuer, I assume you mean to refer to A.T. & T. in your question rather than IBM?

Mr. SCHEUER. Yes. I am sorry. That was a slip of the tongue.

Mr. BAXTER. The 1956 consent decree does require cross-licensing of Bell technology. Bell gets access to other peoples' patents in exchange for the licenses it is required to issue. When the reorganization takes effect, and the 1956 consent decree ceases to be in effect, the obligation to engage in that cross-licensing will end, and A.T. & T.'s proprietary position with respect to its technology thereafter will be the same as that of any other private sector enterprise.

Mr. SCHEUER. Thank you very much.

Thank you, Mr. Chairman.

Mr. RODINO. Mr. Markey.

Mr. MARKEY. Thank you, Mr. Chairman.

Mr. Baxter, the former head of the A.T. & T. trial staff, Phil Verveer, recently characterized the A.T. & T. suit as a complaint against triple monopolies. Local distribution, long distance and equipment, that have been used to reinforce each other. Divestiture takes care of the most critical monopoly, the local loop.

Would you agree with that?

Mr. BAXTER. I would agree with that partially. The difficulty with that statement is that it suggests that three different positions of market power are independently self-sustaining. I don't believe that that is true. The very, very large market share in equipment that A.T. & T. has had over the years is, in my view, largely dependent upon their control over the local exchange carriers.

And, also, their long lines market share is dependent on control over the local exchange carriers. In my view, by severing their control over local exchange carriers, I solve not one, but three of those problems.

Mr. MARKEY. Three?

Mr. BAXTER. Three.

Mr. MARKEY. What about the remaining market power of A.T. & T.? It still has, with the balance of its partnership that still exists, control of 97 percent of long distance after 10 years of competition. And a study done by A.T. & T. indicates that even with intensive competition over the next 10 years they will still have 85 percent of the market. After 20 years of competition, they will still have 85 percent of the market. That would indicate to me that there is still room for debate on what is or is not a monopoly.

At that point, 97 percent, it seems to me that that still does constitute for all intents and purposes a monopolistic share of the market.

Would you agree with that?

Mr. BAXTER. My difficulty is not whether to agree or disagree but to decide what it means. In the first place, I think 97 percent is a little high. But I don't choose to quibble about that. Certainly it is true that at the present point in time the long lines division of A.T. & T. has a very, very major market share of long distance traffic.

Mr. MARKEY. Like what percentage would you put on it?

Mr. BAXTER. At the present time, probably around 95.

Mr. MARKEY. Ninety-five.

Mr. BAXTER. There are some definitional problems, but your number is good enough for all practical purposes. The other carriers have been increasing their market share very, very rapidly. And I have in mind 20, 30, 50 percent per year increases.

Mr. MARKEY. Of what?

Mr. BAXTER. Of their own base. But their own base is very, very small.

Mr. MARKEY. It is a very small base?

Mr. BAXTER. That is right.

Mr. MARKEY. So, if you increase even 100 percent of half of 1 percent and you are still not talking about much.

Mr. BAXTER. That is quite correct. But the point is that with each passing year as their base grows bigger and those growth rates continue, one can expect that the long lines market share will fall at some nontrivial rate.

Now, I do not know the rate at which it will fall, because the rate at which it will fall will depend very strongly on how competitively they behave. The more competitively they behave, the lower they keep their rates, the more service they give, the more success they will be in hanging on to that market share.

Mr. MARKEY. I agree with that. The problem is in your own case, *United States* v. *A.T. & T.* it shows anticompetitive abuses based on dominance of long distance——

Mr. BAXTER. No; it was not based on dominance. It was based on control of the local exchange carrier.

Mr. MARKEY. High-low and data links and private line, that does not have anything to do with the local loop does it?

Mr. BAXTER. Yes; it does have a great deal to do, because unless you can interface with the local loop and get satisfactory access to the local loop, where all messages must——

Mr. MARKEY. They are still going to get satisfactory access to the local loop even after the suit, are they not?

Mr. BAXTER. The other carriers will for the first time get satisfactory access to the local loops. As a result I would expect their market shares to increase much more rapidly than before. But the basic point I would make is this. One must not confuse very large market share with market power. One can have a very substantial market share without having any ability to exploit that market share in terms of earning monopoly revenues——

Mr. MARKEY. I have a problem with you on that, though. I mean last year long distance went up 16 percent. Now, I hope that there is more competition. But we can't have the Justice Department, or a court somewhere telling the FCC what to do next. We need a communications policy that comes from the Congress to say how the Commission regulates if A.T. & T. is no longer dominant. We can't wait a year or two after divestiture and then unscramble the eggs.

You say 97 percent does not indicate anything. But you know, maybe we can differ. Maybe the Chicago school can say one thing and somebody else can say something else. I went to law school, I

am not an antitrust expert, but I just remember a concept called resipso locater, which is "the thing speaks for itself."

Maybe I don't have a complete and total appreciation for all antitrust law. But just looking at it on its face, the 97 percent of the market, and an increase of 16 percent in their rates, and no significant loss of business would indicate to me that there is still a very serious problem there. My concern is that those long distance revenues, that there is not a mechanism, a construct which is a part of your settlement in which you provide for a division between the long lines and Western Electric to insure that there is not that cross subsidization.

I would ask you at this time whether or not you think that additional provisions ought to be provided so that, perhaps not as a separate subsidiary, but that in some form we guarantee that those revenues from long lines are not used to help subsidize Western Electric in their competition with the companies like Digital and Wang and Honeywell and the others that are in my district that I am very concerned about—allowing A.T. & T. to get in and get an undo market share there because of their dominance in the long lines area.

Mr. BAXTER. Well, the cross subsidization about which you are concerned is only possible if a company is in a position to set rates significantly above costs. And once the equal access provisions of the agreement go into effect, behavior by A.T. & T. which set long line rates significantly above long lines costs would invite an extremely rapid expansion of the market shares of the other interexchange carriers. Once the terms of the decree are really operational, I do not feel that there is a problem of cross-subsidization present.

Mr. MARKEY. You don't think there is any danger of cross-subsidization?

Mr. BAXTER. Once the provisions of the decree are fully in effect, I do not think there is any danger of significant cross subsidization.

Mr. MARKEY. How about in the transitional period, 4 years?

Mr. BAXTER. Yes; there is a transitional period of 4 or 5 years.

Mr. MARKEY. Do you see a danger in that period?

Mr. BAXTER. I see a possible problem during that period, and if some temporarily limited precautions against cross subsidizations during that period were to appeal to the Congress, I would certainly understand that. I think there is a danger that when one sets out to solving short-term problems, the solutions may turn out to be problems longer than the problems.

But, if the solution were really tailored to fit the limited dimensions of the problem, that would seem to me a perfectly reasonable thing to do.

Mr. MARKEY. As you know, for very vulnerable small, high-tech firms, the short term is all they have. For them to be able to come in and look for a remedy, it might be posthumous. For A.T. & T. it is fine to look 20, 30, 40 years down the line. But for a high-tech firm that has to get its product out on the market, to be kneecapped by A.T. & T. because there is no protection against cross-subsidization in the short term is not really a minor problem because that is the heart of the high-tech industry in the country,

those small vibrant entrepreneurial entities that make that whole industry go.

Would you not agree with that?

Mr. BAXTER. I certainly agree they are enormously important. But the point I would make is that the right time horizon at which the consumers and telephone users should be looking is also the 10-year horizon, and not the 2-year horizon. As strongly as equity counsels that we might protect some competitors in the short run, we have to be very, very careful that we are not impairing the interests of consumers and users in the long run in our efforts to do so.

Mr. MARKEY. I agree with you. But my concern is the short term. I mean the long term might take care of itself when you have got effective competition in long distance and for computer and data processing.

But I am very worried about the transition period when Western Electric is allowed to compete with these additional cross-subsidies from long lines, from the purchase of equipment by long lines makes from Western Electric, as part of its advantage in competition. And even in the relationship they will still have with the Bell operating companies in the short term.

All of those problems go to the viability, to the continued existence of many of these. They are marginal only in the sense that they cannot compete with such a giant that goes unregulated. Not that they are marginal in the sense that they do not have a good product, and compete in the present frame. So I do not see the short term as being so irrelevant as you do.

And I fear for these smaller companies.

Mr. BAXTER. Well, it may be that our time horizons are different. I tend to attach more importance to a longer time horizon and you to a relatively short one. As I said before, two points I think must be kept in mind. First of all, the FCC will still be there and for some period of time it will have regulatory authority to insure that long line rates are not set at monopolistic levels, and therefore afford minimal opportunities for cross-subsidy.

That process has never been completely effective of course. While I certainly would not be willing to rely on it in the long run, perhaps it can be relied on in the short run. If not, I have already said I would find perfectly reasonable some time limited statutory protection of the kind you seem to be suggesting, although of course I would want to look at it before I expressed any view on any particular approach.

But some explicitly time limited protection of that kind might well appeal to the Congress.

Mr. MARKEY. So you think that legislation is appropriate for the short term, at least, perhaps not the long term, while we wait for the competitive forces to take hold in both these areas. Perhaps it is important for us to put together interim legislation?

Mr. BAXTER. I could imagine short-run legislation that I would not find inappropriate, yes.

Mr. MARKEY. Could you tell us what areas you think might be appropriate for us to look at?

Mr. BAXTER. I think——

Mr. MARKEY. Without giving us any specific recommendations.

Mr. BAXTER. Yes. I think in general to the extent one went looking for a short-run problem, it would inhere in cross-subsidization from the long lines division of the sort that we have seen in the past.

Mr. MARKEY. What kind of remedies do you think we could look at for the short term?

Mr. BAXTER. Well, part of the reason why I am very, very cautious here, is because I think the difficulties are just enormous. If one looks back at the complexities of S. 898 and the layer upon layer of regulation present in S. 898 in its endeavor to deal with this very phenomenon of cross-subsidization, one realizes how difficult and complex it is to guard against that problem.

Yet, I do not know how to do it better than that. I would say this. With reference to this question of time horizons, the Bell System in the form that we know it, and posing all the problems of the kind you suggest, was brought into existence shortly after the turn of the century, almost 80 years ago. Within another 4 years the problem about which we are talking will have gone away. One could be forgiven for thinking that if he had satisfied, eliminated the problems of 80 years as of 4 years from now, that the really significant problem had been solved and we can live with another 4 years.

But I have no doubt you are right. There are companies that might well disappear in that 4-year span of time. And one should not be indifferent to them.

Mr. RODINO. Mr. Mazzoli.

Mr. MAZZOLI. Thank you very much, Mr. Chairman, and Mr. Baxter.

This morning we talked about the A.T. & T. case. I asked you then to what extent Judge Green would look into the public interest. You indicated that he would, whether by a Tunney Act, or just on his own. And you told me then that there was no specificity in the books on what is public interest, what constitutes the public interest.

Let me ask you with respect to IBM. Is there going to be some examination by some judge or court into the public interest, and whether that public interest is served by this settlement and this dismissal?

Mr. BAXTER. No; I do not expect there will be.

Mr. MAZZOLI. Is it that a dismissal is different than a settlement?

Mr. BAXTER. Yes.

Mr. MAZZOLI. In a sense then the avenue chosen by Mr. Lipsky, which you agreed do, which was the dismissal, rather than an attempted settlement, ended the possibility of examining this from the standpoint of whether it serves the public, is that a fair statement?

Mr. BAXTER. First of all, I think whatever errors have been made in this context were made by me, not by Mr. Lipsky.

Mr. MAZZOLI. The memorandum from your colleague is up here as having sent you a memo which was part of the input that you had to work with. In there is recommendation that there be a dismissal rather than a settlement. Given the magnitude of the case that lasted since 1969, it was probably the magnum opus of this field, perhaps hopefully forever, was there not perhaps some

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thought that maybe from the public standpoint, just from appearances, that maybe there should be something other than a flat out dismissal just so that the public might have some shot at seeing just what was going on here?

Mr. BAXTER. No. That is an argument that would not have occurred to me. The case in my judgment was not one that the Government should win, was not one that the Government was likely to win, and was one that was consuming the resources both of IBM and of the Antitrust Division at a very rapid rate. And my inclination was to bring it to a halt just as quickly as I possibly could.

The notion that one should enter into some sort of a cosmetic settlement in order that one could have Tunney Act type hearings is a position that quite frankly did not occur to me.

Mr. MAZZOLI. Well, I wish it had, because I would not really call it a cosmetic settlement, because I am sure after all those years there is plenty of good substance here that could be settled out. If it was taking 10 or 12 of your lawyers, which I read in the paper was what was assigned more recently, you know, it is taking some of their time as well and would seemingly have some advantage for them to settle out, rather than just simply have a dismissal. There might have been some kind of a quid pro quo that could have been determined.

But obviously, there has not been that. In view of the fact that there is a dismissal here, how do we, myself, for example, go back to my constituents and say the Government has just settled this case, and my friends ask me, well, what was the reason for the settlement? And I look at it and say well, it was just that we thought we were going to lose if we had tested the case out. They said well, maybe you might have won.

How do you, looking at this thing, take a look at it from the standpoint that we might have lost, and therefore we decide to dismiss?

Mr. BAXTER. Well, I would tell your constituents that it was not merely a risk of losing, but that it was a case that the Government ought not to have wanted to win. I would tell your constituents that there is a small rotunda outside the office of the Attorney General with a motto carved into it that has always appealed to me. The motto says, "The Government wins its point whenever justice is done to citizens in its court." And justice required that this case be dismissed.

Mr. MAZZOLI. Well, justice done to the citizens, and that I guess gets back to my first point about the public interest. I just wonder again, what sort of an evaluation process looks at it from a citizens standpoint is what I guess I am driving at.

Mr. BAXTER. Ours did.

Mr. MAZZOLI. I appreciate your saying that. You look like a man of confidence and assurance. You are certainly that kind of a man. I have no doubt that in your heart you do believe that this dismissal serves the public interest.

But, you know, one thing that gives me a little more confidence, though I have some misgivings, even about the A.T. & T. case, is because it is going to have to be looked at even from the sort of amorphous standpoint of does it serve the public interest.

But this dismissal has not. You know, I think to that extent maybe if there are any other cases, ponderous cases like this floating around downdown somewhere, it might be looked at from the standpoint of maybe the public paying the bills as it does both for our lawyers and for a considerable part of the IBM overhead here. It would seem like maybe they should be involved.

Anyway, I thank you, Mr. Baxter, and Mr. Chairman.

Mr. BAXTER. I did not mean to suggest for a minute that this committee should not satisfy itself that what I have done is in the public interest. I think probably it should. And I gather it is that process that we are about.

Mr. MAZZOLI. All right.

Mr. BAXTER. But I do not agree that we should have settled it rather than dismissed it so that there could be some judicial hearing process to explore that question.

Mr. MAZZOLI. Thank you.

Mr. RODINO. Mr. Baxter, one question on A.T. & T., and then a few on IBM. And then we will conclude. I am advised that a local official of the C. & P. Telephone Co. stated yesterday evening on a radio program that it was his opinion that under the settlement the operating companies will now be free to go into the cable TV business. Do you have any opinion on that? Do you agree with that opinion?

Mr. BAXTER. The decree, of course, is pretty silent on that topic. The decree says that the operating companies will not engage in activities other than natural monopoly activities subject to regulation, actually subject to regulation. The transmission of television signals originated by others answers that description.

The origination of signals by a company would not.

Mr. RODINO. Does that mean that you do not agree with the opinion?

Mr. BAXTER. It means among other things I am not sure exactly what he is referring to when he talks about going into the cable television business. If he is talking about transmitting signals through people who lease telephone lines from the local company, I see nothing to quarrel with in the statement. If he is talking about originating signals, or picking up signals from a broadcast, then I would not agree with it.

Mr. RODINO. But you feel that the settlement is silent on that question?

Mr. BAXTER. Oh, it is not a matter of feeling, Mr. Chairman. The settlement is silent on that.

Mr. RODINO. Mr. Baxter, turning again to IBM, we see ourselves that a matter of this nature that has been going on for a long period of time, and, as I stated before, has required the expenditure of a lot of time and money and effort, raises serious questions in the minds of many, even now.

Maybe we can prevent future matters of this magnitude from occurring if we get this record straight. And so I am propounding these questions to you.

Did you have a series of meetings with your trial staff and IBM counsel before you arrived at this decision?

Mr. BAXTER. Yes; I did.

Mr. RODINO. Could you tell me whether or not these meetings were in any way helpful in your arriving at that decision?

Mr. BAXTER. They were enormously helpful. You know, the record itself in IBM is of almost unapproachable magnitude. And these meetings enabled me to focus on relatively limited portions of the record that contained the evidence that was germane to the critical points, to look at those portions of the record, to hear their significance argued from both sides.

The hearings were absolutely indispensable to my reaching any conclusion.

Mr. RODINO. Did you keep any formal record of these meetings, Mr. Baxter?

Mr. BAXTER. I do not keep any sort of a diary, other than my desk calendar. From my desk calendar I would be able to identify the Fridays on which these meetings occurred. I think they did all occur on Fridays.

Mr. RODINO. No memos, no summaries?

Mr. BAXTER. In preparation for each of these meetings there were submissions to me, both by IBM and my own trial staff.

Mr. RODINO. Now, if those were the kind of records we were requesting, would those records be made available to us?

Mr. BAXTER. The IBM records would. My trial staff's would not.

Mr. RODINO. The IBM records.

Mr. BAXTER. Yes.

Mr. RODINO. And the trial staff records would not be.

Mr. BAXTER. No. They are intended for my advice, and they come under the concern that I expressed this morning.

Mr. RODINO. Is there any record of what took place at these meetings?

Mr. BAXTER. I believe there is no record, no written record, no one was keeping minutes. But there were other people in attendance. My deputy, Mr. Lipsky, I believe, attended all the meetings. My assistant also, a noncareer appointee, attended all the—Jeff Zuckerman attended all the meetings. I would be more than happy to have your staff talk with them.

Mr. RODINO. My reason for asking is not that I am going to suggest that my staff talk with them. We may, but in view of some of the questions that arise in matters of this sort, assuming that there may be some serious allegations made about improprieties, or what not, the integrity of the process be served they would be made available, these kind of records?

Mr. BAXTER. I do not believe in categorical statements, Mr. Chairman. And I would be very reluctant to say there would be absolutely no circumstance I could conceivably imagine in the face of plausible assertions of impropriety where that would be so damaging to the process that it was not a worthwhile thing to do.

But as a general matter of policy, it seems to me very destructive of the internal deliberative process of the division, I would resist it on those grounds. I would resist it on separation of powers grounds.

Mr. RODINO. Aside from resisting providing us with those kinds of records, do you not think it would be in the best interest of the Department, that has this tremendous responsibility, to be able to reply, respond to potential critics or those who could possibly make

allegations in view of the vast and enormous interests that are involved here?

Mr. BAXTER. The Department policy is to the contrary, Mr. Chairman, and I think the policy is sound.

Mr. RODINO. Let me ask, as a result of your having made some rather categorical statements about what you thought about the government's case, including the statement that, in your judgment, it should never have been brought, is that not the——

Mr. BAXTER. No, I do not believe I said that. What led to the questions to which I think you are referring is not my categorical statements but my noncategorical statements.

Senator, I forget which Senator now, one of the Senators was troubled that in my memo I had said there was no substantial evidence of this and there was no significant support in the record for that. He took that as implying that there was at least some, if not very substantial, evidence. And that was the nature of the colloquy. The government made efforts to prove these things. And they brought forth some material that they at least thought tended to show that these things were true.

It seemed to me that they had brought forth no substantial reason for believing that it was true, and I expressed it in that qualified way.

Mr. RODINO. Based on this experience, then, do you think that you are now in a position to recommend changes in the procedures by which antitrust cases are brought and tried?

Mr. BAXTER. Yes; in a way I think I am. Changes in procedures may not be the best way to describe my response to this problem. Changes in pleading policy, I think, would more nearly accurately capture the point. Again, I would say what I said this morning. I think it is very important that, particularly in cases of great technological and industrial complexity, when the government brings cases, it bring them on the basis of a clearly articulated theory. Or, indeed, two clearly articulated theories, if it wishes, but with a careful distinction between exactly what those two alternative theories are, and recognizing right up front that there are two here rather than one, or only one.

Now of course trying law suits that way runs a risk. People who regard winning as more important than the proper display of governmental attitude toward people who are charged in its courts would prefer not to take that risk. But if complaints are drawn in that way, if theories are clearly spelled out, then it is easy for everybody, including the judge, to tell exactly what is relevant. The discovery process proceeds much more quickly, the trial process proceeds much more quickly. And we do not get into morasses like this.

Mr. RODINO. Do you believe that the resources of the executive and judicial branches of the Government are sufficient to try these monopolization cases, especially in large industries and especially when you consider cases like A. T. & T. and IBM?

Mr. BAXTER. Yes; I do. It seems to me the A. T. & T. case illustrates that point.

Mr. RODINO. How about IBM?

Mr. BAXTER. The IBM case would be a strong counter-example.

Mr. RODINO. Let me ask you this. This is merely because I think that maybe the public may draw the wrong conclusion. All of a sudden we find that two of the largest cases ever tried by Justice Department have been settled. And there are questions that are raised. As Mr. Mazzolli asked a while ago, the question is whether or not the public interest was served.

Do you think that, all of this having occurred in one fell swoop, maybe it sends the wrong message to the people, and maybe we ought to clarify the situation and say, no, we are not just dismissing these huge cases because we do not proceed against antitrust violators, especially those who are big and powerful. We are prepared to do what is necessary to enforce the laws.

Do you think anything like that is necessary?

Mr. BAXTER. Well, I hope not, Mr. Chairman. Although I know in your statement at one point you referred to the two cases as being settled, and at another point to the two cases as having been dismissed. Of course, the truth is that one was dismissed, and representing a loss for the Government. I do not think there is any other fair way to characterize it.

The other was settled subtantially on the terms that we have sought throughout the litigation. It was in equal measure a clean win for the Government against the biggest corporation in the world.

Mr. RODINO. Do you think that that kind of an impression has been conveyed to the public?

Mr. BAXTER. I think it should be conveyed to the public.

Mr. RODINO. But do you think that it has been?

Mr. BAXTER. I have relatively bad feelers as to the perception that the public is receiving at any particular point in time. I would rather let someone else answer that question.

Mr. HYDE. Would the chairman yield.

Mr. RODINO. I yield.

Mr. HYDE. Putting the question another way, do you think failing to dispose of a case because of the possibility of inaccurate public perceptions is a meritorious consideration for the Justice Department to entertain?

Mr. BAXTER. No; I would not think so, although I think were that my anticipation, I would be at great pains to try to see that the public did get the right impression.

Mr. HYDE. It is my experience that justice sometimes is infringed upon, I do not mean the Justice Department, but justice generically, because of fear of public perceptions. I know of prisoners who, because they are political people, are not permitted to enjoy weekend leave or half-way house rehabilitation because people would say, this is a politician, and he is getting a break.

But a mugger, a dope peddler, a criminal who has committed violent crime does get that treatment. And I have often thought that justice is very unequal in its application because of fear of public perception. A person who runs for office knows that only too well.

But I would think it is commendable for the Justice Department and any of its divisions not to let public perception interfere with the administration of justice, whether it is dismissing, whether it is prosecuting or whether it is settling. That is a comment, and I thank the chairman for letting me interject it.

Mr. RODINO. Mr. Baxter, what areas, if any, should the subcommittee explore, in your view, to simplify and streamline complex antitrust legislation? And if you do not have a ready answer for that, maybe you could supply it.

Mr. BAXTER. Well, there has been a good deal of work done on that. There have been studies done by the American Bar Association. I would think perhaps if you wanted to hold some hearings on that topic I would be happy to suggest the names of some of our ablest private litigators around the country who I suspect would be willing to come and share their viewpoints with you.

I do not believe that cases, however large the companies or however complex the issues, require 13 years to be tried properly.

Mr. RODINO. On that point, Mr. Baxter, on page 4 of your information memorandum you state that, and I believe I am quoting:

> Most appropriate relief in cases of this nature may be to impose fines or other penalties commensurate with the gravity of the illegal behavior.

And then,

> However, the government here precluded the possibility of obtaining fines or incarceration of responsible individuals by pursuing a civil, rather than a criminal remedy in 1969. Today the allegations would be time barred.

Does this suggest that a criminal action might be appropriate?

Mr. BAXTER. I did not mean to suggest that. I meant that one crosses a street irreversibly the day one decides to go criminal or not to go criminal, and gives up some sanctions that would have been available if one had gone in a different way. If there had been clearly demonstrable instances of misbehavior by IBM, then it seems to me there would have been a lot to be said for criminally proceeding against them to account for those instances of misbehavior, and imposing sanctions of the kind to which reference is made there.

In fact, there were not. There never was any realistic possibility of proceeding criminally.

Mr. RODINO. In other words, you were not suggesting that there should have been?

Mr. BAXTER. No; I was simply pointing out that people-type sanctions which, in my view, are the most appropriate if you have clearly demonstrable episodes of misbehavior, were not available to us.

Mr. RODINO. One final comment. And this is without any attempt on my part to impose on you and to suggest that you run your department in another way. But going back to a question that I posed about records and whether you kept any records concerning these meetings, and the concern that I had really went to the question as to whether, if something at some later date might become critical, there was a record to refer to. It was not my intention to say that I would disagree with a decision to resist giving them to us if you had them. That is something else again.

But I would think, very frankly, that the public interest would best be served if some records were kept. I do not know what the position of the Department is in this case, but I assume there is no requirement, otherwise you certainly would be living up to the requirement. But do you not think that it would be better to keep

records of those particular meetings which you said you placed so much emphasis on in reaching your decision.

Mr. BAXTER. Well, you see, there is a record of a sort, Mr. Chairman. I have, on a little glass-front set of bookshelves at my desk, 6 feet, I would guess, of black ring binders that consist of the submissions of my trial staff and the submission of IBM on the first meeting of September 20, whatever it was, and so forth.

They constitute a record of a kind. But they are not minutes or transcripts of what was argued about that day, but the submissions. In some instances I have retrospective submissions where, at the end of a day I say, well, you know, here is a loose end we seemed not to get resolved. And how about each of you letting me have a memo within a week or 10 days bearing retrospectively on this issue we opened today, but were not able to dispose of.

I have an enormous quantity of paper in my office which in a sense constitutes a very complete record, but they are of a different character. I am not sure the extent to which that is responsive to your concern.,

Mr. RODINO. I merely wish to lay the suggestion before you. You are the one who has to make the determination as to whether you consider it important, not only for now, but for the future. You know all of us who are public servants are followed by various people. And the public later on may think of us, or judge us in some fashion.

These were two cases, both so complex, so important, involving so much, that one never knows. I just laid that before you as one who, over a period of time, has had the opportunity to inquire into matters that, you know, had they been placed on the record, might have been quickly laid to rest.

Mr. BAXTER. I understand, Mr. Chairman. I thank you for your suggestion.

Mr. RODINO. I would like to say in conclusion, Mr. Baxter, that we will have some written questions which I hope you will respond to on this matter.

Mr. BAXTER. We will

[The information letters and questions were received for the record:]

March 4, 1982

Honorable William F. Baxter
Assistant Attorney General
Antitrust Division
U. S. Department of Justice
Washington, D. C. 20530

Dear Mr. Baxter:

During your testimony at the joint hearing before the Subcommittee on Monopolies and Commercial Law and the Subcommittee on Telecommunications, Consumer Protection and Finance on January 28, the record was held open to allow members to submit written questions for your response.

I am forwarding for your written response questions on the AT&T and IBM matters which have been forwarded to me. Please note that the questions from Congressmen Broyhill and Rinaldo are set forth in a separate letter to me.

So that we can complete the record promptly, I am asking that you respond by March 24.

Sincerely,

PETER W. RODINO, JR.
Chairman

[AT THE TIME OF PRINTING NO RESPONSE HAD BEEN RECEIVED FROM THE JUSTICE DEPARTMENT TO THE QUESTIONS SUBMITTED TO THEM.]

QUESTIONS FOR MR. BAXTER ON AT&T

1. AT A HEARING ON FEBRUARY 4, 1982, FORMER ASSISTANT ATTORNEY GENERAL JOHN SHENEFIELD TESTIFIED THAT "A REVISION OF THE TUNNEY ACT WOULD BE DESIRABLE TO MAKE CLEAR ITS APPLICABILITY TO A SETTLEMENT THAT TERMINATES A MAJOR CASE BY PROVIDING FOR THE RESTRUCTURING OF A MAJOR AMERICAN INDUSTRY, EVEN WHEN THE SETTLEMENT IS IN THE FORM OF A DECREE MODIFICATION IN ANOTHER COURT." WOULD YOU AGREE? IF NOT, WHY NOT?

2. AT THE HEARING ON JANUARY 28, YOU TESTIFIED THAT "AS A MATTER OF STATUTORY INTERPRETATION," YOU DID NOT BELIEVE THAT THE TUNNEY ACT APPLIED TO THE AT&T SETTLEMENT.

   (A) DID AT&T PROPOSE THIS SETTLEMENT TECHNIQUE? DID AT&T BARGAIN FOR IT?

   (B) WHAT TACTICAL OR SUBSTANTIVE ADVANTAGE WOULD ACCRUE FROM THIS FORM OF SETTLEMENT TO AT&T?

   (C) WHY DIDN'T THE PARTIES AGREE FIRST TO TRANSFER THE NEW JERSEY ACTION TO THE DISTRICT OF COLUMBIA, CONSOLIDATE THE PROCEEDINGS, AND THEN FILE A SINGLE CONSENT SETTLEMENT THAT WOULD HAVE BEEN SUBJECT TO TUNNEY ACT PROCEDURES?

3. YOU ALSO STATED IN YOUR TESTIMONY THAT IF JUDGE GREENE FOUND THAT THE PROPOSED SETTLEMENT WAS NOT IN THE PUBLIC INTEREST, THEN THE CASE WOULD CONTINUE FROM THE POINT IT TERMINATED.

   (A) WHAT ASSURANCE DOES THE DEPARTMENT OF JUSTICE HAVE THAT AT&T WOULD NOT INSIST THAT THE CASE BE TRIED ANEW?

3. (B) ARE THERE ANY LETTER AGREEMENTS BETWEEN THE PARTIES WHICH INDICATE HOW THE PARTIES WOULD PROCEED IN THE EVENT THE SETTLEMENT DOES NOT WORK OUT? IF SO, PLEASE PROVIDE THE COMMITTEE COPIES OF THOSE DOCUMENTS.

4. AT THE FEBRUARY 3 HEARING, A NUMBER OF WITNESSES STRESSED THE DIFFICULTY IN PROVIDING MEANINGFUL PUBLIC COMMENT UNDER THE TUNNEY ACT PROCEDURES BECAUSE ONLY THE BAREST OUTLINES OF THE SETTLEMENT WERE KNOWN. WOULD THE DEPARTMENT OBJECT TO ALLOWING FURTHER COMMENT TO THE COURT AFTER THE DIVESTITURE PLAN IS WORKED OUT BY AT&T AND APPROVED BY THE DEPARTMENT?

1. YOUR INFORMATION MEMORANDUM TO THE ATTORNEY GENERAL OF JANUARY 6, 1982, STATES THAT, "I HAVE EXAMINED THE MERITS OF THE GOVERNMENT'S CASE CONCERNING IBM'S 'BAD ACTS' AND HAVE CONCLUDED THAT, WHILE SEVERAL MAY HAVE OCCURRED IN THE MANNER AND WITH THE INTENT ALLEGED, THE MOST PERSUASIVE EPISODES CONCERN COMPUTER SYSTEMS THAT ARE NOT INCLUDED WITHIN THE MARKET IBM IS ALLEGED TO HAVE MONOPOLIZED."
   (A) DO YOU BELIEVE THAT YOUR STATEMENT CREATES THE IMPRESSION THAT THE GOVERNMENT'S PROOF ON THE QUESTION OF ANY 'BAD ACTS' WAS IRRELEVANT TO THE CASE?
   (B) OF WHAT RELEVANCE WAS THIS PROOF TO THE STAFF'S THEORY OF THE CASE?

2. YOUR MEMORANDUM ALSO STATES THAT THE "COMPLAINT ALLEGES THAT IBM MAINTAINED A MONOPOLY POSITION LAWFULLY ACHIEVED. . ."
   (A) DOES THE COMPLAINT STATE THAT IBM ACHIEVED A MONOPOLY THROUGH LAWFUL MEANS?
   (B) AT THE TIME THE COMPLAINT WAS BROUGHT, DID THE DEPARTMENT OF JUSTICE CONSIDER CHARGING THAT A MONOPOLY HAD BEEN ACHIEVED UNLAWFULLY?

3. AS YOU KNOW, AT LEAST THREE MAJOR ANTITRUST CASES -- THE FEDERAL TRADE COMMISSION'S KELLOGG AND EXXON PROCEEDINGS AND THE ANTITRUST DIVISION'S IBM CASE -- HAVE BEEN DISMISSED IN THE LAST YEAR. IN EACH INSTANCE SUBSTANTIAL GOVERNMENTAL RESOURCES HAD BEEN EXPENDED IN THE PROSECUTION OF THE CASE OVER A NUMBER OF YEARS. IN TESTIMONY BEFORE THE SUBCOMMITTEE, MR. LEWIS BERNSTEIN, FORMER CHIEF OF THE SPECIAL LITIGATION SECTION, SUGGESTED THAT IT MIGHT

3. BE APPROPRIATE TO AMEND THE TUNNEY ACT TO REQUIRE THE PROSECUTORIAL AUTHORITIES TO FILE A DETAILED LEGAL MEMORANDUM THAT SETS FORTH THEIR REASONS FOR SUCH DISMISSALS. PLEASE DESCRIBE THE ADVANTAGES AND DISADVANTAGES OF SUCH AN APPROACH.

4. THE STIPULATION OF DISMISSAL STATES THAT THE "PLAINTIFF HAS CONCLUDED THAT THE CASE IS WITHOUT MERIT."
   (A) HOW WAS THE LANGUAGE OF THE STIPULATION DRAFTED?
   (B) WHICH PARTY TO THE CASE SUGGESTED THE PHRASE "WITHOUT MERIT?"
   (C) WERE THERE ANY DISCUSSIONS BETWEEN THE PARTIES ABOUT THIS PHRASE? IF SO, PLEASE RECONSTRUCT THE DISCUSSIONS TO THE BEST OF YOUR ABILITY, STATING PARTICULARLY ANY REASON THAT MAY HAVE BEEN EXPRESSED CONCERNING THE DESIRABILITY OF INCLUDING SUCH LANGUAGE.

5. AT SUBSEQUENT HEARINGS ON THE IBM AND AT&T CASES, WITNESSES IDENTIFIED THE LACK OF CONTINUITY IN THE STAFF AS A PROBLEM FOR THE DEPARTMENT OF JUSTICE IN LITIGATING MAJOR CASES.
   (A) DO YOU AGREE THAT THE LACK OF CONTINUITY IS A PROBLEM?
   (B) IF IT IS A PROBLEM, HOW CAN IT BEST BE SOLVED?

U.S. House of Representatives
Committee on Energy and Commerce
Room 2125, Rayburn House Office Building
Washington, D.C. 20515

January 29, 1982

Honorable Peter W. Rodino, Jr.
Chairman
Committee on the Judiciary
2137 Rayburn House Office Building
Washington, D.C. 20515

Dear Chairman Rodino:

We are sorry that we were unable to attend the hearing yesterday before the Subcommittee on Telecommunications, Consumer Protection and Finance and the Subcommittee on Monopolies and Commercial Law. However, during that hearing, we understand that you invited Members to submit written questions through you to the witness, Assistant Attorney General William A. Baxter. Pursuant to that invitation, we would like for you to address the following questions to Mr. Baxter:

1. Both H.R. 5158 and S. 898 contain provisions which require that AT&T's Western Electric shall sell specified amounts of telecommunications equipment to companies which are not affiliated with AT&T. We understand that the primary purpose of these provisions is to provide a market check on the price at which Western Electric sells such equipment within the AT&T organization. As we recall, you were a primary architect of these provisions. Do you believe that such provisions should still be included in legislation in view of the proposed divestiture of AT&T's local telephone operations, or do you believe that, after divestiture, Western Electric will have sufficient marketplace incentives to sell equipment on the outside to ameliorate your concerns?

2. Both H.R. 5158 and S. 898 require that AT&T affiliates purchase specified amounts of telecommunications equipment from manufacturers who are not affiliated with AT&T. We understand that these quotas were placed in the legislative proposals to promote the development of competition in the equipment manufacturing industry. Since AT&T's local telephone operations are to be divested under the proposed settlement, do you believe that the inclusion of such provisions is reasonable, or do you believe that divestiture of the local telephone operations should sufficiently promote a competitive manufacturing market?

3. Both H.R. 5158 and S. 898 prohibit AT&T from offering information publishing services. We understand that one of the primary reasons for this ban was the belief that AT&T, through its ownership of local telephone exchanges, might be able unreasonably to discriminate against other companies desiring to provide information publishing services. Do you believe that inclusion of provisions that prohibit AT&T from engaging in information publishing is reasonable or do you believe that the proposed divestiture by AT&T of its local telephone operations eliminates the need for the prohibition?

4. Both H.R. 5158 and S. 898 require that AT&T form a separate subsidiary to engage in competitive activities. We understand that a separate subsidiary requirement is thought to be necessary in order to prevent AT&T from subsidizing new, competitive activities with revenues that it earns from its provision of non-competitive, long-distance services. Do you believe that the requirement of a separate subsidiary is based on a valid premise; that is, do you believe that AT&T does not face effective competition in the long-distance markets in which it is engaged today?

[Please answer the following questions if the answer to the above question is that AT&T does not face effective competition.]

5. Do you believe that AT&T will face effective competition in the future? When?

6. What is the appropriate test for measuring the extent to which there is competition in the long-distance transmission markets?

7. Should those who provide services over facilities that they lease from others be counted as providing competition to those who provide services over facilities that they own themselves, or should competition be found to exist only where facilities-based service vendors face effective competition from other facilities-based vendors?

[Please answer the following questions only if you believe that a separate subsidiary is a necessary condition to AT&T's entry into competitive markets.]

8. Do you believe that minority outside ownership of AT&T's separate subsidiary would be justified? Why?

9. Do you believe that the separate subsidiary should be required to manufacture all terminal equipment that it will offer and conduct all of its own research and development activities, or do you believe that it should be allowed to rely on Western Electric? Why?

10. Do you believe that the separate subsidiary should be allowed to own its own transmission facilities, or should it be required to lease such facilities from others? Why?

11. Do you believe that the separate subsidiary should be permitted to offer long-distance services that are similar to those offered by AT&T under regulation? Why?

[Please answer the following question irrespective of your answers to any of the above questions.]

12. What is the policy justification for the provisions in the proposed settlement which, on one hand, prohibit the divested local telephone companies from entering competitive markets in the future but allow the new AT&T to enter monopoly markets in the future?

Thank you very much.

Sincerely,

Honorable James T. Broyhill
Ranking Minority Member
Committee on Energy and Commerce

Honorable Matthew J. Rinaldo
Member
Subcommittee on Telecommunications, Consumer Protection and Finance

Mr. RODINO. I know that you attempted to clarify what your policy is in not providing us with responses to certain requests that we make, whether they be for interviews, whether they be for documents. I would hope that the kind of letter that I write to you, if you do not feel that you are going to be able to comply with the letter, with the requests that are made, I would hope that then you would set down what your policy is, and you would let me have it in writing, so that I may have at least something that I may be able to rely on.

Mr. BAXTER. Surely, I will be happy to do that. Again, I can state the policy quite simply right now, but I will also repeat it at a later time.

I am anxious to get to you the information which constitutes responses to any question on any topic you may wish to ask. The vehicle for getting that information ought not to include procedures that will, not just in my view, but in the view of the Department and its regulations, interfere with the giving of free and frank advice by the career lawyers in the Department.

Mr. RODINO. Well, I can certainly appreciate that, and I respect that. I want to thank you for myself and the subcommittee for the patience you have demonstrated. I know that you had to make a special trip back here early in the morning when we changed our schedule from 9:30 to 9. I appreciate your promptness.

Thank you very much, and that concludes this hearing.

[Whereupon, at 3:26 p.m., the hearing was adjourned.]

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