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## Telecommunications In A Dearth Of Capital: A Changed Paradigm That Requires A New Way Of Thinking

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**TELECOMMUNICATIONS IN A DEARTH OF CAPITAL:  
A CHANGED PARADIGM THAT REQUIRES A NEW WAY OF  
THINKING**

by

Jennifer A. Manner\*

Just a few years ago capital for the construction and operation of telecommunications facilities was readily available to new and long-established entities for both traditional services and expansion into new and innovative telecommunications services offered to consumers. While investments in new infrastructure were not always successful or profitable in their ventures, entities were generally able to raise sufficient capital in the markets to adequately fund their efforts when they had sound business cases. This meant that regulators and policy makers in the telecommunications area had greater confidence that a hands-off approach or an approach of service and facilities enablement would result in their policy goals generally being reached.<sup>1</sup> Of course, not being naïve, policymakers also had a keen recognition that the market would not always fund everything that policy makers wanted to achieve. In those cases, these regulators and market-based policymakers would swerve from their traditional hands-off course of conduct and establish mandates, such as providing emergency communications services or other public interest services.<sup>2</sup>

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<sup>1</sup> See Kathleen Q. Abernathy, *The Nascent Services Doctrine: Remarks of the FCC Commissioner Before the Federal Communications Bar Association*, N.Y. Chapter (July 11, 2002), *available at* <http://www.fcc.gov/Speeches/Abernathy/2002/spkqa217.pdf>.

<sup>2</sup> See Michael K. Powell, FCC Chairman, *Statement on Implementation of Hearing Aid Compatibility Rules* (July 10, 2003), *available at* [http://hraunfoss.fcc.gov/edocs\\_public/attachmatch/DOC-236430A2.pdf](http://hraunfoss.fcc.gov/edocs_public/attachmatch/DOC-236430A2.pdf).

With the recent severe economic down-turn and the arrival of a new Administration in Washington, D.C., many telecommunications industry observers and participants are becoming aware that the hands-off, market-based policies that have governed telecommunications may need to be re-evaluated – for example through the broadband stimulus grant program.<sup>3</sup> This article examines why market-based regulation still is relevant, even in today's capital-starved telecommunications markets. what actions policymakers are taking to ensure continued funding for critical communications services and associated job creation, and what these policy makers should do to ensure that such actions do not result in a distortion of the competitive telecommunications market, which in the past has resulted in substantial consumer benefits.

## I WHY MARKET-BASED REGULATION STILL MAKES SENSE

Any long-term participant in the telecommunications industry will remember the days of heavy-handed regulation in the telecommunications sector. In hindsight, such regulation spurred innovation, as well as reduced rates, and where regulation fell short, competition has stepped in to cure many of the ills that regulation was aimed at correcting. However, it is important to remember the old days of a heavily regulated telecommunications marketplace where there was limited customer choice, expensive rates and where innovation was limited, especially since that type of market continues to exist in certain countries around the world and certain policy choices that are being made in the United States today may require revisiting the imposition of some of these type of regulations.

In the early years of telecommunications, many markets were dominated by a single telecommunications provider.<sup>4</sup> While in many

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<sup>3</sup>See e.g., Press Release, International Telecomm. Union, High Level Forum Will Address Financial Crisis, (Feb. 12, 2009), *available at* [http://www.itu.int/newsroom/press\\_releases/2009/02.html](http://www.itu.int/newsroom/press_releases/2009/02.html); *Media and Telecom Policy Developments 2008*, BENTON FOUNDATION, <http://www.benton.org/node/17461> (last visited Mar. 25, 2009).

<sup>4</sup> See generally JENNIFER A. MANNER, INTERNATIONAL TELECOMMUNICATIONS MARKET ACCESS, at Chapters 1-4 (Artech House 2002).

countries this dominant provider was government owned, in some, like the United States, a virtual monopoly was given to a commercial entity, in this case, AT&T Communications, Inc.<sup>5</sup> While certain important policy goals could often be achieved via a monopoly provider, many others, such as reasonable prices for services, universal service (though not such a problem in the United States, because of other policies), and innovation were often negatively impacted. Because of these hindrances, and because of the development of technology and increasingly open global markets, many countries starting in the 1980s faced pressure to open their telecommunications markets to competition and became market-openers.<sup>6</sup> Governments taking the path towards a liberalized telecommunications market faced at least one daunting problem: how to ensure that a dominant, in many cases monopoly, provider, did not abuse its market-position in such a way that resulted in competition being stalled and new entrants being unable to successfully enter a market.<sup>7</sup>

To remedy this, among other ills, regulators enacted regulations that curbed this potential anti-competitive conduct, to ensure that the new entrants would be able to enter into what can be termed a “level-playing field.”<sup>8</sup> While this type of regulation, which continues today in many markets, was not market-based, it was necessary to ensure that new entrants could enter markets that had previously been denied to them or that they were blocked from entering. In countries where such regulations were effectively enacted and enforced, consumers have been able to gain access to advanced telecommunications services at reduced

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<sup>5</sup> *Id.*

<sup>6</sup> See HANK INTVEN, JEREMY OLIVER & EDGARDO SEPULVEDA, TELECOMMUNICATIONS REGULATION HANDBOOK: OVERVIEW OF TELECOMMUNICATIONS REGULATION 6-2 (Hank Intven ed., McCarthy Tetrault 2000), available at <http://www.infodev.org/en/Publication.22.html>.

<sup>7</sup> See generally WILLIAM E. KENNARD, FCC, CONNECTING THE GLOBE: A REGULATOR'S GUIDE TO BUILDING A GLOBAL INFORMATION COMMUNITY (FCC International Bureau eds., 1999), available at <http://www.fcc.gov/connectglobe/>.

<sup>8</sup> See, e.g., *Id.*; MANNER, *supra* note 5.

prices.<sup>9</sup> Further, the teledensity of the availability of telecommunications services has increased dramatically.<sup>10</sup>

However, savvy regulators and policymakers recognized that as established markets became competitive, and as new markets such as the Internet with no dominant service provider emerged, it was not necessary to retain or enact such regulatory schemes, since there was no real potential for market abuses based on a dominant position.<sup>11</sup> Instead, regulators and policy makers in these areas have focused on a more hands-off approach to regulation, e.g., stepping in to regulate where it makes the most sense, such as generic technology standards to ensure that services can interoperate, and to fulfill public interest goals that might not otherwise be met, such as the availability of emergency communications.

A noticeable success of pro-competitive telecommunications policies is the terrestrial wireless market, where cell phones and other mobile devices have widely proliferated. At least 60 percent of the world's population has a cell phone.<sup>12</sup> Compare this to a figure from less than ten years ago when it was estimated that over fifty percent of the world's population had not even made a voice phone call.<sup>13</sup>

What is equally interesting is how the market has responded to the needs of consumers in offering such services. While there continues to be a wide proliferation of billing in arrears for cellular-type services,

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<sup>9</sup> KENNARD, *supra* note 8, at 2.

<sup>10</sup> MANNER, *supra* note 5.

<sup>11</sup> See Abernathy, *supra* note 1, at 2.

<sup>12</sup> Geoff Duncan, *Sixty Percent of Humanity Has a Cell Phone*, DIGITAL TRENDS, Dec. 26, 2008, <http://news.digitaltrends.com/news-article/18745/sixty-percent-of-humanity-has-a-cell-phone>.

<sup>13</sup> Cees J. Hamelink, *The Digital Advance: More than half the world's people have never made a phone call. Will ICTs assure us change?*, UNITED NATIONS RESEARCH INST. FOR SOC. DEV., June 1, 1998, <http://www.unrisd.org/unrisd/website/newsview.nsf/0/34329FCA3B21925D80256B7B003DCF2A?OpenDocument> (last visited Mar. 25, 2009).

other options have become increasingly popular for consumer segments where a pay-as-you-go or prepay approach makes more sense.<sup>14</sup>

Accordingly, one very successful scheme for policymakers and regulators has been to create a regulatory structure that enables new technologies and services, and to impose few regulatory requirements that are overly burdensome or add significant costs on the provider, except where there are overwhelming public interest requirements that must be met.<sup>15</sup>

Despite these and other successes, even the most advanced thinking regulators and policymakers recognize the need to impose non-market based regulations in some cases. An example of this was the FCC's triennial review proceeding.<sup>16</sup> In this proceeding, the FCC, by majority, turned over to the States the determination of whether to allow unbundled switching. This decision, while ultimately overturned by the courts, left a chill in the air for regulatory certainty and pro-market regulation.<sup>17</sup>

One noticeable attribute of market-based regulation, however, has been the availability of capital for large-scale deployments of telecommunications infrastructure and access to scarce resources, such as spectrum.<sup>18</sup> Unfortunately, with the economic downturn in the United States, this availability of ready capital is in question. Without access to capital, the competitive telecommunications market, without some form of government enablement may not be able to achieve what current and incoming policy makers see as important policy goals. The broadband stimulus legislation thus is timely and important.

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<sup>14</sup> For example, companies such as Virgin Mobile, have made substantial in-roads into the pre-pay cellular market place. See Roger Cheng, *Virgin Mobile Is Set to Ride Budget-Minded Trend*, WALL ST. J., Feb. 3, 2009, <http://online.wsj.com/article/SB123370253990245341.html>.

<sup>15</sup> MANNER, *supra* note 5.

<sup>16</sup> U.S. Telecom Ass'n v. F.C.C., 359 F.3d 554, 360 U.S.App.D.C. 202, 31 Commc'ns Reg. (P&F) 1221 (D.C. Cir. Mar. 2, 2004).

<sup>17</sup> *Id.* at 585.

<sup>18</sup> See FCC: Spectrum Auctions, [http://wireless.fcc.gov/auctions/default.htm?job=auctions\\_home](http://wireless.fcc.gov/auctions/default.htm?job=auctions_home) (last visited Apr. 16, 2009).

## II WHY MARKET-BASED POLICIES SHOULD NOT BE ABANDONED

Based on the actions of the new President and the Congress, it appears that at least for the foreseeable future increased broadband deployment at high speeds to all Americans will continue to be a key goal.<sup>19</sup>

In today's policy debate, there are different ways to achieve this goal, with very different outcomes likely. However, the most interesting part of the current policy debate is a belief that a market-based approach to regulation will not achieve these goals on their own; that is, that the market may not provide the types of broadband access to unserved and underserved portions of the United States without government funding sources. While this may be a fair assessment, and more may need to be done, it is important for regulators and policymakers to be careful where they step in and recognize that providing government funding and taking other similar actions without ensuring that competition is protected may result in substantial future harm to the telecommunications market in ways that are not currently appreciated.

A starting point is to analyze the universal broadband deployment policy goal and the best possible approach to achieving it, recognizing the shortage of capital. In the past twenty years, U.S. policy makers would have created a regulatory scheme that was an "enabler" in enticing the provision of nationwide broadband communications.<sup>20</sup> This approach has been pursued over the past few years with some success. However, even if a regulatory scheme enables the provision of these services, it is questionable whether in today's economic climate such ambitious facilities building projects, which will be necessary to fulfill this goal, can be met unless the government creates financial incentives. Hence, going forward we are likely to see the current and continued efforts to provide funding mechanisms to ensure the deployment of this broadband infrastructure for all Americans, which is a very expensive endeavor.

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<sup>19</sup> See Barack Obama: Technology, <http://www.barackobama.com/issues/technology/> (last visited Mar. 21, 2009).

<sup>20</sup> See Abernathy, *supra* note 1, at 1.

This includes the most recently adopted stimulus legislation, where grants and loans for broadband service are being awarded especially in unserved and underserved areas.<sup>21</sup>

The first problem with such an approach is the right speed (assuming there is only one speed) for the provision of broadband communications in all areas of the country,<sup>22</sup> and how the cost of this build-out will be funded, especially in a capital-starved telecommunications industry.<sup>23</sup>

In terms of required speed for broadband, this is a very tricky question. As most people are aware, the speeds available for data connections keep increasing as technology continues to evolve. Only two to three years ago, many in the United States believed that it would be a tremendous goal if Americans could receive access to one Mbps of capacity each. Today, that number does not even come close to the speeds that are being proposed by policymakers throughout the country; speeds as fast as 100 times this rate are now being considered.<sup>24</sup> These are the sorts of speeds that are being advanced by the high-technology industry players, such as chipset manufacturers, as necessary to carry the data that they believe will be associated with networks in the near future. However, the access to such speeds comes at a cost. For example, many rural areas of the United States today do not even have access to the lower speeds that were envisioned a few years ago. These consumers would likely be happy to have what is now seen as basic service to as compared to broadband, such as wireless or satellite communications, that generally offer lower speed services.

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<sup>21</sup> American Recovery and Reinvestment Act of 2009, Pub. L. No. 111-05, § 6001, 132 Stat. 115 (2009).

<sup>22</sup> See PHILIP J. WIESER, *THE UNTAPPED PROMISE OF WIRELESS SPECTRUM* (The Brookings Institution ed., The Hamilton Project 2008), available at [http://www.brookings.edu/papers/2008/07\\_wireless\\_weiser.aspx](http://www.brookings.edu/papers/2008/07_wireless_weiser.aspx) (recognizing the importance of alternate technologies to achieve broadband build-out).

<sup>23</sup> David Gardner, *U.S. Broadband Speeds Continue to Lag*, INFORMATION WEEK, Aug. 12, 2008, <http://www.informationweek.com/news/telecom/policy/showArticle.jhtml?articleID=210002769>.

<sup>24</sup> See *Broadband Speeds*, <http://www.broadbandwatchdog.co.uk/broadband-speeds.php> (last visited Mar. 25, 2009).



Accordingly, U.S. policy makers must not limit their incentives to a chosen one or two technologies, but look across all platforms to ensure that whatever platform makes the most sense in a geographic area is able to be utilized and can receive financial incentives for infrastructure and deployment. Accordingly, the recent stimulus legislation, which did not mandate speeds, but encouraged high speeds, is right on the mark.<sup>25</sup> However, the legislation still leaves some discretion as to speed requirements with the National Telecommunication and Information Administration of the Department of Commerce, which will administer the broadband grants. The Department of Commerce needs to refrain from imposing speeds in a vacuum without taking into consideration deployment costs in its analysis.

Another possible negative effect of such financial incentives is the potential reduction of competition. By relying on government funding of these systems, how does competition take hold? Are we once again creating a government-funded monster (or perhaps lots of monsters) that future new entrants, who are not beneficiaries of this funding, will not be able to compete with? This could negatively impact the deployment of next-generation technologies that could bring unanticipated consumer benefits to Americans.

It is imperative that the United States government recognize what they are potentially doing if they allow for funding of broadband without appropriate regulatory safeguards in place. In essence, what can be created in order to give juice to additional infrastructure builds is an industry where certain competitors will be allowed to build out their systems with government funding. This will make it extremely hard for new entrants to enter the market place. The only way to prevent such a perversion is to recognize the need for competitive safeguards.

Accordingly, while Congress and other U.S. policymakers are crafting such financial schemes, it is imperative that they also consider imposing certain safeguards to guard against the anti-competitive effects of funding. While the stimulus legislation recognizes the possibility of such safeguards, they are narrowly and ill defined. While they recognize the possibility of non-discrimination and network interconnection restrictions, they do not provide safeguards that will ensure that the use of such financial incentives does not inure to other business lines of the

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<sup>25</sup> American Recovery and Reinvestment Act, *supra* note 21.

receiving company. Cross-subsidization of other areas could negatively affect competition in competing businesses by providing the funded entities with means to their lower their prices to the detriment of their competitors who are not benefiting from the same financial incentives. Further, if there is no ability for new entrants to effectively compete in certain markets, this may result in a monopoly situation, hence allowing the subsidized entities to charge monopoly rates and further harm consumers.

This was similar to what was done early in the telecommunications industry when cross-subsidization of services was permitted in order to achieve important policy goals (in this case, universal service for basic telephony).<sup>26</sup> However, there were no competitive providers of telecommunications services in that era. In fact, when competition was introduced, policy makers were careful to ensure that incumbents did not use the money they earned for monopoly services to fund competitive services. It would seem that as policy makers look at mechanisms to ensure that market distortion does not flow from the introduction of financial incentives to deploy broadband infrastructure, restrictions on cross-subsidization should be revisited and possibly imposed as a condition to funding.

Other problems involve restrictions on reasonable terms and conditions being set on special access to broadband wireline communications. Special access circuits are essential inputs (dedicated telecommunications facilities) that all telecommunications carriers, both wireline and wireless use to reach their customers and connect their networks. Financial incentives are likely to be provided as part of the upcoming stimulus package for broadband special access.<sup>27</sup> To date, even without financial incentives, many parties have alleged that the providers of special access have been engaging in anti-competitive conduct through inflated prices and the imposition of anti-competitive terms and conditions.<sup>28</sup> The addition of financial incentives could cause

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<sup>26</sup> Steve G. Parsons, *Cross-Subsidization in Telecommunications*, 13 J. Reg. Econ. 157-182 (1998), available at <http://ideas.repec.org/a/kap/regeco/v13y1998i2p157-82.html>.

<sup>27</sup> American Recovery and Reinvestment Act, *supra*, note 21.

<sup>28</sup> Press Release, Comptel, NRRI Study Finds Fault in FCC's Special Access Methodology (Jan. 8, 2009), available at <http://www.comptel.org/content.asp?contentid=2381>.

more allegations of anti-competitive conduct, possibly to the detriment of competition. Specifically, artificially inflated special access prices bring increased costs to competitors, and therefore reduce the capital those competitors have available to build new infrastructure, thus harming consumers. Accordingly, before any financial incentives are provided to providers of special access, appropriate anti-competitive safeguards must be in place and well defined.

These examples demonstrate that policymakers must carefully evaluate how to balance the very important goals of increased deployment of broadband service and ensuring that competition continues to be vibrant in the telecommunications market. Failure to ensure that anti-competitive behavior will not be the result of any stimulus legislation could result in a market place that denies consumers the lower prices and innovative services that have been the direct result of a competitive telecommunications marketplace ultimately harming U.S. consumers.