



## **Local Telephone Competition: The Road to Economic Growth**

### ***Introduction***

Nearly five years ago, Congress passed the Telecommunications Act of 1996 (The Act). This groundbreaking law ended the 100+ year local telecommunications monopoly held by the Regional Bell Operating Companies (RBOCs) or Baby Bells. The immediate result of The Act was the creation of a new breed of company called competitive local exchange carriers (CLECs). The nascent CLEC industry competes with the Baby Bells in the \$100+ billion local telecommunications market, providing voice and data services to businesses and residential consumers alike. Five years after the passage of The Act, CLECs have competed vigorously with the RBOCs and now claim 6% to 8% of the local telecommunications market<sup>1</sup>. These emerging competitors have promoted the deployment of high-speed broadband services, ignited the explosive growth of the Internet and contributed to the nation's longest economic expansion in history.

However, bringing true competition to the marketplace has been an uphill battle. For over two years, the RBOCs sued to block implementation of The Act. Even today, CLECs continue to face anti-competitive barriers and marketplace failures in attempting to bring competition to local markets. The three greatest market failures that stymie full, effective competition are: (1) the failure of the incumbent local exchange carriers (ILECs) to open their networks to competition, (2) the failure of building owners to open their buildings to competitors, and (3) the failure of municipalities to approve competitive entry.

### ***The Act, the Internet & Economic Growth***

Realizing the importance of the Internet, Congress instructed the FCC and state regulatory bodies to "encourage the deployment on a reasonable and timely basis of advanced telecommunications capability to all Americans"<sup>2</sup>. This provision of The Act promised to ensure that the United States would lead the world in Internet accessibility and placed a priority on the deployment of advanced telecommunications services (broadband) as a means to economic growth.

When The Act was passed, most Internet users were large institutions (e.g., universities, libraries, etc.). The Act dramatically altered the Internet landscape. CLECs set out to serve an untapped and underserved market among Internet Service Providers (ISPs) and small and medium-sized businesses. These two customer groups required new technologies that could be customized and rapidly deployed. Because the ILECs were unwilling or unable to cater to the needs of ISPs and small business, CLECs found a market niche in which their superior technology, enhanced time-to-market and customized products were enthusiastically embraced.

CLECs have been enormously successful in deploying these new broadband technologies, and now serve over 20% of all broadband customers. CLECs have focused on bringing DSL, fixed

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<sup>1</sup> Federal Communications Commission (FCC). *FCC Releases Data on Local Telephone Competition*. December 4, 2000 & New Paradigm Resource Group (NPRG). *CLEC Report 2001 (13<sup>th</sup> edition)*. December 2000.

<sup>2</sup> The principal section of the 1996 Act concerning advanced telecommunications services is Section 706, Pub.L. 104-104, Title VII § 706, Feb. 8, 1996, 110 Stat. 153, reproduced in the notes under 47 U.S.C. § 157.

wireless, and fiber technologies to the market. The new telecom networks built by the CLECs have fueled the explosive growth of Internet connectivity and economic growth. As Texas Public Utility Commissioner Brett Perlman noted, "providing high quality telecommunications infrastructure will be the key to Texas' economic growth in the 21<sup>st</sup> century. In particular, broadband deployment will become a primary driver of economic development in the Texas economy."<sup>3</sup> What is true for Texas is equally true for the nation as a whole.

### ***Impediments to Fulfilling the Promise of The Act***

Despite the progress made by CLECs, a number of impediments still exist to full, effective competition and broadband deployment:

- ILECs have been unable or unwilling to open their markets to competition (despite their legal obligation to do so). **According to the FCC, after almost five years, the ILECs have opened their networks to competitors in only two states.** As a result, CLECs have great difficulty interconnecting with the Bell Company networks to provide advanced services.
- Building owners refuse to give tenants access to high-quality, affordable telecommunications services provided by competitors. Many building owners give exclusive access to telecom companies they own, and bar entry by unaffiliated competitors.
- Municipalities overregulate competitors and charge CLECs excessive fees. Whether unintentional or not, the cities' actions contribute to perpetuating the ILEC monopoly.

There are financial impediments to fulfilling the Act as well. CLECs have been especially hard hit in the recent market downturn. The *Bear Stearns CLEC Index* shows that the stock prices of the public CLECs are **down 73.1%** since the beginning of 2000. In the meantime, the Baby Bell Companies have grown even stronger by merging instead of competing with each other.

### ***Conclusion***

One of the most significant results of the passage of The Act has been its contribution to the explosive growth of the Internet and the resulting economic expansion in the United States within the last five years. Federal Reserve Vice Chairman Roger Ferguson, Jr. notes that the investments made by the communications industry along with broad deregulatory initiatives (such as the 1996 Act) are the two leading contributors to sustained domestic economic growth.<sup>4</sup>

However, the nation's telecom competition policy, and our nation's economic growth, are in great peril. The competitive community is in an extremely fragile state. Of the over 300 CLECs that began providing service since 1996, only a handful of companies are cash-flow positive today. Several CLECs have declared bankruptcy and several others are on the verge of failing. Not surprisingly, the nation's economy is slowing as well.

Our competition policy is at a critical juncture. The Act launched a new industry, but its long-term success depends upon whether or not the remaining barriers to competition are removed. Now is the time for policymakers to take additional action to promote competition. Only then will investors have the confidence to contribute their capital to the companies that are building our nation's digital future and solving the "Digital Divide."

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<sup>3</sup> 'PUCs Perlman Sees Broadband As Crucial to Development of Texas Economy'. *Texas CLEC Bulletin*. Volume 2, Issue 11 (Nov. 1999). <http://www.puc.state.tx.us/about/perlmaninterview.cfm>

<sup>4</sup> Remarks by Vice Chairman Roger W. Ferguson, Jr. Widener University, Chester, Pennsylvania (April 6, 2000). <http://www.federalreserve.gov/BOARDDOCS/SPEECHES/2000/20000406.htm>