UNITED STATES OF AMERICA
FEDERAL TRADE COMMISSION
WASHINGTON, D.C. 20580

BEFORE THE
FEDERAL COMMUNICATIONS COMMISSION
WASHINGTON, D.C.

In the Matter of
Rulemaking to Amend Parts 1, 2, 21, and 25 of the Commission's Rules
to Redesignate the 27.5-29.5 gHz Frequency Band,
to Reallocate the 29.5-30.0 gHz Frequency Band,
to Establish Rules and Policies for
Local Multipoint Distribution Service and for Fixed Satellite Services)

CC Docket No. 92 -297

Reply Comment of the Staff of the
Bureau of Economics of the Federal Trade Commission(1)
August 22, 1996

I. Introduction

The Staff of the Bureau of Economics of the Federal Trade Commission ("FTC Staff") welcomes this opportunity to comment on proposed regulations concerning eligibility restrictions on Local Multipoint Distribution Service ("LMDS") spectrum licenses in the 28 gHz band.(1) The Federal Communications Commission ("FCC") recently released the *First Report & Order and Fourth Notice of Proposed Rulemaking ("4th NPRM")* in its ongoing proceeding to allocate spectrum in this band.(2) Spectrum in this bandwidth can be used for a variety of purposes, including the provision of LMDS. LMDS uses super-high frequency microwaves to send and receive two-way signals in an area, or cell, approximately 3 to 6 miles in diameter. In some respects, it works like the narrowband operations of cellular telephone systems. However, the video, voice, and data broadband LMDS signals are two-way capable (*i.e.,*subscribers can both send and receive signals). Based on the material accumulated over the course of this proceeding, the FCC has concluded (*4th NPRM,* ¶ 14) that there is a substantial likelihood that LMDS will be able to provide competition to facilities-based local phone companies (local exchange carriers, or "LECs") and to cable television operators.(3)

II. Expertise of the Staff of the Federal Trade Commission

The FTC is an independent agency responsible for preventing unfair methods of competition and unfair or deceptive acts or practices.(4) In response to requests by federal, state, and local government bodies, the staff of the FTC often analyzes regulatory or legislative proposals that may affect competition or the efficiency of the economy. In the course of this work, as well as in antitrust and consumer protection research, nonpublic investigations, and litigation, the staff

applies established principles and recent developments in economics to the analysis of competition and consumer protection matters.

The staff of the FTC frequently has commented on competition issues in communications, beginning with a 1924 report to the House of Representatives about competition issues in radio.(5) More recently the staff has submitted comments to the FCC on the implementation of the portion of the Telecommunications Act of 1996(6) that relates to the establishment of open video systems (OVS);(7) the Prime Time Access Rule;(8) television and radio ownership rules and policies;(9) competition, rate deregulation, and cable television service;(10) common ownership of cable systems and national television networks;(11) the "must carry" rules applied to cable television systems;(12) the rules requiring broadcast licenses to be held for three years before being transferred;(13) network ownership of financial interests and syndication rights;(14) spectrum allocation and standards for digital audio broadcasting;(15) and the regulation of "900" telephone number services.(16)

circumstances) that the former would not find it most profitable to “warehouse” these rights (*i.e.,* hold them idle). But this does not mean that the acquisition of these rights could not be anticompetitive (compared to the acquisition of those rights by an equally efficient third party). This point is most easily seen by simple analogy to horizontal merger analysis. In those horizontal mergers where conditions are conducive to the creation of post-

that “cable television systems remain the primary distributors of multichannel video programming services and continue to enjoy market power in local markets” — remains valid.

A similar conclusion appears warranted with respect to competition in local telephony markets. Although it appears likely that some local markets will witness competitive alternatives to wireline services purchased directly from traditional LECs — a development that likely will be accelerated by the recent FCC action in CC Docket No. 96-98(33) — it would appear, as with MVPD markets, that it is premature to conclude that local telephony is now sufficiently competitive to eliminate competitive concerns that would arise from a LEC acquiring the sole LMDS license in an overlapping service area.(34) Some users — mainly large business customers — have been able to bypass LEC trunk lines by purchasing private line access to the interexchange (*i.e.,* long distance) carriers from “competitive access providers.” But these providers still account for only a very small share of the market for access to local exchange networks. Most small businesses and residential customers are still dependent upon the LECs for access to interexchange carriers, and for the completion of local calls.(35)

As a possible approach to address this issue, the FCC has proposed (*4th NPRM*, ¶ 132) to adopt a rule similar to the cellular/PCS cross-ownership rule. Consistent with this rule, an incumbent LEC or cable operator would be considered "in-region" if 20 percent or more of the population of a BTA is within a LEC's telephone service area or a cable company's franchised service area. While the FTC staff lacks sufficient information to recommend or endorse a particular numerical threshold for such a rule, in principle the use of such a threshold could contribute to economic efficiency.

IV. Conclusion

Until such time as effective competition is present in MVPD and local telephony markets, the acquisition of LMDS spectrum licenses by competing LECs and cable operators presents potentially significant competitive risks.(46) Accordingly, we believe that there is a reasonable basis for restricting these parties from acquiring LMDS licenses when substantial geographic service area overlaps would result. Although we cannot endorse a particular numerical criterion for determining when such eligibility restrictions would be triggered, we believe that the approach suggested by the FCC in the *4th NPRM* is sound.

(1) This comment represents the views of the staff of the Federal Trade Commission. They are not necessarily the views of the Federal Trade Commission or any individual Commissioner. Inquiries regarding this comment should be directed to Mike Vita (202-326-3493).

(2) *First Report & Order and Fourth Notice of Proposed Rulemaking* in the Matter of Rulemaking to Amend Parts 1, 2, 21, and 25 of the Commission's Rules to Designate the 27.5-29.5 gHz Frequency Band, to Reallocate the 29.5-30.0 gHz Frequency Band, to Establish Rules and Policies for Local Multipoint Distribution Service and for Fixed Satellite Services, CC Docket No. 92-297, July 22, 1996.

(3) Currently there is a 50 channel LMDS system operating in Brighton Beach, NY (Brooklyn), that has approximately 5,000 subscribers.

(4) 15 U.S.C. §§ 41-49.

(5) Federal Trade Commission, *Report on the Radio Industry,* GPO, 1924.

(6) Pub. L. No. 104-104, 110 Stat. 56.

(7) CS No. 96-46 (1996).

(8) MM No. 94-123 (1994).

(9) MM Docket No. 91-140 (1991); MM Docket No. 91-221 (1992)..

(10) MM No. 89-600 (1990).

(11) CT No. 82-434 (1982).

(12) MM No. 90-4 (1991).

concern arising from the LEC's acquisition of a potential competitor. Second, if (as seems likely) LMDS providers will require access to some of the LEC's "bottleneck" facilities, then joint ownership of these facilities and the LMDS license could (depending upon the effectiveness of Federal and state antidiscrimination regulations) result in the LEC discriminating in favor of its LMDS affiliate, to the detriment of other local wireline competitors (*i.e.,* full- and partial-facilities entrants, and "resellers"). Third, if the provision of LMDS does not involve the use of the LEC's local physical facilities, this seemingly rules out one source of scope economy that could provide an efficiency rationale for the LEC to acquire an overlapping LMDS license. We discuss further the issue of scope economies in § III.C below.

(35) For a general discussion of these issues, *see* Schwartz, "Telecommunications Reform in the United States: Promises and Pitfalls," in Welfens and Yarrow, eds., *Telecommunications and Energy in Systemic Transformation: International Dynamics , Deregulation, and Adjustment in Network Industries*, 1996, esp. § 4.3.

(36)" Bell Atlantic, *Comments in Response to the 3rd NPRM*, *supra* note 28, p. 6.

(37)" NCTA, *Comments in Response to the 3rd NPRM*, September 7, 1995, p. 5.

(38)" U.S. West, *Comments in Response to the 4th NPRM*, *supra* note 21, p. 3.

(39) The recently issued FTC Staff Report *Anticipating the 21st Century: Competition in the New High-Tech, Global Marketplace (vol. I),* May 1996, ch. 2.III.H, discusses in greater detail evidentiary issues associated with assessment of economic efficiencies in merger analysis.

(40) Basic Trading Areas (BTA) surround a metropolitan area or city and are made up of one or more county boundaries. These areas contain the residents who make the majority of purchases for general merchandise or specialized services such as medical care and entertainment within that metro area. Some Basic Trading Areas contain more than one city because residents may conveniently shop at either one. For example, the New York BTA includes a total of 26 counties from NY, CT, NJ and PA that surround the New York metropolitan area. The Washington BTA, for example, includes the immedi-3(T)1(A)2(, da)4(s)-1(a.)-4(r)-(r)3(om)-2(N)2(Y)2(, C)-3 5.
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(42) As we argued above, given the current structure of most local MVPD markets, acquisition of the overlapping LMDS license by the incumbent cable operator license would likely increase the latter's market power.

(43) A possible example might be when a cable MSO owning a small system contained entirely within the BTA seeks to acquire the associated LMDS license. There, the MSO could alleviate any anticompetitive concerns simply by selling the system. Unless there are substantial efficiency losses to the MSO from this divestiture (or from forgone scope economies; *see* § III.D, *supra*), this will be an efficient way to address the FCC's competitive concerns.

(44) As the *4th NPRM* notes (¶ 132), "LATA lines and cable franchise areas are not coincident with BTA boundaries."

(45) Similar situations could of course arise in the case of cable systems.

(46) We agree with the FCC (*4th NPRM*, ¶ 135) that any blanket restrictions on LMDS license eligibility should be imposed only until there is effective competition in MVPD and local telephony markets.