Letters

We welcome letters from readers, particularly commentaries that reflect upon or take issue with material we have published. The writer's name, affiliation, address, and telephone number should be included. Because of space limitations, letters are subject to abridgment.

After the Legislative Veto

TO THE EDITOR:

In the July/August issue of *Regulation*, Theodore Olson ("Restoring the Separation of Powers") and Michael Davidson ("Reflections from the Losing Side") discussed the Supreme Court decision in *Immigration and Naturalization Service* v. *Chadha*. Messrs. Olson and Davidson both suggest that, in the absence of a legislative veto, it is particularly important for Congress to develop some device to ensure accountability by independent regulatory agencies. In my judgment, the importance of such a mechanism cannot be overstated. Indeed, I believe that in the long run Congress should resolve the status of the independent agencies by addressing their organic statutes.

The Federal Trade Commission, for example, can issue rules to restrain "unfair or deceptive acts or practices." Although the meaning of these terms is not at all clear, Congress has provided little guidance on how this broad authority should be exercised. The courts, in large measure, have said that these terms mean whatever a majority of the commission says they mean. Not surprisingly, with such broad discretion to issue industry-wide rules, the FTC has sometimes been characterized as "the second most powerful legislative body in America."

It will take some time for Congress to consider these enabling statutes. Consequently, in the short run, a way should be found to control excesses that may result from overly broad delegations of power. In particular, I think some form of constitutionally valid congressional veto is needed, at least for independent agencies. Specifically, I believe Congress should consider enacting a modified form of the legislative veto mechanism that might be called simply a "regulatory veto." (My comments here apply only to the regulatory agencies; I express no view on the use of the veto in other areas of government.)

The typical legislative veto consisted of three parts. First, there was a "laying on the table" requirement. That is, any regulation any agency promulgated could not become effective for, say, ninety days, so that Congress had time to act.

Second, the proponents of a veto resolution could use expedited procedures to force it to the floor of the House and Senate for an up-or-down vote. This was absolutely essential to prevent a bare majority of the relevant congressional committee, or even a reluctant chairman, from bottling up any veto initiative.

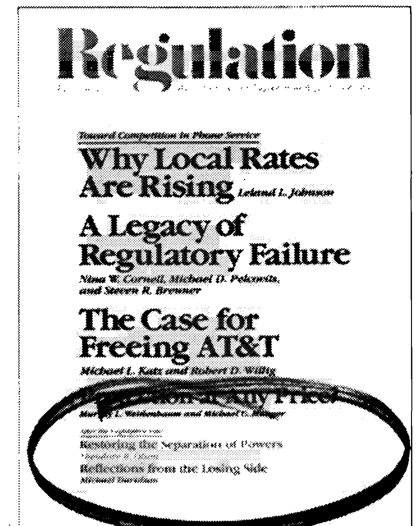
Finally, there were the provisions that raised the bicameralism and presentment clause problems. In some cases, the veto resolution required the vote of only one house (or one house in the absence of offsetting action by the other house). But the essence of the legislative veto was final, determinative action by Congress, without presidential approval or veto override. These were the grounds on which the Supreme Court found the device unconstitutional.

The only changes necessary to make the typical legislative veto constitutional are to provide for concurrent action by both chambers and to include presentment to the President. In short, Congress can retain the delay provision and the expedited procedures, while avoiding the constitutional problems, by turning the veto resolution into an ordinary law through the vehicle of a joint resolution.

I believe such an approach would give Congress the breathing room in which to address authorizing statutes with more precision. It would afford Congress almost as much control over potential agency excesses as the typical legislative veto. It also would allow the legitimate work of the regulatory agencies to move forward, while getting Congress out from under the avalanche it would take on if it tried to require affirmative approval of every new agency rule.

I must admit that this remedy would not solve all the serious problems created by an unresponsive bureaucracy. Similarly, statutory redefinition can go only so far. Congress will inevitably give agencies fairly broad mandates, since it wants them to have the flexibility they need to resolve hard questions. In view of that, how do we make the independent agencies publicly accountable?

In its *Chadha* decision, the Supreme Court took the unassailable position that the Constitution recognizes only three branches of government. The legislature legislates, with presentment to the President; the executive enforces and administers the laws; and the judiciary judges. The Court adamantly disagreed with the argument that some


Regulation

Toward Competition in Phone Service

Why Local Rates Are Rising

Leland L. Johnson

A Legacy of Regulatory Failure

Nina W. Cornell, Michael D. Pelcovits, and Steven R. Brenner

The Case for Freeing AT&T

Michael L. Katz and Robert D. Willig

Restoring the Separation of Powers

Reflections from the Losing Side

agencies in fact legislate and so should properly be checked by a legislative veto. In *Consumers Union* v. *FTC*, the Court implicitly confirmed that the FTC, like the INS, is an executive agency, properly performing purely executive functions.

But does this constitutional taxonomy correspond to regulatory reality? If the FTC is to be called

an executive agency and thus escape legislative control, how, at the same time, can it be argued that it also should be immune from meaningful supervision by the executive branch?

The quasi-adjudicatory function performed by many independent agencies may not be well suited to executive assimilation. But it is much harder to reject the implicit suggestion of *Chadha* that the rule-making function of independent agencies be brought under executive control. What principled reason is there, after all, for bringing rules on the environment or auto safety under the supervision of a popularly elected executive, while rules on unfair trade practices or unsafe products remain entirely immune from such review?

Many regulatory agencies now face a debilitating hiatus because of the *Chadha* decision. But the hiatus affords an excellent opportunity to weigh the alternatives. With luck, the outcome will be more specific legislative guidance and better agency performance because of greater accountability.

James C. Miller III,
Chairman,
Federal Trade Commission

THEODORE OLSON responds:

Chairman Miller starts from the premise that Congress must come up with some replacement for the legislative veto. He fails to explain, however, why we have to replace a mechanism that was not effective in checking agency abuses, disturbed the constitutionally ordained balance of powers, and encouraged excessive delegations of authority, among other undesirable political side effects. I hope we do not rush to fill a perceived vacuum with some other deceptively attractive but counterproductive political invention. We ought to start the analytical process with a clearer understanding of precisely what problem we wish to remedy.

I do agree with Chairman Miller's second point, that we should consider making the "independent" agencies accountable to the President. It is time for the nation to reexamine whether it is necessary or useful to vest responsibility for enforcement of our laws in an array of individuals who are not responsible to our elected President. Alexander Hamilton explained in *The Federalist* No. 70 why he opposed splitting up executive authority, in words that are equally relevant to our system of unaccountable commissions: "The plurality of the Executive tends to deprive the people of the two greatest securities they can have for the faithful exercise of any delegated power, *first*, the restraints of public opinion, which lose their efficacy as well on account of the division of the censure attendant on bad measures among a number, as on account of the uncertainty on whom it ought to fall; and, *secondly*, the opportunity of discovering with facility and clearness the misconduct of the persons they trust, in order either to their removal from office, or to their actual punishment in cases which admit of it."

Toward Competition in Telephone Service

TO THE EDITOR:

Of the three articles on the telephone industry in your July/August issue ("Why Local Rates Are Rising" by Leland Johnson, "A Legacy of Regulatory Failure" by Nina Cornell, Michael Pelcovits, and Steven Brenner, and "The Case for Freeing AT&T" by Michael Katz and Robert Willig), the latter two bridge the gap between fact and fantasy with remarkable agility. They make it look as if it were up to the telephone companies to choose how fast to depreciate their plant. That is absolute nonsense. Local regulatory commissions have always forced telephone companies to depreciate their plant slowly because slow depreciation means a lower rate base, and the commissions want to maintain low rates at any cost. My own company, like all other utilities, has fought the commissions for the right to depreciate our plant at a more realistic rate.

Nor was the so-called overbuilding in plant that these articles deal with so casually done by choice of the telephone companies. The Rural Electrification Administration never permits rural telephone companies to build only the plant they actually require. It forces them to meet specifications set by a bureaucracy as far removed from the practical aspects as are the authors of these three articles. That is why there is plant in the ground that should never, in the best business sense, have been put in place.

The authors' idea that telephone companies should do as Texas Instruments has done in the computer business and write this plant off suggests that the authors have seen too many motion pictures. If a regulated monopoly's decision to put plant in the ground was dictated by a government entity, do the authors really think that shareholders and telephone companies should sustain all the losses that result? Have they considered that writing off such an incredible amount of plant would jeopardize these companies' loans with the various banks and, in fact, throw many of them into bankruptcy?

With regard to the desirability of competition in long-distance communications, not one of the authors notes that the FCC has already deliberately imposed a cosmetic competition on common carriers. MCI had a negative book value just a few years ago of $200 million and the quality of service it provided was (and still is) inferior. Unlike the common carriers, however, it was not asked to meet financial soundness standards or serve remote areas.

When Congress passed the 1934 Communications Act it was aware that there would be a cross-subsidy, because its objective was to prevent wasteful duplication and to create an environment for universal service. The telephone industry did exactly that—whatever the economists may think—and did so at an average rate of 14 cents per message minute. It provides the finest telephone system in the world at the lowest cost and for the most people. This has turned out to be one of the few social decisions government has made that has worked, and it worked because of the people in the industry and their professionalism.

I of course believe that the free enterprise system demands a competitive marketplace, but this presupposes that the rules are the same for all competitors. We cannot go around taking our largest national asset, more valuable than oil in the ground, and encouraging people to duplicate it in order to satisfy the whims or the greed of a few.

Whatever the theoretical notions your writers may hold, we know from our experience in the early days of the industry—when Chicago had nine telephone companies and both the Bell and Keystone systems operated in Philadelphia—that competition is not especially well-suited to an industry that requires equipment compatibility and network planning.

Finally, it might have been a good idea to involve someone from the telephone business in a dialogue such as this. After all, whatever the

competence of the authors, you cannot become an all-pro quarterback by reading a book.

Charles Wohlstetter,
Chairman of the Board,
Continental Telecom Inc.

TO THE EDITOR:

Nina Cornell, Michael Pelcovits, and Steven Brenner argue against the widespread view that long-distance telephone service subsidizes underpriced local service ("A Legacy of Regulatory Failure," *Regulation*, July/August 1983). They suggest that local rates may in fact reflect the true current economic costs of supplying service. In their view, rapid technological change has caused the economic costs of local service to fall well below the book costs of existing plant, kept artificially high by slow depreciation schedules. Accordingly, they feel that regulatory agencies should hold local rates down, forcing telephone company stockholders to bear the losses in much the same way the market would impose losses on stockholders of an unregulated firm.

Regardless of whether their position on local rate subsidies is valid, the authors are proposing an undesirable and unworkable type of regulation. Protecting stockholders of a regulated monopoly from losses resulting from technological change is a necessary and desirable concomitant to restricting the firm's profits. Otherwise the cost of capital to the regulated firm would soar and likely threaten its economic health. After the cost of capital went up, local rates would not remain low for long.

Dan Gallagher,
St. Cloud State University

TO THE EDITOR:

It is difficult to argue with Michael Katz and Robert Willig's conclusion that once all the provisions of the antitrust settlement between the U.S. Justice Department and AT&T are in place, and subject to a possible transition period, competition could replace regulation in the long-distance telephone market ("The Case for Freeing AT&T," *Regulation*, July/August 1983). This appears to be the fundamental premise underlying not only the AT&T settlement ("Modified Final Judgment" or "MFJ") but also most of the relevant decisions of the Federal Communications Commission during the last decade. Since the commission's initial 1971 Specialized Common Carrier decision, which introduced competition into the long-distance market, it has also selectively deregulated, or at least minimized regulation of, numerous competitors which it views as nondominant in this market. Recently the FCC commenced a generic proceeding to determine the appropriate nature and timing of eventual deregulation of AT&T in light of recent developments such as the MFJ. In short, a deregulated market appears to be the commission's acknowledged goal, and one with which few, if any, industry members differ.

The far more complex and immediate question addressed by the authors, however, is how we (the regulators, the industry, and the affected public) get from where we are now to where we want to be. It is the authors' view that there presently exists "good cause for beginning the transition to deregulation [of AT&T] without delay." I believe that this conclusion is premature.

While the MFJ will dramatically alter the structure of the long-distance market by divesting AT&T's local operating companies—and thus removing AT&T's ability to use its control over "bottleneck" local exchange facilities for competitive purposes—divestiture is not the only remedy the MFJ contains. Just as important are its requirements that the divested local companies provide equal access to all long-distance carriers within three years. Such equal access is a fundamental precondition to a truly competitive long-distance market. Under today's form of local access, for example, users of non-AT&T long-distance companies must dial as many as twenty-three digits to place a call and must tolerate greater noise and static on the line.

The MFJ calls for the eventual elimination of these inequities. However, several of the soon-to-be-divested local companies have already indicated that they will have serious problems meeting the MFJ's equal access deadline; the extent of these problems are not yet known. On the regulatory side, the FCC and various state commissions are just beginning to review and approve (or not approve) the dozens of access tariffs by which long-distance carriers will obtain the access to local exchanges they need for originating and terminating their traffic. It is therefore impossible to say, at the present time, that truly equal access will be in place throughout the country at any certain future date.

We are at a similarly early stage in understanding or resolving other problems of industry structure. For instance, the authors place great weight upon the availability of alternative transmission capacity and point specifically to the satellite as a way for the present smaller competitive networks to expand. Because satellite costs (and most satellite capacity prices) are not sensitive to distance, and because the vast majority of telephone calls are of shorter distances such as 700 miles or so, satellite facilities may never prove to be cost-effective alternatives to terrestrial networks (the costs of which generally decrease as mileage decreases) in large segments of the market.

I believe it would be appropriate for the FCC to begin a generic review of its deregulatory options once a truly competitive long-distance market emerges. At present, however, it is far too early to commence actual deregulation of AT&T. Regulators should use the "carrot" of deregulation as an incentive to regulated firms to complete the programs, such as equal access implementation, that are essential to a competitive marketplace. To begin implementing AT&T's deregulation too soon would only compound the difficult transitional issues we now face and reduce the chances that a market will emerge that is competitive enough to let us remove the regulatory constraints on the company.

James M. Tobin,
Lexitel Corporation,
Washington, D.C.

NINA W. CORNELL, MICHAEL D. PELCOVITS, and STEVEN R. BRENNER respond:

Dan Gallagher and Charles Wohlstetter, in their haste to rebut an argument we did *not* make, have endorsed the central theme of our article: that the current local rate requests by telephone companies do not represent economically efficient rate levels. Indeed, Wohlstetter offers further corroborative detail to demonstrate that the book costs of the telephone industry are above its economic costs.

What both men seem most concerned about is the notion that we called for telephone companies to write off a portion of their overvalued assets. They argue that it

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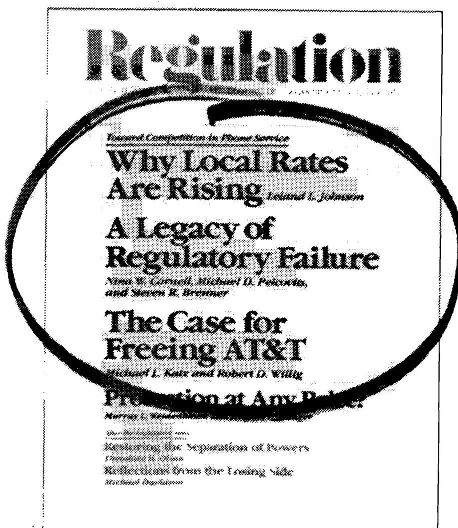
would be neither equitable nor efficient to force stockholders to pay for the difference between historic book costs and economic costs. We did not make such a policy prescription. We merely noted that under a competitive market structure the stockholders would bear those losses.

What we did argue is that legislators and regulators must take account of the fact that the telephone companies' costs do not represent economic costs. Once they recognize this point they have several options, including forcing stockholders to absorb losses, financing revenue shortfalls from general tax revenues, or establishing a tax on telephone usage. We did not try to set out the relative merits of these alternatives. Rather, we argued that it is imperative to realize that the problem is *not* one of preserving a long-standing subsidy of the economic cost of local telephone service. Unless policy makers understand this point, their proposed "cures" will be worse for residential telephone subscribers than the current rate requests.



MICHAEL L. KATZ and ROBERT D. WILLIG respond:

Wohlstetter apparently opposes competition in telecommunications because he fears that it will lead to inefficient investment in facilities. We share his concern about inefficient investment, but argue that the problem does not lie with competition. In fact, vigorous and undistorted competition will make it economically unviable for firms to invest in unneeded or overly expensive capacity.

Inefficient investment arises when the competitive process is distorted by ill-conceived regulation. The cross-subsidization that Wohlstetter believes can prevent inefficient investment has in fact done the opposite. One does not have to have spent a lifetime in the telephone business to know of many instances in which large users have elected to bypass the local telephone network in order to avoid subsidizing other consumers—even though the social costs of self-supply may be higher. Uneconomic bypass is one of a number of socially wasteful investments, made in response to cross-subsidies, that would not take place under *undistorted* competition. That is why we agree with Wohlstetter on one very important point: a regulatory policy of maintaining "cosmetic competition" is a bad one.

Both the structure and the technology of the telecommunications industry have changed tremendously since the early days when, Wohlstetter tells us, competition was inappropriate. Regulators must develop policies that reflect these changed conditions. A futile wish for a return to government-protected monopoly is not a sound basis for policy. After all, even the best quarterback can fumble when he tries to make an end run around reality.

Tobin is rather more sanguine about the prospect of competition in the long-distance market. But, he asks, is the market ready to begin the move to deregulation now? Our answer is yes, precisely because some current regulations are blocking the road to undistorted competition.

That does not mean that all regulations should be wiped out at a stroke. The ones with the largest costs relative to benefits should be removed first. For example, competition to serve large business users may already be strong enough to replace regulation—for calling distances both greater than, *and less than*, 700 miles. Limited regulation is appropriate in areas or service segments where competition alone is not sufficient to promote efficient pricing. But where regulation is retained during the transition period, it is important that it interfere as little as possible with the operation of full competition in those segments where market forces are strong.

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(Signed) William J. Baroody, Jr., Publisher