Telco Structural Separation: The Road to Local Competition

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Phoenix Center, Annual U.S. Telecomms Conference
November 20, 2002
Regulation: *The Road “More” Traveled*

- Economies of scale/sunk costs are significant for many network elements and present insuperable entry barriers
- Intermodal competition will not be robust
- Access to network elements requires detailed conduct regulation
- Time for Divestiture II?
Divestiture II - Guidelines

- The greatest benefit comes from a complete divestiture - not a separate subsidiary
  - changes the incentives of the monopoly firm
- Takes time to implement, so it must be a long-run solution
  - Must be robust with respect to technological change
Today’s Network
Divestiture Options: Today’s Network

- Option #1: **Link-Co**: “connection between customer and carrier”
  - Allows Link-Co to provide muxing and transport
  - Adds EELs to old Loop-Co concept
  - Does not provide customer-to-customer connection

- Option #2: **UNEP-Co**: Wholesale/Retail split
Future Network

**Loop**

- ADSL terminal unit
- DSLAM
- ATM switch (may be ATM concentrator)

**Transport**

- ATM switch
- ATM Network
- ISP/CLEC

*DSLAM/ATM switch connection may include SONET transport if ATM switch is not in local wire center*
Private Virtual Channels ("PVCs") may become the most important monopoly element
- subject to significant economies of scale
- great potential for discrimination under current regulatory regime

Divestiture II should create **Link-Co** to provide PVCs and dedicated connections between customers and carriers (including ISPs)
Conclusions

- Structural remedies are an effective and powerful alternative to conduct regulation, and most appropriate where:
  - monopoly control over inputs can provide powerful leverage into important, dynamic downstream markets
  - monopoly control is expected to be long lived
  - discrimination problems cannot be solved through regulation