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Section 652 Cross-Ownership Ban Shouldn't Apply to Cable Operators and CLECs

by

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U.S. Department of Justice Antitrust Division Chief Christine Varney declared in 2009 that "the vast majority of mergers are either procompetitive and enhance consumer welfare or are competitively benign."¹ But if so, why impose unnecessary regulatory barriers to achieving procompetitive, proconsumer telecom mergers?

Consider the case of Communications Act, Section 652.

Section 652's near total ban on mergers between cable operators and local exchange carriers was once understood to apply only to mergers involving *incumbent* local exchange carriers (ILECs) historically possessing monopolies over local voice services. Unfortunately, the FCC's 2010 Comcast-CIMCO merger order applied Section 652's cross-ownership restriction to a cable operator acquiring a *competitive* local exchange carrier (CLEC).

But mergers between cable operators and CLECs do not pose any special anticompetitive concerns requiring special regulatory restrictions. And we already have a system of regulatory reviews to analyze the competitive effects of telecom mergers. The FCC should resolve the issue of Section 652's application by declaring that it

doesn't apply to mergers between cable operators and CLECs. Or, short of that, the FCC should forbear from enforcing Section 652 against those mergers.

By its terms, Section 652(b) bars cable operators from acquiring "directly or indirectly, more than a 10 percent financial interest, or any management interest, in any local exchange carrier providing telephone exchange service within such cable operator's franchise area."² Section 652(d)(6) does provide a limited exception to the restriction. But the exception requires the cable provider obtain a waiver from the Commission. An FCC waiver, in turn, requires that the cable provider prove to the Commission that "the anticompetitive effects of the proposed transaction are clearly outweighed in the public interest by the probable effect of the transaction in meeting the convenience and needs of the community to be served."³ And it also requires that the cable operator's local franchising authority (LFA) approve of the FCC's waiver.⁴

Section 652 appears to be directed against the purchase of historically monopoly-holding ILECs by cable operators. After all, related statutory provisions likewise prohibit LECs from acquiring cable operators offering cable services within their own "telephone service area," defining "telephone service area" as "the area within which the LEC provided telephone exchange service as of January 1, 1993."⁵ Section 652 was adopted as part of the 1996 Telecom Act's amendments to the Communications Act. So most new entrants into the voice services market, or competitive local exchange carriers (CLECs), didn't come into being until after the 1996 Act, and therefore also after January 1, 1993. It follows that Congress does not appear to have intended Section 652(b) to apply to cable operators' acquisition of CLECs.

Unfortunately, the FCC's 2010 order in the Comcast-CIMCO merger has created regulatory uncertainty and a problematic agency precedent concerning the applicability of Section 652. As mentioned earlier, its order applied Section 652's cross-ownership prohibition and waiver provision to Comcast's acquisition of a CLEC.⁶ This despite the precedent from the FCC's 1996 SouthEast Telephone Ltd. order dismissing as unnecessary a petition for waiver from Section 652.⁷ In that 1996 order, the FCC based its dismissal on the fact that SouthEast was "not purchasing or otherwise acquiring an interest in an *incumbent* LEC that provides service in [its] cable franchise area."⁸

Now in the Comcast-CIMCO order, the FCC concluded that probable, procompetitive effects of the merger clearly outweighed any anticompetitive effects and that it was therefore in the public interest.⁹ But the FCC concluded its waiver was still contingent on the approval of some 274 different LFAs. Pursuant to a set of *ad hoc* procedures the FCC adopted for the proceeding,¹⁰ it determined that 273 LFAs approved of the waiver.¹¹ The city of Detroit, however, objected to the waiver. Despite the FCC's conclusion in the Comcast-CIMCO order that "Detroit fails to provide any specific evidence to suggest why the proposed asset sale is likely to harm competition,"¹² the FCC has no procedural rules or criteria regarding LFA discretion in considering Section 652(b) waiver requests. As a result, Comcast did not obtain a waiver with respect to the Detroit area, with the FCC merely issuing a conditional waiver, effective only if Detroit later changes its mind.¹³

On June 21 of this year, NCTA filed with the FCC with a Petition for Declaratory Ruling, requesting the Commission clarify that Section 652 does *not* apply to transactions between cable operators and CLECs. The Commission should take the opportunity occasioned by the petition to clear up the confusion. The FCC should declare that Section 652 doesn't apply to transactions between cable operators and CLECs. Read in its entirety, including the provisions discussed above, Section 652 addresses ILECs, not CLECs.

And even if one regarded the statute as ambiguous, it is well within the Commission's authority to make clear that cable operators purchasing CLECs are not subject to Section 652. The 1996 Act was concerned with promoting competition, and Section 652, in particular, was aimed at preventing monopoly in voice services resulting from mergers between cable operators and ILECs in the same areas. Mergers between cable providers and CLECs, however, can create efficiencies that lead to more effective competition against ILECs in the voice services market.

Also, in the event that the FCC declines to make such a declaratory ruling, NCTA also filed a Conditional Petition for Forbearance, requesting the Commission forbear from applying Section 652 to transactions between cable operators and CLECs. While there is ample reason for the FCC to make a declaratory ruling that renders forbearance irrelevant, nonetheless there are good reasons why the Commission should forbear from applying Section 652 to mergers between cable operators and CLECs.

First, there is no good reason to give LFAs an essentially unchecked and unreviewable veto power over the purchase of CLECs. In general, requiring dozens or even hundreds of separate LFAs to approve of a Cableco-CLEC merger is unwieldy. Armed with a veto power over Section 652 waivers, LFAs possess the same temptation that federal agencies and state regulators already confront: the temptation to impose conditions on their approval that are extraneous to the competitive effects of the merger.

One should also keep in mind that LFAs such as cities and small towns generally have no authority over CLEC service. They typically have no jurisdictional expertise regarding telecom services and regulation. And were LFAs to lose their veto power regarding Cableco-CLEC mergers under Section 652(b) through forbearance, it would in no way diminish LFAs' existing authority for granting franchises for video services.

Not to be forgotten, Section 652's ban on cable operators acquiring CLECs is unnecessary and unduly burdensome in light of all the other merger review processes currently in place. Even if the Commission forbears from enforcing Section 652 it would leave untouched the existing system of multiple agency reviews for telecom mergers: a federal antitrust review is typically conducted by the U.S. Department of Justice or the Federal Trade Commission, the FCC conducts its own review under its "public interest" standard, and sometimes state public utility commissions or even state attorneys general conduct their own respective reviews. As we have argued previously,¹⁴

redundant reviews drive up costs due to administrative compliance and to agency delays that create regulatory uncertainties and result in lost economic opportunities. Meanwhile, the extra layers of review provide little to no marginal benefit or protection to consumers beyond what review by one or even two agency reviews might provide. Seen in this context, the Section 652 multiplies the multiple agency review problem.

If Chairman Julius Genachowski is serious about regulatory reform and directing the FCC's resources to "identifying outmoded or counterproductive rules,"¹⁵ the Commission should address Section 652 without delay. One way or the other – through a declaratory ruling or regulatory forbearance – the FCC should make clear that Section 652's unnecessary regulatory restrictions do not apply to mergers between cable operators and CLECs.

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¹ Christine A. Varney, Third Annual Georgetown Law Global Antitrust Enforcement Symposium (September 22, 2009), available at: <http://www.justice.gov/atr/public/speeches/250238.htm>.

² 47 U.S.C. §572(b).

³ 47 U.S.C. § 572(d)(6)(A)(iii).

⁴ 47 U.S.C. § 572(d)(6)(B).

⁵ 47 U.S.C. § 572(e).

⁶ Memorandum and Order and Order on Reconsideration ("Comcast-CIMCO order"), In the Matter of Applications Filed for the Acquisition of Certain Assets of CIMCO Communications, Inc. by Comcast Phone LLC, *et al.*, WC Docket No. 09-183, 25 FCC Rcd 3401 (released March 15, 2010), available at: <http://fjallfoss.fcc.gov/ecfs/document/view?id=7020409929>.

⁷ Cable Services Bureau, Order, In the Matter of SouthEast Telephone, Ltd. Petition for Waiver of Section 652 Prohibition on Buy Outs of the Telecommunications Act of 1934, 12 FCC Rcd 2561 (1996).

⁸ SouthEast order, at para. 7.

⁹ Comcast-CIMCO order, at para. 41.

¹⁰ See Comcast-CIMCO order, at paras. 15-19, 25-31; Public Notice, Docket No. 09-183 (January 29, 2010), available at: <http://fjallfoss.fcc.gov/ecfs/document/view?id=7020387108>; Public Notice, WC Docket No. 09-183 (December 1, 2009), available at: <http://fjallfoss.fcc.gov/ecfs/document/view?id=7020352357>.

¹¹ Comcast-CIMCO order, at para. 11.

¹² Comcast-CIMCO order, at para. 34.

¹³ Comcast-CIMCO order, at para. 11.

¹⁴ See, e.g., Seth L. Cooper, "Multiple Government Regulatory Reviews Burden Telecom Mergers with Too Many Conditions," *Perspectives from FSF Scholars*, Vol. 5, No. 31 (December 23, 2010), available at:

http://www.freestatefoundation.org/images/Multiple_Government_Regulatory_Reviews_Burden_Telecom_Mergers_with_Too_Many_Conditions.pdf.

¹⁵ "Statement from FCC Chairman Julius Genachowski on the Executive Order on Regulatory Reform and Independent Agencies" (July 11, 2011), available at: http://transition.fcc.gov/Daily_Releases/Daily_Business/2011/db0711/DOC-308340A1.pdf.