Reed Hundt, Revolutionary Manqué

Reed Hundt
You Say You Want a Revolution: A Story of Information Age Politics
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Whatever else its Beatles-inspired title may suggest, Reed Hundt's account of his four years as Chairman of the FCC is not about starting a revolution. One might fairly claim that his years at the FCC were the beginning of a revolutionary transformation of what is now monotonously known as the information age, but that is not what this book is about. Mostly what it is about is Reed Hundt. Or more precisely, Reed Hundt's excellent Washington adventure, for the book is more in the nature of a diary *cum* gossip column than it is about events, or actions, or issues. It is a chronicle of encounters with friends, adversaries and assorted celebrities – from the glitterati of Hollywood (Clint Eastwood, Steven Spielberg, Sharon Stone), to the captains of industry (Andy Grove, Bill Gates) to his great patron Al Gore. The narrative purpose of the first set of mentionees is obscure; perhaps it is simply to show that an FCC chairman is no backwater bureaucrat. Al Gore, on the other hand, is quite central to the narrative throughout. Gore not only was his political patron, but his chief as well – his "vice king" as he remarks at one point (p.165).[1]

Hundt did not start a revolution at the FCC, but some of his critics would accuse him of throwing a few bombs at his adversaries, particularly at three of his colleagues, whom he labels "The Gang of Three" (the three became "The Gang of Two" after one of them left the Commission at the expiration of his term)

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1 Hundt makes clear at the outset that he regarded himself as "Al's lieutenant"(p.5), and he notes regular meetings with Gore and others to review the policy agenda (p.8). *Humphrey's Executor (Rathbun) v. United States,* 295 U.S. 602 (1935), held that independent agency members do not serve at the pleasure of the President, but that does not prevent them from seeking to serve his pleasure (and that of his viceroy) as Hundt reveals.

(pp.90, 159 & *passim*). Hundt subtitles his book a story about politics, and I suppose it is, although Hundt reveals himself to be the most politically partisan figure in the story.[2] His opponents on the Commission are identified as Republican toadies – except for Jim Quello who is identified as a "pseudo Democrat"(p.19). The Eighth Circuit Court of Appeals that reversed part of the FCC's order on telecommunications interconnection is represented as a group of Republican-appointed judges with a bias in favor of status quo monopoly and states' rights (p.196). At every turn the lines of battle are labeled in terms of political party affiliations. In itself this would not be objectionable if it were accompanied by some real information about the nature of the issues in dispute. Of that, unfortunately, we have little. Hundt's account is more diatribe than description. We learn who the enemy was in various battles that he fought, but we are not told much about the fighting – except that under Hundt's generalship, the good guys fought bravely and generally won.

Paradigms Passing

I said that Hundt's tenure might be fairly described as the beginning of a revolutionary transformation of the information age. But it all depends on what you call a beginning, or how you describe a transformation. I served on the FCC for a brief time (half of Hundt's four years) in the mid 1970s, and those years seemed pretty exciting[3] – the first stirrings of competition in telecommunications, some early signs of new telecommunications technologies (notably cellular radio), and even some promise of deregulation in mass media. As events unfolded, those years turned out to be not even the beginning of the beginning of the revolution. A decade on, telecommunications was transformed by the break-up of AT&T; wireless telephony emerged; cable television became the dominant mass medium; satellite broadcasting was on the horizon (but not yet in the air).

However, these events proved to be only a harbinger of things to come a decade further on, when Hundt was appointed in 1993. In telecommunications Congress set about to rewrite the statute to mandate competition in local telephone markets and to increase competition in long distance markets. The first move quietly marked a paradigm shift in regulatory theory by repealing the "law" of natural monopoly that had been hitherto thought to apply. The second terminated the AT&T antitrust decree, ending a dozen years of regulation by antitrust decree.

Equally transformative was the implementation of an auction system in lieu of administrative licenses for radio spectrum users. Here was a second paradigm shift. When Ronald Coase had first proposed the use of spectrum auctions in 1959 the idea was ridiculed by those few who paid it any attention. Thirty years later, it was government policy.[4] Initially the auctions were limited to non-broadcast users, but by 1997 (Hundt's last year) they were extended to new broadcast licenses (a replacement for the long discredited comparative hearing process).

2 Given Hundt's political partisanship, it nearly took my breath away to read this allusion to classical civic virtue: "In a couple of years, my job, done, I could return to my law practice, like Cincinnatus back to the farm." (p.15) For the record, this Cincinnatus did not return to the farm; he now plows the business consulting field with McKinsey & Co.

3 Of course, for academics the threshold level for excitement is quite low; as Robin Williams quipped: "What does the snail say when it rides on the turtle's back? Wheee."

4 The law, economics, and history of spectrum auctions are examined in a conference symposium, *The Law and Economics of Property Rights to Radio Spectrum*, 41 Journal of Law & Economics 521 (1998).

Most radical of all, by the beginning of Hundt's term, the Internet had become established as a public medium – a third paradigm shift in the concept of how information can be produced and exchanged. In the mid 1970s I had been introduced to its precursor, ARPANET, a packet-switched network run by the Defense Department which connected the Department and a handful of universities. No one then had the faintest glimmer that in only a couple of decades this obscure network would morph into the Internet and the World Wide Web and start a revolution in communications comparable to the invention of the telephone.

Those who have read Thomas Kuhn[5] will appreciate how special it is to witness three such important paradigm shifts in such a short period of time; Kuhn thought that such shifts don't usually occur until those who invested in the reigning paradigms pass from the scene. Here, though, we have three paradigms that passed before their true believers. Unfortunately, none of these remarkable shifts is chronicled in any important way in Hundt's memoir even though they occurred, in part, during his watch.

Making Bombs

Hundt has surprisingly little to say about the first of my three transformations, other than to note that the FCC's implementation of the Telecommunications Act of 1996 was a big and complex job. At the time he characterized it as the regulatory equivalent of the Manhattan Project. Comparing the FCC's project to building an atom bomb doesn't seem quite *les mots juste* for this kind of activity, but the explosive allusion was not inadvertent. Hundt quipped that, like the Manhattan Project, the FCC's project was "not easy to handle and we can't meddle with it too much or we may blow up Chicago."[6]

Thankfully the FCC managed to avoid blowing up Chicago, but some think it did a lot of damage to the telecommunications industry, or at least to the Bell Operating Companies. I think the jury is still out on that issue. Four years after the Act, we still have only a dim view of the probable effect of the FCC's rules; indeed, the legality of the local telephone interconnection rules – which are the linchpin of the overhaul of telecommunications – is still under challenge. Unsurprisingly, Hundt lambastes all who criticize the FCC's efforts. Here is his judgment on a critical judgment from the Eighth Circuit:[7]

> We had written 48 pages of rules and 500 pages of reasoning. The Eighth Circuit Court of Appeals, however, sitting in Kansas City, Missouri, listened to our lawyer for 15 minutes of oral argument and then enjoined the national rules opening the local telephone company monopolies. Judicial activism in Kansas City.
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> … [T]he panel of Republican-appointed judges had revealed a bias toward the Republican – local-telephone-incumbent – states'-rights side of the debate and against the Democratic – new-entrant – federal side. (p.196)

Putting aside the petulant and politically partisan character of this critique, it is disingenuous, confused and misleading. It is disingenuous because Hundt, a lawyer with a leading Washington law firm before he joined the Commission, must know that oral argument plays a tiny role in the disposition of cases on appeal. It is confused because Hundt

5 Thomas Kuhn, The Structure of Scientific Revolutions (1962).

6 Television Digest, Feb. 26, 1996, p.2.

7 *Iowa Utilities Bd. v. FCC*, 120 F.3d 753 (8th Cir. 1997), *reversed*, *AT&T v. Iowa Utilities Bd.*, 119 S. Ct. 721 (1999).

seems to have misunderstood something in his legal education: when the law speaks about the "weight of the evidence" it is not referring to pounds of pages devoted to argument, but to the persuasive power of the facts and reasons therein. The implication that the court should defer to the agency by reason of the number of pages written by its staff is surpassingly silly.[8] It is misleading because the principal thrust of the court of appeals' decision was on a legal issue of statutory interpretation, whether the FCC should be able to preempt state regulatory agencies on how prices should be determined for access to local network facilities. Hundt neglects to mention that on a key substantive issue, what network elements incumbent carriers must allow competitors to access, the court sustained the FCC.

Be that as it may, Hundt provides virtually no information on the nature of the underlying issues. A reader would have no way of knowing that the FCC's interconnection rules requiring incumbent telephone carriers to give access to their network facilities were so broad as to prompt a sharp rebuke by the Supreme Court,[9] or that the FCC's rules governing the pricing of access are at least borderline as to whether they permit the incumbent carriers to earn a fair rate of return on their investment.[10]

Although not part of its "Manhattan Project" the FCC's venture into cable rate regulation provides what might be a more apt illustration of Hundt's quip about "blowing up Chicago." Hundt gives the story more attention than its ephemeral importance warrants – by the time the memoir was written, it had already faded from the scene.[11] Even so, it provides some insights into the ways that the best laid plans of bureaucrats can go astray. That is not, however, the part of the story that Hundt narrates. For Hundt the cable episode represents a consumer victory over the dark side of cable.[12] As he explains, critics of rate regulation complained that rate controls would strangle the introduction of new program services, and more generally retard the growth of the new information superhighway. As evidence for the latter, critics claimed that rate regulations defeated the then-pending

8 Sad to say, Hundt here is reflecting a rather common prejudice among FCC lawyers who seem to think that the way to "bullet proof" an argument is to armor plate it with ten inches of impenetrable prose. When I was on the Commission I once took issue with bureau staff members over a draft report that seemed to me verbal overkill. I suggested that they reduce the verbosity of the report. A week later the report reappeared on the weekly agenda; it was longer than before. My legal advisor, Dan Polsby, explained: "they are punishing you."

9 *AT&T v. Iowa Utilities Bd.*, 119 S. Ct. 721. Interestingly, Hundt later notes with satisfaction the Supreme Court's reversal of the lower court on the FCC's jurisdiction, but again neglects to mention that it reversed that court's affirmance of the substantive access regulations. (p.223) Curiously, in view of his railing against the Republican appointees on the court of appeals, he expresses great satisfaction with the Supreme Court's opinion, written by Justice Scalia, the most conservative (and Republican) member of that Court. Apparently party affiliation is not always a reliable guide to correct judgment; the key is whether you agree with Reed Hundt (and Al Gore).

10 For an extended critique see J. Gregory Sidak & Daniel F. Spulber, Deregulatory Takings and the Regulatory Contract (1997). The same panel of the Eighth Circuit that so vexed Hundt earlier recently invalidated the FCC's pricing methodology in part. *Iowa Utilities Bd. v. FCC*, 219 F.3d 744 (8th Cir. 2000).

11 In 1996 Congress provided for the elimination of rate regulation for cable programming. Regulation of the basic service tier – which includes all broadcast channels required to be carried on the system – is still subject to local rate regulation (pursuant to FCC guidelines).

12 My words not his, but not inappropriate given that the leading spokesman for the cable industry was TCI's John Malone, whom Al Gore once dubbed the "Darth Vader" of the industry. (p.22)

merger of Bell Atlantic and TCI, which was touted as the vehicle for the long-awaited integration of telephone and video program services. In effect the rate controls devalued TCI's stock, making the terms of its acquisition no longer attractive to Bell Atlantic. This was the occasion for the famous quip by John Malone that the best way to get the information superhighway built would be to "shoot Hundt" (p.53).[13]

This much of the narrative is correct, though more entertaining than enlightening. No one worth listening to would claim that the FCC was obliged to protect the inflated value of TCI's stock (reflecting not only ordinary capitalization of the future monopoly rents, but also a special premium that Bell Atlantic was willing to pay to be a player in cable). As for handicapping the information superhighway, the once-proclaimed ambition of the telephone companies to provide video programming service proved to be a passing fancy. In 1996 Congress attempted to facilitate telephone company entry into television; it eliminated a 26-year ban on local telephone companies providing video programming (a.k.a. television) in their home markets,[14] and it also provided for the future lifting of rate regulation for cable program service. But the bloom soon faded on that rose; the local telephone companies are no longer interested in television. Only a few years since railing against the FCC for thwarting its acquisition of TCI, Bell Atlantic – now Verizon since its merger with GTE – is no longer interested in the cable business, at least in the programming end. It wants to be in the Internet business instead. None of the other Bell companies have shown much interest in competing with incumbent cable operators either.

The more interesting part of the cable rate story is not the effect on the Bell Atlantic–TCI merger but the scheme itself. The basic plan was sensible if you accept the notion that rate regulation itself was a worthwhile project: roll back rates to where they were at the time the Act was passed, then adjust them further downward to a benchmark level from which they would be adjusted in accordance with general prices. The benchmark was determined by estimating – by means of an econometric model – what the rates would be in a competitive market. After the monopoly rents were thus squeezed out, cable operators were allowed to increase rates in accordance with so-called "going forward" rules that allowed increases in accordance with a general price index, plus some special incentives for adding new channels. Seemingly straight-forward, this plan turned into a bureaucratic nightmare or comedy – depending on the angle of view. The econometric model was flawed. Although most operators had to cut rates (the planned target for the industry average was 10%), as many as one third actually were able to *increase* rates under the FCC's rate formula. There ensued the expected fury of consumers who saw their rates increase, followed by the equally expected expressions of outrage from Congress (whose members assiduously disguised their complicity in the matter), followed by a scrambling of FCC staffers to see how they could get it right. Back to the econometric drawing board? Not really, although that is

13 The FCC's first set of rate controls was implemented before Hundt's arrival, under Acting Chairman James Quello. The occasion for John Malone's outburst was a second set of rules that forced deeper rate cuts by cable operators when the first round of controls failed to deliver the promised results.

14 The ban was first imposed by the FCC in 1970, incorporated into statute in 1984, successfully challenged by the Bell Operating Companies as a First Amendment violation in the early 1990s, and pending review before the Supreme Court when the Telecommunications Act repealed it. See Glen O. Robinson, *The New Video Competition: Dances with Regulators*, 97 COLUM. L. REV. 1016 (1997).

what Hundt implies and what the FCC claimed at the time. The FCC quickly came to agreement on a "supplemental" reduction based on the ever-reliable Goldilocks methodology: another 10% rollback (once discussed as a possibility) would be too high; half of that would be too low; something between 5 and 10 was just right – the FCC settled on 7%.[15]

This was just the beginning. The rate controls were not self implementing; they had to be interpreted and enforced by an army of bureaucrats at both the local and federal levels (basic tier rate regulation was left to local franchise authorities; however, they were required to follow FCC-prescribed rules for determining what the proper rates should be; cable program tier rates were the exclusive province of the FCC, which was to exercise its jurisdiction only upon petition). In the best of situations the task of regulating rates for some 16,000 franchised systems would be daunting, but enforcing the FCC's rules involved a new order of difficulty. The FCC's rate rules rival the Internal Revenue Code, the Clean Air Act and the Talmud for mind-bending complexity. And they were changed constantly. Supplemental rules were forthcoming at the rate of two or three a year.

In the end, even the most dedicated consumer advocate had to ask if this game was worth the candle. Or necessary: since the root problem was (and is) monopoly, maybe that is where the root solution should be sought as well. Unfortunately, that is not where Congress sought it in 1992. The Congress that found it necessary to institute rate regulation for cable monopolists did not find it necessary to adopt measures to challenge the monopoly directly by facilitating competitive entry. For instance, it gave no consideration to removing its own ban on local telephone company entry into cable, and it paid virtually no attention to the possibilities of promoting satellite broadcasting – as for example by giving satellite operators the same copyright license to carry network signals that cable operators have enjoyed since 1976. These deficiencies have now been addressed, but timing is everything. The telephone companies are no longer interested in cable, as I said, and the satellite broadcasters still labor under regulatory handicaps, as well as the burden of catching up with a long-entrenched monopoly.

Selling the Ether

On the second of my paradigm shifts, the establishment of spectrum auctions, Hundt's views are basically sound, although he has less to say about the remarkableness of the change than about Congress's political cowardice in not carrying it to its full completion. When Congress mandated the use of auctions for all new broadcast license applications in lieu of comparative hearings in 1997, it exempted channels that were set aside to be assigned to existing television licensees as part of the FCC's plan for implementing a shift from analog to digital transmissions. The FCC's plan calls for assignment of a second channel in order to allow stations to simulcast in both analog and digital modes during the period needed for consumers to obtain digitally compatible sets or converters. Hundt complains that Congress should not have given away the second; it should have been put up for auction, open to all spectrum users.

I think Hundt is right. It would have meant the swift and certain end to the FCC's plan for converting to digital: there is no way that

15 The FCC insisted that the 7% roll back was not the result of political and public complaints but of recalculations in its original study. New York Times, Feb. 23, 1994, p.A1. That claim was presumably aimed at the same audience that reads Goldilocks and the Three Bears.

broadcasters could have outbid mobile telecommunications users for this spectrum,[16] and without the ability to simulcast the transition to digital would be extremely difficult to manage. Even so, the matter should have been put to a market test. To continue to consume spectrum for distributing television signals when virtually all television households are within the reach of cable and over two thirds of them subscribe is a profligate use of a resource that has a more highly valued use elsewhere.[17]

That said, it is a little incongruous that Hundt is so willing to abide by market judgments about who gets to use the spectrum but not abide by markets when it comes to deciding what they use them for. One of Hundt's preoccupations in the latter years of his tenure was the need to prescribe minimum amounts of children's educational programming. This should be mandated, according to Hundt, because presumably ordinary market demand for this kind of programming is insufficient. Interestingly, as it happened, reserving the radio spectrum for broadcasters provided a convenient means of solving the children's program objective. Hundt publicly demanded that if the broadcasters were going to get the second channel free, they ought at least to be required to give some in-kind compensation in the form of children's programming. Although the broadcasters at first balked, eventually they saw a deal they could not refuse. To remove any prospect that they might be asked to pay for their channels the broadcasters agreed to provide three hours a week of children's educational television as quid pro quo.

Contrary to what they teach in business school not all bargains are "win-win." In this case what looks like a good deal for the broadcasters looks like a pretty expensive proposition for the American public. The value of the spectrum involved was huge – as high as $70 billion according to an informal FCC staff calculation. Seventy billion dollars for three weekly hours of kidvid? For that amount of money the FCC could have bought Disney studios and produced its own educational television.

The Revolution Ahead

The third of my paradigm shifts, the rise of the Internet, gets some attention in Hundt's memoir as part of his promotion of wiring schools for Internet access, but there is no discussion of how the Internet implicates any of the other parts of the FCC-regulated world of communications. There is a school of thought that says the Internet stands apart from the regulated realm of conventional electronic media. On that account it is quite understandable that Hundt would have little to say about the regulatory implications of this new technology. That account is, however, misleading. While the Internet right now is unregulated,[18]

16 Broadcasters have periodically complained that switching to digital does not translate into higher advertising revenues. Assuming the digital channel is used only to provide high-definition picture quality this is correct, though broadcasters can, and most will, deploy the digital channel to "multicast" several channels of conventional-quality ("standard digital") signals which will clearly yield increased revenues. However, even using the multi-cast option, it is unrealistic to think the advertising revenues generated by another channel of 20-year-old sitcoms would be equal to the revenues that could be derived from another wireless telephone provider.

17 For elaboration see Glen O. Robinson, *Spectrum Property Law 101*, 41 Journal of Law & Economics 609 (1998).

18 I refer here to media-specific regulation of a kind imposed on conventional electronic media. Of course, "regulation" can be used to cover a wider set of legal restraints. In this sense the Internet is already regulated. Napster notwithstanding, Internet users are subject to copyright; a dot-com IPO has to comply with the securities laws; and if, *mirabili dictu*, that company should turn a profit, it will be subject to income taxes.

there is every reason to think this may change. Technologically and functionally the Internet is flanked by regulated media – telecommunications on one side, electronic mass media on the other. It is not quite a full-fledged telecommunications medium like the telephone, and not quite a mass medium like cable television, but this is changing fast. The Internet is becoming both a telecommunications medium and a mass medium. As the Internet assumes functions heretofore performed by conventional, regulated communications it naturally raises questions about whether, and how, it will be regulated.

For example, when the Internet is used to make ordinary telephone calls (a service now being offered under the generic label of IP telephony), the caller gets a special break because she does not have to pay local access charges that are levied on conventional long distance calls. It is hard to see how this discrimination can be continued (although so far the FCC has managed to turn a blind eye to the issue).[19]

Even more controversial than the access charge issue is the battle over "open access" to cable broadband facilities. Initially given public momentum by AT&T's acquisition of TCI, the demand that broadband providers give access to other Internet service providers has gained further momentum from the FTC's consent order conditioning the AOL-Time Warner merger on the provision of open access. For its part the FCC has also opened an inquiry to consider whether to impose open access requirements on all broadband providers.[20]

On the mass media side the regulatory pressures are mounting. An effort to control Internet indecency has twice flunked the First Amendment test,[21] but the struggle to establish Victorian virtue continues.[22] The indecency campaign has not involved the FCC (though it is based on an indecency "jurisprudence" invented by the FCC). It does not require a huge imagination to see how it might become involved, however. When MSNBC decides to stream audio or video coverage of a political candidate will the equal time rules apply? And if – God help us – the Gore Commission's efforts to revive the moribund public interest program standards for "digital broadcasters"[23] were to bear fruit, would such standards be extended to a joint venture between Yahoo! and CBS?[24]

19 Access charges would be owed only to the extent that IP telephony uses the local exchange networks. To the extent IP telephony is offered by means of cable or fixed wireless facilities that bypass the local network – which is the scenario being envisioned by AT&T and others – there is no basis for assessing an access charge.

20 *Inquiry Concerning Access to the Internet Over Cable and Other Facilities*, FCC 00-345 (Sept. 28, 2000).

21 *Reno v. ACLU*, 117 S. Ct. 2329 (1998) (invalidating portions of the Communications Decency Act proscribing Internet "indecency"); *ACLU v. Reno*, 31 F. Supp. 2d 473 (E.D. Pa. 1999) (invalidating indecency provisions of Children's On-line Protection Act).

22 I do not intend the Victorian virtue reference to be quite as snide as might appear. See Glen O. Robinson, *The Electronic First Amendment: An Essay for the New Age*, 47 DUKE L.J. 899, 963 (1997) (commenting on the uses of Victorian values even when they are out of character with observed social practice).

23 Advisory Committee on Public Interest Obligations of Digital Television Broadcasters, CHARTING THE DIGITAL BROADCASTING FUTURE (1998). The FCC has pending an "inquiry" to consider whether to consider rules of the character proposed. *Public Interest Obligations of TV Broadcast Licensees*, __ FCC Rcd ___, FCC 99-390 (1999).

24 Contemplating the convergence of "digital broadcasting" with the Internet must create a migraine in the minds of those (like Al Gore) who want the former to be regulated and the latter to run free. The headache can be avoided only by adhering to an increasingly obsolete model of mass media – old-fashioned broadcasting – and pretending it has no connection with the new model – the Internet.

I do not have answers to these questions (or a hundred others like them). I doubt Reed Hundt does either. I am pretty sure, though, that he has at least some vagrant opinions on them, as I do and as do many others who will read his book. If so, it is a pity he did not take the occasion to express them, so we could all compare notes about where the revolution is headed. GB