Remarks of Commissioner James H. Quello
Before the
Washington Metropolitan Cable Club
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Introduction

I'm always delighted to accept invitations from your president, John Evans, my home town local boy who really made good.

Many of you may not realize that John was rejected for important government service in 1974 for being too young. He thus became an unemployed son from a rich family. So he made a desperation move into the risky fledgling cable business on borrowed bank money. He needed a long distance signal waiver from the FCC to get money from the bank. I told him not to worry because it would be a cinch. It was a 4-3 vote cinch and ARTEC Cable was launched.

Of course, I became well acquainted with most of your struggling cable entrepreneurs back in 1974 and 1975. Cable and I have come a long way together -- we all have done rather well. My cable friends, who pioneered a new promising communication service, are now multi-millionaires and even billionaires. And I, survived the slings and arrows of the contentious Commission life, to earn a secure $45,000.00 a year government pension. But remember, I had fun for 22 years being a kissee rather than a kissor.

Anyway, I'm glad to be here. As a fugitive from the actuarial law of averages, I'm glad to be anywhere.

I'm gratified that performing my duties in accordance with my unassailable 1991 campaign platform of "delusions of adequacy and 75% of my marbles -- a good Washington norm" had found charitable widespread acceptance.

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And I still like to quote these three stages of life -- youth, age, and the final stage, you look great! I'm grateful my physiology hasn't caught up with my chronology, but, I have some homely facts to share with you about aging.

It is an irony of life that the young don't know what to do and the old can't do what they know.

As I mentioned recently at the FCBA lunch, I now read Playboy magazine for the same reason I read National Geographic -- to see fascinating places I'll never get to visit. Another mixed blessing of aging is you no longer have to worry about avoiding temptation, temptation avoids you.

I have also developed a much stronger ecumenical sense as I grow older. I personally now accept all religions because I don't want to blow an opportunity for some kind of merciful eternal salvation on a religious technicality.

Enough for this heavy part of speech, now for the more extraneous issues. You can tell that I agonized over this speech. Now, it's your turn.

I've had the chance to speak with a number of you recently, so based on these conversations I would like to take this time to try and answer some of the questions you may have regarding hot issues at the FCC.

The first question involves leased access. What should the Commission do with leased access rates and where can we be flexible?

The second question is what direction should the Commission go in implementing rules for interconnection?

A third question is what issues are still likely at play when the Commission returns to the OVS decision?

With these topics and questions in mind, I would like to begin to my answers with a few general public policy principles that may serve as themes to some of these key issues facing the cable industry over the next several months.

General Public Policy Principles

As a starting point for discussing the changing telecommunications marketplace, the first principle is that fundamental change in policy must focus on the future. One important consideration for the Commission in preparing for the future is to establish policies that will facilitate the development of a market structure with new competitors and new services, as we witness the continuing trend toward nationwide or global providers of a range of telecommunications services. In this regard, I believe that the Commission's work in minimizing market entry barriers will be especially important.

Second, we need to have a healthy respect for the "limited omniscience" possessed by any government agency. I think that policies implementing legislation need to be flexible enough to permit different strategies, changes in those strategies, and to enable companies to meet their investment needs. In the context of the video marketplace where we are beginning to move toward reduced rate regulation, this most likely will mean facilitating the development of programming services, while all distributors move toward a more competitive environment that will carry on the role of constraining subscriber rates.

The FCC decisions in implementing legislation will play a role in determining the pace at which competition can develop in telecommunications markets. The new legislation presents great opportunities for both industry players and policy makers. Yet, policy makers must acknowledge and avoid possible obstacles to industry development that could occur by clinging to vestiges of past regulatory policies.

With these principles in mind, I would like to discuss briefly some more specific answers to the questions I raised earlier.

Leased Access

I understand that one of the most important issues to this group is the pricing and treatment of leased access programming. In the midst of the noise caused by such a controversial issue, I am aware that leased access is extremely important in terms of its impact on the flexibility and structure of programming packages that you offer to the public, not to mention its impact on future revenue flows.

I also know that there has been a great deal of momentum for the Commission to move away from the "highest implicit fee" standard as the maximum reasonable rate for leased access. Given that the Commission has proposed a formula to determine rates for leased access with the belief that it would better assure access to cable system distribution by parties unaffiliated with the cable operator, it is time to evaluate the record submitted in response to determine whether the Commission's formula or some other alternative is best suited to fulfill the stated purpose. I know that many of the interests represented here today have raised a number of concerns regarding the impact of applying the formula as proposed.

As we consider the merits of the Commission's proposed formula, as well as potential concerns, I would like to highlight several factors that we should keep in mind regarding leased access. First, we must accept that most subscribers are served by cable operators with no channels available, so that in general we are not dealing with scenarios of filling excess channel capacity.

Second, I will observe that the Commission's 1995 Competition Report to Congress demonstrated an increase in number of cable programming services. In the year from 1994 to 1995, the total number of programmers increased from 106 to 129. In addition, the statistics in the Commission's report show that more than half of these programmers are not affiliated with cable interests, which reflects an increase in unaffiliated programmers consistent with the purpose of Section 612 regarding leased access programming. Related to this growth of programming services, it is significant that all programming services have an increasing number of avenues for delivering their services to the public, particularly through the growth of DBS and the eventual entry of telephone companies into the video marketplace through a range of technologies.

With these factors in mind, I think it is necessary to be careful to the extent that the Commission's proposed formula may yield a rate that is artificially low. In that event, we need to pay special attention to the concern that the proposal could amount to an unintended subsidy to certain leased access programmers at the expense of cable industry investment, or at the expense of other cable programming services. In moving to the future telecommunications marketplace, both the level of cable investment and a broad range of programming will be critical factors in affecting the extent to which cable is able to compete with other players seeking to provide one-stop shopping for voice, video, and data services.

Accordingly, I believe it will be important for the Commission to move toward a formula that encourages a reasonable level of flexibility for pricing leased access services relative to other programming services. Along with such flexibility, however, I suggest that it will be necessary to move toward a standard that will lead to leased access rates lower than those established under the "highest implicit fee" calculations. In what is likely to become a very difficult proceeding, I hope that you will continue to offer constructive ideas as to how the Commission can move toward a reasonable outcome.

Interconnection

Next, I would like to raise some issues regarding interconnection. To this point, most attention in this intense debate has focused on the question of federal versus state jurisdiction under the 1996 Act. By no means do I intend to diminish the jurisdictional issues, because if nothing else it has kept the contingent of attorneys on both sides productively employed. In the legal community, I suppose that busy hands are happy hands. More seriously, this will be a critical aspect of the decision and one that no FCC commissioner is likely to make easily.

Nonetheless, I suggest that it is important for all of us to direct our thinking to the question of how to promote reasonable interconnection rates. To the extent that the Commission ultimately may rely in part on the negotiation process as set forth in Section 251 of the 1996 Act, we will need to determine whether the process incorporates a sufficient level of certainty to foster competition and investment by new entrants in local exchange and wireless services. We should keep in mind here that the statute requires interconnection rates to be just, reasonable, and non-discriminatory.

In the course of initiating the interconnection proceedings at the Commission, I observe that there has been a general agreement that interconnection agreements existing prior to the passage of the 1996 Act were flawed, in that the group of agreements: (1) established rates that were significantly higher than incremental costs of interconnection, (2) resulted in one-way payments to LECs rather than allowing for reciprocal payments, and (3) yielded little competition.

With what we can expect in terms of the negotiation and arbitration process for interconnection, I think that a national policy could be very useful. In the first place, a national policy could offer a more certain starting point to all parties. Most importantly, I think that a national policy could allow new entrants to the local exchange marketplace and other competing carriers to move away from the past form of interconnection agreements to more a reasonable transitional ground while the negotiation and arbitration process is at work.

If I may reach back to the general principles I discussed at the outset, we have to remember that this interconnection issue is mostly about how we will move toward a future that is fundamentally different than today's telecommunications marketplace with very limited competition. We will need to consider how to govern a marketplace that is built around offering packages of an array of telecommunications services in a nationwide, one-stop shopping model rather than the intrastate and regional boundaries we have come to know. In this scenario, I think a national policy focused on promoting reasonable, efficiently priced interconnection could be very beneficial.

In a very brief comment on pricing, it is fair to say that the focus of past policies of providing for cost recovery by incumbent LECs now must be balanced with the immediate goal of fostering competition for local exchange services and wireless telecommunications services.

I must say I am not sure that it is useful to require states that have been progressive in fostering interconnection to return to Step One. In those instances, I hope that the Commission will take care to enable the development of competing local services and wireless services with as little disruption as possible. We clearly will need to continue to work with the states in order to put the specific elements of a process together so we all can move forward. In order to do this, however, it is necessary to move beyond the jurisdictional debates of proper federal and state roles and focus more on how this new regime would best work, what forms of flexibility would be useful, and how we can minimize the potential delays in the development of a more competitive telecommunications marketplace.

Open Video Systems

I also am aware that you are very concerned about the Commission's treatment of open video systems, or OVS.

The Commission recently released its Report and Order regarding the treatment of open video systems. I must emphasize that my decision to support the Commission's decision was in spite of many strong concerns. First, I believe that it is necessary to pay attention to the potential implications arising from the fact that this complicated proceeding, unlike many other pressing matters raised in the Telecommunications Act of 1996, must be completed through reconsideration by August 1996.

While the Commission was most careful to follow the express will of Congress in providing opportunity for OVS entry into the video marketplace, I am concerned the compressed timeframe could lead to rules that would yield unintended consequences. I also think that competitive inequities may result from the provision to allow joint marketing of OVS with the incumbent LEC's voice service, as well as the decision not to require separate subsidiaries.

My greatest concern regarding the OVS decision involves the treatment of cost allocation matters. In particular, the Commission provided that OVS operators may file updated cost allocation manuals (CAMs) prior to initiation of service, subject to the resolution of general cost allocation issues in a separate Part 64 cost proceeding. This raises particular concern on my part due to the indication that this Commission may still fail to realize the significance of cost allocation in the process of authorizing LEC-owned multichannel voice and video systems. Throughout the extensive and contentious history of the video dialtone proceedings, perhaps no other issue was as critically important, and yet as tentatively treated, as the issue of cost allocation. While the 1996 Act establishes a new framework for LEC entry into the video marketplace through the advent of open video systems, the same analytical questions have to be answered, because the potential competitive inequities surrounding the treatment of common costs for OVS and voice networks have not in any way been changed. It is my hope that the Commission's treatment of cost allocation issues in the future will reflect greater attention to these concerns.

<u>Conclusion</u>

The three questions discussed today treat contentious subjects with competitors, local and long distance telephone, cable and wireless companies, all seeking a "fair advantage." The FCC in its deliberations and decisions must do its best that in implementing the 1996 Act in a "fair, reasonable and non-discriminatory manner" we don't inadvertently disadvantage key players like cable in the marketplace.

Thank you again for asking me to join you today.