Telco Structural Separation: The Road to Local Competition

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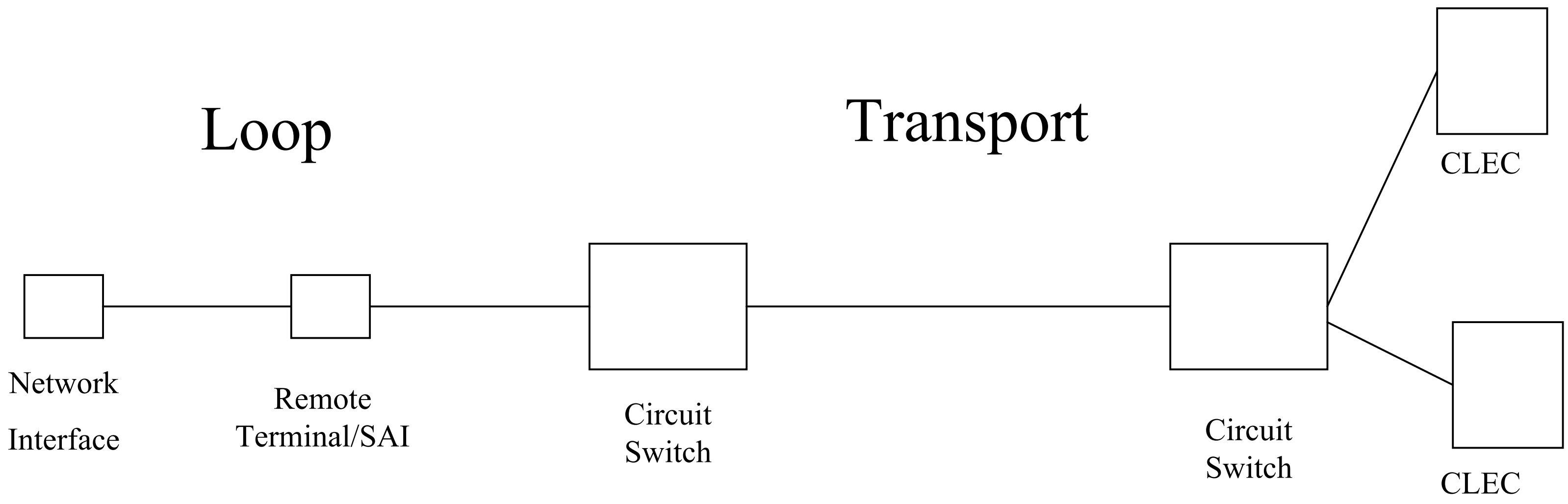
Regulation:
The Road "More" Traveled

- 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

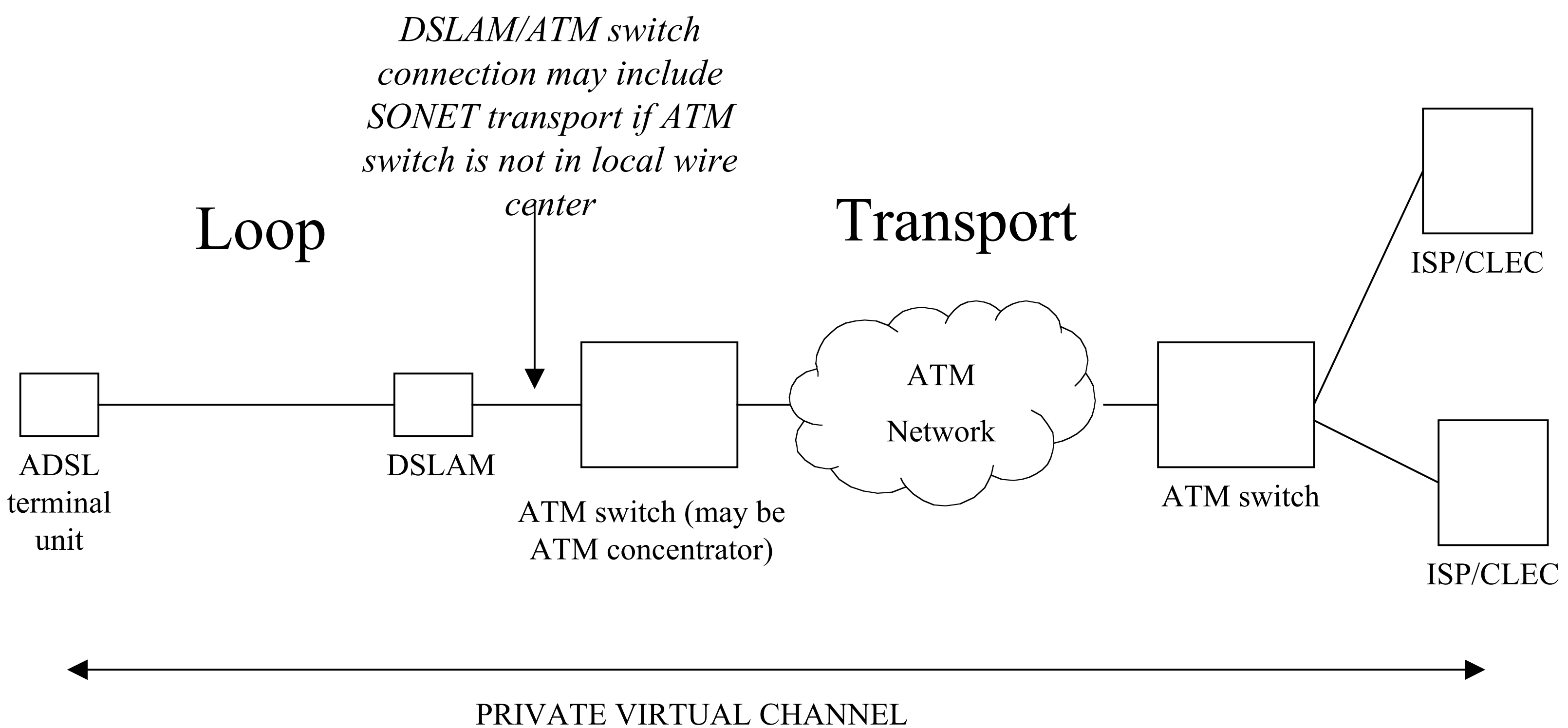
Today's Network



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



Divestiture II - Future Network

- Private Virtual Channels (“PVCs”) may become the most important monopoly element
  - subject to significant economies of scale
  - great potential for discrimination under currrent 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