BOOK II

Bell History and Strategies: Shareholders First, Customers Last

What does the Star Wars' Evil Empire and Bell Atlantic Have in Common?

James Earl Jones was the Voice of Darth Vadar and is the Voice Of Bell Atlantic—

Are There Other Commonalties?

"Food For Thought" Interlude— Conspiracy or Miscalculation?

Book 1 leaves us with a serious dilemma, especially about the I-Way. First, we know straightforwardly that the plans were all scrapped and the announced services were never delivered. But we are left with wondering how both the telephone companies as well as their consultants, were so wrong. Let's look at the options:

There were three massive errors in judgment:

- Mistakes in the costs of rolling out the network
- Mistakes in overestimating demand
- Mistakes by the research/consulting suppliers

Let's walk through each one:

• **Mistakes in the Costs of Rolling Out the Network**: The original cost model for the I-Way was estimated at around $1,200 per household. However, Bell Atlantic stated that the cost of their trials came to $16,000 per line. This includes the cost of the various Info Highway components in the home, described earlier, as well as the cost of the fiber-optic networks.

But, that's a difference per line of 1233%. Of course there are caveats. Most importantly, that the trickle of a rollout was only a "test" of advanced services, and with larger volumes of users, the costs would decline.

In fact, Bell Atlantic's original plans may have actually called for a great deal less spending than $1,200 a line. Bell Atlantic stated it was spending $11 billion dollars and since the company had 18.6 million lines in 1993 — That comes to approximately $591 per line if the company were converting all of its lines, or $917 per line, if the company was only upgrading the residential lines.

Either way you cut it, the cost differential of what it was supposed to cost per line vs the actual costs, is enormous.

There are also numerous hidden technical problems that were revealed with recent ISDN rollouts that also cause the author wonder whether the plans were ever even tested before they were announced. ISDN, a supposedly simpler product that was designed almost a decade before the I-Way is distance sensitive — the farther away the customer is from the "local central office", the worse the service gets to the point that customers over 3 miles away can't get ISDN at all. There are some kludges, where the company can install "amplifiers", which boosts the power, but they are all extra charges.

Unfortunately, various I-Way trials found that amplifiers had to be included also, costing a great deal more than anticipated. But how the phone company didn't know this beforehand is a mystery.

- **Mistakes in Overestimating Demand:** As we demonstrated before, the research from a number of firms showed weak consumer interest.

- **Mistakes by Research/consulting Suppliers:** Then there is the mystery of the consultants. How is it that a major consulting firm, Deloitte & Touche, and numerous other companies who gave testimony at the various state Public Service Commissions, were not accurate? How could they not have been able to examine the data and say "This plan should not be put forward because of numerous problems?"

Plan 2: The Removal of Regulation was a Primary Reason to Announce the I-Way.

From a phone company perspective, the I-Way plans were a win-win situation because while the I-Way doesn't exist, the regulation was still removed. Just look at it from an economics point of view. The removal of regulation has caused massive increases in Bell profits. It also allowed the Bells to hide the actual costs of the networks to competitors, since both the costs and the profits are no longer examined by any regulator..

The removal of regulation on the Federal level over these years has given the Bell's almost all the freedoms they were originally restricted from. Only the prohibition to offer long distance services remains, and that is poised to be removed in the very near future for most of the Bells.

Also, the odds that there would be retributions by the various state regulatory agencies who were supposed to be monitoring the company's deployment plans were nominal, as demonstrated by our New Jersey case study. So it was an obvious choice to take a chance, because the consequences would never be anything but a slap on the wrist.

While the reader may be doubtful, in a follow-the-money scenario, the data will speak for itself. And the data all points to one thing — a disregard by the RBOCs of their primary customers, and a serious shift of focus and purpose since they were created in 1984, to the shareholder.

In order to prove this hypothesis, that the I-Way announcements were done, in a large part, to remove regulation, we need to walk through some necessary background about the Bells, and their notorious mother, Ma Bell, and then present a picture of corporate Bell-Head mentality, revealing a dark side to a group of supposed babies.

Chapter 6 A Brief History of Ma Bell and the Creation of the Baby Bells.

FOR THE TELECOM COGNOSANTI: This chapter is a primer section about the history of the Bell System. If you like, please skip to Chapter 7.

In order to understand the formation and the first decade of the Regional Bells, we need to explore the events leading up to and surrounding the break-up of AT&T, commonly known as "Divestiture."

And believe it or not, the history of divestiture has its roots over a half century ago, in the late 1920s. At the time, complaints about the Bell Systems' monopolistic practices were so rampant that a major piece of legislation, the Communications Act of 1934, was created to set out the parameters for all interstate telecommunications regulation. It also established the FCC with the Commission's initial goal to audit and investigate AT&T.

By this time, "Ma Bell" had just about taken control of everything that was telephone — from the local service and long distance calls, to even the telephone handset itself. AT&T's monopoly consisted of:

- **Local Bell Companies —** which covered 80% of all local telecommunications in the United States through 22 Bell telephone companies, from New York Telephone to Pacific Bell.
- **Long Lines —** which controlled 100% of long distance services.
- **Western Electric —** the division that manufactured all telephone equipment, from the telephone handset to the telephone switches.
- **Bell Labs —** one of the premier research laboratories in the history of the world.

After years of struggle with a non-cooperative AT&T, in 1938 the FCC finally issued the "Walker Report", which found that AT&T had overcharged customers by about $50 million dollars (about $500 million today):

According to "Telephone", by John Brooks (1975 Harper & Row): (131)

> "Western Electric, (the equipment subsidiary of AT&T) through overcharges of various sorts, had been inflating the rate base from which telephone rates were derived, thereby bringing about unwarranted extra costs to telephone subscribers of about $51 million per year. It further contended that Western could cut prices by about 37%."

This report was then rewritten, toned down considerably, and all but forgotten, being overshadowed by world events, including World War II.

It should be emphasized that the concept of regulation was based on a simple assumption — AT&T was a monopoly. Therefore, AT&T had captive customers and had guaranteed, rock-solid income, without risk associated with companies that had competition. People wouldn't just stop using their telephones. Hence, safeguards were needed so that AT&T didn't overcharge its subscribers.

And this same issue still resonates today when discussing the Baby Bell monopoly and the lack of actual Bell competition. (The topic of monopoly power and competition will be detailed in future discussions.)

Then in 1949, the government filed an action in the District Court of New Jersey, stating that AT&T and its division, Western Electric, had:

> "...monopolized and conspired to restrain trade in the manufacture, distribution, sales and installation of telephone, telephone apparatus, equipment, materials, and supplies in violation of the Sherman Act," (the major piece of anti-trust legislation". (132)

According to Judge Harold Greene, the Civil Court Judge that would eventually preside over the break-up:

> "The government requested the divestiture of Western Electric, termination of exclusive relationships between AT&T and Western Electric, divestiture by Western Electric of its 50% interest in the Bell Telephone Laboratories, separation of telephone manufacturing from the provision of telephone service, and the compulsory licensing of patents owned by AT&T on a non-discriminatory basis." (133)

Over the next 7 years (1949-1956) and after various legal movements, a "Consent Decree" was finally issued — a totally watered down slap on the wrist for AT&T. The decree only prohibited Western Electric from engaging in any businesses other than the provision of common carrier communications services, restricted Western Electric from manufacturing any other equipment except that used by the Bell System, and required AT&T to license the patents for royalties.

Along the way there were other various cases, sometimes against AT&T, and sometimes even against the FCC. One short summary appeared in "Telecommunications Deregulation: (134)

> In the **Above 890 decision**, 1959, the FCC opened microwave frequencies above 890 megacycles to private line service by companies other than AT&T. In the **Carterfone decision,** 1968, the FCC ordered AT&T to allow interconnecting devices so that non-AT&T equipment could be connected to AT&T lines. In **MCI Telecommunications Corp v FCC**, 1977, the U.S. Court of Appeals authorized competing uses of microwave systems to service business and data communications markets. The court also concluded that the FCC had no general authority to insist on approval of new services without a finding of "public convenience and necessity". In a part proceeding in the MCI case, 1978, the same court held that the previous decision's mandate required AT&T and the FCC to provide interconnection to MCI.

However, in 1974, the Divestiture ball started rolling seriously. The government filed a separate anti-trust suit against Western Electric, AT&T, and the Bell Telephone companies, which basically stated that AT&T et. al., monopolized a broad variety of telecommunications service and equipment in violation of the Sherman Act.

The government sought "The divestiture from AT&T of the Bell Operating companies and the divestiture and dissolution of Western Electric.". (135) This lead to a series of legal arguments which were divided into 82 separate segments, each segment with major specific disputes and court proceedings on different aspects of the trial, from the issues of anti-trust of the local telephone companies' monopoly on local service to AT&T's antitrust toward competitive services.

And in the late 1970s, Ma Bell had grown by leaps and bounds. She was the world's largest company, with over 1,000,000 employees and revenues almost reaching $70 billion.

However, throughout the 1970's AT&T continued to be an obstructionist, not allowing upstarts like MCI to easily connect to the AT&T network, regardless of the MCI decision. But after thousands of documents, accounting for multiple thousands of pages of information, depositions, and almost 10 years, the final legal decision, known sometimes as "The MFJ" for "Modified Final Judgment", and sometimes as "Divestiture", was done surprisingly, not by Congress or the FCC, but by Judge Harold Greene, as a civil case in a District Court in the District of Columbia.

And so, on January 1, 1984, the telecom world that had lasted for almost a century, had ended. The judgment defined the new world as follows: (136)

- **AT&T:** would remain a long distance company, and it would own the equipment business, Western Electric, and Bell Labs.
  Restrictions: AT&T was restricted from offering electronic publishing/information services.

- **Regional Bells:** There would be seven new companies, known as the "Regional Holding Companies" (RHCs), which would own the 22 local Bell Operating Companies (BOCs). These companies would also be permitted to provide Directory services, including the highly profitable Yellow Pages, and Cellular Services.
  Restrictions: The Regional Bells would initially be restricted to supplying local telephone service and was prohibited from supplying *"any product or service that is not a natural monopoly service actually regulated by tariff."* The companies were restricted from providing:

    - Long-distance service
    - Manufacturing telecommunications products or customer premises equipment (equipment that was on a subscriber's premises, such as a telephone)
    - Information services
    - Cable services

These restrictions were created because of one concern, that the company could use its monopoly advantage to keep out competitors or win customers because of a predetermined, "natural monopoly" market leader position.

However, with the Telecommunications Act of 1996, Long Distance Service is the only restriction left on the Bells, and the Bells have or will all file to offer long distance services.

The Removal of Restrictions

According to Judge Greene, restrictions were supposed to be lifted when the RBOCs could no longer use their monopoly powers to block competitors or unfairly leverage their powers unfairly: (137)

> "It is probable that over time, the Operating companies will lose the ability to leverage their monopoly power into the competitive markets from which they must now be barred. This change could occur as a result of technological developments which eliminate the Operating Companies' local exchange monopoly or from changes in the structures of the competitive markets. In either event, the need for the restrictions upheld will disappear, and the decree should therefore contain a mechanism by which they may be removed."

The legal mechanism allowed the RBOCs to petition the court for "Waivers" to allow them into services when they could justify that their behavior would not be anti-competitive.

AT&T & RBOC Investors and Shares

At the time, AT&T also had more shareholders than any other corporation in America, and the shareholder received one share of each Regional Bell for every 10 shares of AT&T stock. Also, AT&T kept stock ownership of the equipment and manufacturing businesses, in the form of Western Electric and. American Bell, as well as the ownership of the telephone rental set in America's homes.

AT&T would also retain Bell Labs, which in 1997 became a separate company called "Lucent Technologies". And finally, it would retain its largest business, "Long Lines", offering Long Distance services. The exhibit below gives the assets of AT&T as told by the FCC's 1983 Bell System Reorganization Plan. (138)

EXHIBIT 22

AT&T's Assets at Divestiture, 1984

100% of Western Electric
100% of American Bell
100% of 22 CPE subsidiaries
100% of Bell Labs
100% of 22 InterLATA Subsidiaries
100% of Long Lines InterLATA Service
Source: FCC Reorganization Plan, 1983

The Regional Bell's cache of businesses, however, was much larger as a group. The Bells not only received the local Bell phone companies, but also received 100% of the Cellular licenses, as well as 100% of the Directory Publishing businesses, meaning the Yellow Pages revenues as well as Directory Assistance services.

EXHIBIT 23

Regional Bell Assets at Divestiture, 1984

100% of appropriate local operating companies
100% of cellular radio system subsidiary
100% of appropriate directory publishing
Each Bell—One-seventh of the Central Staff
Each Bell—One-seventh of cellular radio system central staff
Source: FCC Reorganization Plan, 1983

RBOC Companies Formed, States Covered

Over the last decade, each Bell has combined their separate telephone companies under one name. Please refer to the Introductory section "Who are the Bells" for states served and the original phone company names.

Division of Assets

AT&T was required to give the new companies "...sufficient facilities, personnel, systems and rights to technical information to permit the Operating companies to perform independently of AT&T". (139)

It was a monumental task by any standard. For example, in 1983 AT&T stated that of the 1,000,000 current employees, 830,000 would remain in their current jobs and their current companies, while 90% would change companies but not change locations or job functions. AT&T would retain only 30% to 40% of the total employees.

In fact, this division of assets also pertained to liabilities and formulas for everything from allocation of debt; reassignment of staff; division of local and long-distance ownership of property; and a wide array of specifics that had to be delineated. The FCC. had the task of overseeing the process.

Equal Access was Mandated

One of the primary reasons for divestiture was because an upstart company named MCI, had serious problems in being able to connect its services to the AT&T network. And in many cases, MCI was supplied inferior connectivity compared to the service provided to AT&T Long Lines.

And the term for connecting MCI or other competitors to the local Bells is different types of **"Access".** Judge Greene wrote: (140)

> "The Decree requires the Operating Companies to provide all Long Distance (interexchange) carriers and information service providers <u>exchange access</u>, <u>information access</u> and <u>exchange services for such access</u> ... that is equal in type, quality, and price to that provided by AT&T and its affiliates."

However, **"equal"** access, meaning equal to AT&T, was also tied to numerous specific problems. AT&T and the local telephone companies were more tied together than a plate of spaghetti. Everything was all-in-one from facilities, including network management, to ownership of the buildings. Therefore, accommodations had to be arranged to try to bridge the gap between the letter of the law and not simply the dismantling of all telecommunications in the United States, and then starting from scratch.

The task of providing equal access to all information and long-distance providers was supposed to be accomplished by September 1, 1986. This time frame was, of course, never met, and as late as 1995 there were still equal access 'holes' in deployment, meaning that competing companies couldn't offer services because the network switches were not adequately upgraded.

And once again, in 1997, **Local Equal Access,** opening the local phone company' networks to offer competitive services, is one of the largest sore points in the current telecom landscape. Though the Telecommunications Act of 1996 has mandated local equal access, the Bells have, like their mother before, put up roadblocks to competitors.

Establishment of Access Fees

Someone would have to pay for the Break-up and letting competitors connect equally. And the costs were not cheap. In 1983, AT&T and the FCC estimated that it would cost the Operating Companies $2.5 billion to provide equal access and reconfigure the network. (141)

At the time, there were a number of proposals on the table for how these new costs should be paid. Over the next decade there would be a series of new charges labeled **"Access fees."**

The primary concept of **Access fees** is straightforward. The local telephone company would charge a fee to a long-distance company for giving them access to the network and the local subscriber, while the local subscriber would also be incurring an access fee for connection to the local telephone network, usually called an **FCC Subscriber Line Charge**.

The original AT&T model had no access fees. Pre-divestiture, AT&T was a holding company, which had the local telephone companies give their entire incomes directly to the parent, who in turn, would "kick back" some of its long-distance revenues to make the companies stay profitable.

In the new era of access fees, everyone from the local consumers and business users to the long-distance companies pays a series of fees to allow their connection to the network. Currently, all consumers pay a $3.50 FCC Subscriber Line Charge (sometimes called "End User Common Line"), while the long-distance companies pay approximately over 40% of their entire long-distance revenue back to the local operating companies in access fees and related charges.

In 1997, the FCC instituted new, additional access charges on residential second lines and business customers, which will be discussed later.

With the Bells receiving over $23 billion in Access fees from businesses and consumers, and estimates by MCI of $14 billion being unjustified, we will return to these charges again. (142)

Division of the World into LATAs

Another problem that the break-up created was one of jurisdiction over a phone call. Was it a long distance call ? Was it local call? Was it a Toll call? So the government created small geographic areas and dubbed them **LATAs** for **Local Access Transport Areas.** About the size of the historical area codes, a LATA boundary, then, determined who owned the call.

And it just created a very large mess. For example, a Toll call, a call within a LATA, but not in the "local calling area," had a different price and was handled differently from the point of view of everything from staffing and pricing to technological access. The Baby Bells were only allowed to handle calls that were "IntraLATA", calls that started and terminating within a specific boundary, while a long distance call was one that crossed LATA lines, even within a specific state. Long distance calls are also known as "InterLATA" and "Interstate" calls, because they cross both LATA lines as well as state lines.

And because of these artificial creations, a call from New York to Montauk, which is only 75 miles away but within the same LATA, only handled by NYNEX in 1992, cost 90% more than a call to California, 3,000 miles away, handled by AT&T.

Forget the geography. We will come back to Toll Calls later.

Computer Inquiry II — Phone Rental Fiasco.

In a separate, but very related case, the FCC issued another decision titled "Computer Inquiry II" in 1982 which *deregulated* the telephone handset and rental, known in the technical jargon as "CPE" (Customer Premises Equipment.). The ruling was summed up by the FCC: (143)

> "The commission would forbore from traditional regulation under Title II of the Communications Act of 1934 in the case of customer premises equipment (CPE) offering of common carriers under the jurisdiction of the Commission."

Divestiture also transferred all equipment that was originally rented to customers by the local telephone company, known as "embedded CPE" to AT&T. A person who was renting a phone through the local telephone company, (and everyone in 1982 rented a telephone) would now either have the choice of purchasing the equipment or continue renting, now from AT&T.

While this law allowed customers to attach other, non-AT&T telephones to the telephone network, deregulation also removed the regulation which allowed the price of the service or product to reach "market value." We found deregulation was also to become a euphemism for simply raising prices without any safeguards for those who still kept the same service they had prior to deregulation.

Aunt Ethel's $1119 rotary phone rental is testament to the success of this endeavor, and this cash cow will be addressed in subsequent chapters.

Deregulation of Inside Wire — More Bad News

Another telecommunication product, **"Inside Wiring",** sometimes referred to as **"Wire Maintenance"** or other regional names such as US West's "Line Backer", was also deregulated in 1982. This federal law basically left each state to postulate its own laws, but all states followed the FCC's lead. (144)

The ruling basically stated that the wire inside a person's residence could either be maintained by the subscriber or rented or maintained from the local telephone company.

We found identical problems to the telephone rental, major increases for anyone who kept this telecommunications product.

State Regulation Remained

Prior to divestiture and continuing today, the states have had the responsibility to monitor and regulate the business done in that state by all local telephone companies. Therefore, all local service offerings have been and continue to be state controlled. The Public Utilities Commissions (PUCs) across the United States have had the primary task of evaluating the costs and quality of service provided, and in most states have the legal power to impose fines and price reductions based on PUC court hearings.

The forms of regulation that each state uses, are all unique, and will be demonstrated later, many times contradictory, leaving America with a Swiss cheese, full of holes, regulatory environment. And the Telecom Act of 1996 didn't fix any of the regulatory problems state regulation has created.

Chapter 7 The Break-up: Opinions About the Future

The breaking up of the world's largest company was one of mass confusion and even the usually opinionated analysts and reporters were unsure of how the Bells would fare, much less the impacts the breakup would have on the consumer or business user.

For example, even the FCC's Reorganization Plan stated that the Bells would have financial risks because they weren't as big as AT&T. (145)

> "The effect of the reduction of size and the regional concentration is likely to increase somewhat the inherent investment risk of each RHC (Regional Holding Company or RBOC) to the present Bell systems. The national diversification of the Bell system combined with its size, has produced earnings stability and low investment risks. Earnings of the RHCs is not likely to be as stable as the earnings of the present Bell systems and the new RHCs are likely to have more investment risk than the Bell system currently exhibits. Investors may require somewhat higher rates of return to compensate for this risk, with these somewhat higher costs ultimately being passed to the ratepayers. "

According to most articles, the majority of sources said that AT&T's break-up would provide a competitive local and national telecommunications environment, which in turn would keep prices low. According to Charlie Brown, then president of AT&T, long-distance prices would decrease about 10% to 15% over five years, while local prices would increase no more than 8% to 10% for the next few years and then level out. (146)

Even the most fundamental issue, who divestiture was supposed to first serve, or more specifically, who the Regional Bells were supposed to first serve, was never fully understood at the time, nor is it at all clear today. Everyone had then, and has now, different viewpoints on this topic. The three primary viewpoints are that divestiture was supposed to first serve:

A) The Ratepayers
B) The Shareholders
C) Business Users

Based on surveying of consumers, business users, and telephone company staff over the last seven years, we found strict conformity to each group believing it was supposed to have helped their own needs.

- **Consumer View -** The overwhelming majority of consumer telephone subscribers believe that the breakup was supposed to bring better services, and that these new companies would be responsive to their needs. Lower prices would come because of direct competition. The RBOCs were supposed to first serve them by providing the best quality at the lowest, regulated price.

- **Business Users -** Business users felt that divestiture was supposed to serve them first, by lowering local and long-distance business rates, which were "subsidizing local consumer services" and that the RBOCs were going to be working to fulfill their supposed manifest destiny, deployment of advanced technologies.

- **RBOCs -** Meanwhile, the RBOCs believed, and still do believe, that these new companies were created to be "market driven," and that therefore the company should select their own priorities. This viewpoint is one which the shareholders obviously feel benefits them the most, since it is their company.

There is a fourth group, which includes a diverse range of interested parties of telecommunication's future, including technology vendors or the cable and newspaper industries, who are on a continuum of opinions, hovering somewhere in between any of the above three responses. Unfortunately, a good deal of all of these beliefs were also based on some serious misconceptions or mistaken premises.

Probably the largest misconception was that the local operating companies weren't profitable in 1983. The reason local rates were going to increase was supposedly because AT&T Long Lines, the long-distance part of the company was, as one writer stated: (147)

"AT&T was plowing back 37¢ on the dollar to bolster up local telephone charges [operative phrase: 'plowing back']. When this money goes away, the local operating companies will have to raise rates to pick up the slack."

It turns out that this viewpoint was completely a matter of accounting practices and political maneuverings. Under the accounting methods used by AT&T prior to divestiture, long-distance services were highly profitable because there were no major expenses, especially no fees paid back to the local company. Therefore, an artificial delineation between the local operating company and Long Lines existed. This "plowing back" was, in actuality, caused because there were no access fees—the post-divestiture fees paid by the long-distance companies to the Bells.

As mentioned earlier, under the post-divestiture picture, the long-distance companies pay the Regional Bells very high fees, over 40%, which include the access for local customers and additional monies paid in separate fees for "Billing and Collection" services. Using this enlightened accounting procedure, the RBOCs were quite profitable in 1983.

And this myth, that local service is unprofitable, has been very pervasive, even though the annual reports tell a much different story. For example, in two different articles quoting NNI research, both Pac Bell and Bell Atlantic stated that local service loses money. Here's Bell Atlantic: (148)

"Kenneth Pitt, a Bell Atlantic spokesman, said that basic phone service is a money-loser for his company." [emphasis added]

Worse, Bill Gates, CEO of Microsoft, thinks that local telephone service is being 'undercharged". In his article titled "Bill Gates predicts what's ahead in '97" (1/2/97) appearing in the New York Post, he stated that current regulation has caused local telephone service to be undercharged while long distance service is overcharged. He also predicts that anyone online will be paying more for local service in the future. (149)

"The rate scheme used to pay for telecommunications in the United States will change dramatically. Regulators will end the current practice that forces phone companies to undercharge for local service and overcharge for long-distance service. As a result, heavy user of the local telephone

> network — including people who keep computer modems connected hour after hour — will see bill rise."

This misconception is based totally on the way the Bells have been able to redefine terms such as "Local Service" or "Basic Service", and then convince regulators and even Bill Gates, that they lose money on local service. We will show that local service is one of the most profitable businesses in America.

Finally, another misconception was that competition would come to all aspects of the RBOC business. In 1984, all RBOCs and long-distance companies were expecting competition, which was expected to keep prices down and create an environment to offer better services. US West states in its 1984 Annual Report: (150)

> "Our philosophy is 'Bring on the Competition.' In all of our companies we focus on serving the market as competitors."

Ironically, IBM was supposed to be AT&T's biggest competitor and vise versa.

Chapter 8 Regional Bell Strategies Since 1984

To the outside world, the Baby Bells' birth was one of confusion mixed with a degree of enthusiasm. However, to those who would take up the reins of these new fiefdoms, the Bell executives that were to become top management in these new companies, the focus was to become mini-AT&Ts, their model of the future. And armed with a great deal of cash, and an intimate workings of their "Ma Bell", the seven would start immediately reshaping their image of the sleepy local Bell system companies.

To this end, over the decade there has been a consistent, specific set of strategies that **all** Baby Bells have in common —The Bell System is still alive.

We will demonstrate that all the Bell's have followed the original Bell System policies, from the removal of regulation, or using lobbying to effectively stop adversaries, whether it be other potential competitors, such as AT&T, or state consumer advocates. Corporately, the Holding Company over the decade redesigned their corporate mission, which does not put the telephone subscribers first. Finally, most of the far-flung new businesses, such as Real Estate and computer leasing lost billions.

In future chapters we track down the money, going through the revenues, expenses and profits of the Bells, demonstrating that the shift of corporate purpose — corporate profits, not subscriber needs, are the first order of business.

While some of these Bell directives were not made public, almost all strategies center around the maximization of the local subscriber revenues, the cash cow, to feed the projects that potentially bring more return on equity for the shareholder.

Follow the Bell System's Edicts: The "Bell-Heads"

> **From 1984 to this day, all of the Regional Bell company presidents and chairmen have come directly from the Bell System ranks. They have been all male, all white, and all middle aged men.**

The Bell System was over 100 years old by 1984, and it was known as a closed group, known as Bell heads, as well as a breeding ground for its own successors. For example, before the break-up, the local Bell presidents would meet regularly to discuss problems and be given the Company's political agenda(s) for the year. This included even the roll-out of products and services.

According to "The Fall of the Bell System", Peter Temin, Cambridge University Press, 1987, after it was finally decided to divide the Bell System up into seven units, all seven presidents were chosen by AT&T, and all were or had been presidents of the local Bell companies. (151)

> "Charlie Brown, (president of AT&T) announced his appointment of the CEOs of the seven regional holding companies at the May President's conference. He chose seven of the existing Bell Operating presidents. The seven presidents were Zane Barnes (Southwestern Bell), Thomas Bolger, (C&P Telephone Company) Wallace Bunn, (Southern Bell), Donald Guinn (Pacific Telephone), Jack MacAllister (Northwestern Bell), Delbert Staley (New York Telephone) and William Weiss, (Illinois Bell). "

And even the later transition, from these original RBOC presidents to their successors, was a very smooth transition, because the inheritors were also from the Bell System. For example in Bell Atlantic's 1985 Annual Report, Thomas Bolger, CEO, is pictured alone, while by the 1988 Annual Report, there is Ray Smith, the current CEO, splitting the page in a glossy color photo.

This same, relatively smooth transition happened with all of the other Bells as well — Weiss of Ameritech begot Richard Notebaert, Pac Bell's Guinn begot Philip Quigley, and NYNEX's Staley begot Ferguson who begot Seidenberg.

It is and remains an inbred, old boy's network, groomed for succession.

And from the beginning the presidents inherited massive amounts of an embedded system of everything — from the way a call is handled with customer service to even the political clout of the Bell system. The primary continuity of the RBOC's actions, almost regardless of which RBOC is discussed, is this Bell mentality. and as we will see, the behavior among RBOC corporate staff has been strikingly the same.

Therefore,

- if one company applies for "Long Distance Service Provision", sooner or later they will all follow suit,

- if one RBOC has increased number of second lines or increases in Call Waiting, you can expect that it is happening in all of the other RBOCs.

- Or if some law suit occurs in one state, such as the improper charging of inside wiring, you can almost bet that the same behavior is happening throughout the Bell system.

The rest of this section demonstrates that the Bell system is still alive and that the RBOC's business strategies and plans over the last decade have been virtually identical.

Chapter 9 Remove ALL Regulation—How? Plead Poverty and Constantly Lobby

From the very beginning, the RBOCs have shouted their belief that all regulation is evil, and it has been stopping the companies from creating a new world of telecommunications. This fundamental point, like a mantra repeated day after day, month after month, year after year, eventually wore down regulators into believing that the Bells were overburdened by laws and they would bring the Info Bahn faster if these laws were removed.

From the earliest Bell annual reports, such as Ameritech's 1985 Annual Report, the investors are informed that regulation controls everything from the service offered to financial success. According to William Weiss, Ameritech's Chairman: (152)

> "Our goal remains unchanged: To have the marketplace, not regulation, determine what we offer, the prices we charge and our financial success. "

US West states in its 1984 Annual Report: (153)

> "Our philosophy is 'Bring on the Competition.' In all of our companies we focus on serving the market as competitors. We welcome competition and ask only that we be permitted to compete on an equal footing. Nothing more. Nothing Less. For that reason, we advocate continued deregulation of our industry at state as well as federal levels. "(emphasis added)

Ironically, **in 1997,** 13 years later, Sol Trujillo, president and CEO of US WEST Communications Group declared almost the exact same sentiment about bringing in competition. (154)

> "We're ready, willing and eager to compete. My pledge from U S WEST and my challenge to competitors is simply this - let's make 1997 the year we deliver on the full promise of competition to the American public."

Southwestern Bell in its 1988 Annual Report stated: (155)

> "Steps to take to make this network of the future a reality: Southwestern Bell needs assistance of those state and federal bodies that regulate our business. We are convinced the current system of regulation doesn't service the best interests of our customers, our owners or the country itself. A new regulatory framework is needed, and we've proposed what we believe are workable alternatives to federal and state regulators."

Southwestern Bell continues in its 1990 Annual Report: (156)

> "Instead of designing public policies that simply protect the consumer from higher monthly bills, regulators need to broaden their view of consumer's interests. They should recognize that telephone consumers are also wage earners, whose paychecks might very well increase if their employers are made more productive by the availability of state of the art network. And regulators should see telephone customers as consumers of community services, too, who stand to benefit a great deal from services that can enrich lives and can be provided efficiently over advanced communication system. "

BellSouth, in its 1993 Annual Report stated that they were "taking aggressive actions to tear down the unfair barriers." (157)

> "With laws and regulation lagging badly behind competitive realities and customer demand, we are turning up the heat in our steady battle to level the playing field. We are mounting a two-pronged legal challenge in the federal courts to the out-dated ban on providing video programming over BellSouth's local telephone network.
>
> "We are taking aggressive actions to tear down unfair barriers in our states, as well. We serve working with progressive legislatures and regulators throughout our region to put pro-competitive rules in effect. The states should play a constructive role in the Information Age by allowing a free and open marketplace to set prices for many telecommunications services."

And there were even threats by the Bells that if regulation wasn't removed, they wouldn't even bother to invest in the network. For example, in 1989, Ameritech's Chairman, Weiss stated that if regulation removal didn't occur, Ameritech would not invest in its own phone companies.

> "If we see constant progress, the company will stick with the phone business. **If regulations are tighter in the next three to five years, we will question plowing money into this business."** [emphasis added] (158)

And the Babies' constant attacks have been very successful, especially in manipulating state controls. For example, in 1994, Ameritech's Investment Alert, stated that the company no longer had any regulatory controls by the states in terms of earnings. (159)

> "Ameritech has led the industry in achieving regulation that removes regulatory earnings caps. . . . All of Ameritech's intrastate operations are off of return-on-asset regulation resulting in freedom from regulatory caps on earnings and no earnings sharing."

By 1995 the company added: (160)

> **"Federal and state regulators no longer limit the company's profits."**
> (Source: Ameritech Investor Alert 1/95)

As we will see, these regulatory changes were all based on the premise that the Info Bahn was going to be financed by these new found profits.

Plead Poverty

Even before the ink was dry on the Divestiture Consent Decree, Southwestern Bell applied to its regulators for a $1.2 billion, 26% rate increase to make up for revenues lost because of the impending break-up. And every other telephone company would apply for massive increases. (161)

By 1986, over $10 billion dollars of increases was granted. Many of these increases were permanent, and therefore NNI estimates that over $60 billion dollars was eventually collected from 1982-1996. These increases are clearly shown in the exhibit below, which give's the FCC's summary of telephone rate cases, 1982-1986. The data was a compilation of state public utility information, and covers not only the amount of money that was granted, but also gives the amount that was requested.

The exhibit reveals that over the five-year period, the Regional Bells were granted $10 billion. This is compared to the $21 billion dollars the Bells requested— a 114% difference. (162)

EXHIBIT 24

FCC Compilation of State Completed Rate Cases, 1982-1986

(In the Millions)

	1982	**1983***	**1984**	**1985**	**1986**	**5 Year**
Requested	$5250	$4511	$7321	$2640	$1758	$21,480
Granted	$2882	$1811	$3875	$1155	$ 290	$10,013
	55%	40%	53%	44%	16%	114%

* data for the last three months of 1983 not available

Source: The FCC, 1993, NNI 1994

As we will see later, almost none of these increases were justified, for the companies did not use it to either increase construction expenditures or staff.

Pleading poverty continued through the next decade, and is still prevalent today. For example, all of the Bell have requested price increases in 1996, claiming that competition has been or will erode their profits. For example, Pacific Bell received a 35% increase in the price of local service when Toll call competition was introduced, (163) while US West has been requesting increases in numerous states, declaring subsidies exist and reducing them will actually encourage competition. (164)

"U S WEST Communications Asks For Changes to Encourage Competition, Align Prices With Costs

> "U S WEST Communications will ask the Iowa Utilities Board to change its prices to align them more closely with costs and encourage more competition for local and long-distance telephone service in Iowa. — The company will ask to: Raise the price of local residential phone service by $2.85 per month, more accurately reflecting the cost of providing local residential service. By reducing the traditional subsidies for local service, the change will help encourage competition in the local-phone-service business."[emphasis added]

A form of Pleading Poverty in 1996 actually reached new heights when the Bells were able to halt the FCC competition Order by taking the FCC to court. This new round of pleading — that the FCC's order is below the companies' costs and is basically a confiscation of their property. Richard D. McCormick, chairman and CEO of U S WEST Inc., put it this way at the 1996 annual convention of the United States Telephone Association, an organization that lobbies for the Bells. (165)

> "The FCC's proposed rules on interconnection, unbundling and resale are not competition; they're confiscation.
>
> "It's as if the government said 'OK, McDonald's: sell your hamburgers to Burger King, below your cost; watch them undercut your price and call it competition.
>
> "The proposed (FCC) rules would allow competitors to buy local telephone companies' services below the cost of providing them.
>
> "The proposed FCC rules are the biggest threat ever, to our industry's ability to improve our facilities, our products and services, and our contribution to society."

As we will see in the Revenues and Profits section, US West is one of the most profitable of the Bells today. Its profits are almost 150% more than other major American corporations with competition. And 95+% of it's profits are from local telephone customers.

Constantly Lobby and Spend More Than Adversaries

NYNEX had breakfast at the White House, according to the New York Times. (166) Meanwhile, the lobbyists for the Bells includes a former governor, former State Majority leader, and even a former Secretary of Defense.

Welcome to a glimpse at how the rich and powerful have kept telecommunications in their hands, not the subscribers.

Soft money, hard money, PACs, contributions, research funding — the Bells, the "Campaign Finance Kings", do it all. In fact, it could be argued that the Regional Bells have shown that their best business skill is lobbying. Their efforts throughout the last decade to keep their local monopoly, avoid critical audits, never have a major media investigation, and have the federal, state and local principalities grant alternate regulations has been a monumental, well-coordinated, and costly job.

In order to keep their control, the Bells have outflanked and outspent any other group opposing them to make sure it gets what it wants, both singularly and collectively. Based on case studies, we estimate that the Bells outspend the consumer advocate side 30 to 1, with overall federal and local lobbying estimated at $225 million annually.

(Also, their mother, MA Bell, had taught her children well. It should be remembered that the RBOC's powers was just an extension of Bell System's original powers.)

The primary methodology has been both a close grass-roots approach, from supporting political candidates, as well as massive local lobbying. This includes everything from specific local and civic groups to massive expenditures on high-paid lobbyists, many with blue-chip credentials.

On the Hill, they have bought control through a series of politicians and others that reflect power and connections. The list goes from Former Defense Secretary Dick Cheney, now a director for US West, to former governors (167)

In some cases the Bells just hired well known state politicians and used their skills and influence to help move through legislation—with their own agenda. Case in point, Stanley Fink, former New York State Senator and State Assembly Speaker, who went to work for NYNEX. A NYNEX press release about his death shows that he helped obtain NYNEX's approval for both a major state Alternate Regulation Case, and influenced people for the Telecommunications Act as well as the NYNEX—Bell Atlantic merger.

The irony is that Fink used to be considered a politician on the side of the consumer. (168)

> "Mr. Fink served as a member of the New York State Assembly for 18 years, the last eight as Speaker.
>
> "As (NYNEX) senior vice president, Mr. Fink developed the corporation's positions on public policy matters and coordinated NYNEX's regulatory and legislative functions in New York. In 1995, he oversaw the approval of a landmark agreement with New York State regulators that dramatically changed decades of monopoly-era telecommunications regulation in the state and froze basic phone rates through the year 2002.
>
> "Last year he led efforts to implement the Telecommunications Act of 1996 in New York, including the continued opening of local telephone markets to competition. <u>For the past year, he also orchestrated the statewide public education and information campaign and the regulatory review process on NYNEX's $23 billion merger with Bell Atlantic.</u>
>
> "In a little over two and a half years, Stanley Fink has had an enormous impact on this business. It didn't take him long to master a new and complex area of regulation. Drawing on his renowned leadership skills, <u>he influenced the making of important telecommunications public policy here in New York, a legacy that will have an impact for decades to come."</u>

And it's on the local level, that the Bell's impact has been so dramatic. According to the Wall Street Journal: (3/15/93) (169)

> "The Bells just don't work Washington - They had some $95 million to bestow on grass-roots causes in 1992 alone, according to FCC records - they had wired the systems from top to bottom.
>
> "Each year the Bells hand out tens of millions of dollars to chambers of commerce, rotary clubs and the like. In turn the phone companies often find support for their legislative agenda in the form of resolutions, letters and phone calls to Capitol Hill. They nurture the grass

> roots one blade at a time, says an admiring AT&T lobbyist, Mike Baudhuin.
>
> "The Bells reach...an influential alliance with the 450,000 employees spread across the country and on the ground presence in virtually every congressional district.

This money was atop an additional $40 million in lobbying for 1992, according to the FCC.

But these figures don't begin to cover the law firms that create filed documents. The consulting firms that work on alternate regulation policies/information highway studies or the series of "contributions" made to make the phone company's good will extend into the communities.

In fact, lobbying expenses may not even be paid for by the Bells. According to an audit by the FCC, released in 1995, the Bells improperly charged $116 million dollars of lobbying fees to telephone subscribers, between 1988 to 1991. (170)

EXHIBIT 25

FCC Audit Results of Improper RBOC Lobbying Expenses, 1988-1991

(In the millions)

Ameritech	$18 million
Bell Atlantic	$21
Bell South	$27
NYNEX	$14
Pacific Telesis	$12
Southwestern	$14
US West	$10
Total	$116

Source: FCC, 1995, Washington Telecom Week.

Washington Telecom Week, 12/1/95, reported that the FCC decided to do nothing about these improprieties. MCI's filed complaint urging the FCC to have the companies make retributions, had little impact. (171)

Then there's something called "Soft Money", where companies donate money to various Democratic and Republican causes. Common Cause, a non-profit organization who monitors campaign financing, found that millions of dollars were spent by both the RBOCs and long distance companies during the 18 month 1996 election cycle—especially geared toward securing their own favors in the Telecommunications Act of 1996.

The two exhibits (172) (173) below highlights the long distance companies' soft money donations, followed by the RBOCs soft money expenditures for both the Republican and Democratic parties. Leading the pact is AT&T followed by MCI. However, as a group the Bells out spent the three major long distance companies by over $400,000.

EXHIBIT 26

Common Cause's Long Distance Soft Money Donations, 1996

Donor	Democrat	Republican	Total
AT&T	$326,680	$417,590	$ 744,270
MCI Corp	$479,303	$270,000	$ 749,303
Sprint Corp	$137,450	$101,400	$ 238,850
	$943,433	$788,990	$1,732,423
Total Long Distance			**$1,732,423**

EXHIBIT 27

Common Cause's RBOC Soft Money Donations, 1996

Donor	Democrat	Republican	Total
Ameritech Corp	===	$ 131,500	$ 131,500
Bell Atlantic Corp	$ 128,000	$ 224,000	$ 352,000
BellSouth Corp	$ 71,750	$ 243,514	$ 315,264
NYNEX Corp	$ 127,500	$ 313,505	$ 441,005
Pacific Telesis Group	$ 117,250	$ 213,100	$ 330,350
SBC Communications	$ 130,500	$ 172,400	$ 302,900
US West Inc.	$ 145,500	$ 172,400	$ 317,900
	$ 720,500	$1,440,019	$2,160,519
Total RBOC			**$2,160,519**

Please note: According to Common Cause, the chart only represents companies that spent over $50,000. Therefore, Ameritech did not spend over $50,000.

In short, in the future sections when the Bell's profits and regulation are discussed, keep in mind that influence and politics can account for much of the Bell's overcharging of customers.

Chapter 10 The New Bells: Shareholders First, Customers Last

GOAL: Redefine the Company to be Global, Entertainment & Information Services Group, Instead of the Local Phone Company.

The clearest indication that the Bells have shifted focus is their own definition of themselves — The Corporate Mission Statements. From their inception, the Baby Bells started to slowly redefine themselves from a telephone utility to be reborn as a global information services and entertainment conglomerate. Notice the change in the definition and corporate mission of Ameritech, first from the 1985 Annual Report then to their corporate profile in 1996. In 1985, Ameritech was still a communications company first serving its monopoly market. By 1996, there is now longer any discussion of its monopoly subscribers. Now they serve 50 states and 40 countries.

1985 Ameritech Annual Report: (174)

> "The Ameritech companies are the leading supplier of advanced communications products and services in Illinois, Indiana, Michigan, Ohio and Wisconsin."

1996 Ameritech (175)

> "A worldwide leader in making communications easy, Ameritech serves millions of customers in 50 states and more than 40 countries. Ameritech provides a full range of communications services, including local and long distance telephone, cellular, paging, security monitoring, cable TV, electronic commerce, on-line services and more. One of the world's 100 largest companies, Ameritech (www.ameritech.com) has 65,000 employees, 1 million shareowners and $23 billion in assets."

US West's definition of themselves in **1984** was as a diversified telecommunications holding company in the Information Industry.(176)

> "US West is a diversified telecommunications holding company, with a growing base of information industry companies. "

By 1993 US West's Annual Report states that it serves "local markets worldwide", the telephone and their regional monopoly all but forgotten. (177)

> "US West is in the connections business, helping customers share information, entertainment, and communications services in local markets worldwide."

BellSouth's quote in its 1993 Annual Report shows the path the RBOCs have taken in their own redefinition of themselves — from a regional telephone company, to now covering 14 countries on five continents. (178)

> "In 1984 BellSouth was a regional telephone company. From our base of 9 states in 1984 in the Southeast, we expanded overseas to serve cellular, paging, wireline, and mobile communications in 14 countries on five continents."

They continue with:

> "Convergence, interactive multi-media, on-demand services. New words, new opportunities for investors."

By 1996 BellSouth doesn't even hint that they are beholden to any local monopoly customers. (179)

> "BellSouth is a $19 billion communications services company. It provides telecommunications, wireless communications, directory advertising and publishing, video, Internet and information services to more than 27 million customers in 18 countries worldwide."

Bell Atlantic, by 1990, was a global communications and information management company: (180)

> "The watchwords of the Bell Atlantic Way are teamwork, accountability, and empowerment, the characteristics we believe will be the key to success in a global marketplace. . . . The objective we have set for ourselves is our vision of being a leading international communications and information management company. "

Bell Atlantic believed that in 1994 their mission was clear-cut — and it included everything from video entertainment to cable television. (181)

> "Our business opportunity and beyond is straightforward — enhance the value of our core businesses by expanding our customer and service base, and develop high-growth businesses in the video entertainment, cable transport, cable television, and information services markets. "

By 1996, Bell Atlantic, as the company, had moved to the "forefront of communications, entertainment and information" and owns a "substantial interest" in the telephone company of New Zealand. (Author's note: The population of New Zealand is three million people and multiple millions of sheep.) (182)

> "Bell Atlantic Corporation (NYSE: BEL) is at the forefront of the new communications, entertainment and information industry. In the mid-Atlantic region, the company is the premier provider of local telecommunications and advanced services. Globally, it is one of the largest investors in the high-growth wireless communication marketplace. Bell Atlantic also owns a substantial interest in Telecom Corporation of New Zealand and is actively developing high-growth national and international business opportunities in all phases of the industry."

The next two quotes, from SBC Communications and NYNEX are simply used to round out NNI's primary finding — that the telephone monopolies have all but hidden the fact that they should be local phone companies dedicated to subscriber interests first and foremost.

NYNEX is also a global communications and now even a media corporation. (183)

> NYNEX is a global communications and media corporation that provides a full range of services in the northeastern United States and high-growth markets around the world, including the United Kingdom, Thailand, Gibraltar, Greece, Indonesia, the Philippines, Poland, Slovakia and the Czech Republic NYNEX has expertise in telecommunications, wireless communications, directory publishing, and video entertainment and information services.

Meanwhile SBC Communications Inc., is now one of the "world leaders in communications.". (184)

> "SBC Communications Inc. is one of the world's leading diversified telecommunications companies and the second largest wireless communications company based in the U.S. SBC's subsidiaries provide innovative telecommunications products and services under the Southwestern Bell and Cellular One brands. Its businesses include wireline and wireless services and equipment in the U.S. and interests in telecommunications businesses in Europe, Latin America, South Africa and Asia; business and consumer telecommunications equipment; messaging services; cable television in both domestic and international markets; and directory advertising and publishing. SBC Communications Inc. reported 1996 revenues of $13.9 billion."

In all of these definitions, there is only one thing missing—the local phone company's primary customers, in their original mandated geographic areas. As we show in future chapters, even with all this hype, it is still the local customer who supplies the overwhelming majority of both current cash and current profits.

From the subscriber perspective, these corporate mission statements should have added the phrase **"Deliver Quality Services to our monopoly subscribers at the best prices possible.".** The lack of consideration in their definitions is also demonstrated by their performance in terms of quality of service and the price to subscriber, which will be addressed in later sections.

Shift Strategy- From Customers First to Shareholders First.

The obvious definitional changes in the Bell's Corporate mission statements over the last 13 years are just a road-sign of a larger corporate shift — to serve the customers last, shareholders first. The signs of this shift are many and obvious. One major change occurred when all of the Bells replaced the local phone company name, such as Ohio Bell or New York Telephone, to with that of the holding company — i.e., Ohio Bell became Ameritech. Ashley Brown, former Ohio Public Utilities Commissioner put it this way. (185)

> "When Ohio Bell became part of the Ameritech Corp., the company executives became less and less trustworthy. They began to use power in ugly ways. They became less and less concerned with local concerns and more and more interested in corporate mucky-mucks in Chicago. Sometimes they were just flat-out dishonest." Ashley Brown, former Ohio Public Utilities Commissioner.

In fact, the removal of the local identity, with changes shown in the Bell's shift in corporate mission, are all just road-signs for the customer to beware.

Or Take the Case for Customer Service Declines.

Regardless of all of its detractors, the Bell system prior to the break-up was a well functioning behemoth, that not only kept prices somewhat reasonable, but more to the point, had a sense of integrity in the work. The Bell System jobs were in high demand, because they were not only well paying and stable, but because of the company's determination to deliver high quality services. In fact, workers considered to be a personal insult if the phones weren't answered promptly.

For example, in "The Rape of Ma Bell", by Constantine Raymond Kraus and Alfred W Duerig, (Lyle Stuart, Inc. 1988), these two former long-time Bell employees bemoaned the break-up of AT&T, and discussed the work ethic of the original Bell system. (186)

> "Service was the goal whether it was in long-term planning or short term programming and installation of plant additions or day-to-day operations and maintenance of the network. The highest quality service and performance were uppermost in the minds of all Bell managers and craftspeople. Whenever a choice had to be made between cost and service, or between revenues and service, quality invariably won out."

Also, jobs at the Bell system were coveted. (187)

> "They were good jobs, coveted ones. When you worked for Bell you worked for life. On the average a manager stayed with the company thirty-two years resulting in a lowest management turnover of any large American company. Longevity was the norm, It was expected. Recognition awards usually weren't given until 25 to 30 years of service."

The largest shift away from customer needs has been the massive local phone company staff cuts that has effected all customer services. Since 1984, the Bells corporate arm has sheared off over 235,000 of the original workforce. Almost all of these layoffs were from the local telephone companies, and almost all of it done with an eye for corporate profits.

Without proper staffing, this has left the customer taking a back seat. It shows in the number of complaints, missed appointments and lack of keeping-up service standards that were all the heart and soul of the original Bell system. According to an LA Times article, (6/18/95) (188) the Ohio's PUC received 10 times the number of complaints in 1994 than the previous year, while NYNEX missed 142,000 appointments in the last three months of 1994 alone. In fact, according to NYNEX's 1996 3rd quarter report, (189) "New York Telephone will be required to issue rebates to customers of at least $102 million for not maintaining adequate service standards. As a New York Post columnist, Irwin Stelzer, recently put it:, 2/26/97 **"NYNEX fails to show up at about 1,000 repair appointments every business day."** (190)

Compare this to the original Bell system philosophy from "The Rape of Ma Bell" and the change is obvious,. In fact, during interviews with some of the remaining staff, the new Bell philosophy is to worry much more about job security and waiting for pensions to be made available. In one interview we found that the staffing of some offices were cut in half, but the work load has been increasing— the staff being forced to deliver services "as best as we can with the limitations". (191)

Chapter 11 Buy Companies, Lose Money: RBOC Investments

Almost from the beginning, the Bells started a process of purchasing companies and entering into new business arenas. This was a no brainer since the companies were secure in the fact that their primary business, local telecommunications services, was protected from direct competition. Before the Telecom Act of 1996, most states restricted other companies from offering any local telephone services. This security also led to a complacency to their local customers, with little new innovation.

And like the siblings that they were, the progeny of Ma Bell, their actions all mimicked each other. In fact, a 1985 report by Link Resources, surveying the Regional Bells' lines of business, stated that the companies' purchases were mostly the same, and there was little differentiation in actions— and little innovation. (192)

> "From the viewpoint of the telephone company customer, the seven RBOCs have done very little in the way of innovations and diversification, and even less in differentiating themselves since divestiture. In addition to the local exchange carriage business, a standard list of new business enterprises across the seven RBOCs include:

Customer premises	Office automation equipment sales
Mobile communications	Directory publishing and advertising
International business	Equipment leasing and financing
Venture capital development	Property management and real estate"

The next exhibit summarizes a Department of Justice's analysis of new Bell businesses. (193) It should be remembered that the Bells were required to file for "waivers" to allow them into new areas, and the list below are from business waivers granted from 1984 to 1985.

EXHIBIT 28

RBOC Line of Business Waivers Granted from 1984-1985

Non-Tariffed Billing Services	**Office Equipment**
Ameritech	BellSouth
US West	NYNEX
	Pacific Telesis
	Southwestern Bell
Real Estate	**Software**
Pacific Telesis	Ameritech
US West	BellSouth
BellSouth	Bell Atlantic
NYNEX	NYNEX
Southwestern Bell	
Bell Atlantic	
Print Media/Directory	**Foreign Business Ventures**
Pacific Telesis	Ameritech —Cellular
Southwestern Bell	Ameritech — Consulting
Ameritech	NYNEX
BellSouth	Pacific Telesis
	BellSouth — Cellular
	Southwestern — Cellular
	US West

Source: Department of Justice, 1986, Link Resources

Considering the outcome of many of these ventures, especially real estate and computer leasing, the approach of purchasing companies has been a continual loss leader --- Some might say a dismal loss. The next exhibit highlights the spending, (mostly losses) from Foreign Investment, Real Estate, Financial Services, Computer leasing. (194)

Exhibit 29

Bell Spending for International and Real Estate, 1984-1996

- $27 Billion Overseas Operations
- $11 Billion Real Estate, Financial Services, Computer Leasing.

Here's some of the details:

RBOC Real Estate and Business Leasing

Probably the largest financial losses by the Regional Bells have been in one of their early investment areas, financial leasing and real estate, as well as other non-telecommunications markets, such as computer services.

Below are the words of the Bells as stated in the annual reports. Across the board, the Regional Bells have lost billions in these areas, and by the early 1990's have all exited the markets, or were on their way.

Each quote shows hundreds of millions of dollars in losses.

US West (195)

> "Weakness in the commercial real estate market persists and disposition of the real estate assets has proceeded at a slower pace than originally planned. The company's current plan is to dispose of its real estate portfolio over the next several years. The Company may hold real estate assets longer than originally anticipated in order to realize book values. 1992

> "The company's 1991 operating results reflect a pretax restructuring charge of **$915 [million]** due to workforce reductions, **projected losses associated with exiting the real estate business and the write-off of certain intangible assets. <u>The portion of the change related to a valuation</u>**

> **allowance for real estate operations was $500 [million] and was intended to cover both carrying costs and losses on disposal of the properties. Real estate revenues of $214.2 [million] less operating costs of $212.8 [million] and interest of $98.9 [million] were charged to the valuation allowance during 1992. The balance of the real estate valuation allowance at December 31, 1992 approximates $402 [million]."**

The US West 1993 Annual Report showed an additional $120 million shown as Real Estate charge in the companies restructuring charges.

Bell Atlantic: (196)

Dealing with computer leasing business, Bell Atlantic states in its 1991 Annual Report:

> "These write downs, which totaled $164 million, were made primarily to recognize competitive changes in both the lease financing and computer maintenance industries."

NYNEX: (197)

NYNEX took big hits on both its real estate and computer businesses. For example, the 1990 results include a pretax charge of approximately $305 million for organizational restructuring in NYNEX's software and systems business, reported in "Other Diversified Operating Expenses." In their 1991 annual report we find that exiting the real estate business, the company took an additional $278 million dollar charge.

> "An additional pretax charge of approximately $278 million was recorded in 1991 primarily for business restructuring. NYNEX has commenced its plans to exit the real estate development and management business and streamline other operating primarily related to Other Diversified operations."

Pacific Telesis 1991 Annual Report (198)

> "Discontinued Operations: Revenues as well as expenses were affected by our decisions in 1990 to discontinue certain operations. Pact Tel Business systems, a wholly owned subsidiary of Pac Tel, ceased operations when we sold most of its assets in first quarter 1991. Additionally, we now charge the results of our real estate subsidiary, Pac Tel Properties, to a reserve set up in 1990. <u>These two events combined to decrease 1991 revenues and expenses by $110 million and $207 million respectively,</u> when compared to 1990, the effect of various one time customer refunds totaling $279 million in 1989."

Pacific Telesis Third Quarter Results, 1993: (199)

> "During first quarter 1993, the corporation recorded pre-tax restructuring charges totaling $418 million. These charges primarily reflect an additional reserve of $347 to **cover potential future losses on sales and estimated operating losses resulting from the corporation's decision to dispose of the real estate portfolio of its real estate subsidiary over the next three to five years.** During 1992, the corporation decided to defer disposing of these properties pending a reevaluation of investment alternatives resulting to its 1990 decision to dispose of these assets. The reevaluation was completed during the first quarter 1993."

The Bell's International Holdings

- NNI estimates that by 1997 the Regional Bells had spent $27 billion overseas and will continue to spend approximately $4.5 billion annually. To date, counting expenditures on acquisitions, foreign investment has been and will remain for the next few years, mostly unprofitable.

Examining annual reports we find that one of the primary uses for the Local Operating Company profits has been the purchasing of a percentage of foreign telecommunications, such as telephone, cable, or cellular firms from Czechoslovakia and Russia to New Zealand and the Pacific Rim. NYNEX, for example, has offices in Hong Kong, Singapore, Geneva, Frankfurt, and London; BellSouth has over 2,000 employees overseas; and Bell Atlantic has over 700 employees in 51 offices, representing 10 nations, while Ameritech states it offers services in 40 countries. (200)

In examining international investments, the only useful analysis is to examine expenditures, the money the companies paid for their overseas holdings. This is because overall, there have been spotty, if any, revenues and many of the deals are partnerships and joint ventures, obscuring the actual details Also, while some quick profits have been made when the foreign government telephone system goes public, most of these investments are quite risky, especially in areas where the economy is slow and current telecommunications is non-existent. For example, the RBOCs have entered cellular businesses in many eastern European and Russian areas, such as St. Petersburg and Czech Republics, Hungary and Poland, where the basic infrastructure isn't in place to deliver service.

Some examples, while profitable, make NNI wonder why the companies have been allowed to spend more on their foreign customers instead of the core business. For example, Bell Atlantic and Ameritech spent $2.4 billion in 1991 for a percentage of the telephone company in New Zealand. New Zealand has a population of 3.4 million, with approximately 1.5 million business and consumer subscribers total (and multiple-millions of sheep). The average expenditure comes to $1,850 per subscriber. (201)

Foreign investments also bring up another sore point from the consumer perspective. Why have the Regional Bells been allowed to spend overseas, when they did not complete their info highway plans? This point will be restated in detail in future sections.

Internationally, the amounts spent and the amounts returned are both hard to track. For example Air Touch, a spin-off from Pacific Telesis's of cellular and overseas properties, has a very varied collection of properties around the world, with varying percentages of ownership.

The next exhibit highlight's some of AirTouch's holdings, (202) highlighted the first column, followed by the number of total service users, as well as total potential subscribers. So, in Germany, AirTouch has operation(s) which represents about a third, 34.8%, of some company. This service has 2.3 million subscribers with a potential of 81 million. Then there is Poland, where AirTouch owns 19% of some entity and it had, to date, 50 subscribers, but a potential of 38.9 million users.

(From the subscriber perspective, the main concern to all Californians should be that Air Touch's properties were funded through the local monopoly, Pac Bell — and even though subscribers were given $60 million dollars when the company was spun off, the assets alone were worth $7 billion in investments.)

Exhibit 30

Air Touch International Cellular Businesses, 1996

		AirTouch Interest (percentage)	Subscribers (in thousands)	Population (in millions)
European Operations:				
	Germany	34.8%	2,313	81.5
	Portugal	50.9%	331	10.5
	Sweden	51.1%	281	8.9
	Belgium	25.0%	410	10.1
	Spain	16.7%	652	39.3
	Italy	15.5%	713	57.5
	Poland	19.3%	50	38.9
	Romania*	10.0%	-	22.7
Asian Operations:				
	Tokyo	15.0%		42.2
	Kansai	13.0%		20.6
	Tokai	13.0%		14.4
	Digital TU-KA Co	4.5%	532.0	46.3
	South Korea	10.7%	290.0	45.3
India	Madras	20.0%	11.0	6.7
	Madhya Pradesh	49.0%	**	72.7

But these are just a few of the Air Touch holdings. Air Touch also has domestic paging in 178 markets, satellite services around the world with Globalstar, A partnership equally owned by the AirTouch/U S WEST venture and Bell Atlantic/NYNEX Mobile titled **Primco Personal Communications** and even **CMT PARTNERS** an equal cellular partnership with AT&T in San Francisco and Kansas City. (203)

- **Domestic Paging:** 178 markets throughout the U.S., including 48 of the top 50 MSAs. Markets include Atlanta, Boston, Chicago, Dallas, Denver, Detroit, Houston, Los Angeles, Miami, New York, Philadelphia, Phoenix, San Diego, San Francisco, Seattle, St. Louis, Tampa/St. Petersburg, and Washington, D.C.
- **Satellite Services:** A partner in Globalstar, with service provider rights in Austria, Belgium, Canada, the Caribbean, Indonesia, Japan, Malaysia, Mexico, the Netherlands, Portugal, Switzerland, and the U.S.
- **AirTouch/US West Joint Venture:** A joint venture that will combine AirTouch's and U S West's domestic cellular assets.
- **Primco Personal Communications** A partnership equally owned by the AirTouch/U S WEST venture and Bell Atlantic/NYNEX Mobile. PrimeCo owns licenses covering nearly 60 million people in 11 markets: Chicago, Dallas, Tampa, Houston, Miami, New Orleans, Milwaukee, Richmond, San Antonio, Jacksonville, and Honolulu.
- **Tomcom:** A partnership owned by AirTouch/U S WEST and Bell Atlantic/NYNEX Mobile formed to develop technical standards for the partners' cellular and PCS services, create a joint marketing and distribution strategy, and implement joint purchasing agreements.
- **CMT PARTNERS:** Equal cellular partnership with AT&T in the San Francisco Bay Area, Dallas and Kansas City.

Here's some of the other RBOC's International holdings.

Bell Atlantic 1995 Annual Report (204)

> • "Omnitel Pronto Italia, Bell Atlantic's consortium operating the second wireless license in Italy, achieved world-record subscriber growth in its first 10 months of commercial operations, signing up more than 560,000 customers to its digital GSM (global system for mobile) service.
>
> • "EuroTel, Bell Atlantic's partnership currently serving more than 100,000 customers in the Czech Republic and Slovakia, has acquired

> 30,000 customers since the inauguration of its digital GSM service in the Czech Republic."

SBC International Operations, 4th Quarter, 1996, Press Release (205)

> "In addition to its United States businesses, SBC has international investments in Mexico, France, South Africa, Chile, South Korea, the United Kingdom and Australia, and is involved in every part of the industry: local service, domestic and international long distance, wireless, video and directory publishing.
>
> • "During 1996, our international ventures made significant progress," Whitacre said. "In France, after building a high quality, nationwide cellular network last year, SFR focused on customer growth and expansion of its distribution channels.
>
> • "The Chilean telecommunications market continues to be dynamic. VTR is now poised to roll-out telephone service through its cable operations, and the VTR/CTC wireless partnership achieved strong growth, with subscribers up 21.8 percent since the merger in June 1996.
>
> • "We remain quite positive about the telecommunications opportunities for Telmex in Mexico, and we believe Telmex is well prepared, both operationally and financially, for increased competition in that growing marketplace," he said. "We are also encouraged by the signs of economic recovery in Mexico."

Even with glowing reports, it is hard to examine International investments for profitability, at least based on information supplied in Annual Reports. For example, NYNEX included its discussion of a new International company which shows numerous operators, each with varying amount of investment.

NYNEX 10Q, 3rd Quarter, 1996 (206)

> "On October 22, 1996 Cable & Wireless plc, NYNEX and Bell Canada International Inc. announced an agreement, to form a new company, Cable & Wireless Communications ("C&W Communications"), to merge the

> operations, and ultimately hold 100 percent ownership, of their United Kingdom subsidiaries and affiliates: Mercury Communications Limited, NYNEX Cablecomms Group PLC and NYNEX Cablecomms Group, Inc., Bell Cablemedia plc and Videotron Holdings Plc. Upon completion of all transactions, which are subject to certain pre-conditions, NYNEX will own 18.5 percent of the fully diluted share capital of C&W Communications."

Sometimes profitability is discussed somewhat obtusely. For example BellSouth states that it lost approximately $100 million dollars over two years based on different losses, some of them in Germany and Denmark.

Bell South 1995 Annual Report (207)

> "The amounts of equity in losses of unconsolidated affiliates were ($65 million) for the nine-month periods ending September 30, 1996 compared to ($46 million) for the same period in 1995. The increased equity in losses of unconsolidated affiliates in the nine-month period was attributable to certain international businesses, principally operations in Germany and Denmark, partially offset by improved results from unconsolidated domestic cellular operations."

One other important point about RBOC purchases, especially in international dealings — most of these new announced ventures are not geared to increasing the core businesses, but are 'sexy investments' allowing the company to offer service overseas, with no care to their local customers.

Chapter 12 Hollywood Calling

In the movie "My Fellow Americans", Jack Lemmon and James Garner portray two former presidents. Lemmon asks Garner "Who did you like meeting the most as president?" James Garner answers "Gorbachev". Lemmon says "I mean really like?" and Garner answers "Ella Fitzgerald".

In truth, while the Bells sold the Highway as a justification for schools and government needs, in the 1990's the Bell's became "Star Struck", trying desperately to change their personas from a stodgy old utility to flashy Entertainment and Information companies, even offering cable services.

With the promises of the laying fiber-optics, all of the companies also pursued becoming a major provider of interactive content on their new networks, competing with the likes of Time Warner. However, the Bells have had dismal failures in almost all of their Interactive investments.

Simba Research, in its 1996 report "Telco's in Interactive Services", put it this way: (208)

> "The telcos have had virtually no success with the interactive information, transaction and entertainment services that have developed and been brought to market. Through their failures they have shown that they are not in tune with the information and entertainment needs of their customers.
>
> "Part of the reason the telcos have so many problems with interactive TV services is that they are reaching beyond their technological expertise and local advertiser relationships. They are trying to develop services that use extremely costly technology and court national advertisers and merchants. The telcos, in particular the RBOCs, simply lack the experience in these areas. As a result, they're had difficulty creating effective broadband transaction services
>
> "Another obstacle for the interactive television has been a lack of consumer acceptance. Consumers have not shown an interest in using interactive TV shopping services, much less paying for these services."

Depending on how you count, the Interactive/media investments have been numerous. They fall into two major areas: Entertainment Programming companies, and purchasing cable services.

Entertainment Failures — Tele-TV and Americast

Two primary new companies created by the Bells, Tele-TV and Americast, were formed to supply new interactive content. With investments of almost $1 billion dollars, their failures to produce have been a clear sign of the Bell's inability to deliver on interactive services. (209)

These two companies' partners include 6 of the seven Bells. Tele-TV was announced in October 94 and consists of three partners: Bell Atlantic, NYNEX and Pacific Telesis. Americast, created to rival Tele-TV, was created in April 95, and consists of Ameritech, Bell South and SBC Communications. as well as Disney and GTE.

EXHIBIT 31
The RBOC's Tele-TV and Americast Partners

Tele-TV	•	Bell Atlantic
	•	NYNEX
	•	Pacific Telesis
Americast	•	Ameritech
	•	Bell South
	•	Walt Disney
	•	GTE
	•	SBC Communication

And these companies started just like a Hollywood movie. According to "Ovitz", the biography of super-agent Michael Ovitz, (210) it was a meeting in early 1993, between Ivan Seidenberg, CEO of NYNEX and Ovitz that got the ball rolling. At the time Ovitz was president of CAA, one of the premier talent agencies. Soon he was flashing movie stars and personalities at the Bellhead, from Michael Crichton and Ivan Reitman, to Aaron Spelling and Warren Beatty. According to "Ovitz", the book: (211)

> "Planning came to a peak in October 1994 when Ovitz and the Baby Bells announced that CAA and the phone companies would be entering into a joint venture with the NYNEX Corporation,. Bell Atlantic and Pacific Telesis to buy or invest in programs that the existing Hollywood studio would turn out.
>
> "We'll bring technology to the home, but you'll have a twenty five inch pipe instead of a two inch pipe," stated Mike Ovitz.

Only months after the deal went through, Ovitz left CAA for a brief stint as the president of Walt Disney, which was the beginning of the end for TELE-TV. However, Ovitz walked away with a reported $50 million dollars. (211)

TELE-TV, now defunct, also employed a number of people from the broadcast industry with impressive credentials including Howard Stringer, a former president of CBS Broadcasting and Sandy Grushow, former president of Fox Broadcasting. At its peak in 1996, Tele-TV had 200 employees

Americast, is still alive, though limping. Headed by non-Bell Steve Weisswasser as president, a former president of a multimedia division at Capital Cities/ABC, and even the fact that this group had Disney Televentures, a unit within Walt Disney Television and Telecommunications, as one of the partners, it wasn't enough to make the company work.

According to a New York Times article, (213) Americast plans have been severely scaled back from its heyday in 1996, when the company had about 100 employees.

> "Americast has shut down two divisions, laid off more than a dozen of its 100 employees, and throttled back its ambitions to develop futuristic television service for its five telephone company backers. "

According to an article in Electronic Media, (214) the company has closed its programming business because interactive programming is unobtainable today.

> "The move is seen as a realization of the fact that true interactive programming is still but a gleam in the eye of modern pioneers."

Some believe that these investments were actually just a strategy to keep the cable industry in its place. (215) The New York Times stated:

> "Americast and Tele-TV were deterrents to keep the cable industry out of the phone business, said Michael J Wolf, a partner in the media practice at Booz, Allen & Hamilton. "When the cable companies decided not to get into that business, the phone companies didn't care anymore. "

Others believe that it was a shifting priorities that was the downfall of these companies. (216)

> "Problems crept into the venture from the start. One of Americast's phone company backers, SBC, announced it was no longer interested in the television business. And some of the other phone companies delayed their plans to offer video services so they could concentrate on other businesses, like long distance. "

Whatever the reason it is clear that the Bells no longer have intentions of delivering the full-motion interactive video that they had promised.

Cable and Entertainment Investments

Other Bell investments in the entertainment business have also been huge, with over $16 billion dollars in the last five years. Below is just a sample of the larger investments.(217)

EXHIBIT 32

Bell Cable and Entertainment Investments

NYNEX	Viacom International	$ 1.2	billion (1993)
US West Cable	Continental	$10.8	billion (3/96)
	Time Warner	$ 2.5	billion (5/93)
	Wometo Cable/ Georgia	$ 1.2	billion (12/94)
SBC	Hauser Cable Properties	$ .6	billion (1/94)

Chapter 13 Liar, Liar — Baby Bell's Pants on Fire

> "The story began like a thriller novel. On October 17th, 1974, T. O. Gravitt, fifty-one year old vice-president of Southwestern Bell Telephone Company, with responsibility for all operations in Texas—a swashbuckling, private-plane-piloting executive who, at the time, was under investigation by Southwestern Bell on suspicion of having misappropriated company funds for his private use—committed suicide by inhaling automobile exhaust fumes in the garage of his home in Dallas. He left a suicide note and various memoranda accusing the company of a litany of mis-deeds, among them the making of political payoffs from a slush fund maintained for that purpose, the illegal tapping of telephone wires, the misuse of company funds, and—most serious of all from the public point of view—the securing of high telephone rates in Texas by providing regulators with false or misleading information.
>
> The suicide note ended, "Watergate is a gnat compared to the Bell System". (218)

Isn't is a shame we can't simply make a wish, like in the Jim Carey movie, "Liar, Liar", and know if the Bells' statements are truthful? One of the primary reasons we are requesting Congressional investigations into many of the Bell activities, including the Bell mergers, the roll-out of the fiber-optic I-Way, and more recently ISDN, is because there has been a documented pattern of misleading, if not down-right deceitful behavior by the Bells, in everything from their promises of technology deployment to their state and federal filings.

But don't take our word for it. Let's start with three quotes — one from Senator Hollings, former Senate Commerce Committee Chairman, one from Judge Frank Robinson, NY State Administrative Law Judge, and Ashley Brown, former Ohio Public Utilities Commissioner.

Quote 1:

"The Bell Companies engage in a political onslaught of misrepresentation and outright fraud". From Senate Commerce Committee Chairman Ernest Holling's letter to Senate Majority Leader George Michell. (219)

Quote 2:

"...the Information Providers (IPs) (companies that provide content on the local, mass-announcement 976 Services) were harmed by the improper, deceitful and grossly negligent way in which New York Telephone provided service to them." Administrative Law Judge Frank Robinson 2/96. (220)

Quote 3:

"When Ohio Bell became part of the Ameritech Corporation, the company executives became less and less trustworthy. They began to use power in ugly ways. They became less and less concerned with local concerns and more and more interested in corporate mucky-mucks in Chicago. Sometimes they were just flat-out dishonest." Ashley Brown, former Ohio Public Utilities Commissioner. (221)

Technology Spending and Deployment

Throughout this book we have shown over and over again that the Bells announced technology deployment plans were virtually never implemented, and statements made in Bell annual reports have been closer to campaign promises than promised business initiatives.

Remember these promises of InfoHighway deployment, none of which were ever rolled out?:

US West, 1993 Annual Report (222)

In 1993 the company announced its intentions to build a 'broadband', interactive telecommunications network...<u>US West anticipates converting 100,000 access lines to this technology by the end of 1994, and 500,000 access lines annually beginning in 1995.</u> [Emphasis added]

NYNEX, 1993 Annual Report (223)

> We're prepared to install between 1.5 and 2 million fiber-optic lines through 1996 to begin building our portion of the Information Superhighway. [Emphasis added]

Truth in advertising? Jonathan L. Petersen, a former government financial analyst, says it's all in the fine print when discussing corporate plans. (224)

> "It's all in the fine print. In reading Ameritech's "Opportunity Indiana", their fiber-optic deployment plan, it is obvious that the company is playing with the meaning of the words. For example, the company states it will spend up to $180 million in network upgrades — "up to" is the top limit and the company can spend whatever it likes below that figure— $2 bucks if it likes. Similarly, the promises of the I-Way construction had numerous "conditional" words, such as "prepared to install" (NYNEX quote), which means that if plans change... "we were prepared, we just didn't do it."
>
> "Is it lying? Well it is misleading in terms of meaning, but it's probably legal. "

And this pattern of misleading the public by rewriting the news hasn't stopped one bit. For example, a press release from SBC Communications, 4/1/97, touting their purchase of Pacific Telesis, stated that Philip Quigley "...led Pac Tel's comprehensive $16 billion network design program". (225) So what if that program was never implemented and the $16 billion dollar figure was only window dressing, not actual spending.

And the promises of ISDN deployment go back even farther — and were also never delivered upon.

Ameritech **1991** Annual Report (226)

> (Illinois Bell's Bill Kallmyer, senior marketing operations manager) says ISDN is available to single-line customers as well as larger firms.

In short, a large amount of technology "promises", have been nothing more than words without any basis in fact.

The Mergers

NYNEX and Bell Atlantic promoted their merger as a 'merger of equals', but instead, Bell Atlantic purchased NYNEX, just like SBC purchased Pac Bell. And NYNEX shareholders got only 77¢ on the dollar — so much for equals. (227)

> "On July 2, 1996, NYNEX and Bell Atlantic Corporation ("Bell Atlantic") executed an amendment to their definitive merger agreement (the "Merger"), effecting a technical change in the transaction structure of <u>the merger of equals</u> announced on April 22, 1996. As amended, the agreement provides that a newly formed subsidiary of Bell Atlantic will merge with and into NYNEX, thereby making NYNEX a wholly owned subsidiary of Bell Atlantic. There is no change in the fundamental elements of the proposed Merger. The exchange ratio for shares is restated to reflect the difference in the transaction. <u>Each NYNEX shareholder will receive 0.768 shares of Bell Atlantic common stock in exchange for one share of NYNEX common stock</u>." [emphasis added] (

The reason for this purchase agreement is simple. This tactic side-stepped required Congressional hearings and approval, as well as placed limits on the states' regulatory involvement.

Pacific Telesis also called it's arrangement a "merger". "Pacific Telesis announced a plan on April 1, 1996 to merge with SBC Communications Inc.." However, the fine print shows that it was a buy-out agreement with Pac Bell shareholders receiving only 73¢ a share. (228)

> "On April 1, 1996, SBC Communications Inc. ("SBC") and the Corporation jointly announced a definitive agreement whereby the Corporation will become a <u>wholly-owned subsidiary of SBC.</u> Under terms of the merger agreement, each share of Pacific Telesis common stock will be exchanged for 0.733 shares of SBC common stock, subject to

> adjustment. On July 31, 1996, the shareowners of the Corporation and SBC approved the transaction, which previously had been approved by the respective Board of Directors of each company. Pursuant to the merger agreement, the Corporation's quarterly dividend per share cannot exceed 0.733 of SBC's quarterly dividend per share."

And just how often do the Bell's make statements that are either misleading or untruthful? Well, other 1997 events would make it appear that it is business as usual. For example, New York State Attorneys General Office asked the New York State Public Service Commission to stop the merger between NYNEX and Bell Atlantic because of untruthful statements. According to the Wall Street Journal, (2/6/97) (229)

> "Attorney General Dennis Vacco said in the brief (to the PSC) that evidence obtained during his office's investigation indicated that Bell Atlantic had 'considered' entering the New York City market as a competitor to NYNEX. <u>That conclusion directly contradicted repeated assertions by Bell Atlantic to federal and state regulators that it never intended to enter the New York market."</u> [emphasis added]

In another case, the FCC rejected Ameritech's bid to enter the long distance market anytime soon because they submitted false documents. According to the Wall Street Journal, 2/10/97 (230)

> "On two separate occasions in the past month, the Chicago-based Bell asserted in its service application to the FCC that it had reached a state-approved pacts to allow AT&T Corp. access to Ameritech's local network in Michigan—<u>assertions the agency later deemed untrue</u>." [emphasis added]

However, there are actual scandals today, especially dealing with Information Providers (IP) and Internet Service Providers (ISP). Because the phone companies have drastically cut staff, those few remaining are having to do more and more work. Unfortunately, these employees are left with a serious problem: How do you service the customers when there aren't enough people, or in some cases deploy technology to actually fulfill the required service provision?

Here's a recent, yet dramatic story which has taken seven years to unfold. It involves NYNEX staff stealing documents, fudging numbers, a whistle blower who was fired, and even out and out deceit on the part of NYNEX, and even its lawyers — a very dark side of NYNEX's business practices. We also found that the rollout and implementation of ISDN and Internet provision to service providers have hauntingly similar problems, from inadequate staff and expertise, to the company not being able to deliver on advertised products and promises made.

The NYNEX Information Provider Info-Scandal

NOTE: The source for this story is from direct court testimony and findings. (231)

On February 17, 1997, Administrative Law Judge Frank Robinson found that:

> "New York Telephone Company has been guilty of gross negligence and willful misconduct.
>
> "...the Information Providers (IPs) (companies that provide content on the local, mass-announcement 976 Services) were harmed by the improper, deceitful and grossly negligent way in which New York Telephone provided service to them."
>
> "Furthermore, the company engaged in willful misconduct in striving to cover up its negligence and to defeat efforts to call it to account. This extended to willful misconduct in the company's litigation of this proceeding."

Judge Robinson recommended that the Public Service Commission award the companies over $25 million dollars.

Background

Numerous Information Providers (IP) provide content on the NYNEX local Mass Announcement 976 Services. This includes everything from weather forecasts, such as 976-1212, to sports information and lottery results. These services garner millions of calls annually, and the billing is performed by NYNEX, who has a total monopoly on these local services.

During September 1990, NYNEX replaced their old, faulty network switch, which gave false accounts of the amount of calls, among other problems, and 'cutover' a newer model designed by Erricson, an equipment manufacturer. Unfortunately, the Court found that the company did not have adequate expertise nor staff to use this equipment properly, and the new equipment greatly undercounted and even blocked calls.

The Court wrote of testimony from one of the Information Providers: (232)

> "Witness Fogel, president of Phone Programs Inc., summed up the picture of alleged gross negligence in connection with the cutover thusly: haphazard planning without managerial oversight; insufficient attention to detail as to differences between Autrax (the old switch) and Ericsson (the new equipment); sloppy field work at end-offices; little or no training for the technicians and field personnel as to quality control or troubleshooting; and misleading and infrequent communication with IPs, the customers. "

The IPs initiated a court case and one conscientious employee, Mr. Lobsco, complained to superiors and even kept a log of the problems, titled "Memo to Self". In September, 1995 he wrote: (233)

> "I have come to believe that the Company and Ericsson are aware, and have always been aware, of systematic problems, either in the network or the IMAS [Ericsson Switch] itself. Every opportunity I had to articulate my concerns fell on deaf ears. As far as Ericsson goes, they have been aware of the software problems plaguing the statistical package and the broadcast feature, from the outset, and have been unable to resolve them to this day. "

He was summarily fired during the case because he would testify against the lawyers and upper management, who told him to not reveal the full problems to his customers, the IPs. In fact the Court wrote: (234)

> "In contrast to the odor of dishonesty in the previous company testimony in which he participated, Mr. Lobosco's September testimony has the ring of candor."

Others at the company also knew of these problems long ago. For example, the Court wrote: (235)

> "As evidence of the company's alleged duplicity and cover-up, the IPs also quote extensively from a December 28, 1990 memorandum from Kingsley Nelson (a mid-level company executive with supervisory responsibility for 976). The IPs say that while the company was publicly telling them that all was well with Ericsson, and minor problems had been corrected, the Nelson memorandum indicates that significant call volume data problems were still being experienced, with the software in question prone to failure fairly frequently. The memo labels these problems 'intolerable', and notes that the company cannot withstand an audit given its lack of actual call counts. "

One employee, a Mr. Cerar, even took home incriminating files, memos and letters so that the company's records couldn't be adequately investigated. The Court wrote: (236)

> "The company, even while producing great volumes of material, to which it can point as supposedly proving its good faith, <u>has hidden, lost, and destroyed reams of evidence, and doggedly deflected legitimate information requests."</u> [emphasis added]
>
> "The IPs assert that Mr. Cerar lied when testifying that he never took home documents... They add that Mr. Lobosco also made reference to a "cache" of documents which Mr. Cerar allegedly said he took home and would not bring forth if they were adverse to the company. The IPs urge a finding that Mr. Cesar purposely secreted or destroyed relevant documents. "

In short, NYNEX was not only unable to provide a working service, but then tried to cover-up the problems by losing files and data and firing the star witness. As Judge Robinson concluded: (237)

> "Furthermore, the company engaged in willful misconduct in striving to cover up its negligence and to defeat efforts to call it to account. This extended to willful misconduct in the company's litigation of this proceeding.
>
> "I also conclude that the IPs were in fact harmed by the improper, deceitful and grossly negligent way in which New York Telephone provided service to them."

Conclusion:

As previously mentioned, we believe that all of the filed Info Highway plans should be re-examined for failure to deliver on promised products and service deployment, i.e., the rollout of the I-Way. Also, based on interviews with various ISPs and other 'new media' experts around the country who have had long battles with the local telco in trying to obtain and maintain ISDN, the states should also investigate the promises made for the deployment of ISDN, and whether the phone companies ever spent the monies required for implementation of these services, including everything from adequate facilities to staff with the proper expertise. Finally, Congress should also investigate the Mergers of the Bells.

Coda: How common are these actual cases of deceit? The Wall Street Journal ran an article, 3/15/97, with the headline "GTE Studied for Allege Destroying or Withholding Data in Billing Probe". The article goes on to say that: (238)

> "GTE Management instructed employees to shred documents that were subject to a prior investigation into fraudulent billing practices at the company."

Therefore, all investigation of the Bells should also include all local telcos, especially GTE.