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20 April 1950

Dr. Stewart and members of the Presidential Communications Policy Board: My name is John O'Gara, I am Deputy Assistant Secretary of State for Economic Affairs and I am appearing before you today to present to the Board the State Department's views on the question of a merger of international record communication carriers, which views were requested in the Board's letter to the Under Secretary of State, dated March 13, 1950. Accompanying me are Mr. Francis Colt de Wolf, Chief of the Telecommunications Policy Staff, and Mr. T. H. E. Nesbitt, Assistant Chief of the Telecommunications Policy Staff.

As the Board is undoubtedly aware, the problem of a possible merger of United Stated international communication carriers has been more or less a current one ever since the domestic merger of Western Union and the Postal Telegraph Company took place in 1943. Within the government and particularly within the State Department, there have been varying and mixed feelings as to whether or not there should be such a merger and if so, what kind and under what conditions.

In 1944 the then Assistant Secretary of State Adolf Berle informally communicated his views to Senator McFarland on the subject of merger and I am informed that at that time Assistant Secretary Berle advocated that legislation be enacted which would allow permissive merger of record companies, excluding the Telephone Company. On April 3, 1945, Assistant Secretary of State Will Clayton, who succeeded Mr. Berle, in testimony before a subcommittee of the Senate Interstate and Foreign Relations Committee espoused the sound conviction that monopoly is prejudicial to the withdrawal of uneconomic facilities and to the liquidation of unprofitable companies. He held that this resulted therefore in higher rates contrary to the public interests. Mr. Clayton declared more expressly "... no showing has yet been made that mergers among competing companies is the means best calculated to protect the general welfare of the people" and that, therefore, "complete merger into one company of our telecommunications facilities, on the basis of our experience to date and evidence at hand, is inadvisable".

The Department agrees today with this expression of general basic policy and would oppose with equal firmness a merger of all telecommunications facilities. However, in light of changed conditions today, with different effect on the three separate services in this general field - record companies, telephone, and air mail - and if given continued strong regulatory supervision, a merger of record companies only (if appropriate) is deemed not necessarily violative of this philosophy.

In view of the Board's present inquiry, the Department has reviewed the position formerly set forth by Mr. Will Clayton.

Although the Department does not have detailed financial and traffic data immediately at its disposal, the data which it has been able to accumulate and information it has obtained at public hearings before the Federal Communications Commission in Docket 8230 indicate that the record companies are in a far different position today than they were when Mr. Clayton testified before the Congressional Committee. Traffic volumes have decreased considerably from their wartime peaks and revenues have shrunken. Trade declines with

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Iron Curtain countries; trade barriers arising out of export controls and increased telephone and air mail competition have in no small measure brought about this condition. Representatives of the record communication companies have expressed their concern to the Department of State on the present unsatisfactory situation in their industry and have also made known their feelings on the subject to Senator McFarland. The telephone industry is not concerned over its own situation as it feels that its operation is on a sound basis.

In assessing the Department's primary interests in a merger of the international record companies, it appears that they are three-fold and are:

(a) The effect of a merger on the transmission of the Department's communications.

(b) The relationship of a merger to the Department's communication policy.

(c) The compatibility of such a merger with the Department's international trade policy.

With reference to point (a) "The effect of a merger on the transmission of the Department's communications", of vital interest to the Department is the rapid flow of its own communications to all parts of the world. We are informed that the Department is the largest single user of international commercial record communications in the United States. The Division of Communications of the Department which is charged with the dual responsibility of expediting the Department's communications and also paying the telegraph bills, feels that a consolidation or an appropriate merger of the record companies should produce a number of economics of operation, thus offering a measure of relief from successive rounds of rate increases. From the operating and transmission viewpoint, the Departmental communicators feel that the present diversity of operating methods would, to a large degree, disappear. Existing at present are substantial differences in methods and procedures which create an effective barrier to the efficient exchange of traffic at the gateway points. There may be regulatory measures which would provide alleviation of these unsatisfactory conditions. If so, a more thorough-going study than the Department can undertake would possibly be persuasive. Special arrangements to meet the needs of the Department of State or other federal agencies would require negotiation with only the single operating company in contrast with the present multilateral negotiations.

It is generally agreed that commonly technological improvements are stimulated by sharp competition; however, there is a real limit to this influence in the face of operating loss conditions.

A vitally important interest within the Department (point b) is reflected in its over-all telecommunications policy. The Department has long felt that the maintenance of an economically sound international record communication system capable of providing a good service at reasonable rates, by the use of radio and/or cable to as many places in the world as is economically practicable and politically desirable, is vital to the national interest. In furtherance of that policy the Department has encouraged the establishment of direct radio circuits for economic and political reasons which include the desire to aid business and promote better relations with foreign countries. In advocating the establishment of direct circuits, the Department has not lost sight of the increasing importance to the national interest of existing cable facilities. During periods of atmospheric and political disturbances, the cables have proven their worth. The security value of a well-rounded cable and radio system is of great importance to this country, particularly in times of war. This is a peculiarly important point as to cables in view of probably technological advances in the field of radio jamming. Seemingly, the present unprofitable situation, particularly in certain parts of the cable industry, constitutes a threat to the extensive circuits which we desire under this policy. A continuation of the present condition may lead to a curtailment of the present services or to costly subsidies either direct or in the nature of higher rates.

Our telecommunications policy is best served by an extensive facilities coverage. Protection for such coverage is essential and the problem seems to be whether such protection is best secured through appropriate merger, reorganization of unprofitable companies or other means. Present conditions in the industry are generally unsatisfactory and point up the need for constructive change.

With reference to point (c) the United States foreign economic policy is designed to establish and maintain an expanding competitive multilateral trade between countries. To this end, our policy calls for reduction or removal of government barriers to international trade such as quotas and tariffs. It stresses the elimination of private barriers, such as cartel arrangements, and the stimulation of competitive conditions in industry and trade. All of the mechanisms being employed or proposed - e.g., the Reciprocal Trade Agreements program, the ECA, GATT, AND ITO - are uniformly directed to the accomplishment of these aims as rapidly as possible. This policy is predicated upon the basic economic concept that the creation of a large market free of artificial barriers with accompanying competitive conditions encourages increased efficiency, greater production and income, and a higher standard of living.

Clearly this policy stands on its own feet as an expression of a fundamentally desirable position. Our problem here today is to see if there be any substantial offense to it contained in any potential merger in the field of the international record communications companies. It is suggested, and held by us in the Department that such offense does no in fact exist, with the strong competitive factor arising out of air mail and telephone when retained as separate services.

Foreign policy is naturally an extension of domestic policy. This suggests that advantage may well be taken of previous related domestic action as pertinent.

The question does arise as to whether or not the present financial conditions of the carriers indicate that it is a declining industry. The Board may wish to weigh the present financial condition of the carriers in the light of the ever increasing competition of the air mail and telephone with the object in mind of determining whether or not a merger would solve the basic problems of the industry. Further, of course, the financial structure of these companies may well be a significant factor in today's profit results.

The Department is much concerned about this complicated problem; its ramifications extend beyond the area of primary interest to the Department, the field of international relation, into National Defense, domestic, economic and political considerations. The Department does not have the source material nor the personnel to make its own comprehensive study of the situation, and it looks forward, therefore, with keen interest to the results of the study presently being conducted by this Board. The Department would like to maintain a close liaison with the Board and continue to cooperate with it in its study of this problem. The Department sincerely hopes that the Presidential Board will make the necessary recommendations on policies and practices to be followed by the Federal Government with respect to our international communication system.

In order that the work of the Board will be facilitated, the Department has authorized me to state that it will not oppose a permissive merger of the international record companies if the Board finds it to be in the national interest. However, in the event there is legislation which will enable some or all of the companies to merge, the Department feels that the following conditions should be imposed in addition to the normal regulatory authority of the Federal Communications Commission:

(a) Preserve the competitive results obtainable by a complete and continued separation of the telephone from the record services, which with the addition of air mail will provide three strong competing services.

(b) Permit no merger which would jeopardize a well-rounded cable service to as many parts of the world as possible.

(c) Maintain the same or better quality of service as is presently enjoyed.

(d) Maintain direct communications with as many places in the world as is practical and politically desirable.

(e) Require that the prognosticated economics which may be foreseen as a result of merger be effected as rapidly as possible having due and appropriate consideration to the labor problems which may arise, and that those economics be passed on to the users in the form of lower rates and better service having due regard for the modernization of plant and the improvement of the Art.

(f) Assure that a merged company will be capitalized on a basis that will insure long range financial soundness, taking into consideration long term traffic trends, competition, and obsolete and duplicating facilities which should be liquidated.

In closing, the Department desires that upon completion of the Board's work, the interested agencies of the government be given the opportunity to comment upon any specific proposal the Board may make which would enable a merger to be consummated.