Fateful Choices: AT&T in the 1970s

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John deButts became Chairman and CEO of a troubled AT&T in 1972. Earnings were flat, service had deteriorated in New York and other cities, and the FCC was introducing competition into selected areas of telecommunications previously reserved for AT&T by a combination of regulatory and company policies. deButts attacked both the internal and the external problem with vigor. Internally, he set in motion a planning process to replace Vail's 1909 organizational plan under which AT&T and the Bell System still operated in 1972. Externally, he tried to use AT&T's great size to influence public policy toward the company. I will argue that deButts had far better sources of information about the internal operations of his firm than about its political environment. The result was that his internal actions were far more successful than his external. In addition, they also were pursued further.[1]

This paper therefore is an example of the new economic approach to business history outlined last year in a paper by Lamoreaux, Raff, and Temin [1997]. We argued in that paper that business history should focus on choices made by business executives. For choices to be real, there must be viable alternatives, and business history needs to explore what might have been as well as what was. We argued further that the information available to decision makers was a critical element determining the outcome of decisions. Accordingly, it is not enough to outline alternatives; one needs also to envisage how these alternatives looked to the business executives facing them.

I focus on the choices made by deButts and try to understand the motivation behind them. There are two decision points in question. The first came when deButts took office in 1972, as described above. The second came four years later when the effects of deButts' initial actions could be seen. This was the opportunity for a "course correction," with the added information about the effect of the initial changes on AT&T's fortunes. The choice made at this time is the most interesting one.

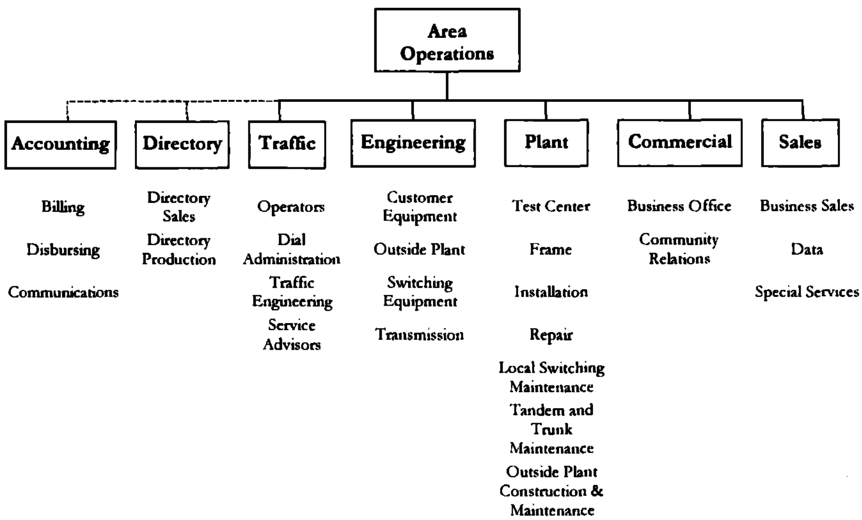
[1] See Temin [1987] for an earlier discussion of this topic and fuller documentation of many of the points made here.

BUSINESS AND ECONOMIC HISTORY, Volume Twenty-seven, no. 1, Fall 1998.
 ISSN 0894-6825.

AT&T's Corporate Planning Organization

Newly installed as AT&T's CEO, deButts called on his staff at AT&T and an external consultant, McKinsey & Co., to initiate the process of structural reform. AT&T's Corporate Planning Organization studied the options and distilled three alternative approaches to reorganizing the Bell System [AT&T Corporate Planning Organization, 1973]. The first option was to keep its traditional functional structure, as shown in Figure 1. This was the organizational structure introduced in 1909 by the legendary Theodore N. Vail. The original Plant, Traffic, and Commercial departments of the 1909 plan had been joined over time by engineering and sales. But those additions had not altered the basic concept of the structure: the departments were organized along skill lines, grouping members of similar crafts together. This organization had worked well as AT&T had grown from a collection of loosely connected local urban telephone companies into the integrated Bell System of the 1970s.

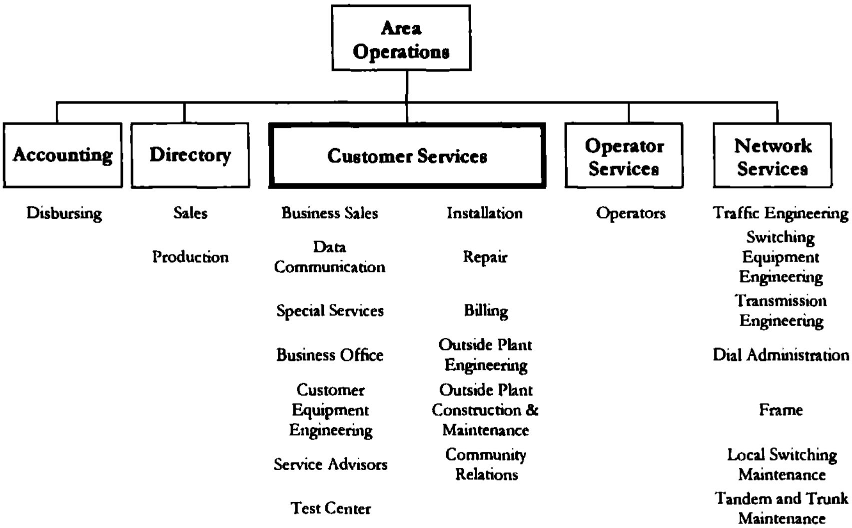
Figure 1: *AT&T Traditional Functional Structure*



Taking its cue from innovations already made by many of the operating companies, the second alternative would reorganize the Bell Operating Companies around work flows rather than craft lines. Restructuring would keep the work on any job within a single department, thus easing the flow of information and commands relevant to the System's traditional activities: responding to customer complaints, servicing and planning for the network, and expanding facilities. The Corporate Planning Organization thought that three departments would be needed to implement this idea, as shown in Figure 2.

Customer Services would contain all those activities relating to terminal equipment and the local loop between a telephone subscriber and a central office. Construction and engineering functions formerly in separate departments would be combined so that the Customer Services Manager would control both the provision of plant and its day-to-day operation. While this department would be in a position to respond quickly to any complaints coming from the local loop, it would not particularly emphasize marketing or give it a new role relative to operations.

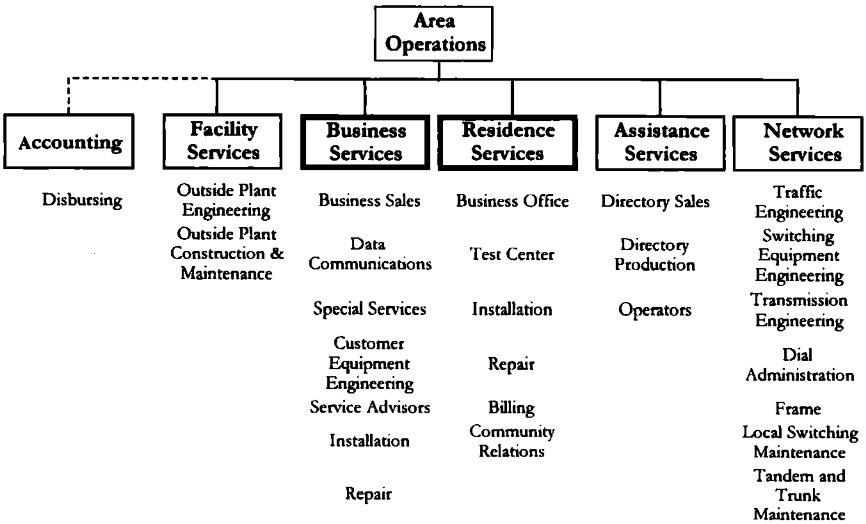
Figure 2: *"Customer Services/Network Services/Operator Services" Structure*



Nor would that be the case in Network Services, which would include activities involving the network between central offices. This department would include network design, engineering, construction, and operation. These functions clearly ranked highest in the Bell System's hierarchy of values. The network mystique was a powerful force, and the network was at this time particularly important to Bell managers in view of the service failures of the late 1960s in New York and elsewhere. Integrating all network planning and operations, it was hoped, would enable the System to avoid such failures by accurately forecasting and providing for demand. Operator Services were all of those activities that involved telephone operators. They could stand on their own because they depended very little on either customer or network services.

The third alternative followed market segmentation lines. It was recommended by AT&T's outside consultants, McKinsey & Co. Labeled the "Competitive Structure," this proposal abandoned the skill orientation of the first alternative and the process orientation of the second in favor of a focus on marketing. It would help AT&T meet competition for business customers, as well as those in the terminal market. The Competitive Structure (shown in Figure 3) shared certain features with the "Customer Services/Network Services/ Operator Services" proposal. But it went much further. Breaking with Bell System tradition, it split customer services into business and residential departments so that all of the sales, installations and repair activities for the increasingly important business customers could be grouped together and coordinated more closely than they had been in the past. The Business Service group would be able to respond swiftly and appropriately to business demand. Similarly, the several activities related to the residential market – including community relations – were combined to provide a total residence customer response under the control of a single manager.

Figure 3: *AT&T "Competitive Structure"*



The alternatives from AT&T's Corporate Planning Organization were like the beds of the three bears discovered by Goldilocks. deButts had indicated clearly by word and deed, most notably by initiating the planning effort, that he wanted to upgrade Bell's marketing and to change the way this function was organized. AT&T was not going to stand pat. The first alternative was too "soft." The choice therefore was between the second and third alternatives, between a middle way and a thorough-going reorganization. But deButts was highly suspicious of the most radical recommendation, the market segmented structure. He had asked in the spring of 1973: "How can we organize ourselves by market segments – the kinds of businesses we are in – without at the same time adopting the motivations of our competitors, thereby facilitating the fragmentation of our responsibilities that our competitors seek and thus jeopardizing the System integrity that has made our business great?" [deButts, 1973]. No one had stepped forward to supply an answer. deButts was determined to promote change in the System, but he was not prepared to renounce Bell's public utility orientation. Indeed, the reaffirmation of that tradition was the central pillar of his program. The third alternative was too "hard."

The three alternatives were presented to the Bell System Operating Company presidents at their semi-annual conference in the fall of 1973, where AT&T's top management's strong preference for the middle alternative was explained [Owens, 1973]. The CS/NS/OS organization, as this structure became known, was introduced after elaborate discussions at all levels of the business. It involved a major reorientation of personnel and the organizational structure of the entire Bell System. It also raised the spirits of the myriad Bell System employees, facilitating the recapturing of Bell's high service standards and the resumption of earnings growth.

The External Challenge

deButts began to deal with the internal challenge posed by the changes of the 1970s by this reorientation of the Bell System, but he needed to deal with the external challenge as well. The challenge came initially from the Federal Communications Commission (FCC). In a series of decisions around 1970, the Commission opened up the areas of terminal equipment and private-line communication to competition. The FCC seemed to be abandoning the concept of AT&T as a public utility, as the steward of the nation's telephone network. The federal courts affirmed the FCC's actions, and other branches of the government assented as well in various ways. The Department of Justice – following the lead of one of AT&T's new competitors (MCI) – filed an antitrust suit against AT&T in the fall of 1974. Like all major antitrust suits, this one took several years to gather speed. But its existence in its early, slow years was a reminder that public policy toward the Bell System was changing, that the innovations introduced by the FCC could result in a redefinition of AT&T's role in the economy.

How should AT&T respond to this external challenge? Opinions among the company's top managers was divided. Mark Garlinghouse, the company's general counsel, wanted to accept the FCC's initiative and work with the Justice Department. Edward Crosland, vice-president for federal relations, wanted to make an end run around the Commission and, presumably, the Justice Department as well. With the proper approach, he reasoned, the System's public utility role would be reaffirmed by Congress. To bolster his position, he reconvened and expanded a panel of outside advisors he had consulted earlier. The panel included such wise old men as Newton Minow, former Chairman of the FCC, and Eugene Rostow, who had served as the chairman of President Johnson's Task Force on Telecommunications in 1968. This panel was the political analogue of McKinsey's organizational advisors.

The political advisors concluded that properly drafted legislation would solve many of the Bell System's policy problems. A favorable bill could be passed by Congress, they said, because of two important "assets" of the Bell System: the System's positive public image, which derived from the excellence of the American phone system, and the separations policy that channeled revenues from long-distance services into support for local service. As a result of separations, the Bell System's interstate rates were subsidizing local operations and keeping local telephone rates low.

However, the advisors continued, separations were widely misunderstood. In particular, while AT&T's long-distance rates were high to support low local charges, the aspiring interstate competitors were free of the obligations to provide universal service and to subsidize local rates. As deButts well knew, when the Bell System tried to meet this interstate competition with lower interstate rates, the competitors and the government objected strenuously. "Confusion and contradiction," said Minow, "thus imperil the nation's communications service." A solution will come only "when national policy makers make a choice between contradictory objectives." The place for them to do so was in Congress, which had passed both the Sherman Antitrust Act and the Federal Communications Act. Rostow concurred.

Minow recommended a two-part strategy. AT&T should first try for Congressional reaffirmation of the need for a unitary telephone network. Failing that, it should push for legislation that would at least put all of the competitors on an equal footing, that is, legislation that would deregulate most of the Bell System's operations. Despite AT&T's strong preference for the first option, the choice would be up to Congress. AT&T would come out ahead if the legislature could be persuaded to make a choice and avoid "the worst of both possible worlds: a combination of rigid regulation and unfair competition" [Crosland, 1975].

deButts, normally receptive to the views of his general counsel, found Crosland's approach more congenial. Direct negotiations with the Justice Department would be avoided because deButts expected AT&T to be fully exonerated in court or to face more sympathetic opponents after the administration changed in Washington. Instead, deButts would present the company's case to Congress. AT&T's leader, like the political advisors, thought that a century of public service would get its just returns on Capitol Hill.

He did not pay much attention to the problems that the largest corporation in the world would be likely to have garnering congressional support or to the opposition that its political activity might arouse. Power in Washington had become more diffuse in the years since World War II as the government grew in size and complexity. This process had accelerated in the "Watergate Congress," elected in 1974 in the wake of the Nixon impeachment hearings. The chairmen of the congressional committees had been forced to surrender some of their power to control committee operations; the various subcommittees, most relevantly the House Subcommittee on Communications, had acquired their own staffs and had become primary loci of power.[2] The legitimacy of all large organizations also was being undermined by inflation, the conduct of the Vietnam War, and Watergate. deButts' Washington experience dated from the 1950s when the government had been very supportive of AT&T in the aftermath of World War II. Spending all his time in the cocoon of the Bell System, he was not sensitive to the new winds blowing through Washington.

The decline in presidential authority, the dispersion of congressional power, and public distrust of large institutions were bound to complicate any

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[2] The Communications and Power Subcommittee of the House Commerce Committee was split in two. Communications went to Torbert MacDonald of Massachusetts, who built a staff led by Harry (Chip) Shooshan. Shooshan's staff was taken over by Lionel Van Deerlin when MacDonald died in 1976, and Van Deerlin became subcommittee chairman. See also Davidson and Oleszek [1977].

legislative campaign AT&T might mount. But Crosland's expert advisors did not stress these political storm clouds; their forecast was for clear skies and a difficult but successful voyage. deButts agreed. He reported to the Bell System Presidents' Conference in November 1975, that the decision to seek specific legislation had been made. The campaign for this bill, deButts said, "may well be the most important public affairs effort we have ever undertaken." This was, he exhorted, "no time to sound retreat but to press every advantage that we have with all the force we can muster. Nineteen seventy-six may well prove the year of decision for our business" [deButts, 1975].

The draft legislation had originated in conversations with the National Association of Regulatory Utility Commissioners (NARUC), and the organization of independent telephone companies (USITA). Independent telephone companies also worked on it with AT&T. Crosland cleared it as well with the Bell System's two big unions, the Communications Workers of America and the International Brotherhood of Electrical Workers. Everyone climbed on board as Crosland walked the bill around the industry, but – despite Crosland's best efforts – it still was known instantly and universally as the Bell Bill.

Its full name was the Consumer Communications Reform Act (CCRA) of 1976. Like a famous 1973 NARUC speech in which deButts "oppose[d] competition, espouse[d] monopoly," the CCRA was designed to provoke discussion [deButts, 1973b]. And like the speech, the bill staked out an extreme position. As a result, it did not seem to be designed for compromise, although – at least in theory – it had been designed to promote it. The bill promised instead to harden the opposing positions. Claiming always to initiate a debate, deButts looked again as if he had tried to end one. The CCRA made it appear in Washington that deButts was digging in, preparing to fight for the principles of his NARUC speech.

The bill was cast as an amendment to the Communications Act of 1934. It reaffirmed the nation's commitment to universal service and went beyond existing law to state that a unified telephone network had been and continued to be essential for the achievement of that goal. The bill bluntly asserted that the existing rate structure, by which it meant primarily separations, had promoted universal service. Competition in interstate services was doubly dysfunctional: the competing carriers duplicated resources, and they imperiled the existing rate structure. The bill would avoid these dangers by setting much stiffer standards for the authorization of new carriers and by approving AT&T's use of incremental, or marginal, cost pricing [U.S. Congress, 1976a].

The Bell Bill would write into law both parts of the contradictory position AT&T had taken before the FCC in the rate cases. While AT&T would be the monopoly supplier of telecommunication services, it would be allowed to price competitively to maintain its monopoly. Consumers would get the benefits of competitive pricing, but competitors would not be encouraged to try to crack the monopoly. Of course, if AT&T's defense of its position was not to imperil the subsidy local operations obtained from interstate service, marginal cost pricing would have to be introduced selectively. The Bell System would have to discriminate in favor of those customers facing competitive suppliers. The CCRA would enhance one goal of the 1934 Act – universal service – at the expense of another – nondiscriminatory pricing [Temin, 1997].

Rather surprisingly, the bill also endorsed the Bell position on terminal equipment. AT&T had argued unsuccessfully before the FCC that the regulation of customer-provided terminal equipment should be left to the state regulatory commissions. One might reasonably claim that the 1934 Act already had left that power with the states, but this contention had been rejected by the FCC (which received the blessing of the courts). The CCRA would draw a jurisdictional line around federal authority, thwarting the FCC and leaving the Bell System in control of end-to-end service in most jurisdictions. This was a vulnerable position to hold in 1976, and a bill designed to foster compromise would have yielded more ground on this point. Some AT&T managers suggested as much to Crosland, but he rejoined that the terminal provisions were needed to get union support of the bill. Neither the workers whose jobs were at stake nor the executives loyal to Vail's ideals had much use for this concession. The Bell Bill, whatever deButts's initial motives, had been drafted to defend the NARUC principles, not to achieve conciliation.

Ill-conceived as a bargaining platform, the CCRA also started its legislative passage under less than auspicious conditions. The measure was introduced late in the 94th Congress, and it would have been truly remarkable if it had passed at that time. Legislation of this magnitude seldom can be passed in a single session of Congress. A comparable bill was introduced in the Senate, and both would have had to pass before Congress adjourned in October.

AT&T apparently anticipated the delay. Its strategy was to gather widespread support for the bills, creating a sense of momentum before pressing for committee hearings, debate, and passage. At first it appeared that this maneuver might work. The House bill collected 175 sponsors and the Senate bill 17 by the time of adjournment. Meanwhile AT&T had launched a formidable public relations campaign to increase grassroots pressure on Congress. Because the Bell System operated in every state, community, and indeed most homes throughout the country, AT&T could generate a considerable amount of political energy. It could reach local political leaders through the Bell Operating Companies, each of which had public relations and public affairs departments that could provide staff support for a broad-based effort of this sort. This network was activated at deButts's personal behest. Bell officials reached out to intellectual and political elites. Literature was distributed describing the threat competition posed to the subsidy that local rates received from long distance [Bell System, 1976]. But the campaign quickly lost momentum; there was no sense of crisis about the phone system among the elites or the general population. deButts had the Bell System running better than ever, and it was difficult for even a sophisticated opinion leader to perceive how the FCC's halting steps toward competition were endangering the public interest. The great debate fizzled out.

This was unfortunate for AT&T, which needed all the support it could get in Washington. It had angered a vital subcommittee in its rush to obtain sponsors for the CCRA, and it would pay dearly for that choice of tactics.

Lionel Van Deerlin, chairman of the House Subcommittee on Communications, and his staff were irritated when a bill in their field of authority was introduced without consulting them. In the normal course of passage, any such bill would have to go through their subcommittee before it could be enacted, but they were not about to hold hearings on a measure that had not even been discussed with them before it was introduced.

Van Deerlin was sufficiently annoyed that he entered the legislative contest on the other side, using the numerous weapons that a subcommittee chairman had in his arsenal. He announced hearings in 1976 on the general subject of competition in telecommunications, in effect, sidetracking the Bell System's drive for the CCRA. It would be virtually impossible to get the rule-conscious House to do anything specific while a respected subcommittee had the general matter under consideration. Van Deerlin clearly had the tactical advantage in his struggle with the phone company.

Bell System witnesses, even deButts himself, did not make a dent in the subcommittee's resistance. In an interchange noted prominently by the subcommittee staff, Congressman Louis Frey, the ranking Republican, tried to elicit from deButts a vision of the Bell System's role in telecommunications during the next generation. But it took five tries before he could get an appropriate response. deButts finally said, "Our business in this industry is to provide people with communications of all forms. We think down the road we should continue to provide all people with all forms of communications using whatever technology is available at that particular time, and doing everything we can to develop new technology as time goes on in order to keep the service good and as inexpensive as possible." It was the kind of speech that found a sympathetic audience inside the Bell System, but not outside, and especially not in Congress. There was considerable concern on the Hill about the size and power of the Bell System, and deButts's repetition of "all" and "everything" seemed to speak to that issue, leaving no room for others to share with Bell. Neither Van Deerlin nor his staff found deButts's vision appealing [U.S. Congress, 1976b, pp. 61ff].

By the close of the 94th Congress, Van Deerlin had stopped the Bell steamroller. The CCRA had bogged down because of the tactics used to introduce it, the bill's unyielding stance toward competition, and effective opposition from the FCC and from Bell's competitors. In particular, the strict provisions on terminal equipment generated opposition. Many small equipment vendors had entered the market in response to increasingly flexible FCC rules. They swarmed around Congress decrying Bell's heavy hand. A bill without the terminal equipment provisions, one that dealt only with the nascent intercity competition, would have had a far better chance of passage.

Although such a compromise would have appealed to Congress, there was no support for it within the phone company's top leadership. AT&T's officers were playing the situation as if all things should be equal between the company and its opponents. But with a corporation of the size and power of the Bell System, with a company whose relations with federal authority had become tense and troubled, the subcommittee arena was not a friendly debating society. Instead of the law it wanted, the Bell System got a slow roasting.

Rather than pushing for a specific bill, Van Deerlin and Frey issued a statement calling for a "basement to attic" revision of the 1934 Communications Act. Congress would not reaffirm its commitment to regulated monopoly, but there was some chance that it would legislate full competition [*Telecommunications Reports*, 1976, p. 11]. Even this prospect was cloudy. The CCRA had generated a fragile coalition of opposing interests which would have a rough time hanging together long enough to promote an alternative measure. Given the number and variety of the concerned parties, and given the complexity of the issues, the only result that seemed guaranteed was a very slow journey through the legislature.

As the process slowed, it expanded. The effort to resolve common carrier questions had been transformed into a complete rewrite of the Communications Act. Issues of pricing – whether marginal or average costs should be used – were mixed with issues of competition in broadcasting, freedom of speech, and children's television. Opposition came from large companies like IBM and newly formed consortia of smaller companies such as the Ad-hoc Committee for Competitive Telecommunications formed by MCI and other aspiring competitors. The Bell Bill became a tar baby that accumulated issues and interests as time passed. The increasing complexity of the political process reduced the power of any interest group, including the massive Bell System, to push through specific legislation it favored. A stalemate became more likely, and AT&T could not afford a tied ball game.

AT&T Reorganizes

deButts could see the results of his twin initiatives by 1977. The internal reorganization had gone ahead, invigorating AT&T's employees and streamlining operations. The Bell System was operating smoothly, and profits were high. The political initiative, by contrast, had gone nowhere. AT&T was beset by increasing demands for competition and by increasing competitive pressure from firms – typically small firms – allowed into telecommunications. The greatest pressure came initially in the area of terminal equipment, increasingly open to competition, but MCI (then a tiny new firm) also was pushing into interstate services. AT&T found itself on the defensive, both legally and economically. The government antitrust suit begun in 1974 lurked in the background of AT&T's leaders' attention. Congressional action looked increasingly remote.

How did deButts respond to these outcomes? He chose to ignore the political failures and extend the internal reorganization of the Bell System. A new set of internal studies was commissioned in the mid-1970s. They documented AT&T's precarious regulatory and legal position as well as the signs of growing economic problems in areas where competition was allowed, particularly terminal equipment. Both corporate earnings and outside pressures on the firm were rising. Curiously, deButts and the rest of AT&T's

management did not address their weakness. Instead they played to their strength; they reorganized the Bell System again.

Why did they make this choice? I suspect that it derived from the limits of their information. deButts had consulted outside experts in both his internal and external operations. The internal experts, McKinsey & Co., had recommended a policy direction that had achieved some success and indicated a clear path for future change. The external experts, Minow and Rostow, had recommended an approach that had run up against a stone wall. deButts did not appear to have access to another approach to AT&T's political problems. There were critics of deButts' policies even within the Bell System, but they had not formulated an alternative approach and did not have access to the Chairman.

AT&T employed a million people in the 1970s. It was almost a nation within a nation. It had its own strong culture, which was formally and fiercely hierarchical. And it was dominated by engineers rather than economists or politicians. deButts was a product of this system, and he was immersed in it. He had little information about the outside demands on the telephone network and less empathy for the impudent upstarts who aspired to enter this growing business.

Charles Brown, then the president of AT&T, thought that more internal restructuring could deal with AT&T's competitive problems. In contrast with the advocates of change to AT&T's political stance, he obtained deButts' approval to move ahead. The Corporate Planning Organization supported reorganization, arguing that a mismatch between internal conditions and external challenges threatened the long run viability of the corporation. It may have been the support of the planning organization that tipped the balance toward internal rather than external reorganization. Those executives who harped on AT&T's legal troubles, like Alfred Partoll, in charge of AT&T's interexchange cases, were relegated to the outer circles of management [Partoll, 1977a, 1977b]. Brown and his corporate planners moved to the center of power.

To cope with the identified mismatch, the corporate planners looked to the literature of business strategy. They made particular reference to Alfred Chandler, and his recently-published argument that vertical integration and a divisional structure organized by product rather than by function had been the keys to success in some of the nation's largest, most important companies [Chandler, 1977]. By citing Chandler's research on private industrial firms – DuPont and others – the planners blended McKinsey's implicit statement that AT&T should abandon its public utility orientation with the legal department's explicit claim that the firm was being forced to abandon its traditional posture [Bell System, 1978].

The plan itself sharply accelerated the process of shifting AT&T's focus from service to sales and its structure from that of a unitary functional business entity to that of a multi-faceted, market-focused organization. Two new entities were to be added: business services and residence/public services. The proposal divided the customer service organization into two distinct market-focused units along the lines of the competitive alternative originally discussed in 1973 (see Figure 3). These two new structures incorporated market planning, product design, and development (which had been relegated to the marketing department under the earlier organization). The basic changes therefore were twofold. First, the very different needs of business and residence customers were to be supplied by two different organizations. Second, the marketing department started in 1973 as a separate appendage to AT&T's main structure was now to become a major element in these two separate organizations, each of which would be vertically integrated and thus capable of dealing with all of its customers' needs.

The reorganization did not propose to restructure terminal equipment manufacturer Western Electric and Bell Labs along product lines, but rather to impose product-line authority on the existing organizations. In place of reconfiguring these corporate entities along business and residential lines, the proposal vested the management of each segment of the business with financial tools to influence that part of Bell Labs and Western Electric relevant to the segment's markets. The managers of organizations dealing with market segments were empowered to make a claim on corporate resources by presenting business cases. The control over financial resources would be the key to transforming the System.

The plan therefore embodied a complicated budget process designed to make the Bell System responsive to demands from individual market segments. It was a dramatic change in the existing budgetary procedures. Under the Vail-to-deButts style of functional organization, financial plans were made largely on the basis of the network's technical needs, as interpreted by the engineers. Projection of demand and crises like those of the late 1960s provided the bases on which allocations were made. Specific funding could be obtained through the Tri-Company Councils (of AT&T, Western Electric, and Bell Labs) or through appeals for particular projects, but the overall outlines of the budget were set along functional lines.

With the 1978 reorganization, Brown attempted to transform the budgetary process into an instrument for pursuing lines of business. Each of the market segment organizations would have to present a formal, detailed proposal for the development and delivery of a new product or service in order to get resources. The proposal would have to include an explicit statement of marketing objectives, expenses, revenues and earnings projections, key target dates and more. It would be presented to a central management body for consideration in competition with other product proposals.

Thomas Bolger presented this plan to the semi-annual conference of Bell System Operating Company presidents in the spring of 1978 [Bolger, 1978]. Here the full implications of Brown's initiative could be seen. The division between residential and business markets abandoned the stance appropriate for a public utility enjoined to treat all customers equally (that is, without discrimination). Under regulation, even small customers had exerted an important influence on telephone service through the regulatory system. Under competition, large customers would have the largest impact.

There had not been enough marketing men in the Bell System in 1973 to staff a functioning department; Archibald McGill had been hired from outside the System and given authority to hire more outsiders to create a marketing department. Now marketing was being given a major role in the departmental structure and power to match. The marketing department, initially an add-on, was projected to take the initiative for product development away from the engineers at Bell Labs. With it would go the commanding position that the engineers had in the System. The internal power structure that had frustrated McGill's efforts to introduce marketing concepts into the Bell System in the mid-1970s would have to change. McGill was made a vice president. "Marketeers," as they were called disparagingly by the conservatives, would supplant the engineers and the network mystique as the driving force behind company strategies.

The power structure within the operating companies also would have to change. Under deButts's system as under Vail's, the company presidents set policy and interacted with AT&T and the outside world; the operating vice presidents ran the business. Clearly, the operating vice president's job was a plum in the Bell System. That was where managers were tested, proved themselves, and set the stage for their advancement. Under Bolger's plan, this position would disappear. The operating vice presidents would be replaced by the heads of the business, residence, network, and operator service departments, who would report directly to the company presidents. Brown insisted that the business marketing department have the authority gained by reporting directly to the president. When asked what would happen if a company chose to continue using an operating vice president, he said that was fine. But when headquarters wanted to talk to someone about business marketing, it would call the head of that department directly, bypassing the operating vice president.

Such calls would increase in frequency because the reorganization would significantly alter the relations between the operating companies and AT&T headquarters at 195 Broadway (in New York). The heads of the departments would report not only to the presidents of their companies, but also to their opposite numbers at AT&T headquarters. The vice president in charge of marketing services in say, Illinois, would owe loyalty not only to his president but also to AT&T's vice president of marketing as well. This form of matrix organization was a severe break from the System's traditional decentralized, geographic structure. It signaled the growth of a new kind of expertise within the Bell System. No longer would knowledge of local conditions dominate the business; knowledge of national markets would become more important. The business market was growing, and increasing attention to the national arena in which these customers operated was needed. Information needed to go both up within the operating companies and across within departments; authority would flow down and across the matrix.

Changes of this magnitude can seldom be effected without opposition, and Bolger's presentation of the reorganization plan was not greeted by universal applause. The Bell company presidents did not like it both because their authority would be diminished, and because their operating responsibilities increased. Without operating vice presidents, they would be far more involved in the actual running of the business than they had been for years. The operating vice presidents themselves naturally were opposed to the abolition of their jobs. They were supposed to be going up in the organization, but as the reorganization was implemented there was no place for them to go but down. The need was for more departmental vice presidents, not higher executives.

Brown, however, was determined to reorient the Bell System and to get the job done quickly. Bell managers asked about the costs and benefits of the change, the problems of transition, and about more fundamental problems as well: "The Bell System reorganization implies a change in mission while it is unclear whether a decision has been made regarding the kind of business the Bell System should be in [in] the future" [Reed, 1978]. Brown admitted that the "future direction of our business is still not entirely clear." Ambiguity and uncertainty had replaced the security of a regulated monopoly, but one thing was clear: the press of competition meant that the System had to become more market oriented [Brown, 1978].

The managers heard, but they were not all convinced. Many thought that the traditional Bell procedures and organization were too valuable to relinquish. Others felt that their own positions and chances for advancement were threatened by the changing corporate orientation. Through all the discussion ran an undercurrent of hostility toward Brown and his "team" – Bolger, McGill, and others – who were leaning hard on the operating companies to fall into line.

While Brown was able to impose his authority on the operating companies, he was not as successful with Western Electric and Bell Labs. They were not prepared to reorganize their own activities along market lines even to the limited extent required by Brown's plan, and they trotted out familiar arguments in favor of the status quo. Bell Labs invoked its own particular mystique, its productive congeniality, its undoubted past accomplishments. Western Electric, making light of the difficulties it was beginning to experience, insisted that it was one of the premier manufacturing operations in the world and that its system of product management was already organized along market lines. Both organizations questioned the wisdom of deviating from their tested formulae.

The basic changes in the System therefore went up to the borders of these two organizations, but did not penetrate them. Bell Labs and Western Electric were left to run in their customary styles. The interesting question is not why they wanted this outcome, but why Brown and deButts let them get away with it. The answer is, in part, that they still had a telephone company to run, and while introducing structural changes, they needed the enthusiastic support of the management of Bell Labs and Western Electric in the day-to-day operations of the System. They had confidence in the judgment of those managers and found it impossible to ride roughshod over their objections. That had not been the way the Bell System managed change, and Brown, like deButts, was a product of the Bell System. He could not resist the appeal to Bell's past technological glory. He seems to have discounted the decline in Western Electric's price advantage as equipment shifted from electromechanical to electronic; he did not believe that other laboratories would over the long haul duplicate Bell Labs' excellence. He reasoned that these two fine organizations would be able to allocate their internal resources effectively themselves.

deButts supported the reorganization in the May Presidents' Conference, but he looked backward rather longingly and voiced his apprehension about the pending changes. He reiterated the Bell System's commitment to service as its primary goal and argued that the advocates of market orientation needed to keep the service component clearly in mind [deButts, 1978a]. He also mentioned the reservations expressed through the System about the wisdom of the new course, reservations that had been encouraged by the knowledge that they were shared by the chairman of the board. deButts said, "Certainly I have reservations. They are reservations, however, about some of the second and third order effects of our restructuring – strengths of our business that we risk impairing if we proceed heedlessly." Brown had obtained his CEO's support for his reorganization, but not his enthusiasm [deButts, 1978b].

Conclusion

Brown succeeded deButts as AT&T's CEO in February 1979, as his reorganization was being implemented. His reorganization and appointment as CEO showed the ability of AT&T to deal with its internal problems. The traditional organization introduced by Vail in 1909 had served the Bell System well. But it was not suited to the 1970s. The Bell System had achieved universal service, and it had to face competition in its business. deButts began the process of turning the System to head into this new wind. Brown carried on, building on ground prepared by his predecessor. The Bell System was changing from a stolid utility to an aggressive competitor.

By contrast, deButts had made a poor choice in his response to the external challenge. He had opted to leave the antitrust suit alone and bring Congress into the picture. Congress did not act, but it made what was still a technical issue in 1976 into a topic of popular debate by the end of the decade. When Brown, deButts's successor, tried to negotiate a settlement to the antitrust suit after he became CEO, he found that the public outcry made agreement hard to reach. The government felt constrained by the press of opinion; it was not able to present a vision of AT&T's role that both it and the company could live with.

The debate about telecommunications policy continued, therefore, and the antitrust suit went to trial. Only after the beginning of a new administration in Washington and the appointment of a new assistant attorney general for antitrust (William Baxter), after the trial was underway before Judge Harold Greene for several months, and after the Senate passed a telecommunications bill, did negotiations for a settlement become serious. They were completed at the start of 1982. The suit was dropped and the Congressional debate was effectively stilled by severing the Bell Operating Companies from AT&T.

The successive reorganizations forced through by deButts and Brown therefore had their primary impact on companies that were separated from AT&T before the effects of the new organization could be realized. The Bell

Operating Companies found themselves in a totally new environment in 1984, and they needed to reorganize themselves again as a result. The changes in the Bell System in the 1970s doubtless helped them, but much more needed to be done.

AT&T found itself in a new environment as well. The reorganizations of the 1970s had their smallest impact on the parts of the Bell System that AT&T retained. As a result of misjudging its external affairs, the leaders of AT&T failed to reap the benefits of their internal actions. They had expended their managerial energy on companies they then spun off. They failed to reposition AT&T politically or to reorganize Western Electric and Bell Labs, the parts of the Bell System they retained under the Modification of Final Judgment.

Why did deButts and Brown make this choice? I have argued that they had far more information about the internal problems of AT&T than about its external challenges. They chose to deal with what they knew and to avoid the unknown. It is not necessary that the leadership of a large firm be isolated from the wider world, but being at the head of the largest non-governmental organization in the world did promote such a view. It is not that deButts and Brown were unaware of the competitive challenges to AT&T. The preceding story has shown that they were reminded over and over again of these pressures. But they never allowed their awareness of these problems to get to the point where creative solutions could be tried.

Could they have done better? I think there were several paths open to them that would have yielded better results for AT&T. They have been foreshadowed in the narrative. In the early 1970s, before MCI had entered the market for ordinary long-distance service, deButts might have moved to settle the anti-trust suit on far more favorable terms than Brown obtained in 1981. In the mid-1970s, when the Bell Bill had ground to a halt, AT&T could have separated the long-distance market from the terminal market. Executives like Partoll were aware of the synergy between these two diverse kinds of entry and recommended giving up the latter to blunt the force of the former. Failing those changes, deButts and Brown could have turned their full attention in 1978 to AT&T's parlous political and legal position instead of to its internal structure. If they had put half the energy they expended in the second internal restructuring into their external problems, it is hard to believe they would not have come up with solutions better (for AT&T) than the actual Consent Decree of 1982. None of these alternatives would have turned the clock back as deButts wished. But they could have had a pronounced effect on AT&T's fortunes and on the path of telecommunications policy in the United States.

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