

Summary

Yes, MCI was run by crooks who deserve their time in the national media spotlight taking their “perp” walk before going off to spend some time in the Big House. And yes, MCI’s corporate competitors are circling like vultures over a dying animal. But if MCI is broken up and sold off in parts, it will be innocent workers, investors, creditors, and customers who suffer.

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Justice is served by punishing responsible individuals. So is deterrence. Neither is served by wreaking punishment indiscriminately on such innocent people as workers, investors, creditors, and customers.

WorldCom’s Bankruptcy: Promoting the Public Good while Staving Off Telecom Vultures

By Richard E. Wagner, Ph.D.

Hearings are now underway before U.S. Bankruptcy Judge Arthur Gonzalez to determine whether MCI WorldCom will be allowed to emerge from bankruptcy or will be dismembered and sold off in pieces. Despite overwhelming support from its creditors, several large and influential telecom rivals, including Verizon, SBC, and AT&T are running a spirited campaign to shut down MCI WorldCom.

These opponents play to people’s sense of outrage at the corporate scandals that rocked the business world last year, as well as to the breathtaking extent of the \$11 billion accounting fraud at WorldCom. Their main claim is that allowing MCI to exit bankruptcy would allow it to profit from its “ill-gotten gains.” Both justice and deterrence, they argue, require that MCI be dismembered, if not put to death.

Such claims understandably strike an emotional chord with America’s scandal-weary public. Yet those claims are wrong all the same. Simply put, MCI retains no “ill-gotten gains” from the accounting fraud. Whatever short-term advantage the company might have gained has already been lost, many times over. In his opinion on the recent litigation between the SEC and MCI, Federal district court judge Jed Rakoff placed the liquidation value of the company at less than \$6 billion. This value pales in comparison with the \$200 billion by which WorldCom’s equity has plunged.

In the overall scheme of things, there can be little doubt but that MCI would be in stronger shape today had the fraud never occurred, than it will be if it is allowed to emerge from bankruptcy.

Despite the fraud, MCI remains a significant presence in the telecom market. The company has always been a vigorous and innovative competitor. It was first to challenge AT&T in long distance, and more recently has been at the forefront of the competitive assault on the Baby Bells’ century-old monopoly over local telephone service. MCI’s competitors would clearly gain by the elimination of the company, for this would reduce competitive pressures at a time of continuing financial distress in the telecom sector.

While MCI's liquidation would be good for its rivals, it would be bad for the consuming public. It would reduce the choices available to many consumers of telecom services, force 20 million MCI customers to find new suppliers, and leave more of the telecom market under the control of the still relatively monopolistic Baby Bell companies. Local phone competition, which has finally started to deliver major savings to consumers in recent years, would take an especially big hit.

An MCI that is allowed to emerge from bankruptcy would continue to be a major player in the telecom market, providing consumers and businesses with a competitive alternative to the old regime of AT&T and the Baby Bells. Intact, MCI will do more to protect consumers' interests than if the company is dismantled and sold off in parts to its rivals.

Also wrong are claims that the liquidation of MCI is a means to secure justice and promote deterrence against such misdeeds in the future. Justice is served by punishing responsible individuals. So is deterrence. Neither is served by wreaking punishment indiscriminately on such innocent people as workers, investors, creditors, and customers.

To penalize an entire corporation for the misdeeds of some of its officials is to spread the resulting loss among all participants in the corporation. If corporate misdeeds are punished at the individual level, deterrence works as it is supposed to work. But if those misdeeds are punished at the corporate level, the deterrence effect is weakened and the injustice compounded.

It would be different if all participants within WorldCom had agreed to engage in fraudulent practice. But this is clearly not what happened. A few crooked executives engaged in fraudulent activity, and the practice was halted and made public when other individuals within the company became aware of it. To punish MCI wholesale would be to punish those innocent individuals and not the guilty wrongdoers.

It is easy to see why the entrenched incumbents are so keen to bring about MCI's demise. The likes of AT&T and the Baby Bells would rather feed on WorldCom's carcass than see it rejuvenated and have to compete with it for business. The public good, however, would be far better served if MCI receives a second chance instead of an early grave.

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