

**Testimony of Washington State Attorney  
General Rob McKenna  
Concerning Antitrust Enforcement and  
Regulated Industries<sup>1</sup>**

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<sup>1</sup> Drafts of these comments have been widely circulated among the Attorneys General and antitrust attorneys within those offices for review and comment, and the authors thank many enforcers for their suggestions and insights.

Thank you for allowing me the opportunity to comment on these important issues. I believe that the interplay between antitrust enforcement and regulated industries is one that is becoming increasingly important as more industries move toward deregulation. I applaud the Commission for studying these issues.

**I. SUMMARY**

I am here today to address several of the questions raised in the request for public comment. First, I believe that antitrust enforcement has an important role to play, particularly in industries transitioning to deregulation. I believe antitrust enforcers and regulators should have complementary, seamless authority to protect consumers from marketplace abuses. While each should be aware of the other's role, each should maintain its unique jurisdictional authority and focus.

Second, I believe that when there is no specific antitrust exemption, none should be implied by the courts simply based on the existence of a regulatory structure. I will elaborate further on my experience here in Washington State concerning the filed rate doctrine and proceedings before the Federal Energy Regulatory Commission.

Third, if a regulatory scheme contains a "saving clause" providing that the antitrust laws continue to apply, that saving clause should be interpreted to give the antitrust laws deference.

Fourth, I believe that Congress may, in appropriate circumstances continue to establish industry-specific standards for particular regulatory decisions, such as the public interest test, that are not identical to general antitrust standards.

Finally, my comments reflect a National Association of Attorneys General Resolution adopted this year entitled "Principles of Antitrust Enforcement." These principles state the strongly held views of the state Attorneys General, supporting the federalist ideals on which this nation was founded and encouraging active and continuing cooperation between the federal and state governments. I would like to quote one particularly relevant section: "[T]he National Association of Attorneys General has consistently opposed legislation that weakens antitrust standards for specific industries because there is no evidence that any such exemptions would

either promote competition or serve the public interest." I believe that statement underscores my position that regulated industries should not be given a blanket exemption from the antitrust laws.

## **II. ANTITRUST ENFORCERS AND REGULATORS SHOULD HAVE COMPLEMENTARY, SEAMLESS ENFORCEMENT AUTHORITY DISCHARGING THEIR RESPECTIVE RESPONSIBILITIES**

Regulators and antitrust enforcers can coexist in a complementary enforcement scheme. Turf battles over jurisdiction only benefit wrongdoers and will ultimately harm consumers and markets if precious resources are spent in procedural disputes. Leaving the courts to discern the intent behind complex statutes and regulatory schemes, and fill in the gaps, risks defeating both the goals of antitrust laws and carefully crafted regulation.

Regulators and antitrust enforcers serve the same goal – protection of consumers and markets from market power abuses. Antitrust enforcers believe that, as a general rule, consumers benefit when businesses are free to compete on the basis of price, quality and service. Antitrust law is typically concerned with, among other things, abuses of monopoly power in competitive markets.<sup>2</sup> However, when competitive markets do not exist or have not yet been achieved, regulators play a vital role. These are typically industries that lend themselves to monopoly in markets where competition does not provide the desired pressure on prices and incentives to improve products and provide services that may not otherwise be available. In these industries regulation replaces competition.<sup>3</sup>

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<sup>2</sup> Monopolies and monopoly power are not violations of antitrust law in themselves. It is the abuse of monopoly power that concerns antitrust enforcers. Abuse of monopoly power is generally described as conduct that reduces competition in a market by means other than competition. *See generally* 1 Areeda and Hovenkamp §100.

<sup>3</sup> "Unrestricted competition enforced by the antitrust laws is sometimes thought impossible or inappropriate in certain markets....But some markets have been thought to require more restriction on competition than others. Congress may then respond by enacting special statutes that modify, complement, or displace the competitive premises and rules of antitrust. Often, but not always, these antitrust 'exemptions' are accompanied by significant direct regulation of price, output, product quality, entry or other elements. Often, but not always, they are also accompanied by the creation of federal regulatory agencies with oversight over the affected rates." 1A Areeda and Hovenkamp, Antitrust Law §240.

I can offer the Commission two examples of scenarios where complementary enforcement works well. First, there are several industries that have been subject to price deregulation, but remain subject to regulation on non-economic factors such as safety. The airline industry was deregulated in 1978 as to pricing, but the Federal Aviation Administration retains firm control over regulation of airline safety.<sup>4</sup> Under this regimen where policy and jurisdictional boundaries are clearly and expressly set out by statute, tensions between the economic policing of the antitrust enforcers and policing non-economic matters such as safety, have not resulted in conflicts.

A second example is found in my state of Washington. The Washington Utilities and Transportation Commission ("WUTC") is granted authority to regulate prices over certain industries such as telecommunications companies operating purely intrastate. By law, any business regulated by the WUTC is exempt from state antitrust law.<sup>5</sup> However, the statutes defining the jurisdiction of the WUTC over these companies contain an express provision stating that whenever the WUTC classifies a telecommunications carrier as "competitive," it loses its status as a regulated business and becomes fully subject to the antitrust provisions of Washington law.<sup>6</sup>

The importance of these examples is that in each one the respective roles and jurisdictional boundaries of the antitrust enforcer and the regulator are clearly set forth. Where price is left to market forces, or where competitive markets exist, antitrust enforcers have authority. Where the industry still requires affirmative oversight by a regulator, the regulator maintains authority.

Whether or not a market is deemed competitive, the shared consumer protection goal can be realized with some carefully considered changes to existing laws that clarify the intent of regulatory statutes, provide a flexible approach that allows for regulatory and antitrust

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<sup>4</sup> Airline Deregulation Act of 1978, Pub. L. No. 95-504, 92 Stat. 1705 (1978).

<sup>5</sup> Wash.Rev.Code 19.86.170.

<sup>6</sup> Wash.Rev.Code 80.36.300-360 (regulatory authority over in-state telecommunications companies); Wash.Rev.Code 80.36.360 (telecommunication companies classified as "competitive" are subject to the Washington Consumer Protection Act, including its antitrust provisions.) Classifying a business as "competitive" under Washington law is analagous to the FCC's practice of detariffing competitive firms, as described in section V. "

enforcement to co-exist. Complementary enforcement and different standards need not create conflict. However, conflict will occur when it is unclear whether or how enforcers or regulators may exercise authority over the participants in a given market. The unfortunate result of this conflict is too often that consumers are left without any meaningful remedy for very real harms. The nature and consequences of that conflict are illustrated by the efforts by regulators and antitrust enforcers to address the harms resulting from the energy crisis of 2000-2001. I will specifically address some of those problems and the lessons we can learn from them in these comments.

### **III. WHERE THE REGULATORY STRUCTURE INCLUDES COMPLEMENTARY ENFORCEMENT THE LETTER AND SPIRIT OF THE LAW SHOULD BE HONORED WHEN DETERMINING THE APPLICABILITY OF THE ANTITRUST LAWS**

I now turn to the necessity of clear statutory language in the context of complementary enforcement. I believe that a clearly defined boundary between regulatory and antitrust enforcement is vital to robust antitrust enforcement. One approach to defining that boundary is the saving clause, which "saves" certain matters for antitrust enforcers while placing others within the authority of regulators.<sup>7</sup>

Two examples illustrate the harm that can occur when a saving clause or other clearly articulated jurisdictional definition is altogether omitted from a regulatory scheme or when it is interpreted by the courts in a confusing manner. The first involves the electricity crisis of 2000-2001. The Federal Power Act does not contain any provision saving antitrust enforcement authority for state or federal antitrust enforcers. In the absence of such a provision the courts have applied an expansive preemption analysis looking to the scope and intent of the statute, and the degree to which the regulatory agency regulates. The Ninth Circuit found that the pervasive

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Harmonizing Antitrust Enforcement With Regulation," *infra*.

<sup>7</sup> The Commission has included a question about saving clauses in the wake of the case of *Verizon Communications, Inc. v. Law Offices of Curtis V. Trinko, LLP*, 540 U.S. 39 (2004). *Trinko* is discussed *infra*. However my comments are not limited only to saving clauses, but apply equally to any means of defining the jurisdictional boundaries between regulators and antitrust enforcers.

nature of the Federal Power Act and FERC<sup>8</sup> regulation creates an *implied* field preemption that creates immunity from antitrust laws for participants in the FERC jurisdictional markets.<sup>9</sup> This immunity applies even where FERC allows those participants to operate free from price regulation under market-based rate tariffs. A clear antitrust saving clause in the Federal Power Act would have prevented the court from reaching such a conclusion, thus allowing state enforcers to proceed on behalf of consumers.

In contrast to the omission of a saving clause is my second example, the Telecommunications Act of 1996.<sup>10</sup> That Act includes an express saving clause<sup>11</sup> in which Congress clearly expressed its intent to preserve a role for antitrust enforcement. On its face, the saving clause says that there is a role for antitrust enforcement. However, in the *Verizon Communications, Inc. v. Law Offices of Curtis V. Trinko, LLP*, 540 U.S. 39 (2004) (“Trinko”) case, the Supreme Court looked to the pervasive nature of the FCC regulation, the comprehensive scope of the Telecommunications Act of 1996 and concluded that the broadly worded saving clause, although valid, should be interpreted very narrowly. The end result was very similar to the decisions construing FERC jurisdiction under the Federal Power Act – which has no saving clause. Specifically, the Court held that where a regulatory statute such as the Telecommunications Act of 1996 was designed to create more competition, violation of the pro-competition provisions of the Act did not give rise to an antitrust claim. Thus, the Supreme Court interpreted the saving clause in a way that at worst appears to render it ineffective and at best has created much concern about its viability.

The first example illustrates clearly why a specific saving clause is necessary to maximize the protection available to consumers. In contrast, *Trinko* teaches us that some of the more egregious misunderstandings can be averted by carefully crafting a saving clause to clearly and specifically delineate what claims are saved, where the boundaries are between regulation and antitrust enforcement and where the two may overlap.

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<sup>8</sup> "Federal Energy Regulatory Commission"

<sup>9</sup> See *People of California ex rel. Lockyer v. Dynegy, Inc.*, 375 F.3d 831 (9th Cir. 2004), 375 F.3d 831 (9th Cir. 2004).

<sup>10</sup> Telecommunications Act of 1996, Pub. LA. No. 104-104, 110 Stat. 56 (1996)

**IV. EXEMPTIONS FROM THE ANTITRUST LAWS SHOULD NOT BE IMPLIED SIMPLY DUE TO THE EXISTENCE OF A REGULATORY STRUCTURE, ESPECIALLY IN INDUSTRIES TRANSITIONING TO DEREGULATION**

As noted previously, Attorneys General oppose antitrust law exemptions as a general matter. Unfortunately, I am able to speak from my own experience in describing why antitrust enforcers are frustrated by antitrust exemptions, especially those implied by the courts when there is no specific saving clause and when the industry is transitioning to deregulation.

In 2000 and 2001, players in the interstate wholesale electrical power industry were operating under market-based rate tariffs approved by FERC. Unlike traditional tariffs, which contain specific price restrictions and reporting requirements, the market-based rate tariff allows the company to compete in the open market on price, charging whatever rate the market would bear. In each case, the companies granted this market-based rate authority had certified to FERC that they lacked market power<sup>12</sup> in the western power markets. As it turned out, some or all of those companies did have market power, and were able to use it to their advantage. The impact was felt across the western United States. California suffered rolling blackouts and the entire western United States suffered under extraordinary wholesale electricity prices.<sup>13</sup> In Washington alone, local utilities spent hundreds of millions of dollars in unanticipated electricity costs and consumers will be paying off those costs for the next several years.

Antitrust enforcers from the western states sought remedies in court but we found ourselves barred by an expansive interpretation of the preemption and filed rate doctrines.<sup>14</sup> The

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<sup>11</sup> 47 U.S.C. 152 note

<sup>12</sup> *E.g., Enron Power Marketing, Inc.*, 65 FERC ¶ 61,305 (1993); *Enron Energy Services Power, Inc.*, 81 FERC ¶ 61,267 (1997)(granting market-based rate authority to Enron Power Marketing and Eneon Energy Services Power on finding that each lack's market power.) *See .Citizens Power & Light Company*, 48 FERC P 61,210 (1989). ( " Market power for a seller exists when the seller can significantly influence price in the market by withholding service and excluding competitors for a significant period of time. Competitors can thwart the exercise of market power if they have access to the market and can supply more of their own service quickly enough to provide customers with an alternative. " )

<sup>13</sup> Wholesale electricity prices had been around \$25-\$35 per MWh for many years. In May, 2000 they soared to ten times that level and stayed high for over a year before returning to their previous levels..

<sup>14</sup> According to the courts' expanded reading of the preemption doctrine in these cases, consumers may not challenge market manipulation and antitrust violations by competitors in the wholesale electricity markets. This bar

filed rate doctrine is a judicially created doctrine that applies where a regulator requires a tariff to be filed. Typically, tariffs govern prices and other contract terms that would be the subject of negotiation if they occurred in a competitive market. The filed rate doctrine, also known as the filed tariff doctrine, holds that where a regulator has approved a tariff the courts will not second guess that approval, and thus will not entertain jurisdiction over any claim that challenges a tariff provision.<sup>15</sup> The filed rate doctrine makes perfect sense where the regulating agency has procedures in place to review rates and address and remedy tariff violations. In this manner, regulation provides an effective substitute for competition and administrative remedies redress the wrongs that occur. However, the filed rate doctrine makes much less sense in cases where the regulator has determined that the possibility of future competition justifies allowing market participants to operate without price regulation and subject only to the constraints of the free market.

Although there is no specific antitrust exemption, the courts have repeatedly held that expansive regulation trumps antitrust enforcement. At the same time, utilities have not received, and may never receive, meaningful relief from FERC, due to FERC's limited remedial authority. Under its current legislative authority, FERC is limited by the extent to which it can order refunds, and it does not have adequate authority to levy meaningful penalties for market violations. As a result, it is difficult for FERC to curb and respond effectively and firmly to anticompetitive behavior, particularly for electricity markets.<sup>16</sup> The Federal Power Act<sup>17</sup>, one of FERC's primary enabling statutes, provides that "any person" may seek a remedy from FERC,

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extends even to cases where competitors operate under market-based rate tariffs and engage in such conduct in the context of active competition on price in the open market. *E.g., Pub. Util. Dist. 1 of Snohomish County, Washington v. Dynege Power Marketing, Inc.*, 384 F.3d 756 (9th Cir. 2004). *California ex rel. Lockyer v. FERC*, 383 F.3d 1006 (9th Cir. 2004) found that the filed rate doctrine applies even in a market-based rate situation, so long as the agency engages in some degree of oversight. *Snohomish and CA v. Dynege* hold that the filed rate doctrine is implicated for civil penalties, which the court believes will be passed on to consumers. These all represent expansions of the doctrine, which prior courts had said was to be construed very narrowly. *See also State of California ex rel Bill Lockyer v. FERC*, 383 F.3d 1006, 1010 (9th Cir. 2004); *Public Util. Dist. of Grays Harbor v. Idacorp*, 379 F.3d 641 (9th Cir. 2004).

<sup>15</sup> See 1A Areeda and Hovenkamp, Antitrust Law §247 and cases cited therein.

<sup>16</sup> Report of the General Accounting Office to Congressional Requesters, "Energy Markets: Concerted Actions Needed by FERC to Confront Challenges that Impede Effective Oversight", GAO-02-656, June, 2002.

<sup>17</sup> 16 U.S.C. 791a-828c

however the Commission's authority is limited to interstate transactions for wholesale electricity. FERC's jurisdiction extends only to those buying and selling wholesale power in the interstate markets. Consumers who buy electricity at retail from local utility companies have no remedy at FERC no matter how egregious their harm.

This example clearly illustrates why antitrust exemptions should not be implied and also illustrates why clear authority outlining complementary enforcement is necessary. If clear, seamless enforcement authority based on whether a market was competitive or not had existed during the energy crisis, it is likely that courts would have already ordered substantial relief to western states' consumers through various court proceedings.

In the telecommunications arena, the filed rate doctrine is even more confused. The 9<sup>th</sup> Circuit held in *Ting v. AT & T*, 319 F.3d 1126 (9th Cir.2003) that the filed rate doctrine did not work to bar civil antitrust suits against detariffed competitors in the telecommunications industry and arising from rates negotiated in the open market. Recently, the 7<sup>th</sup> Circuit issued a conflicting ruling, reaching precisely the opposite conclusion and declining to follow *Ting*. In *Dreamscape Design, Inc. v. Affinity Network, Inc.*, 2005 WL 1560330 (July 5, 2005) that court found that such actions are barred by the filed rate doctrine.

These examples illustrate the necessity for clearly worded legislation clarifying that where industry participants are subject to the free market, whether under a market-based rate tariff, or detariffing or some other form of *de facto* price deregulation, antitrust enforcers are best suited to police and protect competition. The filed rate doctrine impairs complementary enforcement by regulators and antitrust enforcers in the areas of their respective greatest expertise. Legislation that clarifies the roles of the regulator and the enforcer, and expressly provides for antitrust enforcement where market forces are to replace regulation as the primary force keeping competitors in line, would resolve this problem.

V. **IN A COMPLEMENTARY ENFORCEMENT SYSTEM, IT IS APPROPRIATE TO MAINTAIN SEPARATE STANDARDS FOR ENFORCEMENT AND THEY NEED NOT CONFLICT**

Antitrust enforcers make enforcement decisions based on decades of case law, using antitrust standards that are traditional in many respects but still allow for flexibility. Antitrust enforcers focus on free and open competition and do not necessarily consider the impact on an individual business or on circumstances which may be peculiar to the case. Thus, where conduct that may alarm regulators as contrary to the public interest is perceived not to violate the antitrust laws, antitrust enforcers will likely permit it.

Conversely, regulators are often less concerned with traditional ideas of antitrust in free markets, and more interested in factors that impact the "public interest."<sup>18</sup> Where conduct that might not pass muster with free market economists or some antitrust enforcers is outweighed by other societal benefits, regulators may permit or even institutionalize it. For example, the universal service subsidies in the traditional telecom rate setting context has long offended some proponents of deregulation, but the subsidies continue to be maintained in current tariffs. However, they are now presented in more "explicit" forms on customers' bills. These new explicit billing items have ironically given rise to new problems for consumers since some are deceptive or misrepresented as taxes or regulatory fees when they are in fact neither.

Traditional antitrust enforcement and use of the public interest standard can coexist. For example, using the FERC context again, antitrust enforcers and FERC apparently were faced with the common goal of finding out what problems existed in the energy markets, determining whether there was manipulation of the markets or other wrongdoing, stopping those practices

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<sup>18</sup> The "public interest" is a standard applicable in most regulated industries by statute. For example the Federal Power Act incorporates the public interest standard in several provisions. *E.g.*, 16 U.S.C. 824 ("It is declared that the business of transmitting and selling electric energy for ultimate distribution to the public is affected with a public interest, and that Federal regulation of matters relating to generation to the extent provided in this subchapter and subchapter III of this chapter and of that part of such business which consists of the transmission of electric energy in interstate commerce and the sale of such energy at wholesale in interstate commerce is necessary in the public interest, such Federal regulation, however, to extend only to those matters which are not subject to regulation by the States.")

and trying to find an appropriate remedy. In that situation, the public interest doctrine would likely not have conflicted with antitrust enforcement.

Both the FCC and FERC have exercised their considerable expertise to determine that in the markets they regulate pursuant to the statutory public interest standard, the public interest is best served by opening certain products and services to free market forces. This decision is based on well-founded findings that competition will be sufficient to provide the necessary constraints on price and incentives to improve the product and service, and that more exacting regulation is thus unnecessary. I submit that in these circumstances the regulator should also consider that the public interest is best served by allowing those most expert in policing those markets to do just that. In short, when regulators free a product or service from regulation in favor of free market competition, they should also step back and allow the policemen of the free markets, the antitrust enforcers, to take over the primary job of enforcement.<sup>19</sup>

## **VI. HARMONIZING ANTITRUST ENFORCEMENT WITH REGULATION**

There is no "one size fits all" answer to the questions posed by the interplay between antitrust enforcement and regulation. Generally, I believe that where price regulation is the primary goal of the regulatory agency, and where price regulation is performed in a meaningful, timely way, with appropriate remedies for violations, consumers can still benefit from the regulated agencies' continued oversight. However, if pricing oversight is no longer adequate, or if it is based on a market-based rate, antitrust authorities should be allowed to step in when necessary to police the markets. Similarly, any aspect of an industry that is no longer regulated should be clearly delineated as subject to antitrust enforcement.

For example, the Federal Communications Commission ("FCC") has authority to detariff<sup>20</sup> certain services, allowing them to be sold subject only to market forces.<sup>21</sup> As discussed

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<sup>19</sup> By the same token, in markets subject to price regulation, antitrust enforcers should step back and allow the regulators to do their job as well.

<sup>20</sup> "Detariffing" occurs where a regulator relieves certain regulated businesses from the requirement of submitting a tariff governing transactions in a particular product. For example the FCC has detariffed certain long distance rates and related charges. Similarly, FERC allows wholesale electricity generators who certify that they lack market power to operate under a "market-based rate" tariff in an approach similar to detariffing. Exposing products and

above, another example is the Federal Energy Regulatory Commission ("FERC,") which allows certain companies to sell wholesale electricity at market based rates rather than subject to a standard tariff clearly identifying the price per kilowatt hour.<sup>22</sup>

In both of these examples, there have been collisions between antitrust enforcers and regulators. Over the past decade or more, courts have been broadly deferring to regulators as having greater expertise in particular industries and have been expanding certain legal doctrines to reach those conclusions. One result of this trend has been to create a void in the industries that antitrust enforcement previously filled. This has upset what can fairly be called a delicate balance that previously existed between antitrust enforcement and regulation, with some bad results. The balance can be restored anew with guidance from Congress through appropriate changes to the law.

By contrast, there have been successful transformations between regulation and deregulation. Thirty years ago, the airline industry was heavily regulated for many good reasons. Today, that industry is primarily deregulated and successfully functioning in an active and highly competitive market<sup>23</sup>. Similarly, as recently as the 1980s the Interstate Commerce Commission regulated the interstate trucking industry. Today, that industry has generally transitioned to deregulation and enjoys the benefits of active competition.<sup>24</sup> Their success is based in part on a clear division between the roles of the regulatory agencies and the market enforcers.

In sum, antitrust enforcers should be allowed to police markets where competitors are not subject to specific, affirmatively approved, tariffs. Where a regulator has determined that potential competition could be robust enough to justify detariffing or permit companies to operate under market-based rates, that determination should include shifting primary

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services to market forces brings about the potential for market abuses that are traditionally addressed by antitrust enforcement.

<sup>21</sup> See *Dreamscape Design, Inc. v. Affinity Network, Inc.*, 2005 WL 1560330 (July 5, 2005)

<sup>22</sup> See *State of California ex rel Bill Lockyer v. FERC*, 383 F.3d 1006, 1010 (9<sup>th</sup> Cir. 2004)

<sup>23</sup> Airlines remain heavily regulated as "transportation" issues such as safety and pilot schedules. But pricing and new entry are deregulated. See generally 1A Areeda and Hovenkamp, *Antitrust Law*, §241a; Von Kalinowski, *Antitrust Laws and Trade Regulation*, Second Edition, Ch. 67.

<sup>24</sup> "The same thing is generally true of the interstate trucking industry...." *Ibid.*

enforcement authority to antitrust enforcers who can help make open, fair competition a reality in these transitioning markets.

## **VII. CONCLUSION**

I believe that antitrust enforcers and regulators support consumers and healthy markets in ways that are similar, but have important differences. Antitrust enforcement is the best approach to protecting competitive markets from abusive practices from those with power in those markets. This is especially true in newly competitive markets, such as those transitioning from regulation. In these circumstances, the traditional economic tests of healthy competition that are applied by antitrust enforcers should be applied.

In markets in which affirmative price regulation is the most effective approach to protecting the consumer from predatory and abusive practices, regulators should maintain their regulatory authority. Regulators should be able to apply a broader public interest test when considering price and other factors.

As I have described, many of the conflicts between regulators and antitrust enforcers arise from confusion over the boundary between regulation and antitrust enforcement. I propose that this boundary be clearly and expressly delineated to provide guidance to competitors, regulators and antitrust enforcers, and to the courts. These boundaries can be drawn in well-crafted saving clauses, informed by the experiences to date that I have described above. Courts, in turn, should honor both the letter and intent of those clauses.

Furthermore, I submit that competition and consumers would benefit from a Congressional clarification of the scope and limits of the filed rate doctrine, with the general guidance that there should be few if any exemptions from antitrust laws.