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March 24, 1993

Ms. Donna Searcy
Secretary
Federal Communications Commission
1919 M Street, N.W.
Room 222
Washington, D.C. 20554

Re: CC Docket Nos. 91-141 and 92-222

Dear Ms. Searcy:

Please find enclosed a corrected filing of MFS Communications Company's Emergency Petition To Hold Proceedings In Abeyance which was filed yesterday, March 23, 1993. Attachment A was inadvertently omitted from the original filing. A copy of Attachment A is being served today on all parties of record.

We apologize for any inconvenience this has caused.

Sincerely,

Russell M. Blau

Russell M. Blau

cc: All Parties of Record

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Before the
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pricing and GSF allocations before it addresses the equally important issue of unbridled

LEC discounts for interstate special access services. Absent immediate Commission reallocation would be cost justified. It would therefore be irrational and imprudent prior to completion of the volume/term discount inquiry to permit the LECs to reduce these questionable rates even further, without providing any cost justification and without any safeguards against unreasonable discrimination. The initiation of such further rate decreases on top of the virtually unbridled rate flexibility awarded the LECs under volume/term discounting will almost certainly cause serious and irreparable harm to CAPs and leave competitive special access services stillborn.

In the *Expanded Interconnection Order*, the Commission found that, while "reasonable volume and term discounts can be a useful and legitimate means of pricing special access services to recognize the efficiencies associated with larger volumes of traffic and the certainty of longer term deals," nonetheless "[t]he largest of the volume and term discounts cited by MFS, some of which may result in total discounts of more than 70%, however, may be anticompetitive or raise questions of discrimination." *Order*, paras. 199, 200. The Commission concluded that "the largest of the discounts offered by the LECs warrant some additional inquiry to help us determine whether we should promulgate guidelines requiring cost justification of any subset of LEC volume and term discounts," and directed the Bureau to obtain cost support data from the LECs for this purpose. *Id.*, para. 200 (footnote omitted). MFS' pending Petition for Limited Reconsideration and Clarification of the *Order*, filed December 18, 1992, requests that the Commission investigate *all* special access volume and term discounts and that it immediately prescribe rules requiring that discounts be cost justified. From a marketplace perspective, MFS submits that this issue is, beyond question, the single most important competitive issue facing the CAP industry. As MFS earlier argued, failure to resolve this matter promptly would leave special access competition an empty, theoretical concept.

The Bureau, pursuant to the *Order*, requested that four LECs submit cost support data for their most highly discounted special access offerings. As MFS stated in an *ex parte* letter to the Chief of the Bureau, submitted on March 3, 1993 (a copy of which appears as Attachment A hereto), the LEC responses were from MFS' perspective wholly inadequate to permit a competent analysis of their rate levels. MFS therefore requested that the Bureau expand the scope of its inquiry into LEC volume and term discounts, and that it require the LECs to provide additional and more detailed cost data.[3] To date, the Bureau has not released any findings relating to its inquiry nor (to MFS' knowledge) taken any action to gather additional information. Although MFS appreciates that the Bureau is proceeding in good faith to address these issues and that its staff is limited, every day's delay in resolving this threshold issue results in a greater percentage of the special access market being warehoused by the LECs and taken off the competitive playing field for three, five or seven years, or longer. Indeed, it is MFS' experience in its markets that most of the interstate special access traffic of the three largest IXCs nationwide has already been locked up under unbridled volume and term discount arrangements.

[3] Among other things, the Bureau required each LEC to submit cost justification only for one specific discount offering. It is not possible to determine whether unreasonable discrimination exists without comparing rates and costs for services provided to different classes of customers.

In the meantime, while the volume and term discount proceeding kicks into first gear, most of the Tier 1 LECs have filed zone density pricing plans with the Bureau, as authorized by the *Order*, paras. 179-184. These carriers propose to deaverage rates for DS1 and DS3 services in three zones. Under the *Order*, each service is subject to a separate subindex in each zone. As the Commission explained,

> under this system, a LEC could lower prices for DS1 [or DS3] services in the highest density zone by as much as 10% per year adjusted for the price cap index (PCI), and could raise prices for DS1 [or DS3] services in the lowest density zone by no more than 5% per year adjusted for the PCI, without triggering any of the additional cost justification or advance notice requirements contained in the price cap rules.

Order, para. 182 (footnotes omitted). Zone density pricing may be implemented in a LEC study area as soon as "an interconnector has taken the expanded interconnection cross-connect element." *Order*, para. 179 n.411. In the case of those LECs that have interim interconnection tariffs in effect (namely New England Telephone, New York Telephone, Bell Atlantic, Illinois Bell, Centel of Illinois, and Pacific Bell), expanded interconnection services will be purchased under the permanent tariffs immediately after they take effect, which is scheduled for May 17, 1992. Thus, at least in some study areas, LECs would immediately be able to reduce DS1 and DS3 rates in their high density zones by 5 to 10 percent.[4]

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[4] The potential immediate reduction depends upon how far the LEC's current DS1 or DS3 subindex is above its price cap floor. If the subindex is currently exactly at the floor level (5% below the previous year's subindex adjusted for PCI changes), then an additional and immediate 5% reduction would be permissible because of the 10% downward pricing flexibility allowed within zones. If the subindex is currently above the floor level, a greater price reduction would be possible.

These LECs would then be permitted to grant an *additional* 10 percent reduction in their price cap tariffs that will become effective on July 1, 1993, as would the remaining Tier 1 LECs when their zone density plans take effect. Moreover, the LECs have proposed that GSF reallocation be reflected as an exogenous cost reduction in the special access price cap index ("PCI") effective July 1, 1993. If this takes place, then the PCI will be reduced by 5 to 10 percent, depending on each LEC's GSF costs, and since DS1 and DS3 subindex pricing flexibility is *relative* to changes in the PCI, this means that the total July 1 price reductions in the high density zone (i.e., the zone most susceptible to CAP competition) could be as much as 15 to 20 percent above and beyond the already incredibly low levels resulting from unbridled volume and term pricing flexibility. Those LECs who implement zone pricing before July 1 could reduce their rates by approximately an additional 25 percent within a two month period. The potential price reductions are illustrated in the following table, which is based on actual price cap data recently filed by BellSouth:

Table 1

1.	Current Special Access PCI (as of 1/26/93)			98.8839
2.	Current DS1 Subindex (as of 1/26/93)			92.8569
3.	Current Band Limits of DS1 Subindex			
	a.		Upper	98.7929
	b.		Lower	89.5469
4.	Initial Band Limits of High Density DS1 Subindex (illustrative)*			
	a.		Upper	98.7929
	b.		Lower	84.9239
5.	Initial High Density DS1 Subindex (Illustrative)**			84.9239
6.	New Special Access PCI (7/1/93) (Illustrative)***			92.1598
7.	Change in PCI	(L6/L1)		.932
8.	New Band Limits of DS1 Subindex			
	a.	(L2*(L7+.05))	Upper	91.1855
	b.	(L2*(L7-.05))	Lower	81.8998
9.	New Band Limits of High Density DS1 Subindex			
	a.	(L5*(L7+.05))	Upper	83.3953
	b.	(L5*(L7-.10))	Lower	70.6567
10.	Cumulative Allowable Reduction in High Density Zone DS1 Rates	((L2-L9b)/L2)		23.9%

* If zone pricing becomes effective before 7/1/93 price cap revisions.

** Assumes maximum allowable reduction of DS1 rates in high density zone.

*** Assumes 4.0% inflation, 3.3% productivity factor, and 7.5% exogenous cost reduction due to GSF reallocation.

As shown above, a 25 percent reduction in DS1 or DS3 rates—with absolutely no cost data required to be filed in support—is entirely conceivable under the Commission's current rules coupled with its proposal for GSF reallocation. This example, using the conservative assumption of a 7.5 percent reduction due to GSF reallocation, shows that the LEC would be permitted to reduce DS1 rates by almost 24 percent. (Precisely the same rules would apply to changes in DS3 rates.) Some LECs may be able to take even larger reductions. And, as stated in note 2, *supra*, these reductions need not be applied uniformly to all rate elements, so that, as experience demonstrates, some of the most steeply-discounted service options could be reduced by greater percentages.

Significantly, even the grossly inadequate and conclusory cost information provided to date by the BOCs demonstrates clearly that price reductions of 20 percent or more below existing levels (deflated through volume/term discount pricing) would be predatory in the case of the most highly discounted special access services.[5] For example, Bell Atlantic alleges that its monthly cost for DS3C (a DS3 "three-pack") interoffice mileage is $2,187.43 plus $113.74 per mile. It offers this service at rates as low as $2,294.22 plus $375.81 per mile for five-year term customers. Also, Pacific Bell offers a DS3 "twelve-pack" channel termination at a rate of $9,982 per month for a five year term, as contrasted to an alleged monthly cost of $7,627; and Ameritech offers DS3 channel mileage in Illinois at monthly rates of $365 per termination plus $113 per mile for a 60 month term, with an alleged cost of $323.56 per termination plus $75.25 per mile. Even if it is assumed for the sake of argument that the LECs' cost analyses are methodologically correct and accurate—which MFS does not concede—the LECs' own

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[5] All cost data cited in this paragraph are taken from the information submitted to the Common Carrier Bureau on January 15, 1993, by Ameritech, Bell Atlantic, and Pacific Bell, in response to the Bureau's inquiries concerning these carriers' volume and term discounts for interstate special access service. *See* Attachment A.

data concerning their steepest volume and term discounts show that prices reduced by 20 to 25 percent would be below cost in many cases.

At present, absent a Section 208 complaint and its ensuing delay, protestants have little recourse to combat such LEC predatory pricing. Moreover, any such challenge will be extraordinarily time consuming and the standards unclear. Meanwhile, the LECs will be able to continue pricing below cost, while the challenge works its way through the agency pipeline, with an immediate and irreparable effect on local special access competition.

If the Commission were to approve zone density pricing plans and to implement its proposed GSF cost reallocation under these conditions and prior to resolving the volume/term discount inquiry, it would effectively be authorizing LECs to engage in themselves of any additional significant discount pricing until the unbundled volume/term discounts are fully investigated and, as MFS believes, rendered unlawful.

For these reasons, MFS urges the Commission, on an urgent and immediate basis, to instruct the Bureau to defer approval of any zone density pricing plans until after (1) the Bureau has completed its pending inquiry into certain LEC volume and term discounts *and* conducted a similar inquiry into the discounts offered by the other Bell Operating Companies and GTE; and (2) the Commission has reviewed the results of these inquiries and prescribed binding guidelines for cost justification of volume and term discounts. MFS also urges the Commission to hold CC Docket No. 92-222 in abeyance until the foregoing actions have been completed.

Respectfully submitted,

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Attorneys for **MFS Communications Company, Inc.**

Dated: March 23, 1993

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common line element (and therefore in interstate toll rates), while the use of zone pricing to reduce rates in urban business districts will permit offsetting rate increases of up to five percent per year in other zones.

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ATTACHMENT A

March 3, 1993

VIA MESSENGER

Ms. Cheryl A. Tritt
Chief, Common Carrier Bureau
Federal Communications Commission
1919 M Street, N.W.
Room 500
Washington, D.C. 20554

RE: Written *Ex Parte* Filing in CC Docket No. 91-141: Common Carrier Bureau Inquiry into LEC Volume and Term Discounted Rates for DS3 Service

Dear Ms. Tritt:

On behalf of Metropolitan Fiber Systems ("MFS"), I am submitting this letter in response to the data provided to the Common Carrier Bureau on January 15, 1993 by Ameritech, Bell Atlantic, Pacific Telesis and U S West. Pursuant to Section 1.1206(a)(2) of the Commission's rules, an original and two copies of this letter are being filed with the Secretary today. As discussed in detail below, the LEC data are wholly inadequate to permit a competent analysis of the LECs' rates, and are therefore inconsistent with the letter and spirit of recent Commission and Bureau Orders. For these reasons, MFS respectfully requests that the Bureau both expand the scope of its inquiry into LEC volume and term discounted rates, and require the LECs to provide additional and more detailed cost data concerning such rates.

BACKGROUND

In its Collocation Order[1] the Commission responded to concerns raised by MFS[2] and others that LECs had used volume and term discount rate structures to establish discriminatory and likely predatory rates for high capacity services. The Commission noted that:

> The largest of the volume and term discounts cited by MFS, some of which may result in total discounts of more than 70%, however, may be anticompetitive or raise questions of discrimination. . . . Accordingly, we direct the Chief, Common Carrier Bureau to require the submission of cost support data for some of the largest existing discounts.[3]

Pursuant to this directive, on December 18, 1992, the Common Carrier Bureau issued letters to Ameritech, Bell Atlantic, Pacific Telesis and U S West, directing them to provide cost data that "show whether the rates under these tariffs: (1) cover average variable cost, and (2) are otherwise just, reasonable, and nondiscriminatory." On January 15, 1993, in purported compliance with the Bureau's requirement, these four local exchange carriers ("LECs") submitted cost data.

As MFS describes below, the data submitted by the LECs makes a mockery of the Bureau's inquiry -- the LEC responses contain only grossly aggregated data, and are devoid of any useful description of the methodologies used to compute the volume and term discounts. As such, they render impossible any responsible evaluation of the reasonableness of the LEC rates. For this reason, the Bureau must require that the LECs provide much more detailed information, and must expand the scope of its inquiry to encompass additional services and additional LECs.

1/ Expanded Interconnection with Local Telephone Company Facilities, 7 FCC Rcd 7369, 7463 (1992) (Collocation Order).

2/ Ex Parte Submission of Metropolitan Fiber Systems, Inc., filed in CC Docket No. 91-141 on May 27, 1992.

3/ Collocation Order, 7 FCC Rcd at 7463 (footnotes omitted).

THE DATA PROVIDED BY THE LECS IS WHOLLY INADEQUATE TO DEMONSTRATE THE REASONABLENESS OF THE EXISTING LEC VOLUME AND TERM DISCOUNTS

All four LECs fail to provide data that is sufficiently detailed to permit a reasoned analysis of their proposed rates. Instead, all four LECs provide highly aggregated data, with no workpapers showing its derivation, and with little or no discussion of the assumptions and methodologies used in their computations.

The most grossly inadequate showing is made by Ameritech, which provides no explanation of its methodology at all, shows and no derivation of any of its data. Indeed, to the extent that Ameritech provides any data at all, it attaches materials from a 1990 cost study that apparently accompanied its 1990 annual access filing. (That filing can no longer be obtained from the Commission's Washington offices.) Ameritech does not even attempt to show that the 1990 data is a relevant indicator of its current costs.

Bell Atlantic similarly simply lists aggregate investment amounts for various categories, without identifying the individual cost elements that make up the service. Bell Atlantic also fails to discuss allocation of any overhead costs, and provides no detail for its nonrecurring cost computations.

Pacific Bell provides no information regarding the individual cost elements that comprise the total cost of providing its high capacity service. Rather, Pacific merely cites aggregate figures for annual gross investment, which purportedly were derived from a "1993 Investment Study." These aggregate data provide no information concerning the discrete to identify labor time and rates necessary to perform various tasks, unlike any of the other LECs.

Significantly, none of LECs have demonstrated how volume purchases and long term service commitments contribute to cost savings. Absent such quantification, the extraordinary discounts included in these LECs' rate structures cannot be justified.

THE LITTLE DATA THAT THE LECS HAVE PROVIDED INDICATES THAT THE LEC DATA ARE INCONSISTENT AND OTHERWISE FLAWED

While the data submitted by the four LECs subject to the Bureau's inquiry is wholly inadequate to determine whether their discounted rates recover average variable cost, the little data that the LECs have provided demonstrates inconsistencies and omissions that cast significant doubt on the data's veracity. For example, while Ameritech apparently employs a five-year depreciable life in its rate computations, the other LECs use depreciable lives of 9-11 years. Similarly, while Bell Atlantic claims that term discounts are justified because they allow LECs to use longer depreciable lives in establishing their rates, it uses service life estimates shorter than those employed by U S West and Pacific.

The LEC filings are also grossly inconsistent in their handling of overhead loadings. U S West states that its rates were derived using long run incremental cost, implying that overheads were included in its rate computations, although it fails to identify any such loadings. Pacific discusses a number of overhead cost accounts, although it too fails to quantify such cost elements in its data. In contrast, Ameritech and Bell Atlantic make no mention of any overhead loadings, and none are apparent in their filings. These inconsistent and largely undefined ratemaking methodologies preclude any reasoned evaluation of the reasonableness of the LEC's discounted rates.

RECENT COMMISSION ACTION DEMONSTRATES THE INADEQUACY OF THE LEC COST DATA AND REQUIRES ADDITIONAL COST DETAIL AND DESCRIPTION OF THE RATEMAKING METHODOLOGIES USED BY THE LECS

The Commission currently has pending an investigation of below-band rates effected by GTE last year.[4] The investigation was initiated in response to dramatic reductions in certain GTE service rates -- reductions on a par with the 40-80% reductions that LECs have obtained through their use of volume and term discounts. In setting the rates for investigation, the Commission stated its intent to conduct a detailed review of GTE's costs:

> GTOC's average variable cost showing, however, consists only of summary results of incremental cost studies. The full incremental cost studies supporting the summary results are required to evaluate the reasonableness of the filing, e.g., the type and cost of equipment used to provide transport and the usage of the equipment.[5]

In attempting to support its below-band filing, GTE initially submitted a Direct Case that provided the type of highly aggregated investment data that characterizes the LEC filings at issue in the instant proceeding.[6] After interested parties complained to the Bureau Staff that the GTE cost data were wholly inadequate, the Staff instructed GTE to provide detailed cost data. One week later, GTE complied, and released highly disaggregated data that identified the costs associated with discrete pieces of equipment used to provide service: multiplexers, fiber panels, cross-connects, repeaters, span interfaces, channel banks, etc.[7]

Even with that level of detail, the Bureau required additional information from GTE. During the course of Staff

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[4] 1992 Annual Access Filings, CC Docket No. 92-141, 7 FCC Rcd 4731 (1992).

[5] Id. at 4736 (emphasis added).

[6] Direct Case of GTE, filed in CC Docket No. 92-141 on July 27, 1992.

[7] The additional data was hand-delivered to counsel for the Association for Local Telecommunications Services, following execution of a nondisclosure agreement, on August 3, 1992.

review of the GTE data, and in response to comments filed by interested parties, the Bureau Staff required GTE to submit additional data concerning the billing and collection costs[8] associated with the GTE service under investigation.[9] Even with this level of detail, significant issues concerning the adequacy of GTE's cost showing remain unresolved, and the investigation of the GTE rates is still pending before the Commission.

The investigation in CC Docket No. 92-141 centers on the same issue before the Common Carrier Bureau in the instant case -- whether LEC rates recover average variable cost. The Bureau cannot accept a lesser standard of evidence in its review of the LEC volume and term discounts than it has required in its pending investigation of GTE's rates -- failure to impose a consistent evidentiary standard in both cases would be arbitrary and capricious, and would disserve the public interest.

THE BUREAU MUST EXPAND THE SCOPE OF ITS INQUIRY INTO LEC VOLUME AND TERM DISCOUNTED RATES

In a letter to you dated December 27, 1992, we noted that the Bureau's apparent decision to limit its inquiry to a subset of DS3 services provided by Ameritech, Bell Atlantic, Pacific Telesis and U S West is overly restricted, and is inadequate to address the policy concerns raised by the Commission in the Collocation Order. As our earlier correspondence noted, since MFS filed its ex parte survey of LEC volume and term discounts on May 27, 1992, GTE restructured its high capacity rates, and now offers discounts on its DS3 service that are higher than those offered by three of the four LECs that have been subject to the Bureau's investigation. Surely there is no rational explanation for excluding the GTE rates from the scope of the Bureau's inquiry.

In addition, the decision to exclude BellSouth, NYNEX and Southwestern Bell from the Bureau's inquiry is similarly

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[8] It is significant that none of the four LECs subject to the instant Bureau inquiry has provided cost data demonstrating that their discounted rates recover relevant billing and collection costs -- a cost showing that the Bureau expressly required of GTE.

[9] GTE Ex Parte Presentation, filed in CC Docket No. 92-141 on October 21, 1992.

Ms. Cheryl A. Tritt
March 3, 1993
Page 7

flawed. There is no reasoned basis for restricting the Bureau's inquiry to the top four most highly discounted LEC rates. For example, the Bureau has incorporated into its inquiry Ameritech's 47% discount on optical DS3 service, but has excluded New York Telephone's 44% discount. Clearly, there is no basis for finding [illegible] companies and GTE, and that the scope of the Bureau's inquiry be expanded to include all of those LECs' DS3 and DS1 volume and term discounted rates.

Very truly yours,

Andrew D. Lipman
Senior Vice President, Legal
and Regulatory Affairs

cc (by hand delivery):
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<u>CERTIFICATE OF SERVICE</u>

I hereby certify that on this 23rd day of March 1993, copies of an Emergency Petition To Hold Proceedings In Abeyance were sent by first class mail, postage prepaid, to the following:

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