

July 1, 1994

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FEDERAL COMMUNICATIONS COMMISSION
OFFICE OF SECRETARY

Mr. William F. Caton, Secretary
Federal Communications Commission
1919 M Street, NW
Room 222
Washington, D.C. 20554

RE: RM-7913

Dear Mr. Caton:

COMSAT Corporation, through its COMSAT World Systems line of business, hereby submits an original and five (5) copies of its "Petition for Partial Relief from the Current Regulatory Treatment of COMSAT World Systems' Switched Voice, Private Line, and Video and Audio Services" ("Petition for Partial Relief"). Accompanying this Petition for Partial Relief, and bound in separate volumes, are an original and five (5) copies of an Executive Summary, and a study by The Brattle Group entitled "Competition in the Market for Trans-Oceanic Facilities-Based Telecommunications Services," undertaken in conjunction with Dr. Hendrik S. Houthakker, Henry Lee Professor of Economics at Harvard University.

Please associate these filings with the above-captioned proceeding, as they are intended to update the record therein with current market information, and to modify the relief sought by COMSAT Corporation in its January, 1992 "Petition for Rulemaking to Modify the Regulatory Treatment of COMSAT World Systems' Multi-Year Fixed-Price Carrier-to-Carrier Contract-Based Switched-Voice Services." Specifically, this Petition for Partial Relief seeks immediate authority for COMSAT World Systems to file tariffs for all its Intelsat satellite services on a streamlined basis, with 14-days public notice, a presumption of lawfulness, and minimal cost support data.

If you have any questions regarding this submission, please contact the undersigned.

Respectfully submitted,

Howard Polsky
Howard D. Polsky

Enclosures

No. of Copies rec'd 0+5
List ABCDE

**Before the
FEDERAL COMMUNICATIONS COMMISSION
Washington, D.C. 20554**

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JUL 11 1994

RM-7913 FEDERAL COMMUNICATIONS COMMISSION
OFFICE OF SECRETARY

**In the Matter of)
)
Petition for Partial Relief)
From the Current Regulatory)
Treatment of COMSAT World)
Systems' Switched Voice,)
Private Line, and Video)
and Audio Services)**

EXECUTIVE SUMMARY

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EXECUTIVE SUMMARY

Conditions in the international telecommunications marketplace have changed radically since the Federal Communications Commission last analyzed them almost a decade ago. At that time, the FCC determined that COMSAT Corporation (“COMSAT”) had market power in the provision of satellite space-segment services. In doing so, however, the agency also expressly recognized that the provision of international transmission facilities was on the verge of dramatic technological breakthroughs and market developments, and that the basis underlying its 1985 market power decision might well vanish in the near future.

The Commission’s expectations have now materialized. Competition for trans-oceanic telecommunications traffic has mushroomed with the rapid introduction of fiber-optic submarine cables and the launch of new international satellite systems, commonly known as “separate satellite systems.” As a result, COMSAT has been increasingly burdened by now-outdated regulatory constraints which do not apply to its rivals — many of whom, ironically, also number among COMSAT’s largest customers. Current market realities warrant FCC action to restore regulatory equilibrium to the international transmission facilities arena and thus allow the U.S. public to reap the fruits of true competition.

HISTORICAL BACKGROUND

An understanding of the regulatory scheme originally applied to COMSAT is necessary to appreciate fully the impact of recent marketplace changes on COMSAT’s business and, accordingly, the need for FCC action. In the early 1960s, United States policymakers were inspired by satellite technology’s promise for linking the nations of the world and thereby improving international relations. Congress envisioned a satellite system operated by a multinational cooperative as the means to achieve those goals. Thus, in 1962, lawmakers created a private company, the Communications Satellite Corporation (now

COMSAT), to be the United States' sole representative in the international organization. The cooperative, the International Telecommunications Satellite Organization ("INTELSAT"), was established by treaty in 1964.

Early U.S. Policy Utilized Regulatory Mechanisms To Foster Development Of A Global Satellite System

Congress and the FCC recognized that establishing this worldwide satellite system required a completely new regulatory scheme to overcome serious obstacles confronting the venture. These obstacles included high initial start-up costs, the unproven nature of the technology, and the obvious reluctance of existing U.S. international telecommunications carriers to support an alternative transmission system that would threaten their investment in undersea cables and high-frequency radio facilities.

To address those problems, policymakers developed a symmetrical regulatory program that promoted the development and use of INTELSAT's facilities while at the same time protecting incumbent carrier interests. First, Congress established COMSAT as a private corporation and gave the existing international carriers investment opportunities in the new entity. Carriers also were permitted to share with COMSAT in ownership of the earth stations linked to INTELSAT. These financial stakes were designed to counter the carriers' inclination to favor their own trans-oceanic facilities over the INTELSAT system.

Next, the FCC established "circuit distribution" or "loading" guidelines, which required carriers to add satellite and cable circuits in approximately equal proportions. To ensure that these policies did not inadvertently threaten the economic health of the established carriers, the Commission then generally barred COMSAT from competing with other carriers for end users — COMSAT functioned as a "carrier's carrier" by supplying wholesale INTELSAT capacity to the retail carriers. The agency also established traditional rate-of-return regulatory controls on COMSAT, including the obligation to provide full accounting justifications for rates charged. Finally, the FCC required carriers to offer "composite"

rates, which averaged the costs of international satellite and cable service so that many end users obtained the economic benefits of satellite technology.¹

Subsequent U.S. Policy Evolved To Rely Upon Market Forces To Promote Competition For International Transmission Facilities

These government protections succeeded much as U.S. policymakers had hoped, helping the INTELSAT system to settle into the market and flourish. Accordingly, when the FCC analyzed the state of competition in the international telecommunications market in 1985, it was able to conclude that COMSAT should be treated as “dominant” in the provision of space segment and television transmission services. In reaching this determination, the FCC also acknowledged that it would need to revisit that finding as U.S. policy turned toward a greater reliance on market forces to promote competition in international telecommunications.

As INTELSAT matured, the FCC shifted its policies to introduce more competition into the international facilities marketplace. It promoted intermodal competition between submarine cables and satellites by eliminating the international carriers’ investment interests in COMSAT, lifting the loading guidelines, and erasing the mandatory composite rate policies. Intramodal competition was fostered by approving the launch of separate satellite systems that would compete directly with INTELSAT. In addition, the Commission gradually lifted limitations on earth station ownership and use for both carriers and non-carrier users, thereby removing COMSAT from its once-pivotal role in operating the ground links necessary for international satellite transmission. More recently, the FCC removed most of the restrictions that once prevented separate satellite systems from connecting to the public switched telephone network — a step taken in anticipation of the total elimination of those regulatory barriers by 1997.

¹ In addition, so that there could be no dispute regarding allocation of costs between COMSAT’s jurisdictional (*i.e.*, INTELSAT-related business) and non-jurisdictional activities, the Commission later on established regulations governing COMSAT’s corporate structure and its accounting and cost allocation system.

TODAY'S COMPETITIVE MARKETPLACE

Despite these significant changes and their competitive impact, the Commission has yet to revisit its nearly decade-old determination that COMSAT had market power in providing space-segment services. While COMSAT's rivals publicly trumpet their freedom to tailor offerings to customers' needs without the time delay or uncertainty inherent in the tariff approval process, COMSAT — in order to meet the same consumer demand — is burdened with making extensive tariff filings for any new or changed services, with detailed cost justifications, and is subject to a lengthy notice requirement. This regulatory asymmetry is increasingly distorting market competition to the detriment of consumers.

To document the current state of the market for international transmission facilities, COMSAT has filed with the FCC one of the most extensive and detailed analyses of that trans-oceanic facilities marketplace ever undertaken. This independent study, "Competition in the Market for Trans-Oceanic Facilities-Based Telecommunications Services" (the "Study"), was prepared by Hendrik S. Houthakker, Henry Lee Professor of Economics at Harvard University, in consultation with The Brattle Group of Cambridge, Massachusetts.

The Study concludes that "COMSAT faces substantial effective competition in all geographic and service market segments" worldwide from fiber-optic cables and separate satellite systems. These findings therefore provide solid support for COMSAT's Petition for Partial Relief (the "Petition"), submitted concurrently with the Study.² The Petition applies the Commission's established framework for evaluating competition to the marketplace for trans-oceanic telecommunications facilities. The FCC's analysis focuses on an interplay of several factors to determine whether a telecommunications market is sufficiently competitive to prevent a firm from acting in a discriminatory fashion or charging

² COMSAT's Petition for Partial Relief expands upon information already before the Commission with respect to the competitive status of the international telecommunications market. *See* Communications Satellite Corporation, Petition for Rulemaking to Modify the Regulatory Treatment of COMSAT World Systems' Multi-Year Fixed-Price Carrier-to-Carrier Contract-Based Switched-Voice Services, RM-7913 (filed January 30, 1992).

excessive rates. The hallmarks of a competitive telecommunications environment include rivals' ability to accommodate new traffic (high "supply elasticity"); customers' sensitivity to price change and awareness of alternatives (high "demand elasticity"); and the comparability of competitors' costs, quality, and the service terms offered to customers. As outlined below, under the economic standard used by the FCC to measure competitiveness — or any equivalent test — COMSAT possesses no ability to set supracompetitive prices or discriminate unreasonably in the market for international trans-oceanic telecommunications facilities.

COMSAT's Competitors Have Sufficient Unused Capacity To Effectively Constrain Any Theoretical Market Abuses

The Study demonstrates that COMSAT's fiber-optic cable and satellite competitors have enough unused transmission capacity to accommodate COMSAT's customers. Furthermore, the furious pace at which new transmission capacity is being added proves that new facilities and providers are entering the marketplace with ease; that is, entry barriers are low. Additional idle capacity also is available through the use of circuit multiplication and compression techniques that expand the effective capacity of existing facilities. These facts ensure a sufficiently high level of "supply elasticity" to undercut any competitor's ability to obtain or wield market power.

Figures 1-3 graphically illustrate the explosion in the number of facilities added since 1988. By the end of 1996, trans-oceanic fiber-optic capacity for service to and from the United States will stand at almost triple the 1993 levels. Moreover, by that time at least seven separate system satellites over the Atlantic and six separate system satellites over the Pacific will be serving traffic to and from the United States. In fact, as Figure 4 shows, COMSAT's share of available international capacity has already dropped to about half of its 1986 share.

This explosive growth in facilities means that competitors have sufficient idle capacity to constrain any power COMSAT might otherwise have to charge excessive rates.

Figure 2

U.S.-Transoceanic Satellites and Fiber Optic Cables 1993

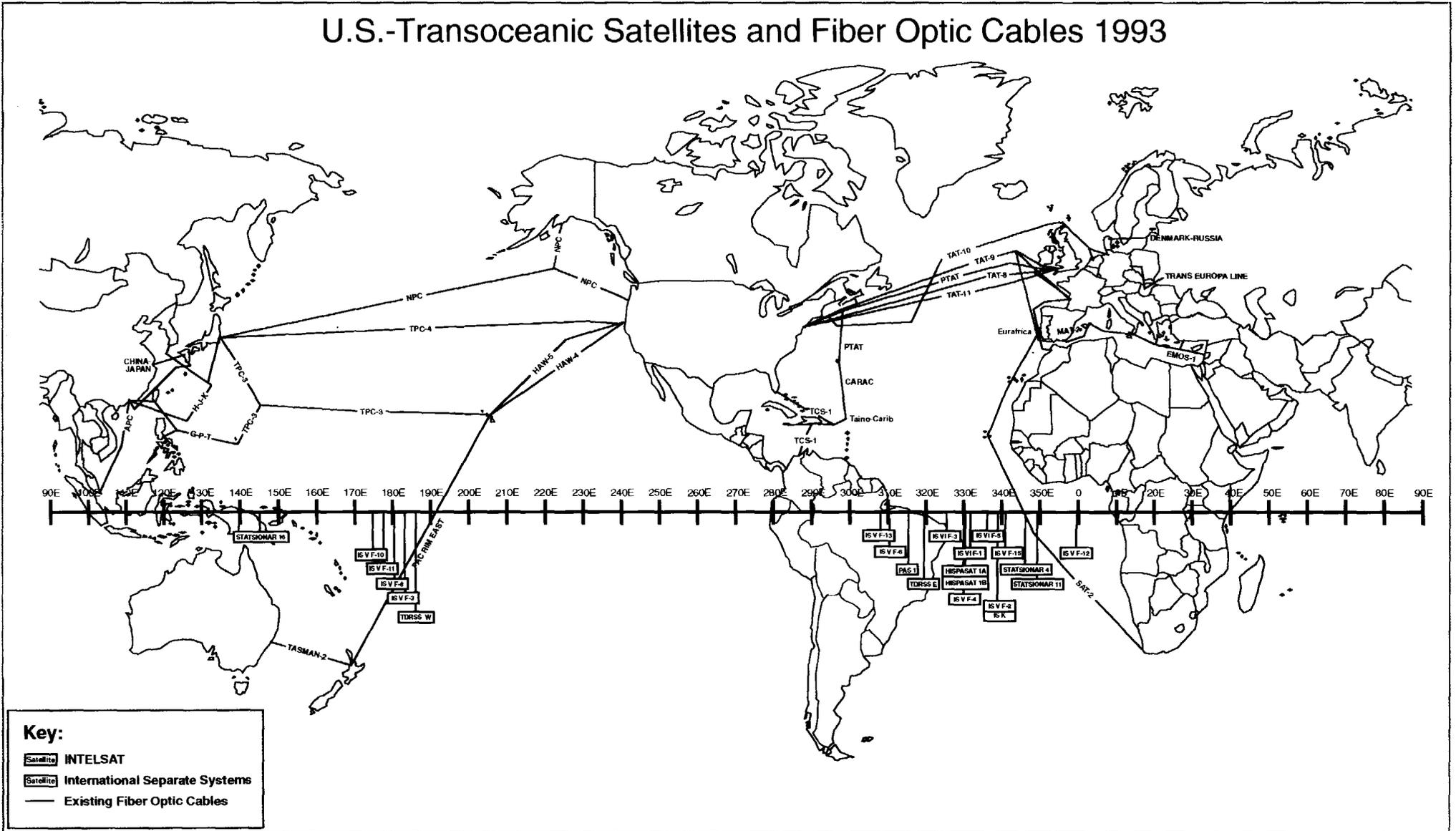


Figure 3

U.S.-Transoceanic Satellites and Fiber Optic Cables 1996

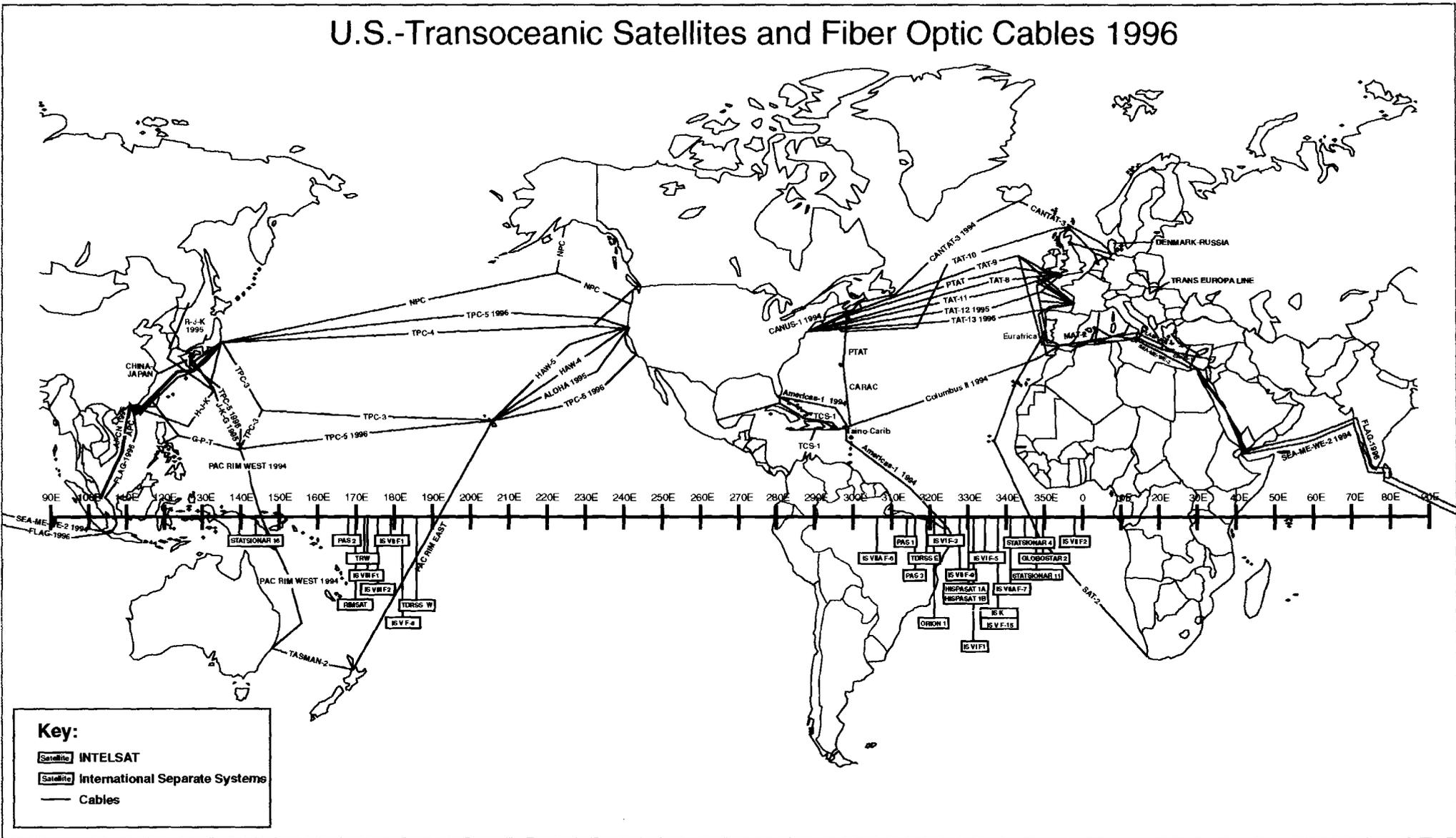
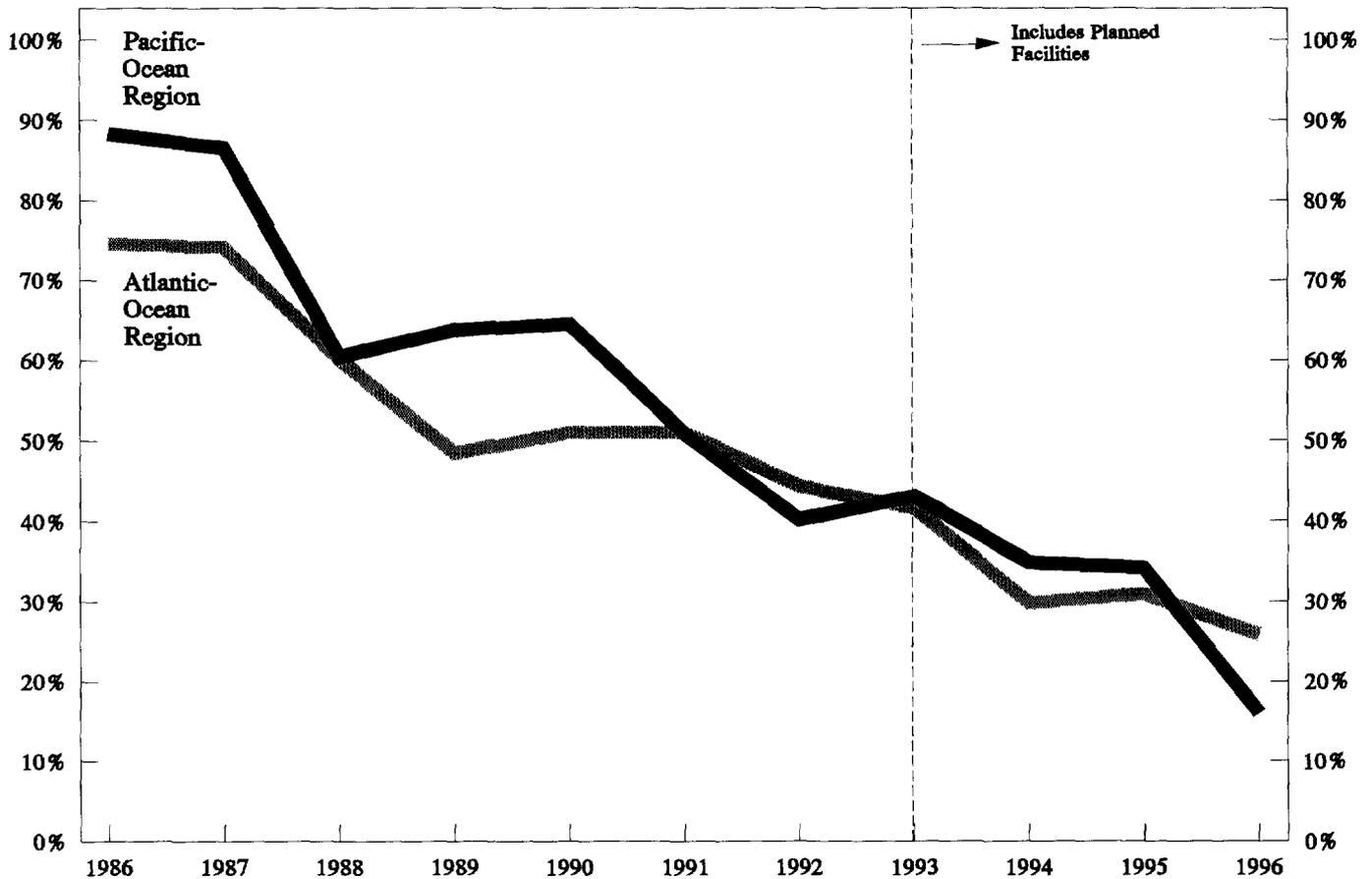


Figure 4
COMSAT Share of Available Trans-Oceanic Capacity
(Based on 64 kbps-equivalent circuits design capacity to and from the U.S.)



NOTES:

Not all of a satellite's capacity will be available for service to and from the U.S., depending on transponder configuration and services in or between regions that do not involve the U.S. (see Study, pages 43-44). Accordingly, the study assumes that the maximum capacity available to COMSAT is 50% of all Intelsat Atlantic and Pacific Ocean Region circuits terminating in the U.S. (i.e., 25% of all Atlantic and Pacific Ocean half circuits). A corresponding amount of available capacity to and from the U.S. is assumed for separate satellite systems.

See Chapters V and VIII of the study for a further discussion of analysis, data sources, and assumptions.

Source: Study, Exhibit HSH-7.1

The Study demonstrates that cable systems linking the United States to the European-Middle East region and to the East Asian-Pacific region have enough unused capacity to absorb all of COMSAT's services to those geographic areas, while idle capacity on trans-Caribbean cables could accommodate most of COMSAT's switched and private-line services to the Caribbean and Latin America.

Geographic areas not easily accessible by existing or planned cable facilities account for only about 6% of total trans-oceanic traffic. In these regions, capacity on existing and planned separate satellite systems is or soon will be sufficient to handle COMSAT's customer traffic. Furthermore, these areas benefit from competition elsewhere by virtue of COMSAT's pricing structure which, with few exceptions, charges uniform rates for services around the globe.

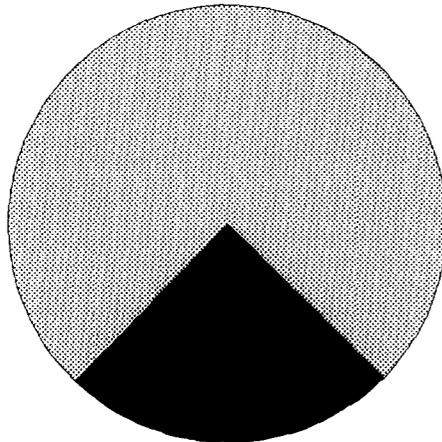
COMSAT's Customers Are Sophisticated Users Who Seek High Value And Quality

By shifting their traffic to follow the most attractive price and service offerings, customers have made clear the extent to which a high level of "demand elasticity" exists today in the international facilities marketplace. These customers — international common carriers, major broadcast networks, and multinational corporations — are highly sophisticated users able to take full advantage of the choices available to meet their needs. Their expertise in international communications is second to none. Indeed, COMSAT's direct rivals in facilities provision number among the largest users of COMSAT's trans-oceanic services.

Market share data demonstrates that these customers readily explore the alternatives open to them. The Study reveals that even though COMSAT's traffic is growing, its share of overall demand has declined. The result of this trend is reflected in Figure 5, which shows that COMSAT's share of switched voice and private line traffic last year was below 50% in each of the three regions which, taken together, account for 94% of the total marketplace.

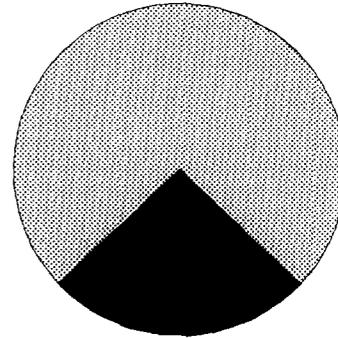
Figure 5
Market Size and COMSAT Market Shares of Trans-Oceanic Switched Voice and Private Line Services (1993)
 (Based on utilized 64 kbps-equivalent circuits to and from the U.S.)

Europe/Mediterranean/Middle East*
 34,000 Circuits Total



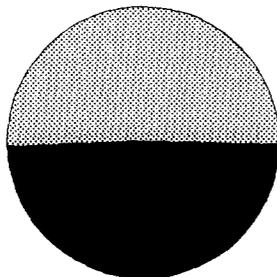
24.8%

East Asia/Oceania*
 21,000 Circuits Total



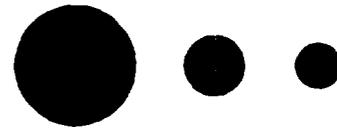
26.0%

Caribbean/Latin America*
 14,000 Circuits Total



48.9%

Rest of AOR
 Rest of Latin America
 Rest of POR
 4,000 Circuits Total



100.0% 99.1% 100.0%

■ COMSAT ▨ Other Facilities

NOTES:

* Geographic market segments with competition from existing and planned cables and satellites.

The relative size of the pies reflects the size of the market segment.

Due to the unavailability of complete data, this analysis does not include utilized capacity for switched voice and private line services on separate satellite systems.

See Chapter IV of the study for a further discussion of geographic market segments.

See Chapters V and VI of the study for a further discussion of analysis, data sources, and assumptions.

Source: Study, Exhibit HSH-5.1

With respect to video and audio services — where fiber optic cables are only now becoming a factor — COMSAT's shares have fallen as a result of separate satellite system competitors who recently entered the market. Figure 6 illustrates that in two of the three global regions, COMSAT is capturing less than half of the “incremental” demand (*i.e.*, demand attributed to growth) for video service. COMSAT's share of video traffic can be expected to decline further as additional competitors become operational.

Furthermore, improvements in prices and service options demonstrate that customers are benefitting as rivals in facilities provision react to competition. COMSAT alone has introduced at least twenty new service packages since the mid-1980s. COMSAT also has implemented substantial price reductions in excess of 35% since 1985, and it is already committed to future reductions in the price of its digital bearer services.

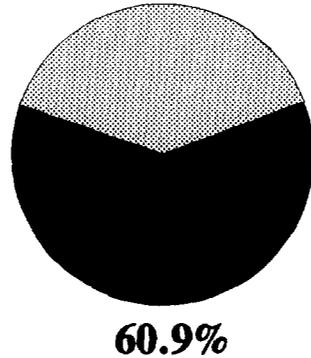
COMSAT Has No Unfair Advantages Over Its Competitors

The Commission's criteria for competitive analysis also looks to whether a firm has certain cost advantages in comparison to its rivals. As the Study demonstrates, costs for trans-oceanic fiber optic cables have decreased so rapidly that cable capacity costs are comparable to — and in many instances lower than — those of satellites. In contrast, technical costs for satellite transmission are generally holding steady at current levels. Notwithstanding the above, separate system satellite competitors enjoy significant cost advantages over COMSAT because of the lesser regulatory burden imposed by the current asymmetrical regulatory program.

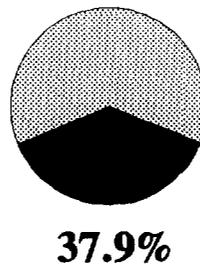
In addition to cost considerations, the FCC has examined whether a firm's mere size and access to resources might somehow “preclude the effective functioning of a competitive market.” No reasonable questions can be raised about whether COMSAT has any such advantages. COMSAT is dwarfed by its competitors by any standard imaginable. For example, COMSAT's total 1993 revenues were only about 1/20th those of MCI or Sprint — and less than 1/110th those of AT&T. Given the size discrepancy and the fact

Figure 6
Market Growth and COMSAT Incremental Market Shares of
Trans-Oceanic Video and Audio Services
(Based on 36/27 Mhz transponder leases to and from the U.S.)

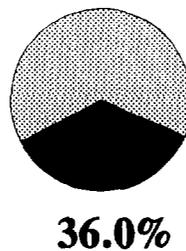
Trans-Atlantic (1989 - 1996)
 79 Total Incremental Leases



Trans-Pacific (1994 - 1996)
 29 Total Incremental Leases



Caribbean and Latin America (1988 - 1996)
 25 Total Incremental Leases



COMSAT
 Other Facilities

NOTES:

Does not take into consideration services on cables, separate satellite systems (other than PanAmSat and Orion 1), or U.S. domestic satellites available for service to the Caribbean and Latin America.

The relative size of the pies reflects the size of the market segment.

See Chapters V and VII of the study for a further discussion of analysis, data sources, and assumptions.

Source: Study, Exhibit HSH-6.1

that these competitors are also COMSAT's largest customers, COMSAT has neither the bargaining power nor the special access to resources that would be required to adversely affect competition in the market.



The Study's findings make clear that the protective policies which once shielded COMSAT from robust competition have been eliminated and that the market for trans-oceanic telecommunications facilities is now fiercely competitive. Therefore, marketplace conditions today support findings by the FCC that COMSAT possesses no market power and that substantial deregulation is warranted.

However, because such a rulemaking proceeding would take considerable time (especially given the Commission's already strained resources) and COMSAT's need for relief is immediate, COMSAT at this time has requested only modest changes. COMSAT currently seeks FCC authority to file tariffs in a manner similar to that afforded to its rivals. Specifically, COMSAT is requesting authority to file its tariffs on fourteen days' notice, with a presumption of lawfulness and a minimal cost support requirement. This streamlined tariff regulation would constitute a significant first step toward restoring balance in the marketplace and thereby guarantee the public the true benefits of robust competition.