Southwestern Bell Corporation

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November 22, 1994

Sandra L. Wagner
Director
Federal Regulatory

Ex Parte

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

Re: LEC Price Cap Review, CC Docket No. 94-1

Dear Mr. Caton:

In accordance with the Commission rules governing ex parte presentations, please be advised that today, Jeff Olson, Pat Bellamy, Harold Nance and the undersigned representing Southwestern Bell met with Anthony Bush and Dan Grosh of the Tariff Division to discuss Southwestern Bell's position regarding the LEC price cap review. SWBT also presented information regarding access competition in the Houston market area. Attached are the handouts provided in the meeting.

If you have any questions, please let me know.

Sincerely,

Sandra L. Wagner

Attachments

cc: Anthony Bush
Dan Grosh

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Washington, D.C. 20005

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Southwestern Bell Position
Price Cap Review

- Need a Simple Plan

- Need the Right Plan

  - Need Plan that is Rational Based on Competitive Environment

    - Competition
    - Customer Needs

  - Need Plan that Allows Market to Create Incentives for Investment in Regulated Business

    - Investment Follows Opportunity

  - Need Plan that Will Assure Reasonableness of Prices Where Markets Cannot

  - Need Plan that Does Not Penalize LEC for Improved Productivity, Increased Demand, or Reasonable Earnings

- Need the Plan Now

Demonstration of Competition in Access Markets: Houston as a Case Study

1. Competition in Access Markets is Significant to SWBT.

Access revenues represent about 26% of SWBT's total revenues.

30% of SWBT's access revenues is concentrated in less than 1% of the land mass served by SWBT (only 44 wire centers -- or only 3% -- of SWBT's 1,287 wire centers). As a result of this concentration, competition is a small portion of the geography can address a large percentage of the access market.

Pockets of SWBT's access markets are hotly competitive today. Regulatory constraints are preventing access customers from benefiting from having SWBT as an active competitor.

2. Houston as a case study for access competition affecting SWBT.

Houston is the most competitive market in SWBT's territory.

Houston is the 4th largest city in the U.S., with metro population of 4 million. It is the largest port in the U.S. (tonnage or value). Houston's economy is dominated by information dependent and information rich industries. It is major center of corporate headquarters (principally financial and oil), medical institutions, research and applied technology centers, high tech manufacturing, and aerospace. Houston is also a magnet for small business formations; Money named Houston as the 6th most attractive area in the U.S. for entrepreneurs (Houston is the largest by far among the top six).

Telecommunications service providers identified Houston early as a primary market for competitive entry. Some of the earliest manifestations of access competition occurred in Houston. Any form of access competition present in the U.S. will have occurred here.

3. Houston Markets are Competitive; Customers have Numerous Choices.

Alternatives to SWBT access services:

Metropolitan Fiber Systems (MFS), Teleport Communications Group (TCG) and Phonoscope have robust fiber optic based networks throughout the Houston metropolitan area. IXCs, electric utilities, private network owners and cable TV providers have built or are building fiber networks.

- Alternate fiber networks

  - MFS
  - Teleport
  - Phonoscope

  - AT&T
  - MCI
  - Sprint
  - Wiltel
  - East Texas Fiberline
  - Electra
  - other IXCs (more than 22 IXCs provide service in Houston)

  - Houston Light & Power
  - other private fiber networks

  - Time Warner
  - TCI

Competitive networks lace throughout the entire Houston metro area. CAPs and other private networks link together the IXC points of presence (POPs). IXCs represent approximately 70% of access demand in Houston. CAPs have service to virtually all the IXC POPs, demonstrating that alternative supply capacity already exists for the vast majority of SWBT's access revenue in Houston. CAP networks are accessible to nearly all of the Houston business communities.

Downtown Houston

The Houston Downtown area contains a very high concentration of employment by firms that are intensive users of telecommunications. CAP networks reach virtually every customer in the area.

The following major businesses are headquartered or have major employment and/or telecommunications demand concentrations in the downtown area:

Bank One	Houston Light & Power	Pennzoil
Coopers & Lybrand	IBM	Shell Oil
Exxon	M.W. Kellogg	Tennaco
First Interstate	Kidder & Peabody	Texas Commerce Bank
Harris County	Nation Bank	Union Carbide
City of Houston	Paine Webber	

In the Clay and Capital wire centers in Downtown Houston, more than 95% of DS1 and DS3 demand originates in buildings where we can confirm today that CAPs already proved access services. This market is undeniably competitive. (But SWBT cannot compete on equal terms.)

For the total Houston market area, more than 88% of DS3 demand originates in buildings where CAPs already have service. Also, Houston-wide, over 59% of DS1 demand originates in buildings with CAP service.

What Can We Learn from Downtown:

CAPs have high capacity service competing directly with SWBT access services in all of downtown Houston. All businesses in Downtown Houston have alternative access suppliers to SWBT.

If SWBT had the flexibility to customize its access services to meet customer needs in Downtown Houston, no current or potential SWBT access customer would be worse off; many would be better off by having SWBT as an effective competitor. It is exactly this type of flexibility to meet customer needs that SWBT contends must be part of the price cap review.

CAPS have access service today in buildings where SWBT has not been able to identify the fiber routes that lead to the buildings. Conversely, CAPs also have fiber to buildings where SWBT has not been able to confirm that CAP access service is currently present within the building. The reach of CAPs in Houston (and elsewhere) is greater than can be indicated by data that SWBT can confirm as definitely correct. The accurate result is that the presence of CAP competitive supply is greater than shown by SWBT.

Medical Center Area

This area is one of the largest and most concentrated areas of medical care, hospitals and research facilities in North America. It contains over 100 buildings, approximately 30 medical care institutions located in close proximity. Approximately 6,700 hospital beds; multitude of research facilities; 1993 employment of 54,700; combined annual operating budget of $7 billion; campus covers 675 acres.

This is a prime example of a large campus that is heavily laced with private networks. CAPs are offering the provision of private high capacity circuits for telecommunications needs within the Medical Center and access to IXC POPs their networks for all other telecommunications needs.

What Can We Learn from the Med Center Area:

Each of these major hospitals already have CAP access service or have been approached by alternative access providers who are ready and willing to provide access services in direct competition with SWBT. Whether or not SWBT can identify that CAP fiber networks are physically present in very close proximity today, the actions of both the CAPs and these customers have demonstrated to SWBT that they are addressable by CAPs today. In addition, these customers have built extensive private networks.

CAPs offer services "in kind" to customers. These services "in kind" do not generate revenues for the CAPs, expenses for the customers or income tax or gross receipts tax revenues for governmental units. Thus, it is impossible to quantity CAP presence using revenue.

Galleria / Greenway Plaza Area

The Galleria and Greenway Plaza areas both contain a heavy concentrations of business and employment. Both areas contain banks, oil companies, oil-related businesses, law firms, engineering firms and other entrepreneurs.

The Galleria is anchored by the Transco Tower, a 64-story office complex. The Galleria complex has led the very rapid growth on the west side of Houston and is made up of smaller office building of 2 to 20 stories. This is the heaviest concentration of retail space in Houston (approx. 2.1 million square feet).

The Greenway Plaza complex is as large as many cities' downtowns. It is a planned business community made up of large office buildings (including the Summit).

What Can We Learn from the Galleria / Greenway Plaza Area

Where supply capacity is not owned by one competitive network provider, other providers are willing and able to lease capacity to each other.

Business consumers from a variety of industry segments have chosen to utilize these CAPs for their Access Services, due to lower prices, greater service flexibility and the ability of CAPs to provide services in real time.

Access competitors have encircled and can address the major concentrations of telecommunications demand.

	Percent of Demand Addressable	
Houston Wire Centers	**Percent of DS3 Demand Originating in CAP Buildings**	**Percent of DS1 Demand Originating in CAP Buildings**
All of Houston	**88%**	**59%**
Clay	**95%**	**93%**
Capitol	**96%**	**97%**

Note: The above percentages were calculated using buildings that had been identified as having CAP service already available as of April 1994. Since that time, SWBT has identified a significant number of additional buildings with active CAP service but has not yet completed an update of the above percentages. Also, SWBT's ability to positively identify buildings as definitely being served by CAPs is incomplete. As a result, the above numbers are an underestimate.

4. Regulation Must be Relaxed to Encourage Competition.

SWBT is prevented by regulation from meeting customer needs in the access markets in the following areas:

- price
- service flexibility
- timeliness to market

Customers will negotiate lower access prices, greater service flexibility and will obtain timely responses from access providers whether or not SWBT is allowed to compete on equal terms.

- Without allowing SWBT to compete, however, customers will not experience the benefits of full price competition and society's resource allocations will be inefficient.

- Market-based price discrimination for access services has already occurred and will increase further with or without SWBT's participation.

For customers to benefit from effective access competition, SWBT must have the ability to:

- response effectively to customer-specific proposals

- reduce prices more flexibly than in zoned-pricing plans or state-wide pricing requirements.

Customers will not be harmed if SWBT is allowed the flexibility to compete for customers on equal terms.

Measured regulatory disengagement from the competitive pricing and service offering process is the necessary step.

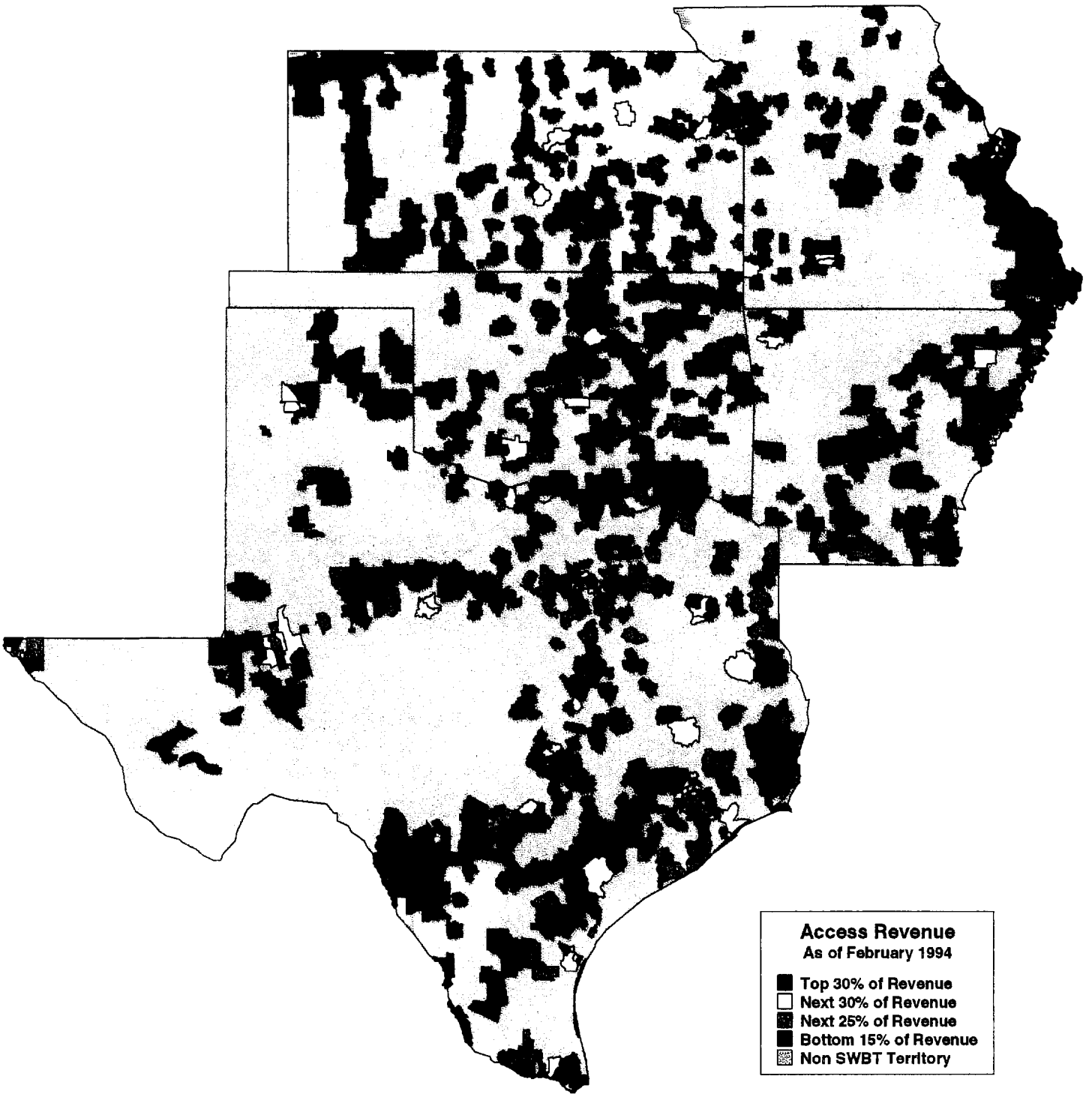
- Eliminate rate element codification

- Shorten tariff notice intervals

- Significantly streamline (and in certain competitive situations eliminate) cost and other support requirement necessary to bring services to market.

The competitive realities of the access markets, and the welfare of customers require that the Commission put this process in motion now.

Southwestern Bell Territory
(Switched and Special Access Revenue)



MARKETING DEPARTMENT
GENERAL MANAGER-MARKETING SUPPORT

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Houston Major Market Area
(Switched and Special Access Revenue)

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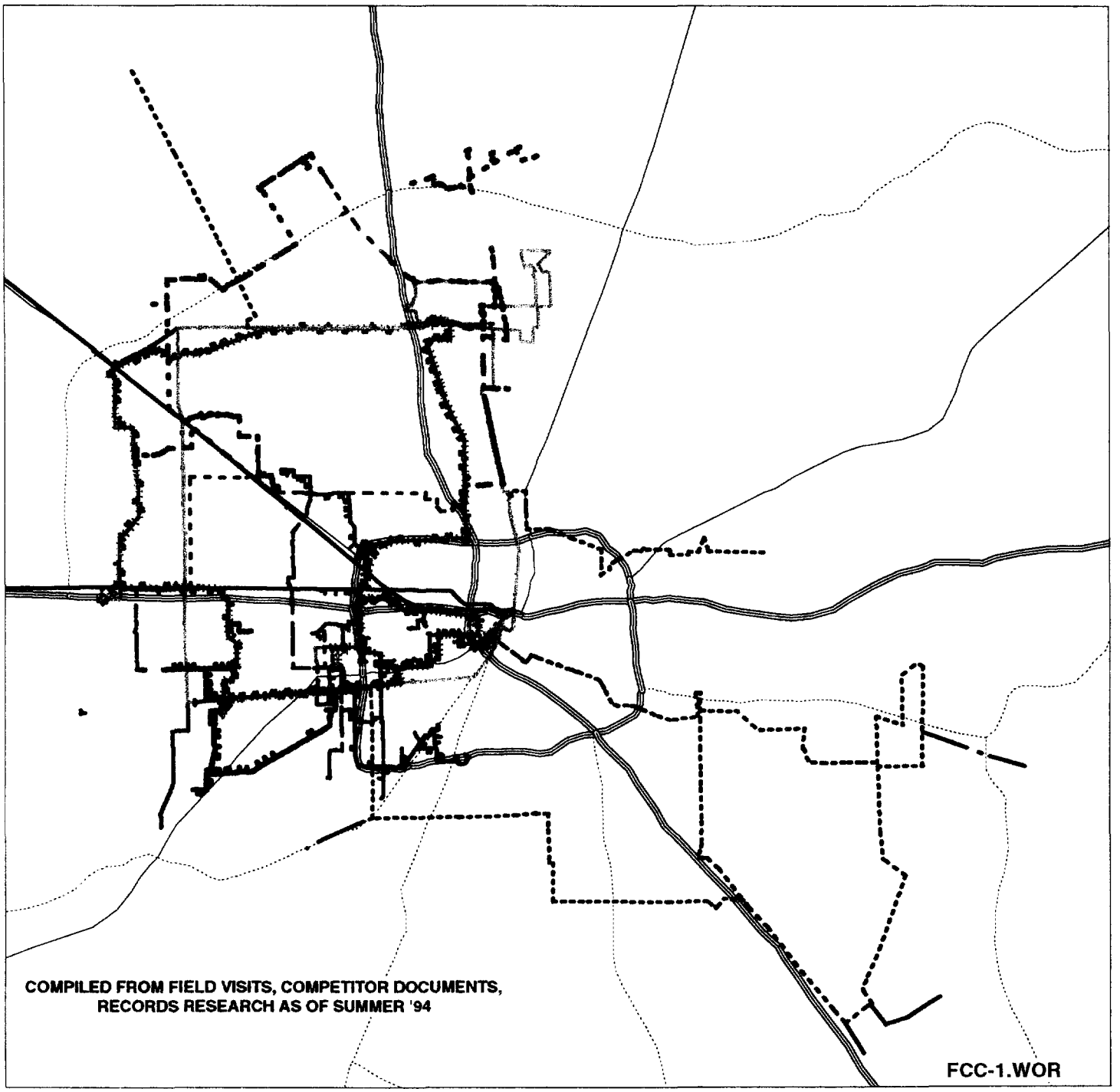
General Manager-Marketing Support
sw_hommarev.wor_m_revenue

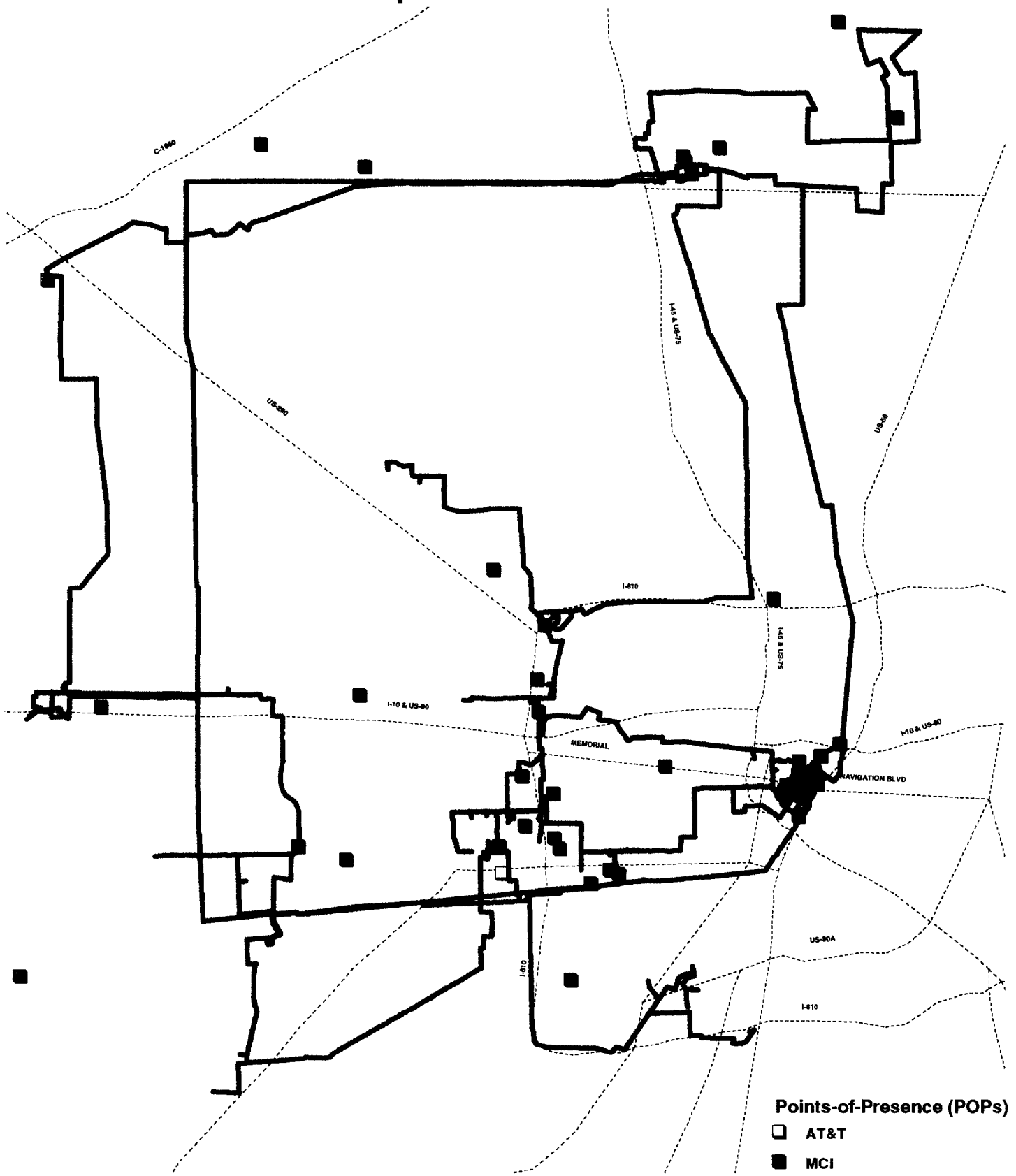
LEGEND

- HL&P
- PHONOSCOPE
- TELEPORT
- MFS
- TIME WARNER
- US SPRINT
- MCI
- EAST TEXAS FIBERLINE
- ELECTRA



HOUSTON COMPETITIVE NETWORKS

CAP Networks
Metropolitan Houston



Points-of-Presence (POPs)

- AT&T
- MCI
- Sprint
- Others

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Competitor Fiber Routes
Downtown Houston

Fiber

- MFS
- Phonoscope
- Teleport

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Competitor Fiber Routes
Downtown Houston

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= *Building connected to a competitor's network*

DS1 & DS3 Locations

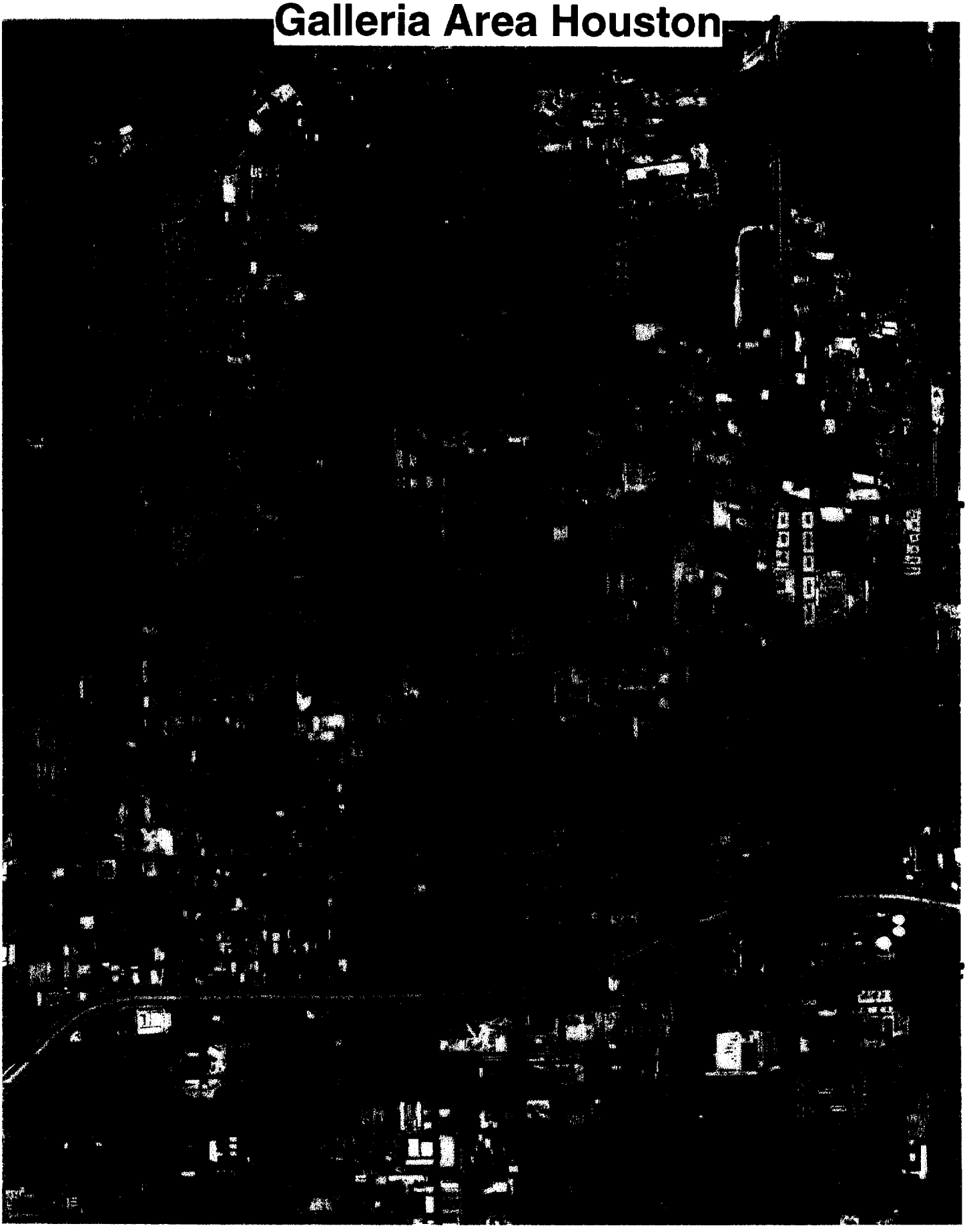
Fiber

M F S

Phonoscope

Teleport

CAP Networks
Galleria Area Houston



CAP Networks
Galleria- Houston

DS1 & DS3 Locations

= Building connected to a competitor's network

M F S Fiber

Phonoscope Fiber

Teleport Fiber

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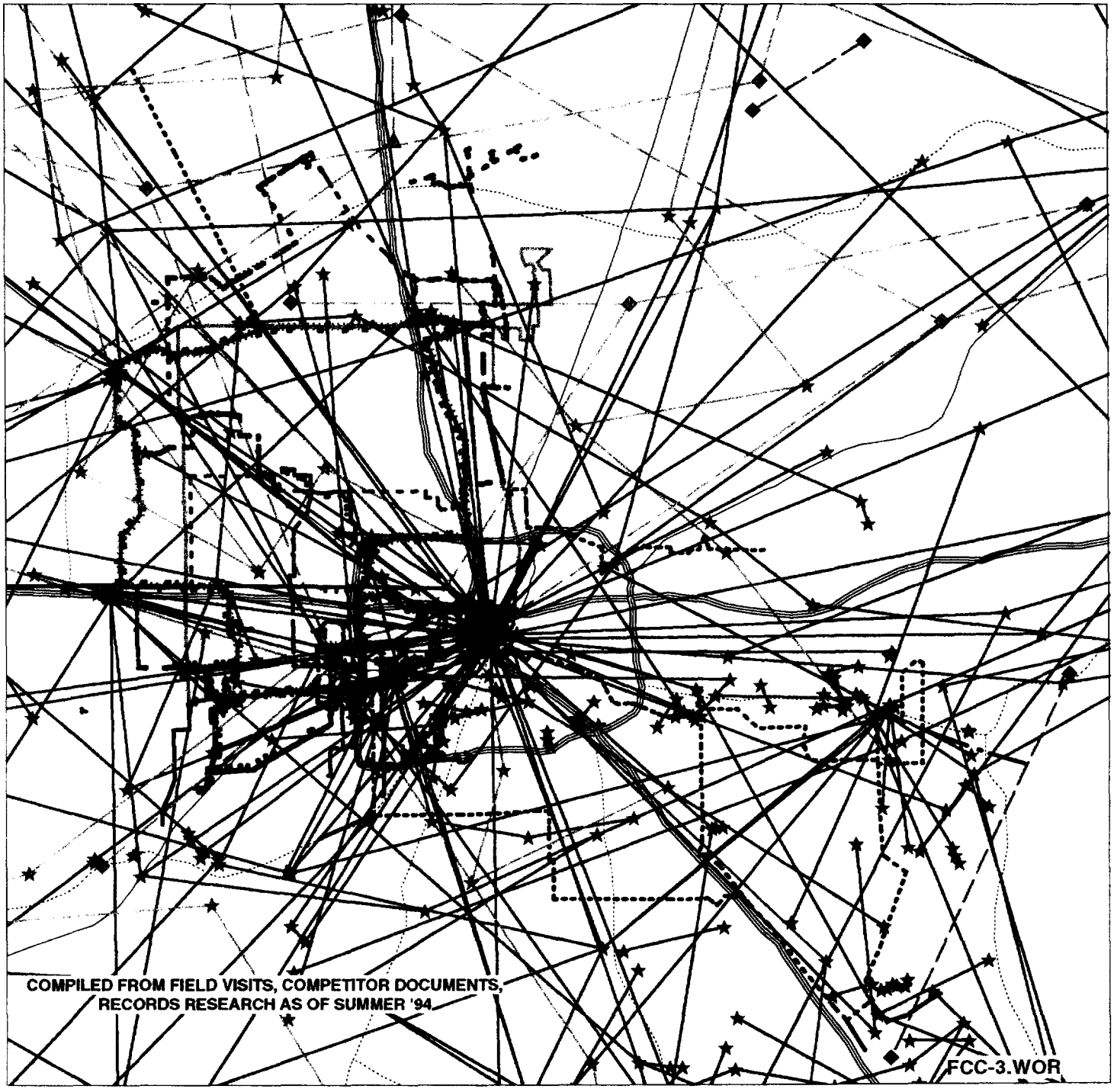
LEGEND

- HL&P
- PHONOSCOPE
- TELEPORT
- MFS
- TIME WARNER
- US SPRINT
- MCI
- EAST TEXAS FIBERLINE
- ELECTRA

MICROWAVE

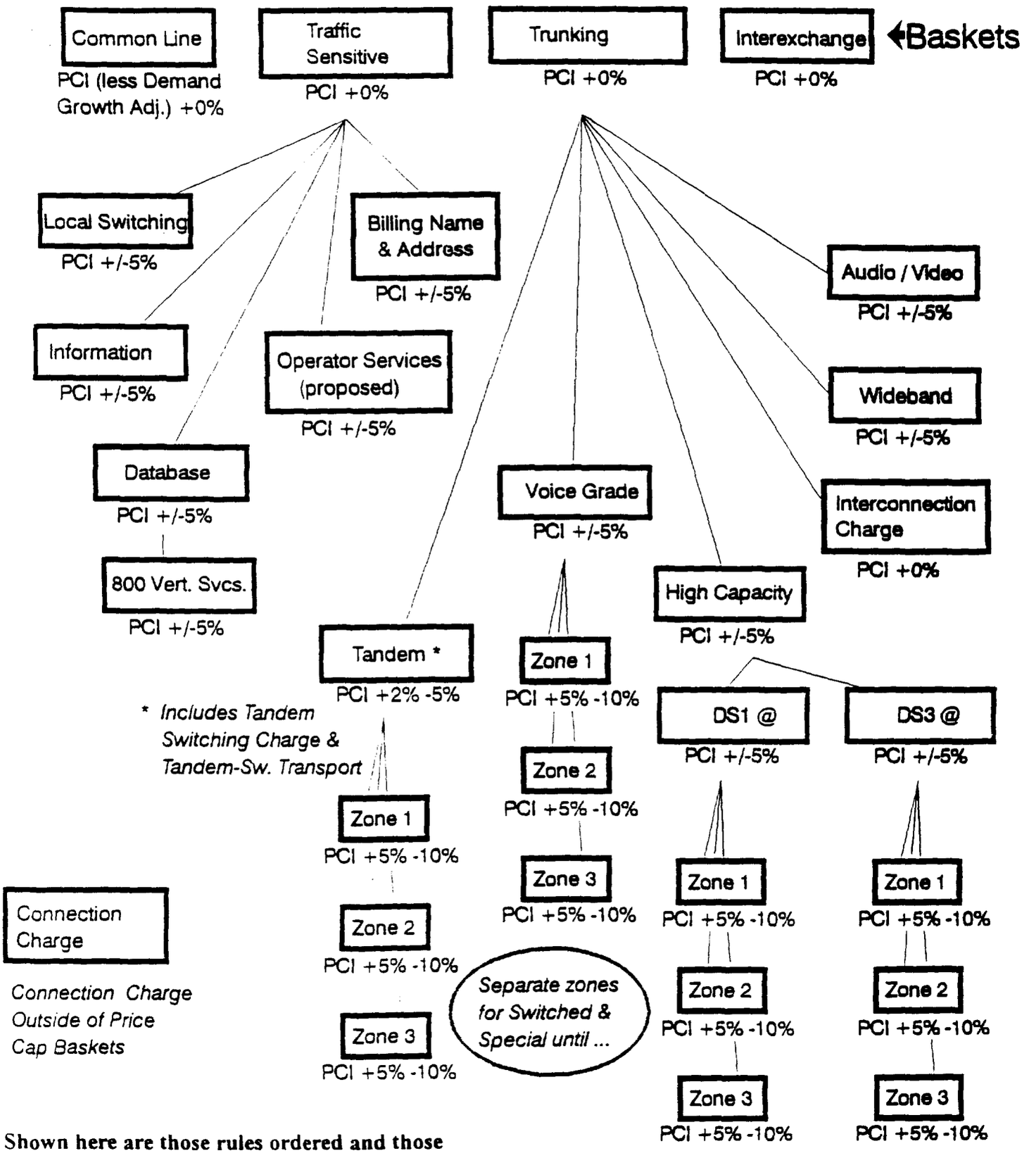
- CELLULAR / PAGING
- COMMON CARRIER
- AT&T
- END USER
- LEC
- SWBT



HOUSTON COMPETITIVE NETWORKS

LEC Price Cap Plan
as of 2-1-94, with Proposed Changes

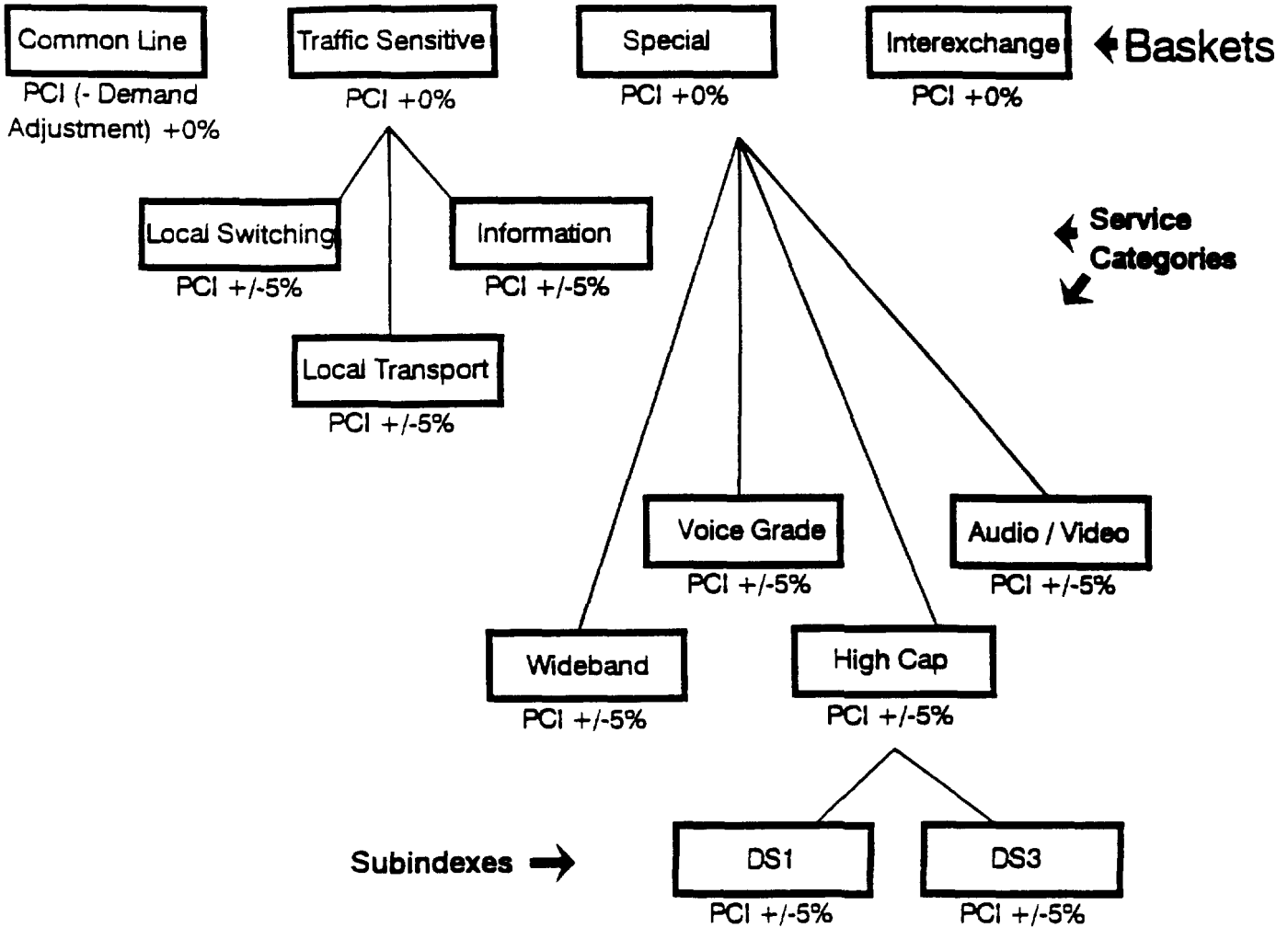
Each Basket has its own Price Cap Index (PCI) = Inflation - Productivity Offset +/- Exogenous.



Shown here are those rules ordered and those proposed by the FCC. The transport structure is that contained in CC Docket No. 91-213, Second Report and Order, released 1-31-94.

LEC Price Cap Plan
At Implementation (1-1-91)

Each Basket has its own Price Cap Index (PCI) = Inflation - Productivity Offset +/- Exogenous.



Productivity Offset 3.3%, with 4.3% option.
50/50 Sharing, with eventual 100% sharing.

Excluded from price caps: special construction; packet switching; PIC change charges; air-ground service; contract offerings in combination with interexchange carriers for services to the Federal Government.