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FEDERAL COMMUNICATIONS COMMISSION  
OFFICE OF SECRETARY

February 15, 1995

**EX PARTE**

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

RE: CC Docket No. 94-1

DOCKET FILE COPY ORIGINAL

Today, Bell Atlantic is filing the attached written Ex-Parte in the aforementioned proceeding. The attached is a copy of Bell Atlantic's Response to the Comments on USTA's Ex-Parte Proposal.

Please include this letter and the attached into this record as appropriate.

Sincerely,



## Attachment

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R. Welch  
K. Wallman  
R. Metzger  
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Before The  
FEDERAL COMMUNICATIONS COMMISSION  
Washington, D.C. 20554

FEDERAL COMMUNICATIONS COMMISSION  
OFFICE OF SECRETARY

_____	)	
	)	
In the Matter of	)	
	)	
Price Cap Performance Review	)	
for Local Exchange Carriers	)	CC Docket 94-1
	)	
Notice of Proposed Rulemaking	)	
	)	
	)	
_____	)	

BELL ATLANTIC RESPONSE TO COMMENTS ON  
USTA'S EX PARTE PROPOSAL

This filing responds to comments critical of the United States Telephone Association's ("USTA") *ex parte* proposal filed January 18, 1995. While most of the comments on the proposal were positive, several commenters were critical of the proposal in general and the portions relating to pricing regulation in particular.

In its direct and reply comments in response to the Notice of Proposed Rulemaking, Bell Atlantic<sup>1</sup> explained why pure price caps stimulate regulated companies to reduce cost, anticipate customer desires for new products, eradicate any conceivable incentive to cross subsidize services, and increase investment in the

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<sup>1</sup> The Bell Atlantic telephone companies ("Bell Atlantic") are Bell Atlantic-Delaware, Inc.; Bell Atlantic-Maryland, Inc.; Bell Atlantic-New Jersey, Inc.; Bell Atlantic-Pennsylvania, Inc.; Bell Atlantic-Virginia, Inc.; Bell Atlantic-Washington, D.C., Inc.; and Bell Atlantic-West Virginia, Inc.

telecommunications infrastructure.<sup>2</sup> At the same time, pure price caps protect customers by forbidding any increase, and indeed requiring a reduction, in the real price of regulated services. In other proceedings, some of the parties that commented against the USTA proposal have themselves benefitted from pure price caps.<sup>3</sup> Moreover, even the cable TV industry recently went on record supporting the adoption of pure price caps for local exchange carriers ("LECs").<sup>4</sup>

Here, however, none of the comments opposing USTA's compromise proposal contradict or even address these fundamental benefits of pure price caps. Instead, they seek to distract attention from these fundamental benefits with irrelevant asides, and even obscure the debate by ignoring the actual impact of the USTA proposal. Bell Atlantic still endorses a move to pure price caps based on historical total factor productivity without additional add-ons to the offset or one-time reductions in indices. Like Ameritech, however, Bell Atlantic recognizes that the USTA proposal on price

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<sup>2</sup> Comments of Bell Atlantic at 7-12 (filed May 9, 1994); Reply Comments of Bell Atlantic at 7-14 (filed June 29, 1994), and attached affidavits of Dr. Alfred E. Kahn at 9-13 ("Kahn Affidavit") and Dr. James H. Vander Weide at 11-15 ("Vander Weide Affidavit").

<sup>3</sup> *Policy & Rules Concerning Rates for Dominant Carriers*, 4 FCC Rcd 2873 at ¶ 251 (1989) (no sharing mechanism adopted for AT&T); *Implementation of the 1992 Cable Act - Rate Regulation*, 9 FCC Rcd 1164 at ¶¶ 89-90 (1993) (no sharing mechanism adopted for cable).

<sup>4</sup> "On pure price caps, we agree that pure price caps ought to be applied to telephone companies . . ." See Audiotape of *Ex Parte* Panel Discussion of Computer III Remand Issues (Jan. 30, 1995).

regulation "*as a package* constitutes a reasonable compromise of all parties' interests."<sup>5</sup>

**The USTA Proposal Is Timely.**

Without citing any rule or limitation on *ex parte* comments, several parties claim that there is some procedural flaw in USTA offering this compromise after the commenting rounds.<sup>6</sup> This ignores the very nature of the USTA proposal -- a compromise of conflicting positions. Only after the positions of the LECs and other parties were fully explored on the record would it make any sense to offer a middle ground.<sup>7</sup> Those parties critical of the proposal ask the Commission to ignore a salient response to the concerns they themselves raise, because it was only offered after they raised those concerns.

**The Moving Average Answers the Critics of Pure Price Caps.**

More fundamentally, the opposition comments ignore the benefits that the USTA proposal offers. For example, parties suggest that the USTA proposal will lower the productivity offset in future years,<sup>8</sup> or that the proposal will fail to capture

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<sup>5</sup> Ex Parte Comments of Ameritech at 1.

<sup>6</sup> *See, e.g.*, Comments of Time Warner at 4-5.

<sup>7</sup> The open nature of the *ex parte* rules foreclose any due process concerns. In addition to the ongoing right to submit comments in this docket, the Commission took the step of placing the USTA proposal on public notice, thereby providing supplementary assurance that all parties had notice and opportunity to comment on the proposal.

<sup>8</sup> MCI Comments at 6.

potential future productivity increases.<sup>9</sup> Such arguments ignore the very nature of a moving average.<sup>10</sup> If, as these commenters suggest, LEC productivity growth is truly moving upward, the moving average will capture that increase and produce corresponding reductions in the price indices for LEC services. Use of a moving average annuls the debate of what is a reasonable expectation of future productivity growth.<sup>11</sup> No matter what the future holds, the

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<sup>9</sup> GSA Comments at 5-6.

<sup>10</sup> Other commenters, such as AT&T, argue that technical concerns over the index and the ease of its implementation counsel against USTA's proposal. These commenters fail to recognize that any *valid* technical concerns can be addressed by the Commission, but cannot outweigh the need for this fundamental advance in regulation. These alleged concerns cannot justify reintroducing flawed alternatives to a proper total factor productivity study. *Compare* MCI Comments at 9 *with* Reply Comments of USTA at 53-61 (filed June 29, 1994).

MCI also is wrong to suggest that there would be no reduction in administrative burdens under the USTA proposal. MCI Comments at 4. On the contrary, the USTA proposal will eliminate the significant burdens inherent in the current system of duplicative price and earnings regulation.

<sup>11</sup> Several parties also point to non-productivity based measures such as earnings to argue that LEC productivity growth is increasing. *See, e.g.*, MCI Comments at 7. But earnings are not a measure of productivity and can not be used as such. To the extent that increased returns are indicative of actual productivity growth, the USTA productivity average will capture that growth. Moreover, these comments focus on accounting earnings which, unlike economic rates of return, rely on arbitrary factors that undermine their value as a reliable measure of a company's returns. *See* Vander Weide Affidavit at 5-8.

price index will reflect actual productivity growth and customers will be protected.<sup>12</sup>

**Other Criticisms of the USTA Pricing Proposals Are Misplaced.**

Arguments against other aspects of the USTA pricing proposals are similarly deficient.<sup>13</sup> For example, MCI argues that Part 69 waiver requirements for new services are still required to evaluate rates and promote uniformity. MCI fails to acknowledge that the required waivers are for **new** services which, by definition, are discretionary.<sup>14</sup> There is no need to regulate rates of these new services, much less require a separate Part 69 proceeding to evaluate rate structure.

Moreover, there is no need to maintain a Part 69 waiver requirement to promote uniformity. The competition for most of

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<sup>12</sup> MCI correctly suggests that the moving average should not apply to LECs' interexchange basket services. As Bell Atlantic previously explained, these and other services for which competitive alternatives should be removed from price regulation altogether, and allow prices to be set by the competitive marketplace. Comments of Bell Atlantic at 21-22 (filed May 9, 1994), and attached Affidavit of Richard E. Beville at 15-17 ("Beville Affidavit").

<sup>13</sup> Consistent with USTA's proposal that the first step in the Commission's evaluation of the current regulation should be the price index mechanism, this **ex parte** does not address comments on USTA's adaptive regulation proposals. Regardless of future competition standards, however, the Commission's initial order should remove from price cap regulation services such as interstate intraLATA toll service and interstate interLATA corridor service, high capacity services and video dialtone that are clearly competitive. See Bell Atlantic Comments at 19-23, Beville Affidavit at 15-20. MCI's arguments concerning retaining current band limitations on competitive high capacity services ignore the reality of competitive alternatives for these services. Compare MCI Comments at 10-11 **with** Beville Affidavit at 17-19.

<sup>14</sup> See Kahn Affidavit at 14.

these services comes from unregulated competitive access providers and even from interexchange carriers like MCI. Uniformity requirements that only apply to LEC prices mean little among these competitors that are not hampered by the same Part 69 requirements.

Regardless of whether Part 69 requirements are retained, the Commission still can evaluate new services and the prices charged for them in the tariffing process, just as it is required to do for Bell Atlantic's competitors.<sup>15</sup>

AT&T argues that a one-time reduction in the price index is "illusory" because LECS already price significantly below their allowed price index.<sup>16</sup> While this suggests that competitive pressure already is supplanting the need for price regulation, it can hardly be used as a justification to impose punitive price reductions that would significantly exceed any price changes that would result from an appropriate productivity formula.

### Conclusion

The Commission recognized the efficacy of pure price caps when it authorized such a structure for the cable industry and for AT&T. Even the cable industry recognizes that the same logic holds true for the LECs. The USTA compromise proposal fully addresses all reasonable concerns originally expressed over the adoption of pure

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<sup>15</sup> *AT&T v. FCC*, 978 F.2d 727 (D.C. Cir. 1992), *cert. denied*, 113 S. Ct. 3020 (1993).

<sup>16</sup> AT&T Comments at 8.

price caps. As a result, the Commission should move forward and adopt pure price caps for LECs.

Respectfully submitted,

The Bell Atlantic Telephone Companies  
By Their Attorneys

Edward D. Young, III  
Of Counsel



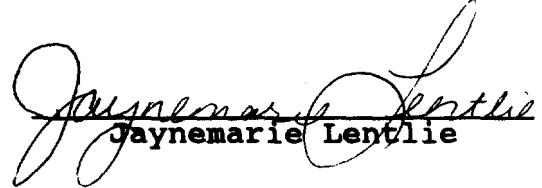
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Dated: February 15, 1995

CERTIFICATE OF SERVICE

I hereby certify that a copy of the foregoing ex parte letter and attachment was served this 15th day of February, 1995 by first class mail, postage prepaid, on the parties on the attached list.

  
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