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March 22, 1995

The Honorable Rachelle B. Chong
Commissioner
Federal Communications Commission
1919 M. St. N.W. Room 844
Washington, D.C. 20554

Dear Commissioner Chong:

I want to thank you for being so generous with your time on the Price Cap issues. I know these matters are complex and time-consuming, but the outcome is critical to the future of the regulated telephone business. In thinking about our meeting, I believe there are three issues that need to be clarified - they are as follows:

Concern #1: "*The Local Exchange Carriers are making too much money.*" We've heard this time and again and it just doesn't comport with reality. Even with the unfavorable regulatory treatment of depreciation, which substantially overstates our reported earnings, we are still very much in line with the S&P 500. And if we could take the same depreciation treatment as the Cable industry, then we'd probably have negative earnings. It also is worth noting, as shown in attachments A & B, that since the LEC price cap plan was implemented on January 1, 1991, a market weighted average price of RHC and GTE stocks has underperformed the S&P 500 and has substantially underperformed IXC stocks. (AT&T & MCI)

Concern # 2: "*The Regional Bell Companies all have a huge free cash flow.*" Free cash flow is defined as operating cash flow less capital expenditures. In BellSouth's case, our 1994 operating cash flow was $5,172M, of which $3,600M was spent on various types of telecommunications plant and equipment. This left the company with $1,572M in free cash flow of which $1,370M was paid out in dividends to our shareowners. That left $202M of uncommitted free cash. By comparison, in 1994, AT&T's operating cash flow was $8,956M of which $4,853M was spent on plant and equipment. Of the remaining $4,103M in free cash flow, AT&T paid $1,870M in dividends. That left $2,233M of uncommitted free cash -- more than 10 times as much as BellSouth's, even though the AT&T operating cash flow was less than double that of BellSouth.

Concern # 3: *"The Bell Companies are monopolies and shouldn't have regulatory relief."* Wrong again. In the interstate exchange access market, which is the market regulated by the FCC, BellSouth has multiple competitors in every one of our states. The FCC, of all people, should understand this issue since the FCC created this competition in the special access and switched access interconnection dockets several years ago, after the first price cap plan was implemented. There is every reason to move away from a rate-of-return based plan and toward the more flexible plan that the Commission has granted to AT&T and the cable industry. The Commission made a conscious and appropriate decision not to impose a productivity number on the cable industry. Nor did the Commission make any upward adjustment to AT&T's productivity factor of 3.0% when it last reviewed AT&T's price cap plan in July 1993. Now why should we be treated differently?

The exchange carriers have reduced their access prices by more than 55% since divestiture, accounting for virtually the entire reduction in interstate long distance rates. Since 1991, the three biggest long distance companies have been raising their rates, and, in fact, have bragged about it. Indeed in it's 1993 annual report to shareholders, AT&T noted:

> "In the latter half of 1993, we (AT&T) raised some of our prices and fees--about $500 million on an annual basis. These increases were primarily for services where customer demand is not very sensitive to price. In late December we filed for 1994 price increases of $750 million on annual basis and also announced a new discount plan for high-volume callers. In January 1994 we also proposed to raise prices for some business services by $165 million on an annual basis...We expect improving economic conditions and higher prices to cause our telecommunications services to grow faster in 1994 than in 1993...Total costs of telecommunications services declined this past year; costs in 1992 were about level with those in 1991. Despite higher calling volumes, access and other

> interconnection costs dropped both years largely because of lower prices from telephone companies to reach customers over local networks."

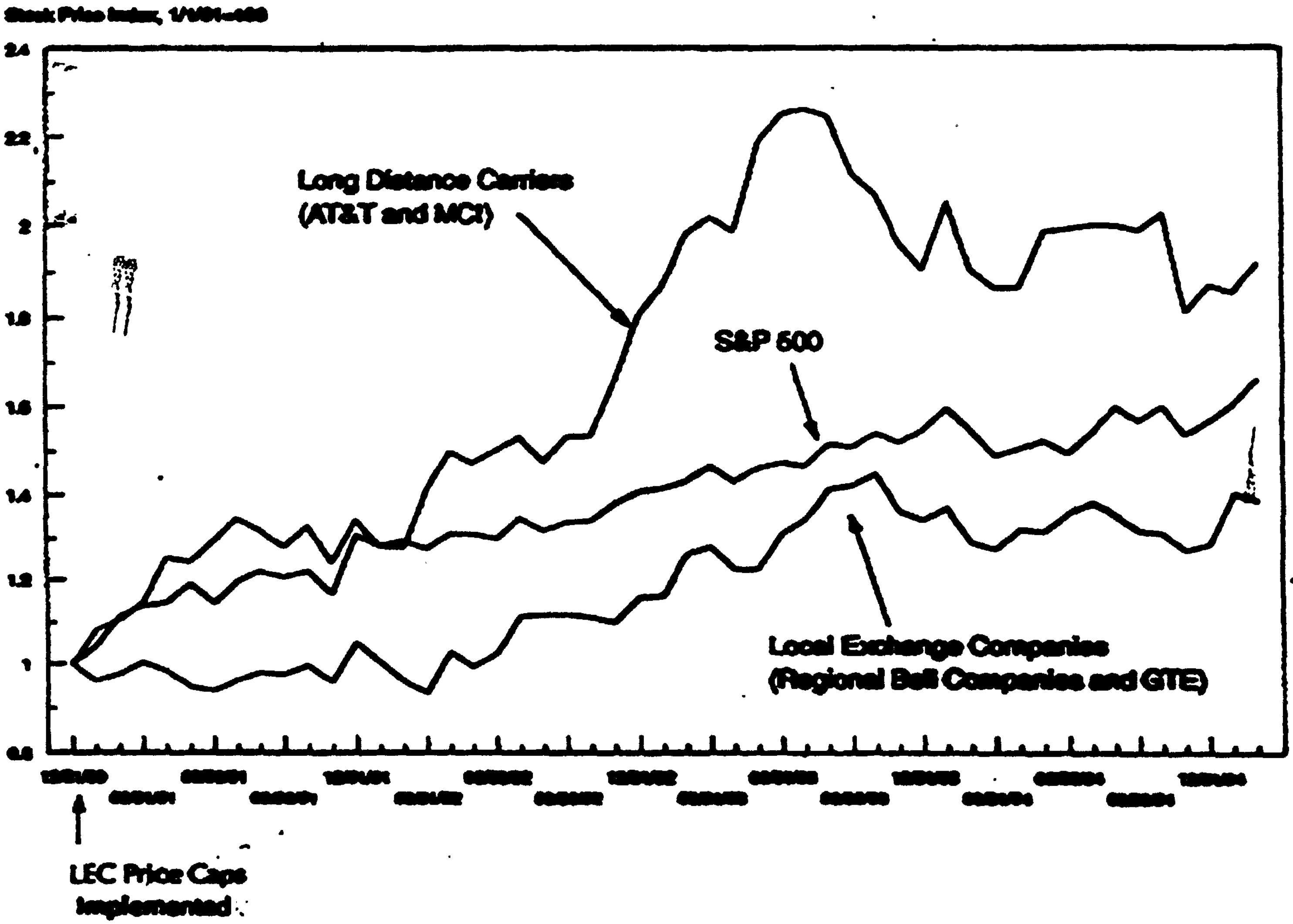
Attachment C contains some quotes from analysts on Wall Street that make it clear that the financial community hasn't been fooled by their activity. And IXC stock prices reflect this, as you can see from attachment B; the IXC's interstate tariffed rates deliver the kind of price trend that Wall Street loves.

Commissioner, it's time for the FCC to realize how quickly this industry is changing and revise the regulatory regime along with that change. The Price Cap docket is the time to do this.

Sincerely,

John L. Clendenin

Trends in Telecom Stock Prices
Since Implementation of LEC Price Cap Plan



Source: One Source; Indices are based on market weighted monthly averages.

Performance of Telecom Stock Prices Since Implementation of LEC Price Cap Plan

Price Per Share	Ameritech	Bell Atlantic	BellSouth	GTE	Nynex	Pacific Telesis	SBC	U S West	LEC Weighted Average
Mar 3, 1995	42.125	52.125	57.250	33.125	39.125	29.375	41.000	38.375	42.612
Dec 31, 1990	27.234	43.058	43.916	23.227	28.058	21.468	23.325	30.887	31.371
% Change	35.35%	17.40%	23.29%	29.88%	28.29%	26.96%	43.11%	19.51%	26.21%

Price Per Share	AT&T	MCI	IXC Weighted Average
Mar 3, 1995	51.250	19.750	46.744
Dec 31, 1990	26.905	9.833	24.075
% Change	47.50%	50.21%	48.50%

Index	S&P 500
Mar 3, 1995	485.408
Dec 31, 1990	293.409
% Change	39.55%

Source: OneSource; weighted averages are based on market values of outstanding shares for individual companies

The View From Wall Street: Competition in the Long Distance Telephone Market

AT&T and its rivals are pushing some prices up after almost 10 years of steady discounting. This gives AT&T more room to grow profits, and it creates an umbrella over MCI and Sprint, allowing them to raise prices, too. *(Kenneth Leon, Bear Stearns, 10/20/93)*

AT&T, MCI, and Sprint all have high-quality earnings because they operate in a stable, oligopolistic industry. . .without serious price competition. [T]he only real threat [is] posed by the Regional phone companies which are unlikely to gain regulatory freedom to enter this business for at least 3-5 years. *(Philip A. Managieri, Cowen, 8/23/93)*

Margins improved for all four [long distance] carriers, reflecting an impact from price increases and steady declines in access costs. *(Daniel P. Reingold and Richard C. Toole, Merrill Lynch, 2/10/94)*

The combination of a cozy oligopoly that wishes to avoid price wars and falling operating expenses primarily due to [exchange] access cost reductions is an unbeatable environment in which to do business. *(Timothy N. Weller and Nick Frelinghuysen, Donaldson, Lufkin & Jenrette, 6/1/94)*

The long distance industry is one of today's premier growth industries. Where else can you find: (1) double-digit unit volume growth, (2) declining unit costs, on a nominal as well as real basis, (3) a $10 billion barrier to entry, (4) a benign, stable oligopoly where the price leader [AT&T] is looking to generate cash to fund other ventures, and (5) a prohibition on competition. . . It is rare to see a full-fledged price war in an oligopolistic market, witness soft drinks. The same holds true in the long distance market. *(G.W. Woodfin and E. Strumingher, Dean Witter, 10/28/94)*

Many investors still seem to believe that there has been some sort of "price war" among the major interexchange carriers. The fact is that although interstate telephone rates have come down by about 50% over the past decade, the entire decline has been "funded" by decreases in the amounts paid by interexchange carriers to the local exchange carriers for "access." *(John Bain, Raymond James & Assoc., 1/12/95)*

Overall, MCI's new Friends & Family program looks like just another round of discounting funded by previously announced increases in the base rates. By focusing on the discount instead of the rate, the industry has been able to quietly raise base rates while spending millions of dollars promoting ever-increasing discounts. *(D. Reingold and M. Kastan, Merrill Lynch, 1/20/95)*

Regardless of your carrier, you are paying higher and higher rates if you are among the tens of millions of Americans who have not signed up for a discount calling plan. The person paying the retail rate is bearing the disproportionate burden. And these are probably the people who can't afford to make a lot of phone calls and therefore [do not] qualify for those cheaper plans. *(D. Briere, Tele-Choice Inc., 1/21/95)*

AT&T now has the same revenues as the entire Bell system just before the break up in 1984, when they spun off about 85 percent of their assets. *(John Bain, Raymond James & Assoc., 1/24/95)*

MCI. . . filed for a 3.9% across-the-board rate increase. We fully expect AT&T, Sprint, and the second tier carriers to follow suit. This move by MCI is extremely bullish for the long distance stocks since it sends a clear message to the investment community that the long distance industry will practice 'safe pricing' which will lead to stable revenue per minute trends. *(Jack B. Grubman, Salomon Brothers, 2/6/95)*