Before the
FEDERAL COMMUNICATIONS COMMISSION
Washington, D.C.

FCC 95-200

In the Matter of

Local Exchange Carriers' Rates, Terms, and Conditions for Expanded Interconnection Through Virtual Collocation for Special Access and Switched Transport) CC Docket No. 94-97, Phase I

REPORT AND ORDER

Adopted: May 11, 1995; Released: May 11, 1995

By the Commission:

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I. INTRODUCTION

1. On February 28, 1995, the Common Carrier Bureau (Bureau) released the *Phase I Designation Order*,[1] which designated key rate level issues in the first phase of the Bureau's investigation of the virtual collocation tariffs filed by the Tier 1 local exchange carriers[2] (LECs) listed in Appendix A.[3] Specifically, the Bureau designated for investigation: (1) whether the overhead loadings[4] established in the LECs' virtual collocation tariffs are justified; and (2) whether the maintenance-related charges in Bell Atlantic's virtual collocation tariffs are justified.[5] The LECs' virtual collocation tariffs were the subject of the Bureau's *Virtual Collocation Tariff Suspension Order* in this docket, which partially suspended the LECs' virtual collocation tariffs pursuant to Section 204(a) of the Communications Act of 1934, as amended (Act), 47 U.S.C. § 204(a), initiated an investigation into the lawfulness of these tariffs, imposed an accounting order, rejected patently unlawful terms and conditions, and ordered other tariff revisions.[6]

2. Based on our review of the LECs' direct cases and accompanying cost support data filed in response to the *Phase I Designation Order*, we conclude that most of the LECs have failed to meet their Section 204(a) burden of demonstrating that their overhead loading levels and, consequently, their virtual collocation rates, are just and reasonable.[7] We

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[1] Local Exchange Carriers' Rates, Terms, and Conditions for Expanded Interconnection Through Virtual Collocation for Special Access and Switched Transport, CC Docket No. 94-97, Phase I, Order Designating Issues for Investigation, DA 95-374 (rel. Feb. 28, 1995) (*Phase I Designation Order*).

[2] Tier 1 local exchange carriers are companies having annual revenues from regulated telecommunications operations of $100 million or more for a sustained period of time. Commission Requirements for Cost Support Material To Be Filed with 1990 Annual Access Tariffs, Order, 5 FCC Rcd 1364 (1990).

[3] Appendix A provides the full and abbreviated names of these LECs as used in this Order.

[4] An overhead loading is the amount by which the direct costs of a service are increased in order to recover overhead costs, which are common costs not directly attributable to a particular service. *See* Ameritech Operating Companies, *et. al.*, CC Docket No. 93-162, Order, 8 FCC Rcd 4589, 4594 n.70 (1993). Overhead costs include general administrative expenses, general support facilities, and other costs, such as marketing, that are not assigned to a specific service.

[5] We will address this issue in a subsequent order in this docket. *See* note 39, *infra*.

[6] Ameritech Operating Companies, *et. al.*, CC Docket No. 94-97, Order, DA 94-1421, 10 FCC Rcd 1960, Appendix C (1994) (*Virtual Collocation Tariff Suspension Order*).

[7] Section 204(a)(1) provides, in pertinent part, that "the burden of proof to show that the new or revised charge, or proposed charge, is just and reasonable shall be upon the carrier ...." 47 U.S.C. § 204(a)(1).

therefore find these rates to be unlawful. In order to advance the competitive goals of this Commission's new mandatory virtual collocation policy, we prescribe in this Order the maximum permissible overhead loading levels for these LECs' virtual collocation rates.

3. As set forth below, we prescribe on a permanent basis the maximum permissible overhead loading levels for virtual collocation rates filed by Bell Atlantic, BellSouth, GTE, United, and US West. In addition, we prescribe on an interim basis the maximum permissible overhead loading levels for SWB pending further investigation of its overhead loadings. At the completion of our investigation, we will prescribe on a permanent basis just and reasonable overhead loading levels for SWB, and, if necessary, for Ameritech and CBT.[8] Our interim prescription is subject to a two-way adjustment mechanism that will protect both customers and LECs in the event refunds or supplemental payments are warranted at the conclusion of our investigation.

II. BACKGROUND

4. In the *Virtual Collocation Order*,[9] this Commission adopted virtual collocation as the basic architecture for providing expanded interconnection services.[10] We required Tier 1 LECs, other than participants in National Exchange Carrier Association pools, to provide expanded interconnection for special access and switched transport services[11] through generally available virtual collocation arrangements.[12]

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[8] As discussed in para. 17, *infra*, SWB, Ameritech and CBT requested confidential treatment of certain cost support data filed with their direct cases. We note that the Bureau's *Virtual Collocation Tariff Suspension Order* did not adjust the overhead loading levels for Ameritech, CBT, and two study areas within the United companies. *See Virtual Collocation Tariff Suspension Order*, Appendix C at 2.

[9] Expanded Interconnection with Local Telephone Facilities, CC Docket No. 91-141, Memorandum Opinion and Order, 9 FCC Rcd 5154 (1994) (*Virtual Collocation Order*).

[10] Expanded interconnection is a LEC offering that enables parties to compete on a facilities basis with certain LEC services by interconnecting their circuits with those of the LEC at the LEC central office. Expanded interconnection through virtual collocation enables an interconnector to terminate its circuits in central office transmission equipment owned by the LEC and under the physical control of the LEC. The interconnector has the right to designate its choice of central office equipment, which is dedicated to the exclusive use of the interconnector, and installed, maintained and repaired by the LEC. *Virtual Collocation Order*, 9 FCC Rcd at 5158.

[11] Interstate access is a service traditionally provided by LECs that enables interexchange carriers and other customers to originate and terminate interstate telephone traffic. *Id.* at 5155 n.2.

[12] *Id.* at 5156.

5. In adopting pricing rules to govern the provision of virtual collocation services, we stated in the *Virtual Collocation Order* that LECs' rates must be derived from the direct costs of providing expanded interconnection service, plus a reasonable amount of overhead costs.[13] We expressed concern that LECs could attempt to load excessive overhead costs on their interconnection charges. Based on the extensive record then before us, we reaffirmed our decision in earlier orders that LECs may include no more than uniform overhead loadings in their rates for expanded interconnection services, or must justify any deviations from uniform loadings.[14] In other words, LECs may not recover a greater share of overhead costs in their rates for virtual collocation services than they recover in rates for "comparable services," absent justification.[15] The Commission explained that the LECs have the burden of demonstrating that their interconnection charges meet this overhead loading standard, and are otherwise just, reasonable, and not unreasonably discriminatory. We noted that we would scrutinize carefully the overhead costs that the LECs propose to recover through interconnection charges to ensure that they are reasonable.[16]

6. The *Virtual Collocation Order* directed LECs to file tariffs offering virtual collocation services[17] on September 1, 1994, to become effective on December 15, 1994.[18]

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[13] *Id.* at 5189-91. In the *Special Access Expanded Interconnection Order*, we required the LECs to create new connection charge elements for expanded interconnection rather than formally unbundle the special access rate structure into separate transmission and connection charges, because the services provided to the interconnectors are not entirely parallel to the services provided to the LEC special access customers. Expanded Interconnection with Local Telephone Company Facilities, CC Docket No. 91-141, Report and Order and Notice of Proposed Rulemaking, 7 FCC Rcd 7369, 7425 (1992) (*Special Access Expanded Interconnection Order*).

[14] *Virtual Collocation Order*, 9 FCC Rcd at 5189.

[15] *Id.*

[16] *Id.*

[17] *Id.* at 5156, 5167-68. The Commission, however, exempted LECs from the mandatory virtual collocation requirement in central offices in which they chose to provide a Title II physical collocation offering. *Id.* at 5156, 5211.

[18] In conjunction with its tariff filing, SWB requested confidential treatment of its cost support submission on the grounds that public disclosure would reveal proprietary vendor data. On November 1, 1994, the Bureau ruled that SWB's cost support submission was exempt from disclosure under Exemption 4 of the Freedom of Information Act (FOIA), 5 U.S.C. § 552(b)(4), subject to limited disclosure to parties to the proceeding under a protective order. *See* Letter from Kathleen M.H. Wallman, Chief, Common Carrier Bureau, to MFS, MCI, and ALTS, Freedom of Information Act Request Control Nos. 94-310, 325, 328, DA 94-1214, rel. Nov. 1, 1994, *app. for rev. pending.* (*November 1, 1994 FOIA Ruling*).

The Bureau's *TRP Order*,[19]
released concurrently with the *Virtual Collocation Order*, required LECs to file certain cost support data in connection with their rates for virtual collocation services. In particular, the Bureau directed LECs to provide information regarding their overhead loadings for virtual collocation services and for their comparable DS1 and DS3 services.[20]

7. The Bureau specified that comparable services include all point-to-point DS1 and DS3[21] special access and switched transport services.[22] The Bureau determined that LECs offer these point-to-point services in two basic forms: (1) as a service providing channel termination without interoffice mileage, connecting the customer premise and the nearest central office; and (2) as a service providing both channel termination and interoffice mileage, connecting the customer to an additional central office.[23] The Bureau also stated that comparable DS1 and DS3 services include the LECs' generic electrical or optical services, discounted volume and term services, and specialized service offerings, such as self-healing networks.[24]

8. On September 1, 1994, the LECs listed in Appendix A filed interim and permanent virtual collocation tariffs and cost support data. The interim tariffs, which were identical in substance to the LECs' permanent virtual collocation tariffs, ensured the

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19 Commission Requirements for Cost Support Material To Be Filed with Virtual Collocation Tariffs for Special Access and Switched Transport, Tariff Review Plan Order, 9 FCC Rcd 5679 (1994) (*TRP Order*).

20 *TRP Order*, 9 FCC Rcd at 5683.

21 DS1 is a digital high-capacity service with transmission capability equal to 24 voicegrade channels with a total transmission rate of 1.544 megabits per second; a DS3 is a digital high-capacity service with transmission capability equal to 28 DS1s.

22 *TRP Order*, 9 FCC Rcd at 5682-83. A point-to-point service provides a connection between the customer premise (which, for an interexchange carrier, would likely be its point of presence) and another location (which may be another customer premise or a LEC central office). All point-to-point services employ the same basic types of equipment, such as a central office entrance cable, an equipment bay containing an optical line terminating multiplexer, and a cross-connect. *Virtual Collocation Tariff Suspension Order* at para. 17. The cross-connect consists of a short cable that connects the LEC distribution frame to the central office electronic equipment dedicated to the interconnector.

23 *Virtual Collocation Tariff Suspension Order* at para. 18. For a description of services providing channel termination and channel mileage, *see* note 92, *infra*.

24 *TRP Order*, 9 FCC Rcd at 5684-85. The Bureau also required LECs to submit direct cost studies for their point-to-point services, as well as the costing methodologies used to develop the direct costs. *Id.* at 5685. *See also Virtual Collocation Tariff Suspension Order* at para. 18.

uninterrupted availability of tariffed expanded interconnection service during the period between the effective date of the interim virtual collocation tariffs and December 15, 1994, the date the permanent virtual collocation tariffs were to become effective. On September 2, 1994, following a preliminary review of the LECs' interim tariffs, the Bureau concluded that these tariffs raised significant questions of lawfulness that warranted suspension for one day, investigation, and imposition of an accounting order.[25] Following that one day suspension, the LECs' interim tariffs took effect on September 4, 1994, subject to investigation.

9. On December 9, 1994, the Bureau released the *Virtual Collocation Tariff Suspension Order* which, *inter alia*, suspended for one day the permanent virtual collocation tariffs, initiated an investigation into the lawfulness of these tariffs, and imposed an accounting order.[26] With certain exceptions discussed below, the permanent tariffs took effect on September 15, 1994, subject to investigation.

10. In the *Virtual Collocation Tariff Suspension Order*, the Bureau found that the LECs' level of overhead loadings was a primary factor affecting the apparently excessive virtual collocation rates. To determine whether the LECs had justified their proposed overhead loadings, the Bureau utilized the overhead loading standard set forth in the *Virtual Collocation Order*. The Bureau's review of the record revealed that none of the LECs used uniform loadings for all of their comparable DS1 and DS3 services. Moreover, the Bureau found substantial differences between the virtual collocation overhead loadings and those applied to comparable services.[27]

11. In the *Virtual Collocation Tariff Suspension Order*, the Bureau determined that the LECs had not attempted to show that the differences in the overhead loadings were due to differences in overhead costs incurred by the services.[28] Based on the record, the Bureau concluded that the LECs were strategically assigning high overhead loadings to deter efficient entry by interconnectors into the interstate access service market. The Bureau found that LECs tended to assign low overheads in markets where they faced actual or potential competition from interconnectors, and high overheads where they did not. The Bureau further determined that it appeared that this Commission's policy of facilitating efficient competitive entry into the interstate access service market would be frustrated by the practice of assigning high overheads to essential LEC facilities upon which interconnectors rely to

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[25] *See* Ameritech Operating Companies, *et. al.*, CC Docket No. 94-67, Order, 9 FCC Rcd 5230 (Com. Car. Bur. 1994).

[26] *Virtual Collocation Tariff Suspension Order* at para. 3. The Bureau also consolidated its investigations of the interim and permanent tariffs, noting that an upcoming order would designate specific issues for investigation relating to both sets of tariffs. *Id.*

[27] *Id.*

[28] *Id.* at para. 21.

provide competitive services, while assigning low overheads to the services against which interconnectors are trying to compete. The Bureau, therefore, found that absent justification, this practice is unreasonable.[29]

12. To facilitate efficient competitive entry into the interstate access service market, the Bureau imposed an interim adjustment pending further investigation of the LECs' overhead loadings. Pursuant to its authority under Section 204(a) of the Act, the Bureau partially suspended for a five-month period that part of the LECs' proposed overhead loadings that exceeded, without adequate justification, the lowest overhead loadings assigned to the LECs' comparable DS1 and DS3 services. The Bureau noted that an "average overhead loading" standard would not preclude LECs from engaging in anticompetitive behavior.[30]

13. The Bureau adjusted the LECs' rates so that the rate for each rate element dedicated to DS1-level expanded interconnection services would reflect the lowest overhead loadings assigned to the LECs' comparable DS1 services; the rate for each rate element dedicated to DS3-level expanded interconnection services would reflect the lowest overhead loadings assigned to the LECs' comparable DS3 services; and the rate for each rate element that could potentially be used with both DS1- and DS3-level expanded interconnection services would reflect the lowest overhead loadings assigned to any comparable service.[31] Finally, the Bureau stated that although it was not partially suspending some LECs' rates because their loadings appeared to comport with the Commission's overhead loading standard, it would examine all of the LECs' overhead loadings during its investigation.[32]

14. The Bureau also concluded that even after its partial disallowance of Bell Atlantic's proposed overhead loadings, the total charge for Bell Atlantic's DS1 virtual collocation service appeared excessive due to its maintenance-related expenses. Based on a comparison of the maintenance-related expense Bell Atlantic reported for its DS1 virtual collocation service with the maintenance-related expense Bell Atlantic attributed to its comparable DS1 electrical channel termination service, the Bureau reduced Bell Atlantic's

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[29] *Id.* at para. 22.

[30] *Id.* at para. 23. The Bureau explained that if LECs used an average overhead loading for services provided to interconnectors and below-average loadings for LEC services with which interconnectors compete, the effect would be to hamper the ability of interconnectors to compete effectively. *Id.*

[31] *Id.* at para. 25.

[32] *Id.* at paras. 21-23.

recovery of total maintenance expense to the level of its maintenance expense for a comparable DS1 electrical channel termination service.[33]

15. In the *Phase I Designation Order,* the Bureau provided the parties with an opportunity to comment on the interim adjustment imposed in the *Virtual Collocation Tariff Suspension Order*. For example, the Bureau asked the LECs to discuss the Bureau's definition of "comparable services." The Bureau also invited LECs to explain in their direct cases how the public interest goal of promoting efficient competition in interstate access service markets would be advanced if LECs use average overhead loadings for virtual collocation services provided to competitors and below-average loadings for their own customers.[34]

16. In addition, the Bureau required LECs to provide certain direct cost data that they had failed to submit in response to the *TRP Order*.[35] The Bureau also directed Bell Atlantic to provide justification for its maintenance-related charges.[36] Finally, the Bureau noted that it would designate additional issues for investigation and establish a separate pleading cycle for discussion of those issues in a subsequent designation order in Phase II of this docket.[37]

17. Pursuant to the *Phase I Designation Order*, all Tier 1 LECs subject to this Order filed direct cases on March 21, 1995. Three LECs -- Ameritech, CBT, and SWB -- requested confidential treatment of their disaggregated direct cost information.[38] In addition, Bell Atlantic did not respond in its direct case to the designated issue regarding its maintenance-related charges. Bell Atlantic claims that it is currently conducting a new cost study that may result in significantly lower maintenance costs. Bell Atlantic states that on June 1, 1995, it will file a revised tariff based on this study. In addition, Bell Atlantic states that until the Commission concludes its review of the revised tariff, it will "voluntarily accept, beyond the maximum five-month suspension period, a continuation of the existing

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[33] *Id.* at para. 37.

[34] *Phase I Designation Order* at para. 19.

[35] *Id.* at paras. 16-17.

[36] *Id.* at paras. 29-36.

[37] *Id.* at para. 2.

[38] *See* Letter from Michael S. Pabian, Ameritech (March 21, 1995); Letter from Alfred J. Titus, Jr., CBT (March 21, 1995); Letter from Thomas A. Pajda, SWB (March 21, 1995). On April 14, 1995, MFS filed FOIA requests to obtain cost support data filed with the direct cases of SWB and CBT.

virtual collocation tariff that resulted from the Commission's partial suspension of the filed tariff."[39]

18. Seven parties filed oppositions to the direct cases on April 4, 1995, and all LECs filed rebuttals on April 11, 1995. The parties filing oppositions, and the abbreviated names of those parties, are included in Appendix B to this Order.

III. THE BUREAU'S INTERIM OVERHEAD ADJUSTMENT

A. Overview

19. In the *Virtual Collocation Order,* we established a mandatory virtual collocation policy in order to preserve the substantial public interest benefits of expanded interconnection following the Court of Appeals' decision in *Bell Atlantic v. F.C.C.*[40] As we explained in the *Virtual Collocation Order*, our earlier decisions mandating expanded interconnection were fundamental to opening the interstate special access and switched transport markets to greater competition.[41] We observed that expanded interconnection will promote increased competition in interstate access service markets, and will benefit consumers through increased efficiency, broader access to services, reduced rates, and the more rapid deployment of new technologies.[42] In the *Virtual Collocation Tariff Suspension Order*, the Bureau took action to encourage efficient entry by interconnectors into the interstate access service market.

20. In the *Phase I Designation Order*, the Bureau provided the LECs with another opportunity to justify the overhead loadings assigned to their virtual collocation services.

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[39] Bell Atlantic Direct Case at 2. In its opposition, MFS demands that Bell Atlantic immediately provide justification for its original maintenance-related charges. MFS Opposition at 4-5. MFS also asks the Commission to impose sanctions on Bell Atlantic for failure to provide these data. *Id.* at 5. On April 11, 1995, Bell Atlantic filed the requested justification as an attachment to its rebuttal. Since the parties to this proceeding have not had an opportunity to comment on Bell Atlantic's justification of its maintenance-related costs, we will address this issue in a subsequent order in this docket. We note that Bell Atlantic's commitment to keeping rates at their partially suspended levels beyond the five-month suspension period, subject to an accounting order, will ensure that ratepayers are adequately protected during the interim period until issuance of our subsequent order.

[40] *Bell Atlantic Telephone Companies v. F.C.C.*, 24 F.3d 1441 (D.C. Cir. 1994) (*Bell Atlantic v. F.C.C.*) (vacating in part this Commission's expanded interconnection orders mandating expanded interconnection through physical collocation).

[41] *Virtual Collocation Order*, 9 FCC Rcd at 5155. We noted that our simultaneous grant of increased pricing flexibility to the LECs enables those companies to compete more vigorously as well, while assuring that we retain necessary controls on dominant access providers. *Id.*

[42] *Id.* at 5159.

Nevertheless, as discussed below, the LECs have again failed to justify adequately the substantial differences between their loadings for virtual collocation services and those applied to comparable services.

B. Procedural Issues

1. Pleadings

21. **Direct Case.** SWB maintains that there was no notice and comment prior to adoption of the *Virtual Collocation Order*, and therefore asserts that the issue of the appropriate level of overhead loadings for virtual collocation was not debated properly. Thus, SWB asserts, it was improper for the Bureau to implement the overhead loading standard set forth in that Order.[43] Alternatively, SWB contends that even if the Commission's overhead loading standard was adopted in an appropriate manner, the Bureau lacked authority to implement this standard because the Commission did not specifically delegate authority to the Bureau to do so.[44]

22. **Oppositions.** Commenters argue that the Bureau's approach to evaluating the LECs' virtual collocation overhead loadings was fair and reasonable, and urge the Commission to affirm the Bureau's findings.[45] Moreover, commenters contend that many LECs raise untimely challenges to the overhead loading standard adopted in the Commission's *Virtual Collocation Order*.[46] MCI observes that the Bureau acted within its authority and consistent with Commission policy when it ordered LECs to apply overhead loadings that are equal to the lowest overhead loadings assigned to other DS1 and DS3 customers. MCI observes that the *Phase I Designation Order* provided LECs with another opportunity to support their overhead loadings.[47]

23. **Rebuttal.** Bell Atlantic argues that the Commission cannot impose a final tariff prescription based on the Bureau's interim overhead adjustment without notice and comment under the Administrative Procedure Act.[48]

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[43] SWB Direct Case at 3.

[44] *Id.* at 3 n.8.

[45] Teleport Opposition at 4; MCI Opposition at 2; Fibernet Opposition at 5-6; MFS Opposition at 6.

[46] *See, e.g.*, Time Warner Opposition at 10-11. MFS and MCI object to SWB's contention that the *Virtual Collocation Order* was not preceded by adequate notice and opportunity for comment. MCI Opposition at 4-5; MFS Opposition at 8.

[47] MCI Opposition at 10 (*citing Virtual Collocation Tariff Suspension Order* at para. 25).

[48] Bell Atlantic Rebuttal at 2.

2. Discussion

24. As an initial matter, we need not consider SWB's collateral challenge to the procedure employed in adopting the *Virtual Collocation Order*. Challenges to the actions taken in that Order must be brought in the rulemaking proceeding itself.[49]

25. In any event, we disagree with SWB's argument that the Bureau lacked authority to implement our overhead loading standard by establishing, on an interim basis pending further investigation, a just and reasonable level of overhead loadings. The *Virtual Collocation Order* specifically stated that LECs have the burden of demonstrating that their connection charges meet our overhead loading standard, and are otherwise just, reasonable, and not unreasonably discriminatory.[50] We find that it was within the Bureau's authority to assess the LECs' compliance with our overhead loading standard, based on its extensive analysis of the cost and rate data submitted with the virtual collocation tariffs, and to establish the level of overhead loadings that is just and reasonable. The Bureau is typically charged with applying administrative standards adopted in rulemaking proceedings to specific circumstances presented by carrier tariff filings.[51] We reject SWB's unsupported assertion that we were required to delegate explicitly to the Bureau authority to implement our overhead loading standard.

26. Finally, contrary to Bell Atlantic's assertion, the *Phase I Designation Order* afforded parties that disagreed with the Bureau's action ample notice and opportunity to comment on the reasonableness of the Bureau's application of our overhead loading standard. The *Phase I Designation Order* provided LECs with an opportunity to address all aspects of the Bureau's determination that the LECs had failed to justify their proposals to recover a greater share of overhead loadings in their charges for virtual collocation services than they recover in charges for their comparable DS1 and DS3 services. This Commission now has

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[49] *Cf. JEM Broadcasting v. F.C.C.*, 22 F.3d 320 (D.C. Cir. 1994) (dismissing as untimely a collateral challenge to procedural genesis of rules). We note that SWB's petition for review of the *Virtual Collocation Order* is pending before the D.C. Circuit in *Pacific Bell et. al. v. F.C.C.*, D.C. Circuit No. 94-1547, filed Aug. 10, 1994. Moreover, our decision in the *Virtual Collocation Order* was based on consideration of the entire extensive record already assembled in the expanded interconnection proceeding, including that compiled in response to petitions for reconsideration of previous expanded interconnection orders. Our decision to reaffirm the overhead loading standard adopted in earlier orders was based on a sizable record that reflected lengthy debate concerning the appropriate level of overhead loadings for virtual collocation. *Virtual Collocation Order*, 9 FCC Rcd at 5156, 5189.

[50] *Virtual Collocation Order*, 9 FCC Rcd at 5189.

[51] *See* Section 0.91 of the Commission's Rules, 47 C.F.R. § 0.91 (authorizing the Common Carrier Bureau to make determinations regarding the lawfulness of tariffs).

before it an extensive record that provides substantial evidence to support a prescription regarding the maximum permissible overhead loadings for virtual collocation services.

C. Identification of Comparable Services

1. Background

27. In the *Phase I Designation Order*, the Bureau asked LECs to address various aspects of its determination that comparable services include all point-to-point DS1 and DS3 special access and switched transport services, offered in the form of channel termination services sold with and without interoffice mileage.[52] The Bureau directed LECs to identify any services they do not consider comparable to virtual collocation services in terms of overhead loading assignment. The Bureau required SWB, in particular, to explain why SWB characterized its comparable DS1 and DS3 services that provide channel termination without interoffice mileage as "rate elements," rather than as services.[53] The Bureau also required LECs to submit current data detailing the percentage of DS1 and DS3 channel termination services that are sold without interoffice mileage.[54]

28. In addition, the Bureau asked LECs to comment on whether there are additional services that should be considered comparable services.[55] In particular, the Bureau directed LECs to address whether a promotional offering should be considered a comparable service.[56]

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[52] *Phase I Designation Order* at paras. 14-17.

[53] *Id.* at para. 17(e).

[54] *Id.* at para. 17(f). Further, in order to examine the LECs' virtual collocation rate elements that may be used with either DS1 or DS3 level cross-connects, the Bureau required LECs to list the virtual collocation rate elements they treated as nondedicated in their tariff revisions filed pursuant to the *Virtual Collocation Tariff Suspension Order*. *Id.* at paras. 20-22. The LECs complied with the Bureau's request.

[55] *Id.* at para. 17(a). The Bureau noted that there may be other services that employ the same basic types of DS1 and DS3 level equipment in the LECs' central offices, and for which this equipment constitutes a substantial, if not predominant share of the total cost of the service. *Id.* at n.39.

[56] *Id.* at para. 17(a). The Bureau stated that LECs addressing the issue of promotional services should explain the criteria used to classify such services as promotional. The Bureau further stated that if a LEC concludes that a promotional service should not be considered a comparable service under some or all circumstances, it should specify the type of promotion that should be excluded and the reasons for such exclusion. *Id.* at n.40.

2. Pleadings

29. **Direct Cases.** Several LECs agree with the Bureau's determination that all DS1 and DS3 virtual collocation services are comparable to the point-to-point DS1 and DS3 services delineated in the *TRP Order*.[57] For example, United maintains that it does not offer any services other than DS1 and DS3 "channel terminations/entrance facilities" that might be comparable to virtual collocation services.[58] Most LECs, however, object to the Bureau's use of point-to-point DS1 and DS3 services as comparable services.

30. A few LECs contend that none of their DS1 and DS3 access services should be regarded as comparable to DS1 and DS3 virtual collocation services. US West argues that from a provisioning perspective, the standard DS1 and DS3 services are not comparable to virtual collocation services.[59] US West explains that DS1 and DS3 services require fiber termination panels, fiber optic terminals, digital cross-connect panels, fiber, repeaters, and monitoring, while virtual collocation services require connecting cables, jumpers, regenerators, and digital cross-connect panels.[60] US West further avers that it does not consider its Self Healing Alternate Route Protection (SHARP) and interoffice mileage offering to be comparable to virtual collocation services.[61] BellSouth argues that it offers no services comparable to those services provided in a virtual collocation arrangement. Rather, BellSouth asserts that the only meaningful comparison is between LEC end-to-end services and interconnector-provided transport services, because the interconnectors assign their own overhead loadings to their services.[62]

31. A number of LECs, such as SWB, object to certain aspects of the Bureau's definition of comparable services, and argue that the Bureau should have characterized the scope of comparable services in a different manner.[63] According to SWB, the Bureau should

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[57] *Id.* at paras. 17-18.

[58] United Direct Case at 1. In addition, Bell Atlantic and GTE state that the services listed in the *TRP Order* are comparable to their DS1 and DS3 virtual collocation services. Bell Atlantic Direct Case at 6; GTE Direct Case at 2.

[59] US West Direct Case at 4.

[60] *Id.* at 7.

[61] *Id.* at 4.

[62] BellSouth Direct Case at 3.

[63] SWB Direct Case at 3 n.8.

not have identified a channel termination as a point-to-point service.[64] SWB contends that a channel termination is a rate element which, together with other rate elements, comprises a point-to-point service.[65] SWB asserts that if individual rate elements are to be considered services, the Commission should establish a standard that reflects the group of rate elements that are most technically equivalent to virtual collocation.[66] SWB acknowledges that 41 percent of its DS1 channel terminations are purchased without interoffice mileage, but insists that most channel terminations are obtained in conjunction with other rate elements.[67]

32. CBT claims that its discounted volume and term services should not be considered comparable to its virtual collocation service. CBT states that even though the investment components of the services may be similar, CBT offers virtual collocation service only on a month-to-month basis.[68] CBT observes that the annual charge factors, such as depreciation, cost of money, income taxes, maintenance expense, administrative expense, marketing expense and other taxes, which are applied to the investment components, are lower for a long-term arrangement.[69] Ameritech contends that the category of services considered comparable to virtual collocation services should be limited to those end-to-end LEC services that compete with interconnector-provided services dependent on the LEC's virtual collocation services.[70] Finally, most LECs object to including promotional services within the scope of comparable services.[71]

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[64] *See* SWB Direct Case at 5, App. 5 at 2-3. *But see* Bell Atlantic Direct Case at 13 (noting that collocation services and channel termination services are comparable, but not equivalent, services).

[65] SWB Direct Case, App. 5 at 2-3. SWB alleges that "[t]here is nothing in the historical record that implies a service with channel mileage is a different service than a service without channel mileage." *Id.* at 3.

[66] *Id.* at 5. In particular, SWB alleges that the overheads on its multiple DS3 rate elements are more comparable than the rate elements selected by the Bureau. *Id.* at 3 n.2.

[67] SWB Direct Case, App. 6 at 1. All of the LECs state that they provide a substantial percentage of channel terminations without interoffice mileage. Ameritech Direct Case at 4-5; Bell Atlantic Direct Case at 6-7; BellSouth Direct Case at 2; CBT Direct Case, App. A at 2; United Direct Case at 6; US West Direct Case at 8.

[68] CBT Direct Case at App. A, p. 1.

[69] *Id.* at 2.

[70] Ameritech Direct Case at 1-2.

[71] *See, e.g.*, Bell Atlantic Direct Case at 1; United Direct Case at 2. GTE, however, declares that promotional services may be considered comparable to virtual collocation services. GTE Direct Case at 2. Besides promotional offerings, none of the LECs proffered examples of additional services that should be considered comparable services. Ameritech Direct Case at 1-2; Bell Atlantic Direct

33. **Oppositions.** Commenters insist that the Bureau properly defined the scope of services that are comparable to DS1 and DS3 virtual collocation services.[72] Fibernet disagrees with SWB's attempt to eliminate channel terminations from the scope of comparable services by drawing a distinction between rate elements and services. According to Fibernet, the bundling of rate elements into services is purely an artificial construct created by the LECs through the tariffing process.[73] Fibernet asserts that the willingness of the LECs to permit end users to purchase a channel termination on an unbundled, *i.e.*, stand-alone basis, determines whether a channel termination is considered a service.[74]

34. ALTS, ELI, McLeod, and MFS contend that US West has failed to provide data regarding its SHARP service, despite the Bureau's requirement that LECs file cost data for self-healing network services.[75] Further, Time Warner asserts that BellSouth's argument, that the only meaningful comparison is between LEC services and interconnector services because the interconnectors will assign their own overhead loadings to their services, ignores the fact that the overheads that interconnectors may apply are irrelevant to the reasonableness of the LECs' overhead loadings for virtual collocation rate elements.[76]

35. Time Warner claims that discounted offerings should be included within the scope of comparable services because interconnectors compete against these services, even if virtual collocation is only offered on a month-to-month basis. Moreover, Time Warner maintains, LECs have the discretion to offer discounts for virtual collocation services. Time Warner claims that if overhead loadings assigned to month-to-month virtual collocation offerings are not considered comparable to those assigned to discounted DS1/DS3 offerings, LECs could prevent interconnectors from offering their customers competing discounted

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Case at 1; CBT Direct Case, App. A at 1; GTE Direct Case at 2; United Direct Case at 1-2.

72 *See, e.g.*, Teleport Opposition at 4. Time Warner observes that virtual collocation services use essentially the same facilities as the LECs' point-to-point DS1 and DS3 services, although virtual collocation arrangements are more limited. Time Warner Opposition at 14; *accord* Fibernet Opposition at 16-17 (asserting that virtual collocation arrangements require less fiber and electronics than any of SWB's tariffed services).

73 Fibernet Opposition at 15.

74 *Id.* at 15-16.

75 ALTS Opposition at 16; ELI Opposition at 4-5; McLeod Opposition at 2-4; MFS Opposition at 16-17.

76 Time Warner Opposition at 24. Time Warner notes that the Bureau rejected SWB's similar claim that LEC overhead loadings would not deter competitive entry, even if interconnectors' profit levels are reduced. *Id.* (*citing Virtual Collocation Tariff Suspension Order* at para. 22 n.58).

offerings.[77] Finally, MFS, Fibernet and Time Warner contend that promotional services should be considered comparable services.[78]

36. **Rebuttals.** The LECs essentially reiterate the objections set forth in their direct cases.[79] SWB argues that the presence of interoffice mileage is "transparent to the service requested by the customer," and that it is inappropriate to exclude channel mileage from the determination of overhead assigned to a comparable service.[80] Although US West again asserts that it does not consider SHARP service to be comparable to virtual collocation service,[81] it maintains that it submitted information regarding SHARP service with its September 1994 virtual collocation filing.[82]

37. US West also contends that it is inappropriate to assign to month-to-month virtual collocation services those overhead loadings that are applicable to comparable term discounted agreements for access services.[83] Finally, US West submits that it is not opposed to allowing a promotional offering to apply to virtual collocation services when failure to extend that promotion would be perceived as unfair or anticompetitive.[84] US West asserts, however, that promotional offerings should be addressed via the tariff process, where an

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[77] Time Warner Opposition at 16.

[78] Fibernet Opposition at 17-19; Time Warner Opposition at 15-17 (asserting that such services are another means for LECs to compete with interconnector-provided services that are dependent on the bottleneck virtual collocation services); MFS Opposition at 19-22 (arguing that LECs should extend promotional nonrecurring charge waivers to interconnectors).

[79] *See, e.g.*, BellSouth Rebuttal at 2.

[80] SWB Rebuttal at 7-9. In its rebuttal, Bell Atlantic adopted SWB's argument that the Bureau should not have based its interim adjustments on overhead loadings for channel terminations without interoffice mileage. Bell Atlantic Rebuttal at 4-5.

[81] US West avers that unlike virtual collocation service, SHARP service is not provisioned as a month-to-month service and includes interoffice mileage. US West Rebuttal at 4. US West generally observes that virtual collocation services only connect the interconnector-designated equipment in the central office with a US West-provided access service within the same central office; they do not extend out to the customer's premises. By contrast, US West notes that DS1/DS3 services connect US West equipment in the central office with a customer's premises. *Id.* at Attachment A.

[82] *Id.* at 7.

[83] *Id.* at 10.

[84] *Id.* at 11 n.31. US West notes, however, that such a consideration is usually not relevant to a business decision to offer promotions at the retail level. *Id.*

interested interconnector can petition the proposed tariff, rather than through the establishment of a prescriptive rule.[85]

3. Discussion

38. **Overview.** The *Phase I Designation Order* directed LECs to discuss the Bureau's determination that DS1 and DS3 virtual collocation services are comparable to all point-to-point DS1 and DS3 special access and switched transport services, a category that includes channel termination services offered with and without interoffice mileage.[86] None of the LECs has presented convincing arguments that we should modify the Bureau's definition of comparable services.

39. **Bureau's Comparison to Point-to-Point Services.** As a general matter, the LECs' arguments demonstrate a basic misunderstanding of the goal of identifying comparable services. In both the *TRP Order* and the *Virtual Collocation Tariff Suspension Order*, the Bureau sought to identify services that it could use as a yardstick to evaluate the overhead loadings assigned to virtual collocation services. The Bureau selected point-to-point DS1 and DS3 services which, like virtual collocation services, are stand-alone services that provide a connection between the customer premise and another location (such as another customer premise or a LEC's central office). The Bureau noted that these point-to-point services use the same basic types of equipment in the LEC's central office as do virtual collocation services. Since point-to-point services are offered in two basic forms -- as services providing channel termination with and without interoffice mileage -- the Bureau included both of these forms within the scope of comparable services.[87] These comparable services did not, however, have to be identical to virtual collocation services in terms of their equipment and provisioning requirements.

40. Moreover, these comparable point-to-point services are services that face actual or potential competition from interconnectors seeking to compete in the interstate access service market. The Bureau reasoned that if the overhead loadings assigned to these comparable DS1 and DS3 services differed, without adequate justification, from the overhead loadings assigned to virtual collocation services, LECs could unreasonably discriminate against interconnectors. The Bureau was concerned, specifically, that by assigning low

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[85] *Id.* at 11-12. *Cf.* SWB Rebuttal at 13 (maintaining that inclusion of promotional offerings would prevent SWB from offering promotional rates for its DS1/DS3 services).

[86] For a more detailed discussion of point-to-point services, *see TRP Order*, 9 FCC Rcd at 5682-83; *Virtual Collocation Tariff Suspension Order* at paras. 17-18.

[87] *Virtual Collocation Tariff Suspension Order* at para. 18. The Bureau noted that because a channel termination facility connects the customer premise to the nearest central office, interoffice mileage is not needed unless the customer wishes to be connected to a different central office. *Id.* at n.50.

overheads to the point-to-point services with which interconnectors compete, and high overheads to the LEC facilities upon which interconnectors rely to provide competitive services, the interconnectors could be disadvantaged competitively.[88]

41. We agree with the Bureau's determination that point-to-point DS1 and DS3 services are comparable to virtual collocation services. We, therefore, find no merit in the LECs' arguments that DS1 and DS3 services should not be compared to virtual collocation services because these two types of services are "provisioned" differently and thus are not technically equivalent. Whether comparable DS1 and DS3 services require different equipment than virtual collocation services is relevant only to the direct costs of these services, not to whether these DS1 and DS3 services are comparable to virtual collocation services for purposes of an overhead loading comparison. Nor are provisioning differences relevant to whether comparable DS1 and DS3 services face actual or potential competition from interconnectors seeking to compete in the interstate access service market.[89]

42. We also disagree with BellSouth's assertion that the only meaningful comparison of services is between the LECs' end-to-end services and interconnector-provided transport services. This proceeding is an investigation of whether the rates charged to interconnectors for virtual collocation services are just and reasonable. We are not, however, investigating the interconnectors' direct costs or the rates that interconnectors assess their own customers. Such a comparison would not be useful in determining whether LECs are assigning low overheads to the point-to-point services with which interconnectors compete, and high overheads to the LEC facilities upon which interconnectors rely to provide competitive services. Moreover, as stated above, this practice could prevent interconnectors from competing in the interstate access service market.

43. **Specific Point-to-Point Services.** SWB agrees with the Bureau's conclusion that point-to-point DS1 and DS3 services are comparable to virtual collocation services, but objects to the Bureau's determination that channel termination services offered without interoffice mileage fit within the category of comparable point-to-point DS1 and DS3 services.[90] SWB's objection ignores the fact that channel termination services sold without interoffice mileage are services with which interconnectors compete in the interstate access

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[88] *Id.* at para. 22.

[89] Further, contrary to commenters' assertions, US West did submit information regarding its SHARP service with its September 1994 virtual collocation filing. The Bureau properly considered this SHARP service data in its analysis of US West's proposed overhead loadings for virtual collocation services. In the *TRP Order*, the Bureau specifically included basic services offering specialized features such as self-healing networks within the rubric of comparable DS1 and DS3 services. *TRP Order*, 9 FCC Rcd at 5684.

[90] *See* SWB Direct Case at 2, 4.

service market. All of the LECs, including SWB, concede that a substantial portion of channel termination services are sold without interoffice mileage.[91]

44. Further, contrary to SWB's claim, the Bureau properly compared the overhead loadings assigned to virtual collocation services with those assigned to channel termination services. The net effect of our expanded interconnection policy is to permit interconnectors to pay a "connection charge" in lieu of a channel termination charge.[92] Prior to the advent of expanded interconnection, the LECs' interstate special access tariffs required interconnectors to pay two channel termination charges, even when interconnectors substituted their own facilities for most of the LECs' transmission segments in order to provide the "premise-to-central office" or "central office-to-interexchange carrier point-of-presence" segments of a special access line.[93] As a result, interconnectors were unable to offer service at economically competitive prices. When we adopted new rate structure requirements to accommodate expanded interconnection through virtual collocation, we required LECs to develop expanded interconnection "connection charges" to replace one of the channel termination charges in special access arrangements.[94] We, therefore, find unpersuasive SWB's assertion that channel termination service is not comparable to the very service that interconnectors may use to replace it.

45. Likewise, we agree with the Bureau's finding that discounted volume and term DS1 and DS3 services should be included within the scope of comparable services because

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[91] *See* note 67, *supra.*

[92] The LECs' special access tariffs generally impose two types of recurring charges: (1) a flat-rate, non-distance-sensitive channel termination charge, which applies to the connections between the customer premise and the central office, as well as to the connections between the central office and the interexchange carrier point of presence or other customer-designated end point; and (2) a distance-sensitive channel mileage charge that applies to the special access connection between LEC central offices, if one is required. *See* Expanded Interconnection with Local Telephone Facilities, Notice of Proposed Rulemaking and Notice of Inquiry, 6 FCC Rcd 3259, 3265 (1991) (*Notice of Inquiry*); *Special Access Expanded Interconnection Order*, 7 FCC Rcd at 7373-74. We noted, however, that the Part 69 access charge rate structure rules did not specify a particular rate structure for the provision of special access services. *Notice of Inquiry*, 6 FCC Rcd at 3264.

[93] Rather, a customer had the choice of either using LEC facilities for the entire special access connection or bypassing the LEC entirely through third party facilities that connected the customer location directly to the interexchange carrier. *Notice of Inquiry*, 6 FCC Rcd at 3260. *See also Special Access Expanded Interconnection Order*, 7 FCC Rcd 7374 (1992).

[94] *See Notice of Inquiry*, 6 FCC Rcd at 3265; *see also Virtual Collocation Order*, 9 FCC Rcd at 5159 (explaining that this Commission's expanded interconnection policy allows a party to purchase only those LEC transmission and distribution links that the party deems necessary).

they are services with which interconnectors compete in the interstate access service market.[95] The volume and term discounted services are the LEC services facing actual or potential competition from interconnectors. LECs may offer these services if they meet certain threshold requirements demonstrating that they currently face competition from interconnectors.[96] We, therefore, reject CBT's assertion that the overhead loadings assigned to discounted services should not be compared to the overhead loadings assigned to CBT's virtual collocation services. Moreover, we note that LECs are free to offer volume and term discounts to their virtual collocation customers.

46. Finally, none of the parties has suggested any particular promotional services that should be considered comparable services that face actual or potential competition from interconnectors. Accordingly, we conclude that the record does not contain sufficient information at this time for us to determine whether promotional offerings should be included within the scope of comparable services. We, therefore, exclude promotional offerings from our analysis of the overhead loadings assigned to the LECs' virtual collocation rates at this time.

D. The Bureau's Overhead Loading Analysis

1. Background

47. In addition to seeking comment on the Bureau's characterization of the scope of comparable services, the *Phase I Designation Order* provided LECs with a forum to address the Bureau's comparison of the overhead loadings assigned to these comparable services with the loadings assigned to virtual collocation services. In the *Phase I Designation Order*, the Bureau noted that most LECs continue to maintain that the overhead loadings assigned to their virtual collocation services are below or comparable to the loadings assigned to their comparable services. Nevertheless, the Bureau stated, it appeared that most of these

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[95] In our *Virtual Collocation Order*, we stated that LEC flexibility to offer volume and term discounts for switched transport services should be linked to a demonstration that the LEC's expanded interconnection offering presents a viable competitive opportunity. *Virtual Collocation Order*, 9 FCC Rcd at 5204.

[96] In the *Switched Transport Expanded Interconnection Order* and, more recently, in the *Virtual Collocation Order*, we permitted LECs to implement volume and term discounts for switched transport rates in a study area when one of the following two conditions has been met: (1) 100 DS1-equivalent switched cross-connects are operational in the Zone 1 offices in the study area; or (2) an average of 25 DS1-equivalent switched cross-connects per Zone 1 office are operational. In study areas with no Zone 1 offices, volume and term discounts may be implemented once five DS1-equivalent switched cross-connects are operational in the study area. Expanded Interconnection with Local Telephone Company Facilities, Second Report and Order and Third Notice of Proposed Rulemaking, 8 FCC Rcd 7374, 7435 (1993) *(Switched Transport Expanded Interconnection Order)*; *Virtual Collocation Order*, 9 FCC Rcd at 5202-04. *See also Special Access Expanded Interconnection Order*, 7 FCC Rcd at 7437-38 (discussing LEC pricing flexibility for special access services).

LECs developed their overhead loadings based on an average of the overhead loadings assigned to all of their comparable DS1 and DS3 services.[97]

48. To assist its evaluation of the LECs' approaches, the Bureau asked them to explain how the public interest goal of promoting efficient competition is advanced if LECs use average overhead loadings for virtual collocation services provided to competitors and below-average loadings for services provided to their own end users.[98]

2. Pleadings

49. **Direct Cases.** A few LECs contend that even if the Bureau properly defined the scope of comparable services for purposes of its overhead loading comparison, its comparison of the overhead loadings assigned to comparable services with those assigned to virtual collocation services was flawed. BellSouth maintains that the Bureau wrongly assumed that virtual collocation services should reflect uniform overhead loadings, absent justification. BellSouth argues that it is not unreasonable for overheads applied to LEC services and those applied to virtual collocation services to vary.[99] US West maintains that because its method of establishing overheads for virtual collocation is the same as that used to establish overheads for services subject to price cap regulation, the overhead loadings assigned to its virtual collocation services cannot be contrary to the public interest.[100] GTE contends that it is unfair to compare newly developed virtual collocation rates with DS1 and DS3 rates that have been adjusted under price cap regulation.[101]

50. Most of the LECs support the Bureau's conclusion that variations between overhead loadings assigned to virtual collocation services and comparable DS1 and DS3 services are based on market conditions. For example, Ameritech maintains that the process of assigning overhead loadings to virtual collocation services is unrelated to the process by which DS1 and DS3 services are priced.[102] BellSouth, however, objects to the Bureau's finding that overhead factors are assigned according to the characteristics of specific market

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97 *Phase I Designation Order* at para. 18.

98 *Id.* at para. 19.

99 BellSouth Direct Case at 4.

100 US West Direct Case at 9.

101 GTE Direct Case at 2-5 (contending that the overhead loadings for virtual collocation rate elements do not differ from those assigned to comparable services).

102 Ameritech Direct Case at 6; *see also* United Direct Case at 7.

segments.[103] According to BellSouth, there is no variation across markets in the overhead loading assigned to a specific access service because BellSouth cannot offer geographically deaveraged rates.[104]

51. Several LECs also challenge the Bureau's conclusion that in order to prevent unreasonable discrimination against interconnectors seeking to compete in the interstate access service market, LECs should assign to virtual collocation services the lowest overhead loadings assigned to their comparable DS1 and DS3 services.[105] SWB argues that an average overhead loading standard would best meet the public interest goal of fostering efficient competition.[106] SWB submits that it used a simple average of all DS1 and DS3 recurring rate elements for all of its comparable DS1 and DS3 services.[107]

52. According to Ameritech, it is unnecessary to require that the overhead loading on a competitive service be no less than the overhead loading assigned to virtual collocation services in order to preclude a price squeeze, especially if the direct cost of the competitive service exceeds the direct cost of the virtual collocation services.[108] Ameritech claims that an average overhead loading will protect interconnectors from a price squeeze, as long as the overhead loadings on the rates for comparable services are sufficient to cover the dollar amount of overheads assigned to an equivalent volume of interconnection services.[109]

53. **Oppositions.** Time Warner, MCI, and Fibernet assert that the LECs have again failed to demonstrate that the wide variations in overhead loadings are due to actual differences in the overhead costs incurred by the different services.[110] Time Warner argues that differences in loadings due to price cap regulation of special access and switched transport services are not relevant to the Bureau's comparison of the overhead loadings currently applied to the comparable DS1 and DS3 services with the proposed overhead

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[103] BellSouth Direct Case at 4. BellSouth notes that all of its DS1 and DS3 services "do not reflect the same loading ... ; nevertheless, all such offerings face competition from [interconnectors]." *Id.*

[104] *Id.* (*citing Virtual Collocation Tariff Suspension Order* at para. 21). *See also* Bell Atlantic Direct Case at 9.

[105] *See Virtual Collocation Tariff Suspension Order* at para. 24.

[106] SWB Direct Case at 4-5.

[107] *Id.* at 2.

[108] Ameritech Direct Case at 7.

[109] *Id.* at 8.

[110] Time Warner Opposition at 4; MCI Opposition at 1; Fibernet Opposition at 8.

loadings for virtual collocation services. Moreover, Time Warner asserts, GTE fails to acknowledge that higher overhead loadings for virtual collocation services mean that interconnectors function at a competitive disadvantage.[111]

54. MCI asserts that because interconnectors will have to compete against the lowest rates charged by the LEC, their costs for essential bottleneck facilities should be equal to those that the LEC charges itself, *i.e.,* the lowest overhead loading assigned to other DS1 and DS3 services.[112] Fibernet maintains that the Bureau's approach will facilitate efficient entry into the marketplace,[113] and ultimately result in increased freedom of choice for interstate access customers.[114]

55. Time Warner and MCI argue that no LEC has attempted to explain how the use of an average overhead loading standard would promote competition.[115] Fibernet asserts that SWB's use of a simple average will prevent the benefits of expanded interconnection from extending beyond the largest end users to include small businesses.[116] Fibernet also challenges SWB's attempt to redefine the concept of "most valued customer." According to Fibernet, the Bureau's policy of preventing anticompetitive pricing properly focused on the relative levels of overhead loadings, not the prices paid by various special access customers on a "per DS3-equivalent" basis.[117]

56. Finally, Teleport contends that since the LECs have been given considerable pricing flexibility as a result of the Commission's zone density pricing decisions, the use of averaged loadings would leave competitors facing excessive costs in markets where competition is most likely.[118] Teleport maintains that the Bureau's overhead adjustments serve to limit the ability of LECs to engage in anticompetitive conduct.[119]

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[111] Time Warner Opposition at 12.

[112] MCI Opposition at 12.

[113] Fibernet Opposition at 5-6.

[114] *Id.* at 11.

[115] Time Warner Opposition at 11, 14 (specifically targeting SWB's argument); MCI Opposition at 12-13.

[116] Fibernet Opposition at 13.

[117] *Id.* at 13 n.25.

[118] Teleport Opposition at 5.

[119] *Id.* at 3.

57. **Rebuttals.** . SWB alleges that commenters' fear of a price squeeze are unfounded. SWB claims that LECs would try to avoid such anticompetitive behavior, and that modern economic literature indicates that neither predatory pricing nor anticompetitive price squeezes are common in American industry.[120] BellSouth agrees with SWB that a price squeeze is unlikely to occur. According to BellSouth, the virtual collocation cross-connect element[121] is too small a cost component to have a significant impact on an interconnector's total service provisioning costs.[122] Ameritech and SWB contend that a price squeeze cannot occur if the total dollar amount of overhead contribution from a virtual collocation service does not exceed the dollar amount of overhead contribution from the comparable retail services.[123]

58. SWB further responds that unless it is permitted to use average overhead loadings for virtual collocation services, interconnectors will have a marketplace advantage.[124] According to SWB, the Bureau's overhead standard forces SWB to charge average overheads for access services provided to its own customers, while interconnectors pay below-average overheads on virtual collocation service.[125] In response to MCI's argument, SWB asserts that the use of an average overhead amount would include all the rates that the LEC charges itself, not only the lowest of these amounts.[126]

59. Finally, SWB and Bell Atlantic assert that the "most favored" customer may not be the customer paying the lowest overhead loading, because in some cases services with the lowest unit charge carry higher overhead loadings than services with higher unit costs.[127] For example, Bell Atlantic asserts that it provides interconnectors with month-to-month

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[120] SWB Rebuttal at 15.

[121] BellSouth maintains that apart from certain support functions (*e.g.*, electricity), the only service provided to the interconnectors in a virtual collocation arrangement is the DS1/DS3 cross-connect. BellSouth Rebuttal at 2.

[122] *Id.* at 4.

[123] Ameritech Rebuttal at 7; SWB Rebuttal at 14.

[124] *Id.* at 4-6.

[125] *Id.* at 12.

[126] *Id.* at 5 (quoting MCI Opposition at 12). *Accord* Bell Atlantic Rebuttal at 2 (favoring use of the range of overheads assigned to a "family" of comparable DS1/DS3 access services).

[127] SWB Rebuttal at 7; Bell Atlantic Rebuttal at 2-3.

virtual collocation rates that have lower overhead loadings than the comparable month-to-month access service charges.[128]

3. Discussion

60. **Overview.** In their direct cases, the LECs assert that even if the Bureau properly defined the scope of comparable services for purposes of its overhead loading comparison, the Bureau's methodology for comparing the overhead loadings assigned to comparable services with those assigned to virtual collocation services was inappropriate. As explained below, we find that none of the LECs has raised valid objections to the Bureau's overhead loading analysis. Rather, the LECs' arguments generally demonstrate a misunderstanding of our overhead loading standard and a failure to admit that the interconnector's dual role as competitor and customer of the LEC necessitates careful scrutiny of the overhead loadings assigned to interconnection services. We, therefore, conclude that the Bureau's overhead adjustment represents a reasonable approach to preventing unreasonable discrimination against interconnectors seeking to compete in the interstate access service market, without hampering the LECs' ability to compete effectively.

61. **LECs' Failure to Meet Overhead Loading Standard.** In the *Virtual Collocation Order*, we adopted a broad overhead loading standard. We stated that if a LEC chooses to use nonuniform overhead loadings, it may not recover a greater share of overheads in charges for virtual collocation services than it recovers in charges for comparable services, absent justification.[129] This standard does not imply, as BellSouth mistakenly claims, that LECs are required to use uniform overhead loadings for the comparable services. Rather, our standard requires that LECs justify variations in overhead loadings between their comparable DS1 and DS3 services and their virtual collocation services.

62. In the *Virtual Collocation Tariff Suspension Order*, the Bureau reviewed the LECs' tariff submissions and related pleadings and determined that although all LECs used nonuniform overhead loadings, none had attempted to show that the differences in the overhead loadings between services were due to the differences in overhead costs actually incurred by the two types of services.[130] Instead, the Bureau found that the LECs generally concede that the variation in overhead assignment is not due to actual cost differences among individual services, but rather to market conditions.[131] Due to the interconnectors' need for

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[128] *Id.* at 3.

[129] *Virtual Collocation Order*, 9 FCC Rcd at 5189.

[130] *Virtual Collocation Tariff Suspension Order* at para. 21.

[131] Most LECs tended to assign low overheads in markets where they faced actual or potential competition from interconnectors, and high overheads where they did not. *Id.* at para. 21.