COMPTEL COMPETITIVE TELECOMMUNICATIONS ASSOCIATION

EX PARTE OR LATE FILED

Genevieve Morelli
Vice President & General Counsel

ORIGINAL

RECEIVED

AUG 7 1995

FEDERAL COMMUNICATIONS COMMISSION
OFFICE OF SECRETARY

August 7, 1995

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

Re: CC Docket No. 94-1
<u>Ex Parte Communication</u>

Dear Mr. Caton:

On August 4, 1995, Genevieve Morelli and Joseph Gillan, representing the Competitive Telecommunications Association ("CompTel"), met with Jim Casserly of Commissioner Ness's office, Richard Welsh of Commissioner Chong's office and Karen Brinkmann, Anthony Bush and Les Selzer of the Common Carrier Bureau to discuss CompTel's position regarding the pricing flexibility issues to be addressed in a Further Notice of Proposed Rulemaking in the above-captioned proceeding. The attached materials, which detail CompTel's position, were distributed during the meeting.

Please address any questions concerning this letter to the undersigned.

Sincerely,

Genevieve Morelli

Genevieve Morelli

cc: Jim Casserly
Richard Welsh
Karen Brinkmann
Anthony Bush
Les Selzer

No. of Copies rec'd 021
List A B C D E

Ex Parte
CC Docket No. 94-1
August 3, 1995

Summary

* Switched access rates are not aligned with underlying costs.

* Competition is unattainable for the vast majority of switched access revenues and cannot be relied upon to correct switched access price levels or rate relationships.

* The consequences of inflated, non-cost based switched access rates are increasing in an environment of network unbundling and RBOC entry to the long distance market.

* Modifications to the Commission's Price Cap and Access Rules should be structured to guide rates towards their underlying costs.

    * The Commission should focus its Further Notice on the fundamental disparity between access rates and their underlying costs, recognizing that competitive incentives will not correct the problem.

    * The Further Notice should recognize the relationship between access pricing and local competition and the unique pricing problems presented by the potential reentry of the Bell Operating Companies to the long distance market.

I. Switched access rates are not aligned with underlying costs.

A. State regulatory proceedings have consistently shown that interstate access prices far exceed the underlying resource cost to provide the service. For example:

South Central Bell Cost Analysis - Mississippi (1993)[1]

Service Category	Ratio of Revenue to Direct Cost
Local Access & Usage	0.6[2]
Vertical Services	8.3[2]
Directory Service	1.2
PBX and ESSX	1.2
IntraLATA MTS[3]	2.2
IntraLATA OCP[3]	2.9
Switched Access	11.5

B. Interstate access service is functionally equivalent to the "local interconnection" service that is a predicate to local competition. State regulatory investigations have recognized that "local interconnection" and "switched access" are equivalent, but have generally concluded that existing access prices are so far above their cost that they shouldn't be used.

For instance, the Illinois Customers First proceeding established cost-based rates, with contribution, for the termination of traffic at end-offices and tandem locations that were substantially less than interstate access rates:

---

[1] Docket No. 94-UA-0536. LDDS/Metromedia Testimony filed April 27, 1995.

[2] Local exchange service and vertical services (such as customer calling features) are frequently purchased together. Consequently, it is reasonable combine the revenues/costs from these services when performing profitability analysis.

[3] Non-access component estimated by LDDS/Metromedia.

Comparison of Cost-Based Termination Rates to Interstate Access Rates

	End Office	Tandem
Interstate[4]	0.022866	0.024152
ICC Order	0.005000	0.007500

C. Recent petitions for access pricing flexibility (in particular, NYNEX's USPP filing) are at their foundation requests to reduce access prices closer to the economic resource cost.

D. The most significant factor affecting the level of switched access prices is the allocation of overhead. The Commission's current price cap system has no mechanism to correct discriminatory allocations of overhead between access services or customers. The Commission has shown concern for the competitive implications of overhead loadings as *new* services are introduced -- expanded interconnection and ONA are two examples -- but there has been no comprehensive evaluation of the identical problems raised in the context of switched access, even though these are comparable uses of the same network.

II. **Competition is unattainable for the vast majority of switched access revenues and is unlikely to provide the appropriate incentives to correct price levels and rate relationships.**

A. The vast majority of switched access revenues are recovered at the first point of switching.

B. The first point of switching is decided by the subscribers' choice of local telephone company, not the long distance carriers' "choice" of switched access provider.

C. Standard competitive incentives do not -- and *will not* -- exist in the switched access marketplace. Local networks compete for subscribers through retail price competition, not lower access prices to other service providers.

---

4 Assumes 0 miles of transport.

D. State experience with local competition confirms the de minimis influence of "competition" on access pricing.

1. Maryland and Illinois both recognized that entrant local service providers have no incentive to "compete" for switched access business.

2. MFS's access tariff in Maryland confirms the absence of competitive pressures on elements of access except dedicated transport. See Attachment 1 (Comparison of MFS and Bell Atlantic access rates).

3. Digital Signal's Michigan proposal mirrors Ameritech's switched access rates.

E. Conclusion: Competition will not force most switched access rates towards cost because access rate reductions will have little influence on the success of a local service provider in attracting or retaining end user subscribers. Long distance carriers cannot threaten to "take their access business elsewhere" since the access provider is predetermined by the end users' choice of local service provider.

III. The consequences of inflated, non-cost based switched access rates are increasing in an environment of network unbundling and RBOC entry to the long distance market.

A. In the past, inflated access prices have discouraged long distance calling, but have not influenced the end user's choice of long distance carrier. Inflated access prices were imposed on all long distance carriers relatively uniformly.

B. If access prices are not corrected prior to RBOC entry to the long distance market, these inflated charges would provide the RBOCs a dramatic competitive advantage over all other purchasers of access service.

1. RBOCs could introduce toll services with prices close to access charge rate levels because they would continue to receive the profit levels embedded in switched access rates.

2. If access charges are established at (or near) their economic resource cost, then all long distance providers would share the same real cost of access and could then compete on their skill and expertise as long distance carriers.

C. The availability of unbundled loops will enable some carriers, in isolated markets, an opportunity to avoid inflated originating access charges by installing local switches and combining these switches with unbundled loops to replace the local telephone company. These entrants can establish a geographically concentrated base of local subscribers, attracting business from both local and long distance carriers, in part because the price of the "access" they pay is low relative to interstate access charges imposed on long distance companies.

D. It is impractical to anticipate extensive duplication of the local telephone industry's local switching capacity by long distance carriers.

1. In 1993, the local telephone industry switched over 525.5 billion calls. During the same period, the long distance industry switched approximately 54.3 billion calls.[5]

2. AT&T, with 60% of the market, serves the entire nation from 134 switches.[6] The RBOCs themselves have nearly 10,000 local switches deployed; including the independent local telephone companies increases the number of local switches to over 18,000.[7]

E. Long distance carrier customer bases are geographically dispersed and cannot be feasibly served through unbundled loops. These long distance carriers can best compete by continuing to rely on the local telephone companies' networks, but

---

[5] Source: Statistics of Communications Common Carriers, 1993/94 Edition, Federal Communications Commission. Table 2.10.

[6] Source: Testimony of AT&T witness Jane Medlin, Application of AT&T for a Local Exchange Certificate in the State of Michigan.

[7] Source: Infrastructure of the Local Operating Companies Aggregate to the Holding Company Level, Industry Analysis Division, Common Carrier Bureau, Federal Communications Commission, April 1995.

only if these networks are priced more closely to their actual cost. Once the RBOCs are able to offer their own long distance services (i.e., after MFJ relief), however, they will lose any incentive to reduce access charges to their long distance rivals.

F. The FCC should take steps now, in anticipation of RBOC long distance entry, to assure that vibrant long distance competition will continue.

IV. Modifications to the Commission's Price Cap and Access Rules should be structured to guide rates towards their underlying costs.

A. The Commission's Further Notice should be structured to recognize the unique competitive issues concerning switched access service, its historic overpricing, and the necessity for reform in anticipation of local competition and the potential of RBOC entry to the long distance market.

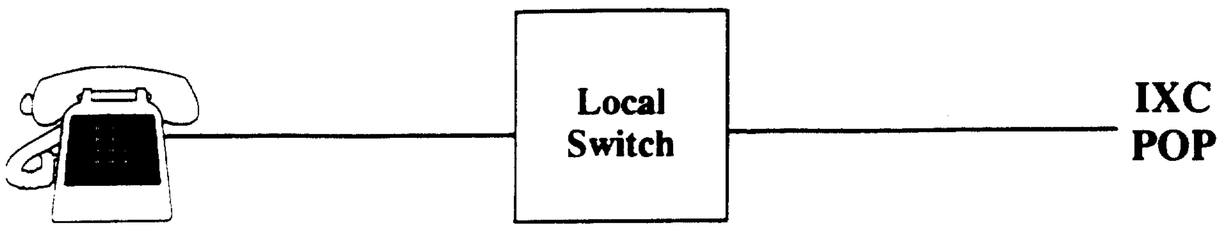
B. Loop unbundling and local competition exposes the overpricing of access service by providing selective rate relief to only one class of customer (the entrant that provides both local and long distance service). The Commission should correct this problem at its source by reforming the level of access charges and not by targeting relief to particular market participants such as ESPs (ONA), CAPs (expanded interconnection) and entrant local providers (unbundled loops and local interconnection).

C. The Commission should investigate the magnitude of the over-pricing problem by comparing the direct economic resource cost to provide switched access service to the overhead allocations imposed on this service. The necessary data already exists (it has been used in a variety of state proceedings) and its review by the FCC would provide the necessary information to evaluate a reform of access charges.

D. The Further Notice should specifically seek comment on rate realignments -- including an increase in the subscriber line charge -- that would result in more economically efficient and reasonable switched access rate levels. Rate rebalancings such as those contained in the recently approved NYNEX USPP plan should be considered as a possible way to provide reasonable transitions to more rational pricing.

E. The Further Notice should address the particular discrimination and pricing concerns that would arise if the Bell Operating Companies are provided relief from the line of business restrictions in the MFJ.

Switched-Access "Competition" Will Not Occur



The IXC *pays* the switched access rates for the local loop, local switch and residual interconnection charge, but the provider is *decided* when the end-user selects its local provider.

$7.6 Billion

IXC selects transport provider.

$0.6 Billion

Over 90% of switched-access cost are not within the IXC's control.

Attachment I - Access Rate Cross-Reference

Rate Element	MFS-I Tariff Rate	MFS-I Tariff Section	BA-MD Tariff* Rate	BA-MD Tariff* Section
Service Install Charge	$35.00	4.1.1	Note 1	
Access Order Charge	$105.00	4.1.1	Note 1	
Engineering Charge	$80.00	4.1.1	Note 1	
Service Date Charge	$25.00	4.1.1	Note 1	
Design Change	$25.00	4.1.1	Note 1	
Carrier Common Line	$.01767	4.1.2	$.01767	Note 2
Local Transport				
Entrance Facility - Monthly	$175.00	4.1.3(A)	$225.00	6.9.1(A)(2)
Entrance Facility - Installation				
1st	$830.00	4.1.3(B)	$830.00	6.9.1(A)(2)
Additional	$240.00		$240.00	
Entrance Facility - Rearrangement				
1st	$210.00	4.1.3(B)	$210.00	6.9.1(A)(2)
Additional	$105.00		$105.00	
Common Switched Transport				
Local Transport Termination	$.000222	4.1.3(B)	$.000222	6.9.1(B)
Local Transport Facility (per mile)	$.000048		$.000048	
Dedicated Transport				
Fixed	$40.00	4.1.3(C)	$50.00	6.9.1(C)
Per Mile	$24.00		$30.00	

Attachment I - Access Rate Cross-Reference (continued)

Rate Element	MFS-I Tariff Rate	MFS-I Tariff Section	BA-MD Tariff* Rate	BA-MD Tariff* Section
Interconnection Charge	$.008094	4.1.3(D)	$.008094	6.9.1(H)
Network Blocking Charge	$.0079	4.1.3(E)	N/A	
Common Channel Signaling Access				
STP Port Termination	$932.58	4.1.3(F)	$932.58	6.9.1(M)
STP Link Transport (per mile)	$2.38		$2.38	
SS7 Signalling Option Conversion	$125.00	4.1.3(G)	$125.00	FCC 1 - 6.9.1(M)
Local Switching	$.012559	4.1.4	$.012559	6.9.3(A)(1)
Automatic Number ID	$.0004	4.1.4	$.0004	6.9.3(A)(2)
Local Access	$.061	4.1.5	$.061	PSC 216 - 3.C.1.d
800 Database Access	$.003080	4.1.6(A)	$.003080	6.9.3(A)(2)
800 Optional Features	$.000327	4.1.6(B)	$.000327	6.9.3(A)(2)
Presubscription Change	$5.00	4.2.1	$5.00	FCC 1 - 4.2(P)

---

* Tariff P.S.C.-Md. No. 217, unless otherwise noted.

Note 1 - Section 13 of P.S.C.-Md. No. 217 contains hourly charges for additional engineering an labor; these rates are not directly comparable to MFS-I's proposed rates.

Note 2 - BA-MD Carrier Common Line charge has been estimated by dividing BA-MD's annu revenue requirement of $39,400,000 (monthly requirement of $3,283,333, as shown in BA-MD's tari PSC 217 - Section 3.8(A) multiplied by 12) by its 1993 intrastate access minutes of 2,230,154,000.

The Commission further finds that the 5% billing threshold, calculated on a per-minute basis, is reasonable because it should adequately account for any skewed traffic balances between Ameritech Michigan and City Signal, while reducing billing costs when traffic volumes are essentially balanced. In contrast, the Commission is not persuaded that a 50% threshold will permit cost recovery. In addition, the Commission clarifies that when traffic exceeds the 5% billing threshold, compensation for all calls should be paid, not just the amount that exceeds 5%.

As to AT&T's requested clarification, the Commission finds that, for local calls within the plus or minus 5% threshold, Ameritech Michigan and City Signal should follow generally accepted accounting principles for tracking costs and revenues associated with the termination of that traffic.

Finally, the Commission finds that City Signal's proposal to charge access rates that are identical to Ameritech Michigan's access rates during the transitional period is reasonable. As Mr. Clift explained, Ameritech Michigan's access rates can be considered the market rate for access services in the Grand Rapids District Exchange. Furthermore, as a non-dominant carrier, City Signal may file and use rates with the FCC subject to one-day's notice, and there is no requirement that those rates be based on any preset criteria. (5 Tr. 497.)

In making the foregoing determinations, the Commission specifically rejects the argument that it is giving an advantage to newly licensed competitors. To the contrary, the Commission's finding is an attempt to strike an appropriate balance between the competing interests in this case on a transitional basis. The Commission emphasizes that, like many of the other issues, the compensation arrangements will be examined further in a subsequent