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August 17, 1995

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FEDERAL COMMUNICATIONS COMMISSION
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BY HAND DELIVERY

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

Re: Notice of Ex Parte Filing in CC Docket No. 94-1

Dear Mr. Caton:

On behalf of WorldCom, Inc., d/b/a LDDS WorldCom, please include in the record of the referenced proceeding the following comments of LDDS WorldCom filed in other proceedings:

- Comments of LDDS Communications, Inc. in FCC CC Docket No. 95-20 (filed April 7, 1995).
- Response of LDDS Communications, Inc. to Petition for Rulemaking, FCC RM-8614 (filed April 10, 1995).
- Response of LDDS WorldCom to Motion of the United States for a Modification of the Decree to Permit a Limited Trial of Interexchange Service by Ameritech, filed in U.S. v. Western Electric Co., Inc., D.D.C Civ. No. 82-0192 (HHG), May 31, 1995.

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Mr. William F. Caton
Acting Secretary
August 17, 1995
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Copies of the referenced comments are attached to this letter. I have hereby submitted two copies of this notice to the Secretary, as required by the Commission's rules. Please return a date-stamped copy of the enclosed (copy provided).

Please contact the undersigned if you have any questions.

Respectfully submitted,



Linda L. Oliver
Counsel for WorldCom, Inc.,
d/b/a LDDS WorldCom

Enclosures

**Before the
Federal Communications Commission
Washington, D.C. 20554**

In the Matter of)	
)	
<u>Computer III</u> Further Remand)	CC Docket No. 95-20
Proceedings: Bell Operating)	
Company Provision of Enhanced Services)	

COMMENTS OF LDDS COMMUNICATIONS, INC.

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April 7, 1995

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SUMMARY

LDDS assumes that as the Commission reconsiders the need for structural separation of RBOC enhanced services, it will redo the cost-benefit analysis underlying its original decision to abandon separation. We submit that the costs and benefits affecting this analysis are very different in 1995 than they were when this proceeding opened. First, the cost of separation is substantially less than originally anticipated because RBOCs will be establishing new subsidiaries for other competitive purposes anyway. Second, the need for separation now has been confirmed by actual experience demonstrating the failure of nonstructural regulation to work as intended. As a result, the Commission only can respond to the California III decision by reinstating structural separation requirements.

The initial rationale for dropping structural separation rested in large measure on the Commission's projection that separation would impose heavy costs on the RBOCs. The Commission feared that if the RBOCs were required to create subsidiaries simply for enhanced services, they would face substantial additional operating expenses, and be prevented from marketing enhanced services with basic services. The Commission concluded that new (and therefore untested) nonstructural regulations, most notably ONA, would be adequate to prevent access discrimination against enhanced service providers ("ESPs").

This analysis cannot stand today. To begin with, it is increasingly apparent that RBOCs will be required to establish new separate subsidiaries from which they will market interLATA long distance and probably other competitive

services. Parties may disagree over when and under what circumstances interLATA entry should be permitted. But there is widespread consensus that structural separation will be a central element of that entry. Furthermore, it is likely that the RBOCs will choose to (or be required to) market other competitive services through these subsidiaries.

It follows that the cost to the RBOCs of also providing enhanced services through these subsidiaries would be small if not trivial. It also follows that just as an RBOC subsidiary will be required to purchase access from its operating company affiliate for purposes of providing interexchange services, the subsidiary similarly can purchase access from its operating company for enhanced services. Indeed, the new subsidiaries may become the RBOCs' primary retail arms, also purchasing and reselling local service obtained from their monopoly operating company. In any event, the RBOC will be free through that retail subsidiary to market enhanced and basic services together, addressing one of the Commission's original concerns with separation.

Just as the costs of separation are less than originally anticipated, experience now shows that the benefits of separation were underestimated when the Commission abandoned that requirement. The Commission hoped that its nonstructural ONA policies and other rules would be sufficient to meet ESP requirements and prevent discrimination. However, this theory now can be tested based on several years of actual practice. LDDS understands that in fact the RBOCs have seen no material demand for ONA services. It is difficult, therefore, to

conclude that the ONA structure actually is effective in preventing access discrimination against ESPs. The Notice points to the existence of several large national value-added network companies. However, it is not possible to conclude that ONA or other nonstructural rules have prevented RBOC access discrimination against these firms. Importantly, the MFJ interLATA prohibition has kept the RBOCs from participating in this market, and therefore eliminated much of the incentive for discrimination. If the interLATA restriction is lifted, other safeguards against RBOC discrimination will become much more important.

In short, a new cost-benefit analysis leads directly to the conclusion that separation is necessary and appropriate. The real question is not *whether* but *when* separation should be required. LDDS believes that the Commission never should have abandoned separation, and that separation rules should be restored as soon as possible. This action would immediately improve the competitiveness of the enhanced services market. And it would have the additional benefit of establishing a framework for RBOC provision of other competitive services in the future.

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COMMENTS OF LDDS COMMUNICATIONS, INC.

LDDS Communications, Inc. d/b/a LDDS Worldcom ("LDDS")

respectfully submits its comments in response to the Commission's Notice of Proposed Rulemaking in the above-captioned proceeding, FCC 95-48, released Feb. 21, 1995 ("Notice").

INTRODUCTION

This proceeding responds to the decision of the United States Court of Appeals remanding the Commission's removal of structural separation requirements in the Computer III rulemaking. See California v. FCC, 39 F.3d 919 (9th Cir. 1994), cert. denied, 65 U.S.L.W. 3721 (1995) ("California III"). The Commission has solicited comments on whether it should rely completely on its ONA and related nonstructural regulations to prevent access discrimination by RBOCs in the enhanced services market, or alternatively whether structural separation should be reimposed on some or all RBOC enhanced services.

In its Comments here, LDDS first explains why structural separation requirements are logical and nonburdensome given the increasing likelihood that

RBOCs will be establishing new subsidiaries to offer interexchange and other competitive services. LDDS then discusses weaknesses in the current nonstructural rules that demonstrate the need for separation to ensure full competition in the future. LDDS believes that the principal issue in this docket is not *whether* RBOCs should provide enhanced services through separate subsidiaries, but *when*. LDDS believes separation would improve the competitiveness of the enhanced services market, and therefore supports reinstatement of separation as soon as possible. This decision is required by the court's decision in Computer III. More importantly, it will establish a framework for RBOC provision of other competitive services in the future. These matters are addressed further below.

I. THE PAST RATIONALE FOR ELIMINATION OF THE STRUCTURAL SEPARATION REQUIREMENT WILL BE MOOTED WHEN THE RBOCS BEGIN TO OPERATE SUBSIDIARIES FOR OTHER COMPETITIVE SERVICES.

LDDS believes that the Commission should not simply consider the structural separation question through the narrow prism of the remand proceeding or even of enhanced services. Rather, the Commission should ensure that decisions made here are harmonized with broader changes occurring in the telecommunications marketplace.

The most relevant of these developments is the increasing likelihood that the RBOCs will be required to establish new separate subsidiaries from which

they will market interLATA long distance and other competitive services. Such a subsidiary is a central requirement of the telecommunications legislation now before the Senate, and is expected to be part of the House bill to be introduced soon. The Justice Department similarly has made clear that creation of a separate subsidiary is a central precondition to any relaxation of the interLATA restriction, and Ameritech has agreed to create a separate subsidiary in its "Customers First" plan.

This is not the place for LDDS to explain in detail why it believes that RBOC provision of interLATA services would be premature at this time. We agree with the Justice Department that this element of the MFJ should be removed only if, when and where IXCs have an opportunity to provide local exchange service -- on both a resale and facilities basis -- that is economically equivalent to the opportunity RBOCs will have to enter the long distance market. In part this means that RBOCs must offer unbundled "carrier's carrier" bulk local service products so that interexchange carriers can easily add local service to their product line. InterLATA "carrier's carrier" products -- offered on a competitive basis by LDDS and other IXCs -- will be immediately available to the RBOCs as soon as the interLATA restriction is lifted. Comparable local service offerings must be available to IXCs.

In any event, widespread consensus exists that, assuming appropriate preconditions for RBOC long distance service are met, the RBOCs should provide that service through separate subsidiaries. It is agreed that such subsidiaries will

be necessary to protect against the strong residual incentives and abilities that the RBOCs will have to discriminate in favor of themselves in the provision of local exchange access to competing IXCs.

It is possible that local competition will not develop, either because legislation does not pass, the RBOCs may stymie the conditions necessary for such competition, or perhaps underlying cost conditions limit its development to isolated areas. The RBOCs then might not create separate subsidiaries for interLATA service anytime soon because such service would remain prohibited. However, LDDS believes that the wiser course is for the Commission to assume that at some point within the next few years the RBOCs will form separate subsidiaries as part of their eventual entry into the interLATA market.

LDDS believes that is likely the RBOCs will market a wide range of services through these subsidiaries. It is possible, in fact, that those separate subsidiaries will evolve to be the primary retail arms of the RBOCs, marketing "one-stop shopping" packages of long distance and other competitive services to the public. In that event, this new RBOC "retail" subsidiary would not only purchase and resell interexchange access from the preexisting RBOC exchange carrier. The RBOC subsidiary would also purchase and resell the basic local exchange services of its operating company affiliate, as well as the unbundled features and functions necessary for enhanced services. This structure already is in place in Rochester, New York under the Rochester Open Market Plan.

In short, as the Commission evaluates the costs and benefits of separate subsidiaries for RBOC enhanced services, it should recognize that the Computer III proceeding is in a sense coming back full circle to where it started. The Commission opened that docket in 1986 in large part because it perceived that it would be inefficient to require the RBOCs to establish separate subsidiaries. The Commission concluded that "fundamental unbundling" of the RBOC local network and other safeguards would be less costly than the maintenance of separate subsidiaries limited to the narrow purpose of providing enhanced services. The Commission also wanted RBOCs to be able to market local and enhanced services together. Consequently, the Commission began a process of developing ONA requirements and related rules to address the undisputed dangers of RBOC cross-subsidization and discrimination. The Commission hoped that these non-structural rules would enable it to excuse the RBOCs from the structural separation requirements that then bound them. The test it applied was whether the costs of structural separation were outweighed by the benefits, and whether alternative nonstructural means could accomplish the same goals at lower cost.

In the Notice the Commission requests comment on the adequacy of various regulatory policies it has adopted to prevent anticompetitive discrimination with regard to the provision of enhanced services. This is the issue on remand from the Court of Appeals, which correctly challenged the adequacy of the record on these points. LDDS remarks on them briefly in the following section.

More importantly, however, the Commission should use this proceeding to reassess its previous conclusion that separate subsidiary requirements are too costly and inefficient. For purposes of argument, one might accept that this could be true if, as in the past, RBOCs would have to establish a separate subsidiary solely to market enhanced services. But as discussed above, the telecommunications world is in the process of change. RBOCs are likely to be operating separate subsidiaries soon -- perhaps not this year, but as soon as they are permitted to provide interLATA services in their respective regions, that will be positioned to offer the full range of competitive retail services. 1/

In these circumstances, the cost of requiring the RBOCs to provide enhanced services through these same separate subsidiaries would now be relatively small if not trivial. RBOCs would incur few additional administrative costs beyond those already inherent in the operation of the subsidiary to market interLATA and perhaps other competitive services. Furthermore, to the extent that the Commission originally deleted the separate subsidiary requirement because it wanted RBOCs to be able to market enhanced services together with basic service, the "new" RBOC subsidiary could do that as well. However, that subsidiary would have to purchase ONA features and a wholesale local service from its "old" exchange carrier company on a non-discriminatory basis, just as the new subsidiary would buy access for long distance services on that basis.

1/ RBOCs will operate separate subsidiaries even sooner if they are permitted to provide interLATA service outside their regions through such subsidiaries at an earlier date.

In short, as the Commission develops its response to the court, it should take a broader perspective regarding the alleged cost burdens of requiring RBOCs to offer enhanced services through separate subsidiaries. The more likely it becomes that the RBOCs will establish such subsidiaries to satisfy other requirements, the less burdensome it becomes to require them to market their enhanced services through such entities.

II. NON-STRUCTURAL SAFEGUARDS ARE NOT ADEQUATE TO PREVENT ANTICOMPETITIVE DISCRIMINATION.

The emerging consensus on structural separation is particularly important given the problems with the non-structural safeguards that the Commission has adopted in lieu of separation. Although the Commission suggests in the Notice that those safeguards have been effective, the court in California III expects this hypothesis to be tested rigorously in the remand proceeding here. LDDS believes that when the Commission does so, it will be forced to conclude that the safeguards, while not meaningless, have not proven sufficient to prevent anticompetitive discrimination. The important benefits of separation are therefore more clear than ever.

A. ONA

The Commission suggests, first and foremost, that the ONA plans provide significant safeguards against anticompetitive RBOC conduct. The

Commission takes this position even while acknowledging its retreat from the "fundamental unbundling" it originally argued was critical.

The starting point for this analysis should be an empirical review of the use that enhanced service providers ("ESPs") 2/ actually have made of unbundled network elements to date 3/ The Commission now has several years of experience since the ONA plans took effect. If unbundling and related ONA rules are useful, one would expect to see many ESPs purchasing services out of the ONA tariffs for use in competition with the RBOCs.

But to LDDS's knowledge, ONA has not proven useful. Indeed, at the time the LECs originally filed their federal ONA tariffs, they themselves projected little or no ESP demand for ONA services, 4/ and subsequent tariff filings have

2/ LDDS recognizes that the Commission sometimes has taken the position that ONA safeguards are applicable to RBOC services provided to ESPs for use in connection with enhanced services, but not to similar services provided to IXC's if the services are characterized as basic transmission. See, e.g., Third Memorandum and Opinion and Order, Transport Rate Structure and Pricing, CC Docket No. 91-213, at para. 73 (released Dec. 22, 1994). Thus, one set of cost rules sometimes applies to a switching function that can be used by ESPs (and IXC's) such as ANI, and another set of rules may apply a different function on the same switch that supposedly is not used by ESPs. LDDS believes that these distinctions constitute unlawful discrimination in violation of Section 202 of the Communications Act. However, that is not an issue presented directly here. We make the point only so that our references here to ESP use of ONA services is not misconstrued otherwise.

3/ The Commission apparently tracks ONA service availability, but it is less clear that the Commission has required the RBOCs to provide adequate information regarding how much those services actually are used by ESPs.

4/ See, e.g., Petition of the Competitive Telecommunications Association for Suspension and Investigation of the ONA Access Charge Tariff Filings at 9; US Sprint Petition to Reject or Alternatively Suspend and Investigate the ONA Access Tariffs at 3-8 (filed Nov. 26, 1991).

confirmed the accuracy of those initial projections. In their most recent TRPs the RBOCs show little demand for ONA beyond the unbundled feature groups that IXC's (not ESPs) use for access. And that unbundling does nothing other than substitute for preexisting access service that the IXC's already were purchasing in bundled form. ONA has not created any materially new demand or opportunities for ESPs. For example, in their 1994 Annual Access Tariff Filings RBOCs reported the following percentages of interstate switched minutes that were ONA-related:

	<u>Percent</u>
Nynex	0.01%
Bell Atlantic	6.26%
Bell South	0.03%
Ameritech	3.12%
SWB	0.03%
US West	0.07%
Pacific	0.01%

LDDS would expect that most of even these minutes are attributable to feature group unbundling and purchased by IXC's, not ESPs.

LDDS is not opposed to unbundling per se -- far from it. But the question here is whether the unbundling actually provided by the RBOCs in their ONA tariffs has been done in a useful and nondiscriminatory manner. If the ESPs are not making significant use of ONA, then this would suggest that the tariffs as currently written (in structure and price) fail to meet the needs of RBOC competitors. The absence of substantial ESP demand suggests that the RBOCs have been able to manipulate ONA to their own advantage, and that ONA without structural separation is not sufficient. Perhaps the anticompetitive discrimination

is in the features offered by the RBOCs; perhaps it is in the ONA price charged ESPs; 5/ perhaps it is in the provisioning. 6/ In any event, with structural separation, the RBOC exchange company would, by definition, have more incentive to create unbundled ONA services that both its separated affiliate and other ESPs can find useful, and discrimination can be more easily monitored and prevented.

B. Market Forces

The Commission also suggests that market forces in the enhanced and basic services markets may check RBOC access discrimination against competing ESPs. See Notice at para. 32. But the Commission should move cautiously before reaching this conclusion, and in particular not mix apples and oranges. For example, the Commission points to large national enhanced services providers such as EDS, MCI and IBM. Id. at n.81. But the success of these companies has occurred in an environment in which the MFJ's interLATA service restriction has prevented the RBOCs from competing directly. That restriction, of course, rests on

5/ In principle RBOCs presumably must charge themselves the same rates for interconnection and features as they charge their competitors. However, it is unclear whether any meaningful protection is accomplished by standards which allow the LEC to recover its common costs from all providers, while its competitors may only recover these costs from their own customers.

6/ The Notice suggests that discrimination in provisioning has not occurred, pointing to the RBOCs' "nondiscrimination reports" comparing the quality of provisioning provided to the ESPs with that provided to the RBOCs themselves. See Notice at para. 29. But these reports still beg the question of how widely ESPs use ONA services in the first place. The Commission also notes that no formal complaints have been filed alleging access discrimination. Leaving aside the well-known infirmities of the Commission's complaint processes, however, the more relevant fact is that ESPs may not complain about discrimination in the provisioning of services they do not want, and do not purchase.

a fundamental recognition of the ability and incentive the RBOCs to discriminate. So long as the RBOCs are unable to operate in those national market segments, they have less incentive to discriminate among the participants.

As a result, the current competitiveness of the national value-added network market says nothing about the need for or efficacy of current non-structural safeguards. If anything, future elimination of the MFJ would make it all the more important that the Commission have effective rules in place to prevent access discrimination against ESPs as well as IXCs. ^{7/}

Furthermore, the competitiveness of the national market for VANs says nothing about the local market where the RBOCs now are free to compete, particularly insofar as participants in that market might rely on the use of RBOC network functions. The court of appeals rightfully can expect the Commission to present empirical evidence that its current safeguards are working in this market. Unfortunately, the absence of demand for ONA suggests otherwise.

C. Price Caps

The Notice is strikingly silent on the relationship between price cap regulation and discrimination. This is not surprising, for price caps were not

^{7/} The Notice suggests that large value-added service companies could be expected to monitor their access, "reducing the ability of the BOCs to discriminate." Notice at para. 33. However, the Commission presumably is not intending to suggest that once the RBOCs are allowed to compete with these companies, they will not discriminate against them simply because those firms are large. Obviously a serious concern remains that RBOCs will discriminate against IXCs once the RBOCs are in the interLATA market, even though some of those firms are much larger than the value-added networks ("VANs").

designed to prevent access price discrimination in any meaningful respect. The problem is the reverse; the Commission's reliance on the current defective price cap system prevents it from identifying and correcting anticompetitive access discrimination by the RBOCs.

LDDS has explained in the Price Cap Review Proceeding why and how price cap regulation fails to address discrimination. For present purposes, we incorporate our comments in that docket here by reference. ^{8/} Put simply, the Commission does not have any meaningful tools to prevent a RBOC from unreasonably raising the price of a BSE used by one of its ESP competitors, and lowering the price of a different BSE used for its own services, so long overall the price cap limitations are not exceeded.

In order to respond adequately to the court of appeals, the Commission must be able to demonstrate how the RBOCs will be prevented from engaging in discrimination in the pricing of both unbundled BSEs, and the local, intrastate and interstate transport services that go with them to make up the enhanced service. Absent such a showing, which LDDS does not believe can be made, the Commission will be hard-pressed to justify its abandonment of structural separation.

^{8/} See Comments of WilTel, Inc. (filed May 9, 1994) and Reply Comments of WilTel, Inc. (filed June 21, 1994), CC Docket No. 94-1. LDDS acquired WilTel earlier this year.

III. THE COMMISSION SHOULD REQUIRE CREATION OF SEPARATE SUBSIDIARIES NOW.

To summarize, the Commission's current regulatory policies are not sufficient to prevent access discrimination by RBOCs against their ESP competitors. It follows that the Commission should more closely examine the benefits of structural separation for RBOC enhanced services.

When the Commission reviews structural separation, it should conclude that this safeguard is just as necessary to prevent anticompetitive RBOC access discrimination against ESPs now as it will be to prevent access discrimination against IXC's when the RBOCs begin to compete in the long distance market. Because separate subsidiaries will be required for the latter purpose anyway, the cost burden of placing enhanced services in the new "competitive service" subsidiary will be small. And this structure need not interfere with the RBOCs' ability to market enhanced services with basic local service as well as interLATA service. "One-stop shopping" is particularly suited to a separate subsidiary environment, as the Rochester Open Market Plan suggests.

In the end, the only question for the Commission is not whether the RBOCs should be required to sell enhanced services through a separate subsidiary, but when. LDDS submits that the Commission should respond to the California III court by ordering the creation of RBOC separate subsidiaries as soon as possible. Such subsidiaries will increase the competitiveness of the enhanced services market. They also can provide the foundation for RBOC provision of other competitive services in the future.

CONCLUSION

The Commission should recognize that discrimination in the provision of residual monopoly local services, whether to an ESP or a carrier (or a firm acting as both), will be its primary regulatory problem as the RBOCs increasingly compete with other providers. The importance of this problem should not be underestimated as a result of the difficulty in measuring the full harm of RBOC discrimination. Put simply, anticompetitive discrimination is a "silent killer"; it often prevents the development of new service providers altogether, so they are not able to complain and their absence is not obvious. We did not see the arrival of hundreds of IXCs until the MFJ and divestiture reduced discrimination in favor of AT&T. Similarly, we do not know how many creative new enhanced service providers now would be present in the local market if the RBOC operating companies had less ability and incentive to discriminate in favor of themselves.

Structural separation of competitive RBOC services -- including the enhanced services at issue here -- will be central to the Commission's ability to prevent such discrimination effectively, with the fewest resources, and with the least interference with market forces where, in the more competitive sphere, they exist.

In short, as it reviews the record here, the Commission should not again try to justify elimination of separate subsidiaries to the court of appeals. Rather, the Commission should take a fresh look at this issue in light of changing

conditions, the likelihood of separate subsidiaries for interLATA and other services, and real world ONA experience. The Commission should then restore structural separation as soon as possible.

Respectfully submitted,

LDDS Communications, Inc. d/b/a
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April 7, 1995

CERTIFICATE OF SERVICE

I, Patricia A. Green, hereby certify that on this 7th day of April, 1995, copies of the foregoing "Comments of LDDS Communications, Inc." were served by mail, postage prepaid, to the following:

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