EX PARTE OR LATE FILED

HOGAN & HARTSON

L.L.P.

COLUMBIA SQUARE
555 THIRTEENTH STREET NW
WASHINGTON DC 20004-1109
(202) 637-5600

DOCKET FILE COPY ORIGINAL

RECEIVED

AUG 17 1995

FEDERAL COMMUNICATIONS COMMISSION
OFFICE OF SECRETARY

LINDA L. OLIVER
COUNSEL
DIRECT DIAL (202) 637-6527

August 17, 1995

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 Communication in CC Docket No. 94-1

Dear Mr. Caton:

On August 16, 1995, Genevieve Morelli, General Counsel, CompTel; Joseph Gillan, on behalf of CompTel; and I, on behalf of WorldCom, Inc., d/b/a LDDS WorldCom, met with Mark Uretsky, Assistant Chief of the Common Carrier Bureau. The purpose of the meeting was to discuss the position of CompTel and LDDS WorldCom in CC Docket No. 94-1. The attached handouts were used in our discussion.

I have hereby submitted two copies of this notice to the Secretary, as required by the Commission's rules. The filing is submitted today because of the late hour of yesterday's meeting. Please return a date-stamped copy of the enclosed (copy provided).

No. of Copies rec'd 0+1
List A B C D E

Please contact the undersigned if you have any questions.

Respectfully submitted,

Linda L. Oliver

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

Enclosures

cc: Mark Uretsky
Genevieve Morelli

FILE COPY

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.

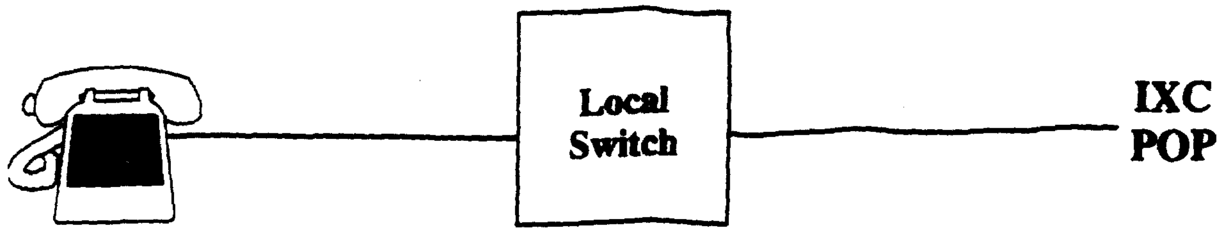
B. Loop unbundling and local competition exposes the overpricing of access service by providing selective rate relief to only one class of customer (the entrant that provides both local and long distance service). The Commission should correct this problem at its source by reforming the level of access 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	

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(
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.
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)(
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 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 ann revenue requirement of $39,400,000 (monthly requirement of $3,283,333, as shown in BA-MD's ta PSC 217 - Section 3.8(A) multiplied by 12) by its 1993 intrastate access minutes of 2,230,154,00(

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

Comparison of NYNEX and ACC-Syracuse
Switched Access Rates

Intrastate InterLATA: Day

	NYNEX	ACC	ACC-MP
CCLC	$0.0202	$0.0200	$0.0202
Local Switching	$0.0085	$0.0155	$0.0160
Interconnection	$0.0000	$0.0000	$0.0025
Total	$0.0287	$0.0355	$0.0387

Intrastate InterLATA: Evening

	NYNEX	ACC	ACC-MP
CCLC	$0.0172	$0.0170	$0.0172
Local Switching	$0.0072	$0.0130	$0.0136
Interconnection	$0.0000	$0.0000	$0.0025
Total	$0.0244	$0.0300	$0.0333

Intrastate InterLATA: Night/Weekend

	NYNEX	ACC	ACC-MP
CCLC	$0.0141	$0.0140	$0.0141
Local Switching	$0.0060	$0.0110	$0.0113
Interconnection	$0.0000	$0.0000	$0.0025
Total	$0.0201	$0.0250	$0.0279

ACC: Rates that apply when only ACC facilities are used.

ACC-MP: Rates that apply when ACC is reached using facilities of another LEC in addition to ACC.

ACC Syracuse Telecom Corp.

First Revised Page 25
Supercedes Original Page 25

RATE ATTACHMENT

CARRIER ACCESS SERVICES

Reference: Section 12.3

All charges per minute unless otherwise noted

	Direct Access	Clear Access On-Net	Clear Access Off-Net
Intrastate InterLATA Day:			
Carrier Common Line:	.020000	.020200	.020200
Local Switching:	.015500	.016000	.016000
Intercept:	0	.000122	.000122
Interconnection:	0	.002500	0
Local Transport:	.002600	.010400	.005200
Local Transport Mileage: #	.000200	.000207	.000207

Rate assessed per minute per mile.

Date Issued: June 5, 1995

Date Effective: [redacted]
Aug 19, 1995

Issued By: Michael L. LaFrance, President
400 West Avenue
Rochester, New York 14611

ACC Syracuse Telecom Corp.

First Revised Page 26
Supercedes Original Page 26

RATE ATTACHMENT

CARRIER ACCESS SERVICES

Reference: Section 12.3

All charges per minute unless otherwise noted

	Direct Access	Clear Access	
		On-Net	Off-Net
Intrastate InterLATA Evening:			
Carrier Common Line:	.017000	.017200	.017200
Local Switching:	.013000	.013600	.013600
Intercept:	0	.000104	.000104
Interconnection:	0	.002500	0
Local Transport:	.002200	.008800	.004400
Local Transport Mileage: #	.000170	.000176	.000176

Rate assessed per minute per mile.

Date Issued: June 5, 1995

Date Effective: [redacted]
Aug 19, 95

Issued By: Michael L. LaFrance, President
400 West Avenue
Rochester, New York 14611

ACC Syracuse Telecom Corp.

First Revised Page 27
Supercedes Original Page 27

RATE ATTACHMENT

CARRIER ACCESS SERVICES

Reference: Section 12.3

All charges per minute unless otherwise noted

	Direct Access	Clear Access On-Net	Clear Access Off-Net
Intrastate InterLATA Night/Weekend:			
Carrier Common Line:	.014000	.014100	.014100
Local Switching:	.011000	.011300	.011300
Intercept:	0	.000085	.000085
Interconnection:	0	.002500	0
Local Transport:	.001825	.007300	.003650
Local Transport Mileage: #	.000140	.000145	.000145

Rate assessed per minute per mile.

Date Issued: June 5, 1995

Date Effective: [redacted]
Aug 19, 95

Issued By: Michael L. LaFrance, President
400 West Avenue
Rochester, New York 14611

ACCESS SERVICE

3. Carrier Common Line Access Service (Cont'd)

3.8 Rates and Charges

The rate for Carrier Common Line Access is:

Transitional Charge	Day	Rate** Evening	Night	
Premium Access Charge				
InterLATA FGA terminating,* Access minute, each	$0.0240#	-	-	(C)
InterLATA FGA, originating Access minute, each	0.0198#	-	-	
InterLATA FGB, C, and D Access minute, each	0.0202	0.0172	0.0141	
IntraLATA FGA terminating* Access minute, each	0.0240#	-	-	(C)
IntraLATA FGA originating Access minute, each	0.0163#	-	-	
IntraLATA FGB, C, and D Access minute, each	0.0166	0.0100	0.0058	
Non-Premium Access Charge				
InterLATA FGA terminating* Access minute, each	0.0240#	-	-	(C)
InterLATA FGA originating Access minute, each	0.0121#	-	-	

* FGA Monthly Rate, as set forth in 6.8.7(A) also applies. (C)

** Time of Day usage rates apply as set forth in 6.7.1(A)(1),(2) and 3 following.

\# Time of Day usage rates do not apply to FGA.

Effective date of revision postponed to 10/24/94 see supplement No. 106

ACCESS SERVICE

6. Switched Access Service (Cont'd)
6.8 Rates and Charges (Cont'd)
6.8.3 End Office

(A) Local Switching

	*Rate Per Access Minute			
	Day	Evening	Night	
LS1				
- Feature Group A***				
- terminating**	$0.0330	0.0297	0.0264	(1)
- originating**	0.0242	0.0218	0.0194	(1)
LS2 - InterLATA				
- Feature Groups B, C and D	0.0085	0.0072	0.0060	
LS2 - IntraLATA				
- Feature Groups B, C and D	0.0085	0.0051	0.0030	

Effective date of revision postponed to 9/24/94 - see supplement No. 10

* Time of Day usage rates apply as set forth in 6.7.1(A)(1), (2) and (3) preceding.

** FGA Monthly Rate, as set forth in 6.8.7(A) also applies. (C)

*** A Volume Discount applies to FGA as set forth in 6.7.1 (G).

(1) Reissued material scheduled to become effective July 1, 1994.

EX PARTE PRESENTATION OF LDDS WORLDCOM

LEC PRICE CAPS FURTHER NOTICE
CC DOCKET NO. 94-1

QUESTIONS THAT SHOULD BE INCLUDED IN THE PRICE CAP FURTHER NOTICE

A. General Issues

- Retail/Wholesale Distinctions. How does discrimination in the pricing of wholesale inputs to competitors (access, interconnection, loops, etc.) differ from discrimination in the pricing of retail services to end users? Should price cap regulation distinguish between the two? Should more stringent regulation apply to wholesale services?

- RBOC Reentry. How much would interLATA entry by the RBOCs increase the incentives for discrimination in access pricing? How should that be dealt with (a) in the regulation of wholesale services used by RBOC competitors?; (b) in the regulation of retail RBOC interexchange services?

- Impact of Separation. Does the transition to a more competitive telecommunications environment require new safeguards in addition to changes to price cap regulation? For example, assuming separation of RBOC retail long distance services is required, should different price cap rules apply to the wholesale interconnection and access rates of the original subsidiary than to the retail long distance rates of the new separated entity?

- Relationship to Local Competition. How will the FCC's price cap rules intersect with attempts to create local competition? To the extent that wholesale LEC network facilities will be used by competitors to provide local service, how will the FCC's regulation of those facilities for interstate access be harmonized with state regulation?

- Distinction between local and access competition. The local service provider will retain bottleneck power over access to its customer required by other vendors such as long distance companies. How should this problem be reflected in price cap considerations for LECs? How should the Commission treat the market power of new LECs over access to their developing customer bases?

- Extent of Competition. At the most general level, how will local network competition develop? Where will it grow first? What elements will present continuing market power problems?

B. Price Cap Specific Issues

- What protections against discrimination can be built into the price cap plan?

- How can increased pricing flexibility be implemented so as to minimize the risk of discriminatory and anticompetitive pricing?

- Should the Commission adopt general guidelines for evaluating the allocation of shared network costs and overheads for access services (similar to those it has adopted in its review of expanded interconnection and video dialtone tariffs)?

- Should the new services test be modified to guard against discriminatory pricing of new services vis-a-vis existing services?

- How should the Commission ensure nondiscrimination in going-forward rates (after the new services test has been satisfied)?

- Should existing access rates be reviewed with discrimination concerns in mind? If not, what other tools should be used to address discrimination in preexisting LEC rates?

- What is the relationship between price cap changes and overall "access reform"? How much discretion should LECs be given in this process, and how will it impact discrimination concerns?

BACKGROUND

I. LEC PRICE CAPS PRINCIPALLY ADDRESS OVERALL RATE LEVEL PROBLEMS -- NOT DISCRIMINATION

- The price cap band and basket system was designed for AT&T, whose ability to discriminate is constrained by the existence of hundreds of IXC competitors, including both facilities-based carriers and resellers.

- Price caps were simply imported into LEC regulation, without extensive consideration of why discrimination concerns are more significant in the access sphere.

- But discrimination is a problem in the access market. Failure to protect against access discrimination can have serious consequences for competition in other retail markets:

(a) Discrimination in access is *more damaging to competition*.

Access is the primary input to a product (long distance), so discrimination among purchasers of the access product materially impacts their respective ability to compete. Outside of long distance, there are virtually no industries where a monopolist provider supplies an input that constitutes approximately 40% of the cost of the final product.

In contrast, discrimination among customers of long distance services is less damaging to society because long distance is virtually never the principal operating cost in an industry, so such discrimination is not competitively significant.

(b) Discrimination in access is becoming *more dangerous.*

- LECs (and in the future perhaps RBOCs) compete with those who depend upon access to their local loops, and for the most part other elements of the local network.

- Because access is a wholesale input for downstream retail services, access price discrimination has competitive consequences.

- Insofar as flaws in price cap regulation leave RBOCs free to discriminate, they are a key reason not to modify the MFJ.

(c) <u>Discrimination in access is becoming *more likely*.</u>

- In a fiber world an even greater amount of LEC costs relate to use of common network plant and overhead, costs that can be shifted in a discriminatory fashion.

- In a world of incipient competition, LECs have increased incentives to discriminate against those customers with the fewest competitive alternatives.
-
- The Commission's concern for discrimination in the recovery of common costs and overheads -- which it has made clear in connection with expanded interconnection and video dialtone -- is also critical in connection with access pricing.

(d) <u>Access competition *will not prevent discrimination.*</u>

- Until competition has developed in every access product and geographic market, the LECs will have the incentive and ability to recover the shared and common costs of the network, and overheads, from those services that are less competitive.

- Competition for tandem-switched transport remains virtually nonexistent.

- The Commission therefore cannot rely on competition to prevent discrimination.

(e) <u>Local service competition is *not* the same thing as access competition.</u>

- For example, even if a LEC loses 5% of its local customer base to a new local service provider, it will still have bottleneck control over access to the 95% of customers that remain with the LEC.

- Conversely, IXCs and others will be just as dependent as before on access to the LEC customers. The only difference is that now they also will be dependent on the new local service provider to reach the rest of the local customer market.

- The new local service providers also will be dependent upon the traditional LEC in their market.

- As a result, price cap changes cannot be driven by local service competition <u>per se</u>. LECs will have dominant market power in the wholesale access market for the foreseeable future.

II. THE COMMISSION MUST ADDRESS DISCRIMINATION UNDER LEC PRICE CAP REGULATION

In the Further Notice, the Commission should ask for proposals to address price discrimination within the context of price cap regulation. Such proposals might include the following, which LDDS WorldCom 1/ supports:

1. Structural Reforms: Price cap baskets and bands alone are not sufficient to prevent discrimination. The Commission should re-assess LEC rate relationships and consider measures such as price indexing across baskets to curb the LECs' ability to discriminate in the future. The Commission should also consider other access charge changes that would move access pricing closer to cost.

2. The New Services Test: The current test gives the LECs broad latitude to engage in strategic and discriminatory pricing. It sets a floor to prevent predatory pricing, but does not adequately address the LECs' ability and incentive to discriminate in the recovery of network overheads.

The Commission should propose the adoption of pro-competitive pricing principles to evaluate new and restructured LEC services:

- Prospective (not historical) costs should be used.
- Direct costs for all services should be determined using a long-run incremental cost approach.
- Uniform overhead allocations across all price cap services should be required (except as justified by LECs on a case-by-case basis).
- Other common costs or subsidy amounts should be recovered on a nondiscriminatory basis across all services.
- LECs should be given additional pricing flexibility only if price indexing is in place.

Each of these principles is necessary; failure to adopt any one would leave a large loophole for discrimination.

1/ WilTel, Inc., discussed these proposals at length in its comments filed in the LEC price cap review proceeding. LDDS WorldCom acquired WilTel early in 1995.