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Before the
FEDERAL COMMUNICATIONS COMMISSION
Washington, D.C. 20554

In the Matter of	)	
	)	
Price Cap Performance Review for Local Exchange Carriers	)	CC Docket No. 94-1
	)	
Treatment of Operator Services Under Price Cap Rules for AT&T	)	CC Docket No. 93-124
	)	
Revisions to Price Cap Rules for AT&T	)	CC Docket No. 93-197

COMMENTS OF TIME WARNER COMMUNICATIONS HOLDINGS, INC.

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SUMMARY

The NPRM appears to be based on the presumption that LECs face competitive pressures that are sufficient to justify increased regulatory flexibility. This presumption, however, is premature given the current and utter lack of true choice and competition in the market place. Relaxing price cap safeguards and granting LECs increased pricing flexibility prior to a conclusive showing by the LECs that they face actual competition would significantly impede progress toward the Commission's goal of developing a sustainable robust competitive marketplace. The Commission could better utilize its resources at this time by focusing on actions that will serve to eliminate entry barriers. The expeditious completion of the virtual expanded interconnection tariff investigation and telephone number portability proceedings will go much further in meeting the Commission's policy objectives than the unwarranted granting of pricing flexibility to the LECs.

The Commission's proposal to eliminate the lower service band limits would not effectively advance its efforts to promote competition. Rather, such drastic action at this time and for the foreseeable future would most likely result in LECs abusing this opportunity by reducing prices to preclude CLECs from effectively competing. The market place is many years away from having developed enough depth or restraints to prevent such abuses.

Any proposals for relaxed regulatory treatment must be

conditioned on LECs substantiating the existence of effective facilities-based competition. A competitive checklist could provide a starting point for Commission analysis of market entry barrier status, however the checklist proposed in the NPRM must be further refined and developed before it can be implemented. Although such a checklist represents an important tool for determining whether the potential for competition exists (i.e., whether barriers to entry have been eliminated), the ultimate indicator of whether a LEC faces real, rather than hypothetical, competitive pressure is whether its potential competitors have gained and managed to hold significant market share. Care must be exercised to not inadvertently trade short-term price gains for the long-term benefits to the consumer that a truly competitive marketplace will bring.

Should the Commission determine that some reductions in the price cap regulatory requirements are warranted, it is critical that the Commission proceed cautiously and implement relaxed regulations or pricing flexibilities gradually so that the Commission can properly monitor the affected markets. Finally, the Commission must, at a minimum, adopt procedures that provide competitors and other interested parties with adequate notice when a LEC requests relaxed regulatory treatment. Interested parties should have an opportunity to monitor LEC actions and to ensure that LECs are not able to exert their continuing market power in an anticompetitive fashion.

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COMMENTS OF TIME WARNER COMMUNICATIONS, HOLDINGS, INC.

INTRODUCTION

Time Warner Communications Holdings, Inc. ("TW Comm")[1] has substantial reservations regarding the Federal Communications Commission's ("FCC" or "Commission") tentative plan, set forth in its Second Further Notice of Proposed Rulemaking ("NPRM"),[2] to modify the Local Exchange Company ("LEC") price cap plans by implementing specific changes to interstate access price regulation based on unproven changes in the marketplace. The modifications being proposed are largely unrelated to changes taking place in the competitive landscape for local service carriers, arise out of misperceptions regarding the relationship between price caps and pro-competitive behavior, and, as

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1 TW Comm is a wholly-owned subsidiary of Time Warner Entertainment Company, L.P.

2 In re Price Cap Performance Review for Local Exchange Carriers, Second Further Notice of Proposed Rulemaking, CC Docket No. 94-1, FCC-93-393 (Sept. 20, 1995) (hereinafter "LEC Pricing Flexibility NPRM" or "NPRM").

structured, could impede the very competition that the Commission is trying to nourish.

A. TW Comm's Global Concerns Regarding Modification Of LEC Price Cap Plans

The NPRM is extensive, with over 130 operative paragraphs and 21 multi-part issues. Although TW Comm responds herein to each of the 21 issues identified in the NPRM, TW Comm's individual responses must be read in the broader context of various global concerns that TW Comm has regarding the regulatory regime proposed in the NPRM.

The NPRM sets forth three gradations of increasingly less stringent price regulation. At the first level, additional downward pricing flexibility would be granted to LECs by changing the service baskets and categories within the LECs' price cap plans. The additional pricing flexibility would be effective for all price cap LECs without regard to the current level of competition. At the second level, all price cap LECs that are able to demonstrate substantial competition for particular services within a geographic market would be able to remove those services from price cap regulation in that market and place them under streamlined regulation. LECs would be allowed to file tariffs on 14 days' notice. The LECs' tariffs would be presumed lawful for purposes of review, would be filed without cost support, and would no longer be subject to price cap ceilings or upper or lower pricing limits. Finally, at the third level, a price cap LEC that demonstrates that it no longer exercises

market power for particular services in a geographic market would qualify for non-dominant regulation as to those services in that market and the LEC would be able to file tariffs on one days' notice with no cost support.[3]

Even at the first level, the regulatory framework proposed in the NPRM raises difficult issues given the context and history of price caps. Price cap regulation was originally implemented in the absence of meaningful competition and was designed to provide LECs with an incentive to be more efficient under those circumstances, not to provide incentives to become more competitive. TW Comm is concerned that the NPRM's proposals for modifying LEC price caps based on competition represent an exercise fraught with significant risk to both LECs and emerging competitors, since there is a high likelihood that either over or under estimation of the amount of actual competition that exists in the market could occur. To the extent that the Commission adjusts price cap baskets and bands in response to the mere potential for competition, rather than based on the existence of actual competition, the LEC will not be incented to remove entry barriers and competition will clearly suffer. It is therefore critical that the Commission accurately establish the presence and level of competition utilizing a comprehensive competitive checklist, coupled with an inquiry as to the LECs' actual market share, before modifying the existing primary restrictions on LEC anti-competitive behavior: the price cap baskets and bands.

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[3] Id. at paras. 2, 34.

The NPRM's proposal to provide LECs with greater regulatory freedom is premature. TW Comm does not disagree with the NPRM's assertion that "increased competition for LEC services is inevitable"[4] but strongly disagrees with the NPRM's determination regarding the timing of when competition will fully emerge. It is at best overly optimistic to believe that it is necessary or even possible to decide today when the time will be ripe to permit streamlined regulation of price cap LECs. To reach its goal of achieving a robust competitive marketplace, the Commission's and the industry's resources would be far better utilized in moving forward with eliminating existing barriers to entry.

Moving ahead with pro-competition issues such as virtual collocation and true number portability, rather than future relaxation of regulatory restraints on price cap LECs should be the Commission's first priority. While some progress has been made on these issues, they are far from resolved and, more importantly, the pro-competitive impact of the Commission's recent initiatives has not been felt by emerging competitors. The NPRM, however, presupposes that the Commission's competitive initiatives not only have been completed, but that they have had the desired effect of stimulating competition.

The Commission should not engage in that presupposition. Regulatory oversight of the LECs should not be loosened in anticipation of a competitive market, but rather it

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[4] Id. at para. 133.

should be loosened only in response to the existence of a competitive market. The mere fact that the Commission appears to be seriously considering at this time the possibility of greatly reduced oversight of LECs sends a chilling signal to potential investors in emerging facilities-based competitors. The NPRM therefore raises significant difficulties, both practical and theoretical, that must be carefully examined and resolved.

1. Relaxed Regulatory Requirements Are Not Warranted At This Time

The Commission's stated goals of moving prices toward costs, encouraging efficient investment in infrastructure, and ultimately producing robust competition will not be accomplished if the proposed modifications to LECs' price cap plans are implemented prior to the LECs demonstrating that existing barriers to competition have been eliminated.

Loosened regulatory controls prior to the LECs satisfying an objective set of competition criteria, including a demonstration that competitors have gained and can sustain substantial market share, would discourage efficient investment in infrastructure. Lessened regulation is appropriate only where the LECs can conclusively demonstrate that true competition exists for a particular service within a prescribed geographic market. If a lower degree of regulatory oversight is implemented prior to a showing of true competition, all potential facilities-based carriers will face dramatically increased business risks since the incumbent LECs, prematurely released from pricing

restraints, have every incentive to specifically target with predatory pricing the services being offered by emerging facilities-based competitors. These circumstances could raise the emerging facilities-based providers' cost of capital significantly, or result in required financing being uneconomic or unavailable. Robust competition will only be possible if customers have a choice of providers and facilities. Without true facilities-based competition, the Commission's goal of creating a sustainable and robust competitive marketplace cannot be obtained.

The framework and structure of the NPRM appears premised upon the presumption that the LECs currently face significant competitive challenges in the marketplace and that these challenges necessitate immediate modifications to the price cap regime. This presumption is not supported by actual marketplace conditions. The LECs' market power remains virtually unfettered today and they continue to be the dominant force in the local exchange market.[5] Relaxing the pricing restrictions and associated regulatory requirements for LECs under price caps is therefore premature. There is simply no need on the part of the LECs for the degree of regulatory flexibility that the NPRM tentatively proposes to provide to them.

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[5] The Commission recently found that the LECs retain considerable market power, even though some services are available on a competitive basis. See In re Price Cap Performance Review for Local Exchange Carriers, First Report and Order, 10 FCC Rcd 8961, para. 25 (1995).

2. Market Share Is A Primary Indicator Of Competitive Success

Before any significant relaxation of regulatory requirements is granted to the LECs, they should be required to demonstrate the existence of substantial competition for particular services within a specific geographic market. Although competitive checklists are important tools for determining whether the conditions for competition to develop exist, the ultimate indicator of whether a LEC faces real, rather than hypothetical, competitive pressure must be based on an analysis of whether potential competitors have gained and hold significant market share. Market share is the best indictor of competitive success.[6] Until LECs demonstrate that their competitors have managed to obtain and hold on to significant market share, the Commission should not consider granting further relaxation of pricing constraints.[7]

3. Long-Term Benefits Should Not Be Traded For Short-Term Price Gains

While the immediate removal of certain low price bands may temporarily lower the rates charged to some consumers, ultimately consumers would be harmed by such an action by being

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[6] While competitive checklists are useful tools, the checklists must be adjusted or modified if they are not producing the desired result; i.e., competition.

[7] The Commission should not lose sight of the significant pricing flexibility LECs already enjoy under the current price cap regulations.

denied the even greater price benefits that they would have obtained if facilities-based competition was allowed to emerge. If price cap restrictions are removed to such a degree that the LECs are able to use their overwhelming market power to prevent the emergence of such competition the public interest cannot be served.

The inherent tension between a long-term strategy which results in true competition between multiple facilities-based providers and a short-term strategy which provides an immediate reduction in consumer prices must be recognized. To survive, facilities-based providers must be able to derive revenue support from all forms of local service since doing so is the only way that they can effectively support their large fixed cost investment in facilities. Thus, the Commission's activities in this docket addressing the access market are closely linked to the success or failure of the competitive local services market. Competition in both markets, not just one or the other, must be encouraged.

4. <u>While No Conceivable Justification For Streamlining Notice Requirements Exists At This Time, The Framework Adopted Must Provide Adequate Notice To Competitors</u>

To the extent that the Commission elects to implement a new "reduced requirement" regulatory regime for LECs, it must allow the LECs' competitors adequate notice and a fair opportunity for them to determine, at a reasonable cost, the LECs' proposed actions, the impact of those actions on the markets, and whether or not the LECs' actions are consistent with

the Commission's new rules. With adequate notice, competitors can protect their own interests, and at the same time they will assist the Commission in effectively monitoring the LECs' compliance with the Commission's requirements.

5. The AT&T Criteria And Milestones May Be Applicable, But The Milestones Have Not Been Reached

The criteria and milestones utilized by the Commission in reaching its determination to grant AT&T additional regulatory flexibility may be applicable but such application is premature in the instant proceeding. The Commission loosened regulatory controls on AT&T only after many years of experience in dealing with the development of competition in the interexchange carrier market. By the second half of 1995, competition in the provision of IXC services was well-established and two very powerful competitors, MCI and Sprint, had emerged to wrest significant market share away from AT&T. By contrast, no competitors have yet succeeded in wresting significant market share from LECs in the local services markets.

No case can presently be made that LECs have lost sufficient market share to justify lessened regulation. Nor should the Commission believe that such market share loss will occur in the near future. Most state commissions have just begun to address the removal of barriers to entry for local competition. LECs, moreover, have exhibited strong resistance to the implementation of pro-competitive policies, as evidenced by the ongoing investigation of LEC tariffs for expanded

interconnection and by LEC resistance to implementation of true service-provider number portability. Further, the building of competitive networks to provide local switched service is highly capital intensive and will require years to accomplish. The Commission should not be persuaded that market share losses as a result of resale alone will sufficiently diminish LECs' market power, since LECs will continue to control and receive substantial revenue for the underlying facilities.

DISCUSSION OF ENUMERATED ISSUES

Issue 1a New Service Requirements Should Not Be Relaxed Since LECs Still Have Market Power

The NPRM proposes to modify the Commission's rules pertaining to the treatment of new services, such as shortening the notice requirements for restructured services, dividing new services into two categories - Track 1 and Track 2 - and excluding Alternative Pricing Plans ("APP") in the definition of new services.[8] The relaxation of the regulatory requirements relating to new services is premature since the LECs retain their tremendous economies of scale and scope, and continue to control a remarkably high percentage of the market.

If the Commission relaxes its regulatory scrutiny of new services at this time and under the existing market circumstances, the LECs will be free to utilize their preexisting market power to destroy nascent competition. The likelihood of

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[8] LEC Pricing Flexibility NPRM at paras. 39-52.

this occurring is increased in the situation where the relaxed regulatory treatment would allow LECs to label unbundled pieces of pre-existing services as new services. By utilizing pricing flexibility for new services, a LEC could quickly establish uneconomic rates for the unbundled pieces of various "old" services that emerging competitors must purchase from the LEC. As a consequence, granting LECs pricing flexibility for such "new" unbundled pieces of their existing services would grant them significant leverage and the direct ability to impair the economic viability of emerging competitors. The current level of regulation of new services remains appropriate and the LECs have failed to demonstrate adequate reasons for modifying that level. Even though maintaining the existing requirements may impose a burden on LECs, the burden is justified by the benefits, particularly since the burden will not markedly hinder the efficient introduction of new services. This is amply illustrated by the fact that the LECs have been able to freely introduce many new services over the last several years. They will continue to be able to do so in the future.

Should the Commission elect to divide LEC services into categories depending upon their potential impact upon competition, the proposal to establish two tracks is not without merit. Track 1 services would remain fully subject to current notice, cost support and other regulatory requirements. Track 2 services would receive reduced regulatory scrutiny and would be granted only to new services where no competitive implications have been shown to exist.

Track 1 services should include all new services that are essential to the LECs' competitors and, therefore, Track 1 treatment should be applied to virtually all interconnection services. TW Comm supports an "essential services" definition for Track 1 treatment since such a definition would allow competition to develop by ensuring that potential competitors can access the necessary and fundamental building blocks of the network.

The alternative proposal, that Track 1 service include only those services that are not "close substitutes" for an existing service,[9] should be rejected. First, the NPRM proposes determining that a service would be a "close substitute" if a LEC reasonably expects customers of its existing service to migrate to the new service. This standard of determining whether a service is a "close substitute" would place an emerging competitor in the unenviable position of challenging a theoretical argument by a LEC that it "reasonably expects" customers of an existing service to migrate to the new service.

Second, the "close substitutes" test implies that if a new service is a "close substitute" it will automatically be eligible for Track 2 reduced regulatory scrutiny. In fact, emerging local service competitors, such as TW Comm, are concerned the most about new services that are close substitutes of existing services or that are composed of unbundled pieces of existing services. It is in these areas that the LECs retain the

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[9] Id. at para. 47.

greatest market power and thus the ability to unfairly compete with the emerging competitors' service offerings. Rather than granting new services that are close substitutes of existing services reduced regulatory scrutiny, such services should continue to receive the highest degree of regulatory oversight.

Should regulatory requirements be reduced for Track 2 services, LECs must be required, at a minimum, to demonstrate that the price of the service will recover the direct cost of providing it with reasonable contribution to common overheads. Without this assurance, the LECs could easily price certain services below cost for the sole and predatory purpose of driving their competitors out of business.

The notice period provided should also be longer than the 14 days tentatively set forth in the NPRM. Emerging competitors with limited resources require more time to monitor the actions of the LECs and to determine whether such actions are consistent with the Commission's rules. Finally, even if a service otherwise qualifies for Track 2 treatment, wherever the Commission has prescribed special, specific cost and other filing requirements these special requirements should be maintained. In almost all instances, these requirements were imposed to rectify or prevent LEC abuses and these valuable consumer protection continue to be necessary.

Issue 1b The Definition For New Services Should Include APPs

The NPRM proposes revising the definition of new services to exclude APPs.[10] APPs are services that permit customers to "self-select" an optional discounted rate for a service that continues otherwise to be offered to customers at a non-discounted rate. New services should not exclude APPs since APPs can and do have a significant impact on the marketplace. TW Comm does not dispute that LEC customers may be protected adequately if APPs were excluded from new services. The original service offering was subject to normal regulatory review and the LECs' customers always have that service choice available to them.

However, competitors of the LEC are not similarly protected by this exclusionary policy. From a emerging competitor's perspective, APPs have the identical impact as an unfiled and unchallenged new service offering. That is, the potential exists for LECs to manipulate APPs to "lock-up" markets and customers to the exclusion of new entrants. For this reason, APPs should be defined as Track 1 new services subject to full regulatory requirements.

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[10] Id. at para. 52.

Issue 1c The Definition Of Restructured Services Should Be Retained With Little If Any Modification

Like "close substitutes," restructured services that are created by unbundling or repackaging separate pieces of existing LEC services raise competitive concerns. The current 45 day notice requirement for restructures should be retained since that period of time generally is necessary for LEC competitors to have an adequate opportunity to address a restructure and any discriminatory pricing issues that such filings might raise.

At a minimum, however, CLECs will require more than the 7 days notice tentatively proposed in the NPRM for rate decreases. Such a short notice period would not allow LEC competitors an opportunity to assess and respond to anti-competitive impact of the LECs' proposed restructured services.

Issue 2a APPs Should Be Treated Like New Services With Full Regulatory Oversight

The NPRM seeks comment on whether LECs should be allowed to file APPs and, if so, under what terms.[11] LECs should not be allowed to simply file APPs with little or no regulatory oversight. A LEC wishing to introduce optional discount plans for a service that it currently provides, in addition to the volume and term discounts that are currently permitted, should be required to treat the discount as a new service under the current rules. This treatment would prevent predatory pricing by the

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[11] Id. at para. 59.

LEC. Should the Commission allow LECs to offer additional optional discount plans for an existing service, LECs must bear the burden of demonstrating that the discounts have adequate cost support. In addition, a clear rationale regarding the LECs' allocation and treatment of costs must be made available to the public.

Issue 2b Before Offering Discount Services, LECs Must First Demonstrate That Competition Exists

If the Commission elects to prohibit LECs from introducing APPs as defined in the NPRM, TW Comm does not oppose the continuation of the existing appropriate volume and term discounts for switched access services. Such discounts must be premised on a showing by LECs that effective competition exists in the relevant market and that any discounts for switched access services are cost-based. If, and only if, a LEC can make these required showings should the Commission allow volume and term discounts. A discount that is neither for a competitive service nor cost-based should not be allowed.

Issue 3 A LEC Offering Service At ICB Rates Must Show That No Basis Exists For Establishing General Rates

The NPRM proposes that LECs seeking to offer common carrier services on an individual case basis ("ICB") should be allowed to do so upon making a showing that the service is so unlike any existing service that the LEC would have no reasonable

basis to develop generally available rates.[12] ICB rates could no longer be used when limited circumstances no longer applied, such as when a LEC has more than two customers for a service, or has provided the service for six months or more.

As the NPRM correctly recognizes, ICB pricing should remain, at all times, subject to the condition that if a carrier has more than two customers for common carrier service <u>or</u> has provided the service for six months or more, that it be presumed to have adequate experience to tariff the service. LECs seeking to offer common carrier services at ICB rates, except for special construction, should be required to show that these conditions for ICB pricing have been met and that the service is so unlike any other existing service that the LEC has no reasonable basis to develop generally available rates.

To ensure that LECs are in full compliance with this requirement, they should be required to file all ICB rates in a manner that sets forth the exact parameters of the service being provided under the rate. The LEC should also be required to make detailed information on the service readily available to interested parties. Any ICB filing by LECs also should be accompanied by a <u>clear</u> statement of the rationale of how the LECs' fixed costs were allocated to the particular service. Detailed cost support regarding associated variable costs should be required as well. To ensure that necessary information is available to prevent abuses of ICB pricing, written rationales

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[12] <u>Id.</u> at para. 65.

for the allocation of the fixed costs to an ICB service should not be subject to confidentiality protection. Interested parties must be able to freely review the rationale for the ICB pricing in order to understand the basis for the pricing scheme.

Issue 4a The Commission Should Articulate A Clear Standard For Part 69 Waivers

The NPRM proposes to modify the need for LECs to seek waivers of the Part 69 rules for new switched access services.[13] If the waiver process continues to be utilized, the Commission should establish a term certain during which filed waiver requests will be determined. Currently, the delay in resolution of waiver creates a level of uncertainty in the market place that is unfair to both LECs and potential competitors. The Commission should seek to rule on waiver requests within the same maximum 120 day notice period required of tariff filings.

Furthermore, the Commission should strictly enforce its existing policy that waivers should not call into question the validity of the underlying Commission rule or rules. In many instances, the LECs appear to be utilizing the waiver process as a method to seek additional pricing flexibility that, in essence, challenges the validity of some provisions of Part 69 itself.[14]

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[13] Id. at para. 70.

[14] See Pacific Bell Petition for Expedited Waiver of Part 69 of the Commission's Rules, filed June 19, 1995; BellSouth Telecommunications, Inc. Petition for Expedited Waiver of Part 69 of the Commission's Rules, filed June 30, 1995; GTE Operating Company Tariff F.C.C. No. 1, Transmittal No. 988, (continued...)

The existing Part 69 waiver process has added little to the certainty that all carriers reasonably expect regarding the way in which the Commission's rules will be administered. If the Commission intends to continue to grant waivers in this area, a clear articulation of the standards it will utilize in granting such waivers must be established. Perhaps a better course of action than continually struggling with waivers is to modify the underlying regulations in a manner that exempts specific areas from the waiver process such as making Part 69 inapplicable to new services that are based on new technologies. Explicit standardized exceptions would be administratively less burdensome and would promote regulatory certainty.

Issue 4b New Procedures Adopted By The Commission Must Not Be Administratively Burdensome

Comment is sought on how Part 69 waiver procedures should be coordinated with the process of determining whether a new service is Track 1 or Track 2.[15] TW Comm supports proposals that would conserve administrative resources while still meeting

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[14](...continued)
filed Aug. 25, 1995; Southwestern Bell Telephone Company Tariff F.C.C. No. 73, Transmittal Nos. 2433 and 2449, filed April 21, 1995. (The Commission Designated the issue of Southwestern Bell's Tariff filing for investigation on August 25, 1995. On November 29, 1995, the Commission terminated the investigation finding Southwestern Bell's Request for Proposal provision unreasonably discriminatory. In re Southwestern Bell Telephone Company Tariff F.C.C. No. 73, Order Terminating Investigation, CC Docket No. 95-140, FCC 95-476 (Nov. 29, 1995)).

[15] LEC Pricing Flexibility NPRM at para. 74.