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FEDERAL COMMUNICATIONS COMMISSION
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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 Regulation	)	CC Docket No. 93-124
	)	
Revisions to Price Cap Rules for AT&T	)	CC Docket No. 93-197

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REPLY COMMENTS OF TELEPORT COMMUNICATIONS GROUP INC.

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SUMMARY

Most of the Incumbent Local Exchange Carriers ("ILECs") ask that price caps be substantially relaxed on the basis that the present state of "competition" justifies such action. Such proposals are premature given the current, nascent state of competition. Price caps were implemented as a substitute for actual competition. Any significant modifications to price cap rules should, therefore, be directly tied to the presence of actual, measurable competition.

NYNEX proposes to tie price cap relaxation to the satisfaction of competitive checklists and to the "presence" of a competitor in the market -- regardless of the competitor's size, effectiveness, market share, or staying power. NYNEX's proposal to base regulatory relief on the "presence" of competitors is an unworkably subjective standard, in which ILECs will have every incentive to "detect" competitors behind every bush and tree and rush to deregulate themselves. There is, in the final analysis, no substitute for actual market share data -- competitors' net

revenues and customers served -- as a tool in evaluating the true "presence" of competition.

The Commission should, therefore, tie relaxation of price cap rules to meaningful changes in market conditions, including satisfaction of "competitive checklists." In particular, implementation of "bill and keep" compensation arrangements should be defined as a presumptively satisfactory compensation arrangement in establishing the criteria for satisfaction of such a checklist. Finally, price cap relief must be tied directly to changes in ILEC market conditions and market shares, as measured through systematic and verifiable processes, such as those under development in the Commission's Telecommunications Access Provider Survey proceeding.

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REPLY COMMENTS OF TELEPORT COMMUNICATIONS GROUP INC.

Teleport Communications Group Inc. ("TCG") offers the following Reply to the comments filed in the above captioned proceeding.

I. INTRODUCTION

The Comments filed by the Incumbent Local Exchange Carriers ("ILECs") support the vast majority of the Commission's proposals, such as those to establish Alternative Pricing Plans, eliminate the requirement for Part 69 waivers for new services, reduce notice periods, and

eliminate the lower Service Band Index limit. They advocate that these changes be made without regard to the presence of actual, measurable competition. A few ILECs propose to tie price cap relaxation to the satisfaction of competitive checklists,[1] while most ILECs go even further and ask that price caps be loosened on the basis that the present state of "competition" justifies such action.[2]

TCG submits, however, that the Commission's proposals to relax its price cap regulation are premature at this time, given the current, nascent state of competition.[3] Price caps were implemented as a substitute for actual competition. Any significant modifications to price cap rules should, therefore, be directly tied to the presence of

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1. *See, e.g.*, NYNEX at 30.

2. *See* SBC Communications at 52, US West at 31, BellSouth at 40, Pacific at 34, Bell Atlantic at 15, USTA at 10.

3. In particular, reduction of cost support requirements and notice periods for tariff filings will substantially reduce the ability of the Commission staff and interested parties to evaluate the reasonableness of ILEC tariff filings and seek suspension or rejection of improper filings. Reduced tariff notice periods will have the effect of channeling all objections to tariffs into Section 208 complaints, a remedy that is of limited usefulness when the tariff is preemptive of the market, or harms the competitive market.

actual, measurable competition. In that regard, TCG supports those proposals that would establish a direct linkage between regulatory relief for the ILECs and (1) the presence of the necessary preconditions for competition in the market, in particular the implementation of "bill and keep" reciprocal compensation, and (2) the existence of a meaningful and measurable degree of actual competition in the market.

II. PRICE CAP REFORMS SHOULD BE LINKED TO REAL AND EFFECTIVE COMPETITION AND APPROPRIATE RECIPROCAL COMPENSATION POLICIES

A. There Has Been No Significant Change in the Competitive Characteristics of the Marketplace Since the Commission Last Addressed Its Price Cap Rules.

The Commission last revised its price cap rules in April 1995. At that time, the Commission found that the record contained sufficient information to allow for a modest increase in downward pricing flexibility, and felt it necessary to retain a requirement that below-band rate reductions be accompanied by cost support.[4] The Commission

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4. *See* First Report and Order, 10 FCC Rcd at 9139-40.

now proposes to remove completely the lower price band limit, and with it the requirement that a LEC justify that the service is priced at or above cost, as well as to eliminate or relax other aspects of its price cap rules.

Given the Commission's refusal only nine months ago to further relax its price cap rules, any rapid reversal of that position must be based on a showing of a substantial change in the competitive environment in the succeeding period. No such showing can be made, and indeed the ILECs provide no credible, factual evidence of actual market share gains by competitors.

The few attempts by the ILECs or USTA to justify the position that the competitive market has changed are unconvincing.

The United States Telephone Association ("USTA") claims that competition "continues to emerge at a phenomenal rate."[5] However, USTA's evidence for this "phenomenon" is nonexistent. For example, USTA says that AT&T is reportedly "readying" itself for competition. Whatever the truth of that allegation, it is obvious that a company which is

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5. USTA at 4.

"readying" itself is not a company which is currently and actively providing local exchange service.[6] USTA also claims that competitive carriers are building networks and are forecast in several years to have substantial revenues. Again, this "evidence" does not demonstrate that ILECs have experienced any meaningful local competition, or that the character of that competition has changed significantly in the last nine months. In short, USTA's Comments only show that competitors may be coming -- not that competition has arrived.

TCG's experience is that the interstate access market has not become "competitive" in any sense in the last nine months. For example, New York State, presumably one of the jurisdictions where competition should be most noticeable, lacks any real switched local competition. TCG's New York market share for Switched Access was reported in April 1995

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6. It is also important to distinguish between local competitors that are constructing their own facilities, versus those that are simply reselling the ILEC's services, in analyzing the degree of competition. Resellers are in essence functioning as sales agents for the ILEC, and competition that is exclusively or predominantly resale-based does not provide the same character of competition as facilities based competition.

at less than 1%, even after ten years of operation.[7] TCG does not believe that its share of that market has increased in any significant degree in the months since. Moreover, TCG has been forced to petition this Commission to obtain essential number resources which New York Telephone had refused to provide to TCG,[8] demonstrating the degree of market power (and bottleneck control) that NYNEX continues to wield in the switched access market.

B. NYNEX's Proposed Framework for Gradual Price Cap Reform Is Acceptable in Theory but Incorrect as Proposed

TCG agrees in theory with NYNEX's proposal to match the level of regulation with the level of competition in a given market. NYNEX is, however, far off the mark in its proposals as to the "trigger points" for price cap relief.

NYNEX proposes a three phase plan for price cap reform. It further proposes to subdivide "Phase 1" into three parts

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7. *See* Notice of Ex Parte Communication, NYNEX Transition Plan -- DA 93-1537, Letter of J.Manning Lee, April 6, 1995.

8. *See* Teleport Communications Group Emergency Petition for Declaratory Ruling, NYNEX Refusal To Provide Central Office Code Assignments, filed October 16, 1995.

called 1-A, 1-B and 1-C.[9] The three gradations are a way for NYNEX to "frontload" its regulatory relief, since they will allow an ILEC to receive substantial regulatory relief without demonstrating that any meaningful competition exists.

Phase 1-A would include "streamlined procedures for introducing new Switched Access and Special Access services, greater downward pricing flexibility, and inclusion of Operator services in the Information Services category."[10] In Phase 1-B the Commission "should allow rate deaveraging by zone and by multi line/single line categories, alternative pricing plans and volume and term discounts for usage-based Switched Access services, market trials, consolidation of service categories, and greater downward pricing limits."[11] Lastly, in Phase 1-C, "A LEC should be allowed to deaverage its rates further into 'small' and 'large' business categories, to deaverage the EUCL charge, to offer individualized tariffs in competitive bidding

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9. NYNEX at 5.

10. *Id.* at 6.

11. *Id.* at 7.

situations, and to combine services into two price cap baskets, Switched and Trunking."[12]

NYNEX's three parts of Phase 1 are triggered based upon two criteria: the "presence" of competitors and the removal of barriers to entry. The problem with NYNEX's proposal is that the trigger points for regulatory relief are too low. In Phase 1-A, NYNEX proposes to award ILECs with regulatory relief in the absence of any actions by the ILEC to facilitate the introduction of competition by satisfying competitive checklist items, or any consideration of the actual presence of competition in the market.

In Phase 1-B, additional relaxation would be granted based on the satisfaction of a competitive checklist and the fact that at least one competitor is "present" in the market -- regardless of the competitor's size, effectiveness, market share, or staying power. And while the use of a checklist is a good starting point, the Commission cannot assume competition will appear because an item on a competitive checklist has been "checked off."[13] As Ad Hoc

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12. *Ibid.*

13. Ad Hoc cautions that the removal of entry barriers as stated in a competitive checklist "is not the same as the

recognizes, "the pricing, terms and conditions under which items on the 'competitive checklist' are provided is so important that the checklist should not be considered satisfied if rates, terms, and conditions are not found reasonable."[14]

For example, TCG recently filed with the Commission an Emergency Petition for a Declaratory Ruling asking for the Commission's help in overcoming NYNEX's refusal to provide TCG with six NXX codes.[15] Although NYNEX would presumably have "checked off" the allotment of numbering resources to competitors on a competitive checklist on the basis that it had in the past given TCG some codes, its subsequent refusal

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existence of a level of competition sufficient to constrain LEC anti-competitive and monopoly pricing practices." Ad Hoc at 22.

14. *See* Ad Hoc at 23. *See also* AT&T at 16 ("A showing of effective actual competition cannot be based simply on meeting a 'checklist' ...") GSA's Comments in this proceeding argue that the Commission need not concern itself with market share or competitive checklists but should simply grant the ILECs pricing flexibility. At the same time, GSA's Comments in the Telecommunications Access Provider Survey proceeding advocate substantially increased reporting of just that kind of information -- an inconsistency wholly unexplained in either GSA filing.

15. *See* Teleport Communications Group Emergency Petition for Declaratory Ruling, NYNEX Refusal To Provide Central Office Code Assignments, October 16, 1995.

to fairly allocate this bottleneck resource until threatened with regulatory action demonstrates that the satisfaction of a "competitive checklist" condition cannot be equated with the establishment of a competitive market, or with the existence of fair opportunities for competitors.

In order for competition to flourish, more attention must be paid to the linking of price cap reform with actual removal of barriers to entry. In that regard, TCG would suggest that the Commission require that reciprocal compensation arrangements that are provided on a "bill and keep" basis should be presumptively considered as reasonable for purposes of satisfying the compensation portion of a competitive checklist.[16] Any other form of reciprocal

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16. The Commission has recently proposed the use of "bill and keep" as the appropriate intercarrier compensation arrangement in the wireless market. A number of state public utility commissions and state legislatures have similarly recognized the virtues (in simplicity and fairness) of bill and keep, which has been the standard inter-LEC compensation arrangement for decades in the telephone industry. Because a bill and keep arrangement does not permit an ILEC to trap its competitors in a choking cost-price squeeze, it should be presumptively lawful. By contrast, usage-sensitive reciprocal compensation arrangements can place new competitors, who must send 95% or more of their customers' calls to the ILEC for completion, in a fatal cost-price squeeze, and therefore cannot be presumed to create conditions appropriate for a competitive market.

compensation must be presumed *not* to satisfy the checklist, with the burden on the ILEC to demonstrate that such other form of compensation does not disadvantage a competitor in addressing any portion of the local and toll switched market. Accordingly, while satisfaction of a competitive checklist is a useful indicia, it cannot be a "stand alone" criteria for regulatory relief.

Phase 1-C would also be dependent on a showing that competitors had "established a competitive presence in areas representing 40% to 50% of a LEC's total business access lines with regard to Switched Access, or 40% to 50% of a LEC's Special Access/transport revenues, whichever was applicable."[17] Again, the difficulty with this standard is that "establishing a competitive presence" is a nebulous and entirely subjective term susceptible of many different interpretations.

For example, a carrier with a collocation arrangement at a given central office might be presumed by the ILEC to have "established a competitive presence" with respect to all the customers served by that central office. However,

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17. NYNEX at 30.

if the ILEC's rates for unbundled loops are so high that few if any of those customers can actually be served by the competitor, it is inappropriate to treat those customers as having a competitive alternative, and the ILEC as "deserving" regulatory relief. Consider also a competitive carrier with a network that passes 100 buildings on a street. The ILEC might argue that the competitive carrier has a "competitive presence" as to all the customers in those buildings -- even if 85 of the buildings are owned by landlords who do not permit the competitor to enter the space but welcome the ILEC.

Accordingly, even if one accepted the concept that a competitive "presence," or the related concept of "addressable markets," has meaning, the characterization of a customer or market segment as addressable or within the presence of a competitor cannot be made on the basis of raw proximity, simple geographic relationships, or even the availability of collocation arrangements. Any such analysis must examine whether those customers, or that market, is legally, technically, economically, and practically reachable by a competitor. Customers or markets which are currently not actually or practically servable by a

competitor cannot be considered to be addressable or within the presence of a competitor for purposes of calculating the portion of a market subject to competition.

The difficulties inherent in subjective standards such as addressability of "presence" simply demonstrates that there is, in the final analysis, no substitute for actual market share data. The use of actual market informtion, such as competitors' net revenues and customers served, is more certain, verifiable, and probative in evaluating the true "presence" of competition, or in understanding how "addressable" a market is for competitors. The efforts of NYNEX -- and other ILECs -- to dance around the use of market share data and propose various tortuous alternatives to market share information is, by itself, a clear hint where the right answer lies.

NYNEX's Phases 2 and 3 move toward large scale deregulation of the ILEC. NYNEX proposes that these substantial regulatory benefits will be dispensed based, finally, on measures of actual competition, with Phase 3 granted on a virtually automatic basis a year after Phase 2. NYNEX's suggestion that the criteria used for AT&T's

deregulation are too stringent is unconvincing.[18] NYNEX overlooks the fact that AT&T's facilities-based competitors rapidly ceased to depend on AT&T for services, whereas NYNEX's new local competitors will be critically dependent on NYNEX for essential interconnections for years to come. This continuing dependence of new local competitors on dominant LECs suggests that extreme caution must be exercised in considering the substantial deregulatory steps in NYNEX's Phases 2 and 3.

III. THE COMMISSION'S PROPOSAL FOR INDIVIDUAL CASE BASIS RATES ("ICBs") IS APPROPRIATE.

In its Notice, the Commission proposed that ILECs should be allowed to use ICBs for services that are so unlike existing services that the ILEC would have no reasonable basis for developing generally available rates. In addition, the Commission proposed that if the carrier has more than two customers for the ICB service or has provided the service for more than six months, the carrier should be able to develop averaged rates and should be required to

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18. NYNEX at 36-7.

classify the ICB as a new service. For cost support, the Commission proposes that the requirements of Section of 61.38 applicable to non-price cap carriers, should apply to the tariff filings establishing ICB rates. Additionally, the Commission proposes to continue excluding ICB tariffs from price cap regulation.[19]

Many ILECs oppose the Commission's suggestion and argue that ICB rates should not be limited in any way. ILECs, however, have the potential for pricing ICB offerings in an anti-competitive and unreasonable discriminatory manner, and indeed have done so in the past.[20] USTA, in fact, indicates only one motivation for ICB offerings -- "customers desire ICB pricing."[21] The primary motivation for ICBs should instead be based on the need for unique services, not customer desire for special pricing. When an ILEC's desire to give a favored customer a lower price is the primary motivation for introducing an ICB, the potential

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19. Notice at p. 32-33.

20. *See* Local Exchange Carriers Individual Case Basis DS3 Service Offerings, CC Docket No. 88-136, 4 FCC Rcd 8364 (1989).

21. USTA at 30.

for unreasonabe discrimination is obvious.[22] The Commission's proposal seeks to ensure that ILEC ICBs are offered on an appropriately limited basis. The Commission should, therefore, adopt its proposed policy on ICBs.

IV. ALTERNATIVE PRICING PLANS SHOULD NOT BE ADOPTED

The ILECs argue that Alternative Pricing Plans ("APPs") will encourage more efficient pricing of existing access services.[23] However, because the Commission's proposal would allow reduced cost-support requirements and shortened notification schedules, detection of cross-subsidization would be difficult. According to the California Cable Television Association ("CCTA"), "without the detailed cost support of the current regulatory requirements for new services, the Commission and the LECs' competitors will lack the information necessary to challenge any cost-shifting

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22. In a related vein, the Competitive Telecommunications Association ("Comptel") suggests that the Commission should in fact prohibit ILECs from offering any ICB rates to their long distance affiliates to further inhibit anti-competitive ICB pricing practices. *See* Comptel at 30.

23. *See, e.g.*, Pacific at 11, Bell Atlantic at 22.

from competitive services to monopoly services."[24] TCG also agrees with the concerns of the National Cable Television Association ("NCTA") that "the offering of APPs by LECs would enable dominant carriers to target customers considered most susceptible to competition, and thereby delay the competitive results that the Commission seeks."[25]

ILECs also theorize that the continued availability of the existing, non-discounted, service will guard against setting APP prices that are too high.[26] These parties state the obvious. It is not *high* prices the Commission should be concerned about when considering the appropriateness of APP rates. Rather, the Commission should concern itself with the real potential of ILECs pricing their services in a discriminatory fashion. Moreover, the Commission cannot assume -- as it apparently does -- that an ILEC could only cross subsidize by increasing its prices. In a declining cost industry, prices do not have to increase to provide the

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24. California Cable Television Association at 23.

25. National Cable Television Association at 25.

26. *See* Bell Atlantic at 14, GTE at 16, Southwestern Bell at 19, and US West at 13.

necessary "cushion" for cross subsidization -- static prices can do so where costs decline.

V. THE COMMISSION SHOULD NOT CHANGE THE PART 69 WAIVER PROCESS OR REMOVE LOWER SERVICE BAND INDICES.

The Commission proposes two separate but related changes: elimination of the Part 69 waiver process for new switched access services, and elimination of the lower Service Band Index ("SBI"). Both of these changes will inappropriately diminish the Commission's ability to curtail anti-competitive activity.

With respect to the elimination of the Part 69 waiver process, Pacific Bell and Nevada Bell argue that this proposal is appropriate because new services make a positive contribution to consumer welfare by adding to consumer choice, "new services are in the public's interest *per se*" and "should be presumed lawful and effective upon a short notice period."[27] USTA echoes this refrain and takes it a verse further. USTA comments that "the burden to demonstrate that the service is not in the public interest

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27. *See* Pacific Bell and Nevada Bell at 6, 18 (emphasis in original).

should rest upon those opposing the new service. The opposing party should be required to demonstrate that the introduction of the new service will result in consumer harm."[28]

This hands-off policy with respect to new services is completely inappropriate in an essentially non-competitive environment. The burden of proving a LEC price is anticompetitive should come *before the rate is introduced* to the marketplace rather than waiting until competitors have felt the effect of below cost rates.[29] TCG agrees with the Comments of Cox Enterprises that "the burden on a competitor to prove that the LEC price is below cost is a practical impossibility because of LEC capability to control and manipulate cost and pricing data."[30]

Further, elimination of the waiver requirement would, as AT&T states, "almost render the Part 69 rules

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28. USTA at 20.

29. It should be noted that the Commission has rejected switched access Part 69 waivers in the past, finding the proposed rates to be unjustified. *See* Bell Atlantic Telephone Companies, Petition for Waiver, 4 FCC Rcd 7210 (1989).

30. Cox Enterprises at 5.

obsolete."[31] ILECs may be encouraged to submit modified, restructured, or slightly altered existing services as "new" services subject to little or no regulatory review. While the introduction of truly new, efficiently-priced services is a worthy ambition, it is clear the complete elimination of the Part 69 waiver process is not likely to achieve the Commission's goal.

The Commission's proposal to eliminate the lower SBI limit is similarly mistaken. The Commission only nine months ago concluded that the evidence supported, at most, an increase of 5% in the lower limit. Nine months later, on the basis of no new evidence, the Commission now proposes to eliminate the lower band entirely. Not only would such an abrupt reversal of position be difficult to defend before the Court of Appeals, the new proposal simply invites discrimination and predatory pricing.

Even the Commission's lone effort to discourage predatory pricing with the elimination of the lower band -- its suggested limitations on subsequent price increases -- comes under ILEC attack. Pacific Bell, for example, argues

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31. AT&T at 35.

that ILECs should be free to raise prices, pointing to the air transportation industry's ability to make "rapid, substantial price increases."[32] While TCG does not object to price increases (or decreases) that are cost-based and within the existing price cap limits, it does object to the concept that ILECs should be free to make "rapid, substantial price increases," since the ILEC's competitors could be selectively (or disproportionately) made the targets of such increases.[33]

VI. CONCLUSION

For the reasons stated above, TCG does not believe that market conditions today justify the Commission's proposals to significantly relax or eliminate major elements of the LEC price cap rules. The Commission's proposals will not

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32. Pacific Bell at 20.

33. Whatever one's view of the merits of airline pricing practices, it cannot be denied that when, for example, United Airlines makes a "rapid, substantial price increase" on a particlar route it does not affect the underlying *costs* of the carriers competing with it on that route. By contrast, ILEC competitors will inevitably be substantial customers of the ILECs and could be caught in just such a cost-price squeeze.