affirmatively concluded that it would "continue to review new services for possible discrimination."[100]

There has been no change that would conceivably warrant a departure from this conclusion. IXCs and their customers remain vitally dependent on the LECs to obtain new access services at reasonable, nondiscriminatory rates. Relaxation of cost support requirements would frustrate this objective.[101] The SFNPRM's proposal to reduce cost support requirements would significantly impair access customers' ability to scrutinize new offerings to ensure that the rates are not set at monopolistic levels or in whatever discriminatory manner LECs may choose.[102] Because customers do not have effective alternatives to innovative new LEC services, they will be placed in the untenable position of either foregoing the offering or subscribing to an offering which is priced too high. In either case, they will lack the cost information needed to evaluate whether a new offer is unreasonably discriminatory. All of these outcomes are

[100] First Report, 10 FCC Rcd. at 9143 (¶ 418).

[101] In addition, inadequate review of new LEC offerings would only allow LECs greater opportunity for anticompetitive conduct against their competitors. ICG at 2-3; ITTA at 2-5; MFS at 3-4 (urging clarification of uniform overhead loading requirement so that LECs cannot shift costs from new services to bottleneck interconnection services); Time Warner at 11-12.

[102] Ad Hoc at 8; AT&T at 22-26; CompTel at 26; MCI at 8, 10; Sprint at 14.

contrary to the Commission's duties to protect consumers under the Communications Act.

Similarly, because restructures supersede the existing variant of an offering, they (like new services) warrant careful review. The careful scrutiny required for restructures is confirmed by the extensive proceedings associated with the introduction of the LECs' restructured local transport and 800 data base offerings. If the Commission nonetheless decides to reduce the notice period for LEC tariffs introducing new services and restructures, it should require that such tariffs be filed on at least 30 days' notice.[103] This would afford potential intervenors 15 days to file their petitions and allow for timely Commission review.

B. The Part 69 Waiver Process Should Not Be Relaxed.

Several LECs suggest that the Part 69 waiver process should be eliminated because it has delayed the introduction of new services and has created uncertainties in the availability of new technologies.[104] Some LECs claim that the codified Part 69 rate elements are unnecessary and should be eliminated, and that, in any case, because new

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[103] See AT&T at 25 n.53; Sprint at 14.

[104] See, e.g., Bell Atlantic at 9, 12; BellSouth at 22-24; Frontier at 6; GTE at 23; Pacific at 16; USTA at 9, 16-19; U S WEST at 22, 24.

services add to customer options, the waiver process improperly assigns the burden of proof to the filing carrier (rather than the party objecting to a new offering).[105] Alternatively, several LECs assert that if the Part 69 elements are not eliminated, the Commission should adopt an outside time limit for resolution of Part 69 waivers.[106]

As AT&T showed (at 32-33), the Commission expressly required the LECs to continue to adhere to the switched access rate elements prescribed by the Part 69 rules because the rate structures embodied in those rules are designed to eliminate unreasonable discrimination between service users. The Commission correctly found that, given the LECs' significant market power in the provision of interstate access, rules that discourage unreasonable discrimination and its potentially adverse impact on competition are more important than the benefits that might come from the LECs' ability to depart from the Part 69

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[105] Ameritech at 15; BellSouth at 20-24; GTE at 22, 27; SWBT at 29; USTA at 20-21.

[106] BellSouth at 25 (15-day notice of intent prior to filing new service); GTE at 25 (10-day notice of intent to file and if not denied, tariff may be filed); SNET at 10-11 (14-day resolution period for waivers); USTA at 19 n.39, 21 (45 days should be outside time limit for waiver resolution); U S WEST at 24 (agrees with USTA, but suggests 14-day waiver resolution limit for Track 2 services).

access rate structure.[107] And, the Commission again recently concluded that it must continue to review new LEC services for possible discrimination.[108]

Moreover, there is widespread agreement among the commenters that the Commission should move forward with its planned access reform proceeding and implement fundamental changes that address the anticompetitive and uneconomic subsidies that currently inhere in the access and separations rules.[109] That access reform proceeding (and

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[107] LEC Price Cap Order, 5 FCC Rcd. at 6826 (¶ 325); see AT&T at 34-35; Time Warner at 18. The LECs' further assertion that proceedings under Section 203 (tariff review); Section 204 (tariff suspension and investigation); and Section 208 (complaints) provide effective procedural safeguards is wrong. Bell Atlantic at 10; Pacific at 18; SWBT at 28; U S WEST at 23. The tariff review process is not the appropriate context in which to review rate structures that do not conform to the Part 69 rules. Indeed, the tariff intervention process places the burden of raising issues as to the lawfulness of a proposed tariff on the party seeking rejection or suspension of the tariff. By contrast, the Courts have cautioned that a request for waiver assumes the validity of the general rule, which clearly assigns the burden on the carrier which filed the tariff and is seeking a waiver. WAIT Radio v. FCC, 418 F.2d 1153, 1158 (D.C. Cir. 1969), aff'd, 459 F.2d 1203 (D.C. Cir.), cert. denied, 409 U.S. 1027 (1972). After the fact remedies, such as the complaint process, offer insufficient protection because they would permit nonconforming tariffs to take effect and remain in place, without regard to the nondiscrimination requirements embodied in the Part 69 rules.

[108] First Report, 10 FCC Rcd. at 9143 (¶ 418).

[109] AT&T at 38; CompTel at 18-19; LDDS at 3, 32; NYNEX at 8; Sprint at 2; TCG at 6; U S WEST at 5.

not this LEC price cap flexibility review) is the appropriate context in which to determine whether the Part 69 rules should be modified or replaced to provide for nondiscriminatory switched access services.[110] Access reform would also likely stem the tide of ad hoc piecemeal waiver requests by creating rational cost-based rate structures that could more readily accommodate emerging technologies.[111]

At the same time, AT&T does not wish to delay the availability of new service offerings that serve the public interest. AT&T therefore supports a prompt resolution of each waiver, after presentation of information by the filing carrier adequate to illuminate the issues raised and sufficient time for analysis by access customers and competitors potentially affected by the filing. In this respect, AT&T supports MCI's suggestion that the Commission should ensure that "LECs provide complete and detailed information" in support of their waiver requests so that interested parties and the Commission staff will be readily able to understand and analyze a waiver request and to obviate the filing of unnecessary oppositions.[112]

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[110] MCI at 12.

[111] Sprint at 20.

[112] See, e.g., MCI at 13, 17-18. MCI suggests the filing of the following four categories of information: (1) a list of the rate elements that the LEC proposes to charge, as

(footnote continued on following page)

C. The Proposals for Individual Case Basis Offerings Should Be Adopted to Codify Existing Policy.

The LECs are generally opposed to the Commission's proposal to require them to file generally available tariffs under the price cap new service rules once they have provided an individual case basis ("ICB") offering outside of price caps to more than two customers or for longer than six months.[113] The LECs claim that the six-month time limitation may be too short to create averaged rates and that the two customer limit is also too stringent.

The SFNPRM's proposal as to ICBs is fully consistent with established Commission policy, which allows "ICB prices . . . only for new service offerings for which the carrier does not have enough experience to develop averaged rates." As the Commission recently reiterated, "a LEC may use an ICB rate only as an interim measure and . . .

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well as the costs that each element would recover and how the element would be priced (e.g., per minute, per query); (2) sample tariff pages; (3) an explanation of why the request meets the waiver standard; and (4) an explanation of the competitive effects the new structure is likely to have on the interexchange and access markets. Id.

[113] Ameritech at 19 (no advance limitations on ICBs should be created; six months may be too short); BellSouth at 20; GTE at 20-21; USTA at 30; U S WEST at 18. BellSouth (at 20) asserts that LECs should be permitted to justify multiple ICBs.

averaged rates must be developed within a reasonable amount of time."[114]

Sprint correctly points out that there is no reason to deviate from these policies, because "ICBs should not be used to offer special prices to certain customers in evasion of normal tariff requirements" and "assuming that the ICB was not intended to offer unreasonably discriminatory rates to a select customer(s), the tariffing LEC should have no objection . . . to mak[ing] the ICB attractive to as many potential customers as possible."[115] And AT&T demonstrated that the Commission's proposal

[114] See Southwestern Bell Telephone Company, Transmittal Nos. 2433 and 2449, CC Docket No. 95-140, Order Terminating Investigation, FCC 95-476, released November 19, 1995, ¶ 20 ("SWBT Order"); see also, e.g., Investigation of Access and Divestiture Related Tariffs, 97 F.C.C.2d 1082, 1143 (1984); Local Exchange Carriers' Individual Case Basis DS3 Service Offerings, 4 FCC Rcd. 8634 (1989); Bell Atlantic Telephone Companies Transmittal Nos. 224 and 226, 3 FCC Rcd. 1621, 1622-23 (1988); BellSouth Telephone Companies Transmittal No. 346, 6 FCC Rcd. 373, 374 (1991).

U S WEST (at 18) erroneously contends that the Commission may not require carriers to provide general offerings, citing Southwestern Bell Telephone Company v. FCC, 19 F.3d 1475 (D.C. Cir. 1994). That case held only that the Commission must determine whether a service is common carrier in nature before it can conclude that when a carrier has sufficient experience to develop averaged rates, it must do so. No LEC has disputed that its ICB offerings are common carrier services. In any case, the Commission can only enforce its ICB proposal with respect to such services.

[115] Sprint at 18-19.

properly recognizes that instances of ICB pricing in noncompetitive markets should be strictly limited to avoid unreasonable discrimination.[116]

D. The LECs Should Not Be Permitted To Respond To Requests For Proposals On A Contract Tariff Basis.

Several LECs contend that they should be permitted to respond to requests for proposals ("RFPs") on a contract basis, even under baseline regulation.[117] Considering the LECs' near-total power in the existing access market, there is no basis to afford them such relief prior to the time they face sufficient competition to be eligible for streamlining generally.[118] BellSouth (at 58) is thus correct that contract carriage should be allowed "only as an

[116] AT&T at 32; see also CompTel at 30; Frontier at 13; MCI at 14-15; NCTA at 26; Time Warner at 16-18.

[117] CBT at 12; GTE at 18-19; SWBT at 8; USTA at 28; U S WEST at 20. Some LECs propose additional monitoring conditions to provide some assurance that a competitive bid was made for a specific RFP. See, e.g., USTA at 28. This would not only be administratively burdensome, it could also create incentives to create "phantom" bidders that would enable LECs to discriminate in the absence of any real competition.

[118] AT&T would not oppose a LEC's use of contract carriage, under the terms described in the SFNPRM, for streamlined services (for entities not affiliated with the LEC) after the Commission has found there is substantial competition in a relevant market. See also Ameritech at 40-41. Prior to that time, however, the potential ability of one competitor to supply a single customer in an admittedly non-competitive market does not provide sufficient competition to permit contract tariffs.

adjunct to streamlined regulation," and only after "the ultimate check on discrimination -- competition -- will be present."

The Commission has already rejected the LECs' contention that they should be permitted to respond on a contract tariff basis to customer-issued RFPs. As the Commission ruled just a few weeks ago, RFPs do not qualify under any of the recognized exceptions to the rule requiring geographically averaged rates throughout a LEC study area.[119] Services offered via RFPs are typically not new services which would qualify as ICBs even for a limited period of time.[120] Rather, they are services that are already generally offered at averaged rates.[121] Thus, the RFP contract rate would simply allow the LEC to offer a preferential rate to a particular customer.

Because of the significant risk that contract-based tariffs could be used to unreasonably discriminate between customers, the Commission has only permitted contract carriage for streamlined IXC services and for

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[119] 47 C.F.R. § 69.3(e)(7); see SWBT Order, ¶¶ 19-28.

[120] SWBT Order, ¶¶ 19-20.

[121] Accord, GTE at 19-20.

nondominant carriers.[122] LEC access services do not fall within this exception. Further, although the Commission did not determine whether a LEC would be permitted to make competitive necessity justification to support an RFP rate, it flatly rejected the assertion "that, as long as the RFP states that it involves a 'competitive bid situation,' the existence of an RFP is sufficient to justify [a LEC's] charging a RFP rate."[123] There is no basis to revisit these conclusions now. To the contrary, as AT&T and CompTel showed, the Commission should enforce its ICB test strictly to limit instances of unreasonable discrimination and in no instance should a LEC be permitted to employ ICB (or RFP) pricing for itself or an affiliated entity.[124]

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[122] SWBT Order, ¶ 21, citing 47 C.F.R. § 61.3(m); see also Competition in the Interstate Interexchange Marketplace, 6 FCC Rcd. 5880, 5903 (¶ 130)(1991).

[123] SWBT Order, ¶ 27. The Commission determined that "the existence of a request for proposal, even if it requests bids from more than one vendor, does not demonstrate that there is a lower priced competitive alternative," which is the first prong of the competitive necessity test. Id. (citations omitted). As the Commission found, the "existence and degree of competition might be determined by the existence of responses to an RFP, not by the existence of the RFP itself." Id. (emphasis in original).

[124] AT&T at 32; CompTel at 23-25, 30, 40; LDDS at 1-2; Sprint at 4 (LECs' incentives for discrimination are magnified many-fold if they have interexchange affiliates); see also BellSouth Europe Comments (at 7) and BellSouth NZ Comments (at 10) regarding the likelihood of cross-subsidization between access providers' monopoly and competitive lines of business.

E. Lower Service Band Index Limits Should Be Eliminated, Provided Safeguards Against Cross-Subsidization and Predatory Pricing Are Imposed.

As expected, the LECs support the Commission's proposal to eliminate the lower service band indices ("SBIs") for the service categories and subcategories within the traffic sensitive and trunking baskets to give them additional downward pricing flexibility, and they oppose any new constraints on subsequent upward price increases.[125] Although the LECs claim that elimination of the lower SBIs would permit access rates to move closer to cost, they also assert that the proposed 1% upper SBI limit for the bands in which they make price reductions based on the new flexibility would create a disincentive to reduce access prices, contrary to the Commission's objectives.[126]

The only reason the Commission proposes to eliminate the lower SBI limits is to allow the LECs to move their access prices more quickly toward economic cost. Given this fact, there is no reason a LEC should expect to later increase a price it has lowered, unless the cost of providing the service increases. This is most unlikely,

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[125] Ameritech at 21; Bell Atlantic at 21-22; BellSouth at 29; CBT at 9-10; GTE at 28-29; SNET at 15-16; Pacific at 18, 20; USTA at 30-32; U S WEST at 26-27. Compare NYNEX at 14, 22 (proposing 15% and 50% downward pricing flexibility limit during Phase IA and IB, respectively).

[126] See, e.g., Pacific at 43.

because access costs have been declining even though access prices remain substantially above cost. Moreover, price caps are adjusted annually for inflation. Therefore, any subsequent changes in the cost of providing these access services should not normally be more than the annual changes in the price cap. Thus, contrary to the LECs' contention, the proposed 1% upward price limit should not create a disincentive for a LEC to reduce prices.[127]

Several LECs suggest that the 1% upward price limit will prohibit lawful procompetitive pricing because in competitive markets firms often need to increase their prices to seize upon profitmaking opportunities.[128] Until the LECs' market are fully competitive -- which they are not today -- there are compelling reasons to restrict LEC pricing flexibility. As AT&T and other commenters demonstrated, safeguards -- such as limiting the LECs' upward pricing flexibility to 1% in bands that are priced below the current SBI limits and requiring the LECs _not_ to compensate for their below-band price reductions with price

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[127] In all events, the 1% upper SBI limit does not mean that a LEC would not be permitted to increase prices by more than 1% (as adjusted for the PCI), if service costs rise. A proposed price increase that exceeds the upper SBI limit would not be presumed lawful, but the LEC could provide "supporting materials establishing substantial cause for the proposed rates." _See_ 47 C.F.R. §§ 61.49(c) and 61.58(c)(3).

[128] SWBT at 34-35; Pacific at 20.

increases in the other service bands -- are necessary to protect LEC customers and the LECs' nascent competitors from predatory pricing and cross-subsidization.[129]

USTA's contention that the LECs would be "penalized" if a 1% upper flexibility limit were imposed is misleading.[130] USTA contends that if a LEC reduced prices by 12% in a band subject to the 1% upper limit, it would be forced to reduce its prices in the same band by another 2% if there were a 3% PCI reduction the following year, whereas no further price reductions would be required with a 5% upper band limit. USTA's argument improperly ascribes the need for further reductions to the proposed 1% upper limit. As part of the normal operation of the current price cap structure, and regardless of what the upper SBI limit is or what price reductions were made in the previous year, if the PCI reduction in any given year exceeds the upper flexibility of any band, the LECs must reduce the price in

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[129] AT&T at 39-45; see also Ad Hoc at 19; CCTA at 18-19; CompTel at 33 (suggests 0% upward limit); Frontier at 13 (opposes elimination of lower SBI); ITTA at 8 (suggests 0% upward limit); MCI at 6-7 (advocating no additional pricing flexibility until access prices move toward cost; otherwise LEC would simply fund rate decreases for some customers with increases for others); NCTA at 21-22 (opposes elimination of lower SBI, which is needed to guard against below-cost pricing); Sprint at 21 (if lower SBI eliminated, must constrain upward pricing to guard against predation); Time Warner at 21-22 (do not eliminate lower SBI until competition emerges).

[130] USTA at 30-32 n.50 and Att. 4.

that band in an amount roughly equal to (% PCI reduction - % band upper limit).[131] Thus, the result USTA has incorrectly labeled as a "penalty" is not unique to bands that would be subject to the 1% upper SBI limit.[132]

In short, eliminating lower SBI limits could result in cross-subsidization and predatory pricing. Therefore, sufficient safeguards must be put in place to protect the LECs' customers and potential competitors against these practices. No party has shown that any legitimate LEC pricing behavior would suffer unwarranted restraints as a result of these conditions. In fact, the

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[131] For example, as shown in Appendix F (at 1), a 3% PCI reduction would require a 1% reduction in the tandem switched transport band (which has a 2% upper SBI limit) and a 3% reduction in the RIC (which has a 0% upper SBI limit). Appendix F (at 2) also shows that with a 6% PCI decrease, a LEC would have to make some price reductions in all bands, because the upper limits of all bands are less than 6%.

[132] Similarly, SWBT (at 34) is also incorrect that a LEC could, as a result of the 1% upper SBI limit, be anomalously required to make extensive involuntary price reductions because of an upper SBI limit that is determined by current base period price reductions. Any extensive price reductions can trigger the need for subsequent price reductions, even under the current price cap structure, if the price reductions are more than the weighted upper pricing flexibility of a basket. This can happen because the weighted lower pricing flexibility is already more than double the weighted upper pricing flexibility in the traffic sensitive and trunking baskets. In all events, AT&T's suggestion (at 41-42) that pricing below the lower SBI limit should not create PCI-API headroom would mitigate SWBT's concern regarding the need to make involuntary price reductions.

proposed conditions will help ensure that this additional downward pricing flexibility will, in fact, assist in achieving cost-based pricing.

F. Zone Pricing Should Not Be Extended To Additional Rate Elements.

A number of LECs contend that the Commission should allow further geographic deaveraging of access rates by extending zone pricing to all price cap baskets and interstate access services, and most importantly, to local switching, carrier common line, and the residual interconnection charge ("RIC") rate elements.[133] These commenters claim that the zone differentials that justified the zone pricing for various switched transport elements (i.e., entrance facilities, direct-trunked transport, and tandem-switched transport) apply equally to other access elements.[134] Virtually all of them also suggest that extension of zone pricing to these additional elements

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[133] See BellSouth at 31; GTE at 13 (also Information Surcharge); NYNEX at 22-24 (when a substantial portion of a LEC's territory is open to competition, Phase I-B); SWBT at 9; Sprint at 3, 12 (advocates zone pricing for local switching and carrier common line); USTA 33-34; U S WEST at 27. GTE (at 31) and NYNEX (at 24, 30-32) also assert that the Commission should consider deaveraging the end user common line charge ("EUCL").

[134] BellSouth at 31; GTE at 31 (claiming that both switching and loop costs are higher in low density areas); NYNEX at 23 (alleging significant cost variance between urban and rural areas and between high-volume business and low-volume residential customers).

should be allowed irrespective of competition, claiming that it will permit access prices to move toward cost.[135] BellSouth further asserts that experience has shown that deaveraging of access prices does not lead to deaveraged toll rates.[136]

The SFNPRM does not propose, and the Commission should not allow, further deaveraging of switched access rate elements. First, the LECs have presented no evidence that zone pricing would lead to rates more closely aligned with costs. Moreover, the recent telecommunications legislation presents both an opportunity and imposes an obligation on the Commission to conduct a rulemaking on rate averaging issues. In that proceeding, the Commission will need to consider the degree of averaging in both LEC access and IXC rates. Until that rulemaking is completed, the Commission should not upset the current level of averaging in LEC rates.

Contrary to the LECs' assertion, zone pricing of contribution or subsidy elements, such as the CCLC or RIC, cannot be justified on the basis of costs. The CCLC and RIC are not based on underlying costs. Accordingly, any zone-based differential in the price levels of these contribution

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[135] See, e.g., BellSouth at 31; Sprint at 12; USTA at 33-34.

[136] BellSouth at 31.

rate elements would be inherently arbitrary and would simply allow LECs to discriminate among customers by recovering a greater portion of the subsidy from the lower density zones. Instead of causing rates to be more closely aligned with costs, zone pricing of contribution elements would thus increase the divergence between price and cost in low density zones.

Furthermore, zone-based pricing of the CCLC and RIC would perpetuate the current system of uneconomic subsidies of other LEC services. Rather than fashioning mechanisms that perpetuate or enhance existing barriers to entry, AT&T urges the Commission to address recovery of contribution and support issues in the context of its upcoming proceeding on access and universal service reform, and to create a competitively neutral mechanism for collecting and distributing universal service support.

The LECs' request for zone pricing flexibility for local switching is equally unwarranted. Not only is there an absence of competition for local switching, but the cost structure of switching is likely to differ considerably from that of transport. There is little, if any, evidence on the record as to how switching costs vary by zone, or how the incremental costs of switching vary with volume or geography. Moreover, because carriers can augment switching capacity in increments, the costs of switching -- particularly the incremental costs associated with additional capacity -- are unlikely to vary with volume and geography in the same manner or degree as the costs of transport. In any event, the record here does not show that zone-by-zone rate differentials for switching would align LEC access rates more closely with costs.[137]

Furthermore, contrary to the LECs' claims and as the Commission has recognized, zone pricing for local switching, the CCLC and the RIC would significantly increase the economic pressure on IXCs to deaverage their rates.[138] In allowing zone pricing of switched transport, the Commission observed that the transport elements "represent[] a fraction of the total access revenues that the LECs receive."[139] Thus, deaveraging of switched transport did not have the sweeping impact that deaveraging of other switched access elements would. Indeed, the Commission recognized that permitting further deaveraging and volume pricing of switched access was particularly sensitive, noting that it "is a substantial departure from our past practice and must be done cautiously."[140] The commenters

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[137] See AT&T at 30; MCI at 32-33.

[138] OPASTCO at 3, 9.

[139] Expanded Interconnection With Telephone Company Facilities, 8 FCC Rcd. 7374, 7384 (¶ 15) (1993) ("Switched Transport Expanded Interconnection Order").

[140] Expanded Interconnection With Local Telephone Company Facilities, 9 FCC Rcd. 5154, 5204 (¶ 183) (1994)

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have not shown any valid basis for extending zone pricing to other switched access rate elements, and AT&T submits there is none. In all events, issues relating to deaveraging should be considered in the rulemaking on rate averaging called for by the recent telecommunications legislation.

G. The Price Cap Baskets And Service Categories Should Not Be Revised At This Time.

Several LECs propose revisions to the price cap baskets and service categories. They ascribe many rationales for these changes, including the ability to provide themselves additional pricing flexibility, to align the services along functional lines, and to make the baskets more consistent with anticipated access reform.[141]

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("Virtual Collocation Order") (discussing switched transport term and volume discounts).

[141] See, e.g., USTA at 36-37 and Att. 5 and 6; BellSouth at Att. 2; GTE at 39-40; U S WEST at 28. For example, as part of baseline regulation, USTA (supported by BellSouth, GTE, SWBT, and U S WEST) suggests consolidating service categories in the traffic sensitive and trunking baskets (which would be renamed "switching" and "transport", respectively). See USTA at Att. 5. Alternatively, USTA proposes to allow LECs the option of creating "small access customer" and "large access customer" baskets, each of which would contain service categories for local switching; common line and EUCL; whereas the information and database categories would be included in the transport basket. See USTA at Att. 6. NYNEX and Pacific make their own basket revision proposals. See NYNEX at 11 and charts; Pacific at 29-30.

By contrast, Ameritech and Sprint (on behalf of United and Centel) either do not advocate or affirmatively oppose basket revisions or service category consolidation. See Ameritech (no change suggested);

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These claims are baseless. Except for the creation of certain new services categories in the traffic sensitive basket needed to protect consumers,[142] the Commission need not, and should not, modify the basket and service category structures at this time.[143] Future rulemakings may be required to address whether basket revisions are appropriate for some LEC markets after a demonstration of changed marketplace circumstances.

First, there is no need to modify the price cap baskets to create additional pricing flexibility for the LECs. The Commission created the LEC price cap baskets and the service categories and bands within the baskets to "replicate the effect of competition" in the exchange

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Sprint at 22 (no changes needed). Bell Atlantic (at 18) has proposed eliminating the interexchange basket, alleging that its services in that basket are fully competitive. As AT&T has showed in a separate proceeding, the interexchange basket cannot and should not be deemed nondominant (or competitive) as long as the LEC controls bottleneck facilities, as Bell Atlantic unquestionably does. _See_ AT&T Comments, filed August 25, 1995, in _Petition to Regulate Bell Atlantic as a Nondominant Provider of Interstate Interexchange Service_, DA 95-1666.

[142] _See_ Section IV.H, _infra_, as to the need for separate service categories in the traffic sensitive basket for the LECs' operator and LIDB services.

[143] AT&T at 45-52; CCTV at 17; CompTel at 34-36; GSA at 8 (service category consolidation not beneficial to consumers, because it would provide LECs additional headroom); MCI at 19; NCTA at 29; Sprint at 22; TRA at 25; Time Warner at 23-24.

market.[144] Thus, the price cap plan was intended to create economic incentives for the LECs to improve their productivity and to offer new services. At the same time, the structure was designed to protect consumers because "[s]ubdividing LEC services into baskets substantially curbs a carrier's pricing flexibility, as well as its ability to engage in unlawful cost shifting between the broad groupings of services."[145] The LECs that propose new basket structures, in particular USTA and its supporters, have ignored this important function of the current basket structure, and they have not shown any basis that would permit the Commission to conclude that the current level of

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[144] Price Cap Performance Review for Local Exchange Carriers, Notice of Proposed Rulemaking, 9 FCC Rcd. 1687 (¶ 38) (1994).

[145] LEC Price Cap Order, 5 FCC Rcd. at 6811 (¶ 200); First Report, 10 FCC Rcd. at 8974, 9126-27 (¶¶ 29, 379).

Within the traffic sensitive and trunking baskets, the Commission grouped similar services in service bands for the purpose of limiting "the LECs' ability to shift costs between services in a potentially anticompetitive manner." First Report, 10 FCC Rcd. at 9126-27 (¶ 379). As the Commission explained in the SFNPRM (¶ 93):

> "We created separate service categories in the price cap plan to group together services with high cross-elasticities of demand. This limits the LECs' ability to offset rate decreases for more competitive services with rate increases for less competitive services."

customer protection embodied in that structure is no longer needed.[146]

USTA, for example, recommends a revised basket structure that would group together rates for equivalent functions, consolidating a number of current service categories within the traffic sensitive and trunking baskets. This proposal disregards the fact that the current service categories are based on the grouping of services with high cross-elasticities of demand in order to limit the LECs' ability to offset rate decreases for more competitive services with rate increases for less competitive services. Services that may appear similar do not necessarily have high cross-elasticities and thus would create unwarranted opportunities for cross-subsidization.[147]

Further, the Commission correctly points out that if the lower service band index limits were eliminated as

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[146] Moreover, USTA's proposed restructuring does not provide the 'much-needed simplification' that it strives for. USTA at 36. Indeed, adoption of USTA's proposal would result in a <u>more</u> complex price cap structure, because it would eliminate service band indices at the service category level for those service categories which USTA asserts should be zone-priced. As a result, each zone would become an independent service category, creating 12 service categories in the trunking basket, instead of the six that currently exist.

[147] For example, voice grade and video are two different services with no cross-elasticities of demand. Similarly, due to significant differences in capacity (one DS3 is equal to 28 DS1s), DS1 and DS3 have different customer bases with limited cross-elasticities of demand.

proposed, then "consolidation of service categories would not provide any additional downward pricing flexibility, but instead would provide [solely] additional upward pricing flexibility by creating 'headroom' for services that are in the same service category with services for which the LECs have lowered their rates."[148] Allowing the LECs any additional pricing flexibility to increase their rates is detrimental to all of the Commission's major policy objectives. Given the lack of effective competition in the access and local exchange markets, it is abundantly plain that the price cap basket structure should not be revised at this time to afford additional pricing flexibility to the LECs. Nothing has occurred since the Commission's most recent revisions to the price cap baskets in the Second Report and Order less than five months ago that suggests it is no longer necessary to maintain the existing balance between LEC and ratepayer interests.[149]

Moreover, basket/band changes should follow and conform to structural changes in the access charge rules, as illustrated by the sequence of access and price cap changes

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[148] SFNPRM, ¶ 94.

[149] Price Cap Performance Review for Local Exchange Carriers, CC Docket No. 94-1, Second Report and Order and Third Further Notice of Proposed Rulemaking, 10 FCC Rcd. 11098 (1995) ("Second Report and Order") (establishing a separate price cap basket for video dialtone services).

associated with the local transport restructure.[150] Historically, the Commission has modified price cap basket and service categories only after changes in market conditions or Part 69 rule changes have required such modification. Even then, due to the complexity of introducing, realigning and consolidating baskets and the impact of such changes on both the LECs' ratepayers and their potential competitors, the Commission has adopted modifications in the price cap structure only after extensive deliberations and analysis.[151] The Commission has announced the need for (and the recent telecommunications legislation requires) comprehensive access and universal service reform. Given that the Commission will be

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[150] See Frontier at 6; LDDS at 3 (in connection with access reform, the Commission could consider the commenters' numerous proposals to modify the existing price cap baskets and categories). In that context, AT&T generally supports Sprint's proposal (at 7-11) to phase out the carrier common line charge and the residual interconnection charge as soon as feasible. On the other hand, AT&T vigorously opposes USTA's (at Att. 6), NYNEX's (at 34), and BellSouth's (at 47) proposal to combine switching and common lines into one basket. These services are neither functionally equivalent nor cross-elastic. Moreover, they are likely to have very different competitive characteristics, including the availability of competing facilities and the geographic area in which competition may be available.

[151] See AT&T at 47. USTA's proposals for basket and service category revisions are not based on any demonstrated changes in the LECs' markets. Rather, USTA's proposals are supposed to ". . . facilitate the streamlining process by making it easier for exchange carriers to remove groups of service subcategories from price cap regulations." USTA at 37.

addressing access reform in the near term, it is inappropriate to revise the baskets and bands now, in advance of determining what the revised access charge rules will be.

Realignment of baskets and bands would also require readjustment of the LECs' productivity or X-factor, which the FCC is currently calibrating in light of the current structure.[152] The Commission's ability to measure the LECs' productivity gains would be rendered substantially more complex if the Commission continuously revised the composition of the baskets, because changes in productivity cannot be measured without comparison with historical productivity gains. If the Commission were to start moving major service categories from one basket to another, and creating separate baskets for large and small customers, it would be almost impossible to measure LECs' productivity gains.[153]

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152 See Fourth Further Notice of Proposed Rulemaking, CC Docket No. 94-1, FCC 95-406, released September 27, 1995 ("X-Factor Notice").

153 USTA's optional basket structure, which combines the local switching and common line baskets and establishes separate combined baskets for large and small customers, respectively, would likely require recomputing the appropriate productivity factor which was set on a company-wide basis, but was designed to be appropriate for each basket. See LEC Price Cap Order, 5 FCC Rcd. at 6812 (¶¶ 209-10).