

"[T]he geographic aspect of the relevant market must [also] reflect considerations of supply and demand substitutability." Memorandum Opinion and Order, Application of GTE Corp. & S. Pac. Co. for Consent to Transfer Control of S. Pac. Communications Co. & S. Pac. Satellite Co., 94 F.C.C.2d 235, 250 (1983). Here, "patterns of demand across geographic points favor a nationwide geographic market." Fourth Report and Order, 95 F.C.C.2d. at 574. See also NPRM, ¶ 51 ("customers typically purchase ubiquitous calling that enables them to make calls to all domestic locations").<sup>37</sup> And "supply substitutability [also] shows that the relevant geographic market of interexchange telecommunications suppliers is nationwide," because "[s]everal interexchange suppliers have nationwide networks with the capability to provide alternate geographic routings," GTE Corp., 94 F.C.C.2d at 250, and because "carriers have been able to enter and expand rapidly to serve a pair of points by constructing new facilities to supplement their networks, interconnecting, or

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<sup>37</sup> (...continued)

geographically limited basis is entirely irrelevant. See, e.g., id. at 1312-13 ("A national geographic market for these carriers' interexchange services is warranted because of supply and demand substitutability, even though [they] do not offer originating interexchange services nationwide"); Memorandum Opinion and Order, Application of MCI Communications Corp. & S. Pac. Telecommunications Corp. for Consent to Transfer Qwest Communications, Inc., 10 FCC Rcd. 1072, 1075 (1994) (relevant geographic markets "are not defined by the areas served by one of many market participants").

<sup>38</sup> In this regard, it is plain that domestic long distance customers evaluate interexchange carriers not by comparing rates for a single point-to-point call, but on the basis of expected monthly costs associated with diverse calling patterns to multiple locations, which the customer often will not even know in advance.

reselling the services of other carriers." Fourth Report and Order, 95 F.C.C.2d at 574. See, e.g., Rothery Storage & Van Co. v. Atlas Van Lines, Inc., 792 F.2d 210, 219 (D.C. Cir. 1986) (the nationwide market of interstate carriage of goods includes companies that move goods to and from particular geographic locations because no firm "could raise prices appreciably without attracting competitors' trucks from adjacent territories").<sup>39</sup>

Thus, it is unsurprising that fifteen years ago after initially proposing the same "point-to-point" approach proposed here, see NPRM, ¶¶ 49-50, the Commission soundly rejected it.<sup>40</sup> And only two years ago, the Commission again held that "it would be inaccurate to segment the market into distinct city pairs or even domestic regions. . . . because many networks have alternative routing capabilities with nationwide or near nationwide service areas." Memorandum Opinion and Order, Application of MCI Communications Corp. & S. Pac. Telecommunications Corp. for Consent

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<sup>39</sup> The NPRM errs in suggesting (¶ 51) that the Commission ignore supply substitution and treat the practice of geographic rate averaging as establishing that there is a single national market. Even a requirement that there be geographic rate averaging would be neither necessary nor sufficient to establish that there is a single national market. Where costs vary from location to location, there will still be a national market if any firm can enter on a national basis and if prices move in tandem, Rothery, 792 F.2d at 218-19, and, conversely, a requirement of geographic rate averaging will have no relevance if firms can enter only in particular locations -- which would be the case if there were wide variations in access prices by location and a geographic rate averaging requirement were nonetheless imposed.

<sup>40</sup> See Further Notice of Proposed Rulemaking, Policy and Rules Concerning Rates for Competitive Common Carrier Servs. and Facilities Authorizations Therefor, 84 F.C.C.2d 445, 498 (1981); Fourth Report and Order, 95 F.C.C.2d at 573-74 (the capacity of interexchange carriers' networks "cannot be segmented into distinct city pairs or even domestic regions").

to Transfer Control to Qwest Communications, Inc., 10 FCC Rcd. 1072, 1075 (1994) (noting "supply substitutability and low entry barriers"). In short, only a national geographic market is consistent with the "realities of the marketplace."<sup>41</sup>

Finally, recent experience with AT&T's "de minimus" 800 directory assistance and analog private line offerings, see AT&T Nondominance Order, ¶ 103, provide no basis for abandoning the established single market definition. As the Commission recognized in the AT&T Nondominance Order, AT&T's pricing of 800 directory assistance is constrained by precisely the same supply substitutability principles that constrain carriers' pricing of other interexchange services. See id., ¶¶ 102-03. That is why the Commission did "not foresee a significant danger that AT&T [would] raise substantially the price of this service to the detriment of consumers," id., ¶ 103, notwithstanding that AT&T was, at that

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<sup>41</sup> For the reasons stated in Section IA, supra, it is plain that no meaningful conclusions could be drawn from a LEC's share of the entire national interexchange services market. That is because such figures could never properly account for the clear market power generated by monopoly control of bottleneck facilities in a particular region. Nor, as AT&T explained in its comments in another pending proceeding, see AT&T Comments, Bell Operating Co. Provision of Out-of-Region Interstate, Interexchange Servs., CC Docket No. 96-21 (filed Mar. 13, 1996), would it be meaningful to measure LEC shares in a more limited "market" that does not exist. Although such a regional approach might be relatively more likely to yield the appropriate market power conclusion than would measuring the LEC's share of the actual national market, it would nonetheless be a poor substitute for the Commission's existing focus on direct evidence of market power. Even in the more limited "market," the LEC's initial share as a new entrant might well be too low to generate the appropriate concern under standard market concentration models designed to measure the market power of non-bottleneck monopolists.

time, the only 800 directory assistance provider.<sup>42</sup> Not only do other carriers have the ability to utilize existing facilities to provide 800 directory assistance in competition with AT&T -- all that is necessary to constrain prices and to mandate inclusion of 800 directory assistance in the same market as other interexchange services -- at least one carrier (SNET) has indicated an intention to do so.

The Commission's recognition that "analog private line customers are migrating to digital and virtual private line services" provided by numerous carriers, see AT&T Nondominance Order, ¶ 104, likewise precludes any finding that analog private line service is a separate market. The fact that all but a relative few private line customers have now abandoned analog service in favor of new digital technology, see id., ¶ 105,<sup>43</sup> conclusively demonstrates that those services are substitutes and that they are therefore part of the same market -- the single

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<sup>42</sup> Courts have consistently rejected any attempt to limit a market to a single product simply because that product is manufactured by a single firm. See, e.g., Nobel Scientific Indus., Inc. v. Beckman Instruments, Inc., 670 F. Supp. 1313, 1323 (D. Md. 1986) (citing cases); Neugebauer v. A.S. Abell Co., 474 F. Supp. 1053, 1066 (D. Md. 1979) (same). Rather, a separate product market exists only when the single firm can profitably sustain a price increase -- i.e., when consumers will not switch to other products and producers of other products will not switch their facilities to production of the product in question. See also Hunt-Wesson Foods, Inc. v. Ragu Foods, Inc., 627 F.2d 919, 924 (9th Cir. 1980) ("[b]lind reliance upon market share, divorced from commercial reality, give[s] a misleading picture of a firm's actual ability to control prices or exclude competition").

<sup>43</sup> AT&T's 1995 analog private line revenues fell to less than \$8 million, barely one quarter the 1992 level, as compared to increasing digital private line revenues, which currently exceed a billion dollars annually.

relevant market for interexchange services -- even under the Commission's tentatively proposed demand-focused approach. The Commission's apparent focus in the NPRM on the few remaining analog customers is misplaced. As the Commission itself has previously held: "The relevant question in defining markets is not whether there are substitutes for a given product that can be used by those who want that particular product with exactly the same specifications and properties. . . . [A carrier] is constrained to price competitively . . . [by] other services that are close substitutes for many messages and customers." Fourth Report and Order, 95 F.C.C.2d at 572 n.59 (emphasis added) (declining to find a separate market for telex services that were rapidly being replaced by more modern technologies).<sup>44</sup> In sum, the economic, legal, and factual support for the Commission's existing single interexchange services product market is overwhelming -- absent some unique structural advantage such as control over bottleneck facilities, no carrier conceivably could "monopolize" an individual interexchange service (either nationally or in any more limited geographic area), and thus all such services are in the same national market.

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<sup>44</sup> See also Smalley & Co. v. Emerson & Cuming, Inc., 13 F.3d 366, 368 (10th Cir. 1993) (declining to find separate markets because "[p]urchasing constraints on a single consumer" are irrelevant; "the fundamental objective of our antitrust laws is to promote fair competition for the benefit of all consumers"); J.T. Gibbons, Inc. v. Crawford Fitting Co., 704 F.2d 787, 795-96 (5th Cir. 1983) (that a manufacturer's product is not interchangeable with other similar products is not sufficient to establish a separate market where products perform the same function); General Business Sys. v. North Am. Phillips Corp., 699 F.2d 965 (9th Cir. 1983).

**II. THE COMMISSION SHOULD IMPOSE ADDITIONAL SEPARATION REQUIREMENTS ON LECs' OUT OF REGION INTEREXCHANGE SERVICES.**

The NPRM suggests that LECs have far less ability to use local monopolies to harm competition when interexchange services originate, and the selection of the interexchange carriers occurs, outside their regions. That is principally because the LECs do not there provide the originating access services for which there is an obvious and ready ability to discriminate in the pricing and provisioning of the physical facilities used to originate virtually all interexchange calls in that region. Instead, each LEC will necessarily provide terminating access for only a small fraction of calls that originate outside their regions and for which the selection of interexchange carrier occurs out of region. These are the reasons the 1996 Act now permits the BOCs to provide out-of-region, but not in-region, interexchange services.

At the same time, both the BOCs and the independent LECs retain a significant ability to use their in-region monopolies to obtain illicit advantages with respect to calls that originate outside their regions. First, while the volume of out-of-region calls that terminate in any one BOC's or independent LEC's service territory will be a fraction of the total number of out-of-region calls, they will represent a substantial expense, particularly now when terminating (like originating) access is priced at many times its real economic cost. This leaves the BOCs and independent LECs substantial opportunity to price terminating access in ways

designed improperly to favor interexchange affiliates,<sup>45</sup> and effect price squeezes and cross-subsidies.<sup>46</sup>

Second, control over local in-region monopolies -- and, necessarily, the ordering, provisioning, and maintenance of access -- gives the BOCs and other LECs other opportunities to obtain illicit advantages with respect to out-of-region interexchange services. For example, the leading interexchange carriers provide and market their interexchange services on a national basis, and, as a condition of obtaining access, are required to disclose their future marketing plans and access needs to all LECs. These disclosures are made both to Bellcore (controlled by the seven RBOCs), to individual LECs, and to standard setting bodies. Absent appropriate regulations from the Commission, BOCs and independent LECs could readily use the information they obtain from national interexchange carriers to advantage their own out-of-region interexchange services businesses.

Third, BOCs and other LECs obtain added opportunities for misconduct to the extent that business customers are located in multiple States and consumers have more than one residence. For instance, a BOC may induce in-region customers to purchase its out-of-region services by "bundling" those services with reduced rates

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<sup>45</sup> For example, a LEC could deny cost-justified volume discounts on terminating access, manipulate the relative price of direct-trunked transport versus tandem-switched transport arrangements, and otherwise regularly change and tailor access pricing to meet the requirements of its out-of-region interLATA affiliate.

<sup>46</sup> For these reasons, it is critical that maximum feasible steps be taken to assure that all interexchange carriers obtain access services at the same economic (not just tariffed) cost that the BOCs and other LECs incur.

for local service or by raising the prospect of inferior (or the promise of superior) local arrangements for such in-region customers.

For these reasons, AT&T previously opposed, even as an interim measure, the Commission's proposal to permit BOCs to provide out-of-region interexchange services on a nondominant basis if they merely comply with the three separation conditions that have applied to smaller independent LECs -- i.e., that they (1) maintain separate books of account; (2) not jointly own transmission or switching facilities with the local exchange company; and (3) obtain any of the exchange company's services at tariffed rates and conditions.<sup>47</sup> While these are necessary conditions, they do not address the serious risks that BOC interexchange affiliates would engage in joint marketing with, or obtain customer information or other benefits arising from, their monopoly local affiliates' operations.<sup>48</sup>

Now that the Commission is considering the proper separations requirements that should apply to the provision on a nondominant basis of out-of-region interexchange services by the BOCs and other LECs, it should explicitly acknowledge the considerable opportunities for leveraging of the local exchange bottleneck to the improper advantage of out-of-region interexchange

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<sup>47</sup> See AT&T Comments, Bell Operating Co. Provision of Out-of-Region Interstate, Interexchange Servs., CC Docket No. 96-21 (filed Mar. 13, 1996); AT&T Reply Comments, Bell Operating Co. Provision of Out-of-Region Interstate, Interexchange Servs., CC Docket No. 96-21 (filed Mar. 25, 1996).

<sup>48</sup> See id.

affiliates. The most effective separations requirements for addressing these risks are the full structural separations requirements of the Second Computer Inquiry proceedings. The costs of such requirements, moreover, are substantially mitigated to the extent the LECs will be required to provide in-region interexchange services through a fully separate subsidiary, a matter that the NPRM defers to another proceeding,<sup>49</sup> but a requirement which the Act explicitly imposes on the BOCs.<sup>50</sup>

In all events, there is no basis to lessen or eliminate the existing requirements. To the contrary, as AT&T has demonstrated here and in response to the Commission's proposal to permit BOCs to provide out-of-region interexchange services on a nondominant basis, the existing separations requirements for LEC provision of interexchange services on a nondominant basis are patently inadequate to guard against the very real potential for abuse, even for out-of-region interexchange services. At a minimum, all LECs should be additionally subject to requirements that they not engage in joint marketing or any sharing of information between their interexchange affiliates and their monopoly in-region local operations. These additional requirements should impose no considerable additional costs on LECs that are currently offering out-of-region interexchange services in compliance with the existing separations requirements, which the

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<sup>49</sup> See NPRM, ¶ 61.

<sup>50</sup> See 47 U.S.C. §§ 271, 272.

Commission has previously found to impose no unreasonable burdens.<sup>51</sup> Indeed, the most significant cost to the LECs would be that they could not obtain the illicit advantages that the separation requirements would be designed to prevent.

### **III. RATE AVERAGING AND RATE INTEGRATION REQUIREMENTS**

Section 254(g) of the 1996 Act requires the Commission to adopt rules regarding rate averaging and rate integration for interexchange services. The rigid and inflexible application of rate averaging and rate integration requirements apparently proposed in the NPRM, however, goes well beyond the requirements of the 1996 Act, would be directly contrary to congressional intent, ignores the central pro-competitive thrust of the Act and the discretion Congress intended for the Commission to exercise, and would necessarily result in higher prices. Particularly in light of Congress' clear expectation that the Commission's rate averaging and rate integration rules will incorporate appropriate use of its forbearance authority, the Commission should substantially modify the proposed rate averaging and rate integration rules consistent with the principles described below.<sup>52</sup>

Until now, large IXCs, driven in part by the Commission's relatively flexible rate averaging policies, have generally focused

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<sup>51</sup> See NPRM, ¶ 58.

<sup>52</sup> By definition, the rate averaging and rate integration rules mandated by Section 254(g) will be applicable to all interexchange carriers. Accordingly, the NPRM (¶¶ 73, 79) correctly concludes that the rules adopted in this proceeding generally will supersede AT&T's existing voluntary commitments in those areas. Although AT&T's rate integration commitments regarding Alaska would technically continue in effect, AT&T assumes that the policies adopted here will also apply in Alaska.

on the entire national market.<sup>53</sup> This has allowed such carriers to develop and maintain nationwide averaged rate structures. Entry of large regional carriers such as GTE and SNET, however, alters the competitive considerations.<sup>54</sup> In this environment, rigid rate averaging and rate integration requirements, which necessarily limit carriers' ability to establish prices that reflect underlying costs, would inhibit national carriers' ability to compete with regionally-based competitors in low-cost areas, thereby discouraging carriers from offering service to customers in rural and high-cost areas -- as the Commission has recognized. See NPRM, ¶ 69 n.154 ("if new entry substantially increases competition in areas with high volumes and low costs, nationwide interexchange carriers may be placed at a competitive disadvantage if they are not permitted to offer regional discounts in such areas"). It is absolutely critical that the Commission's rate averaging and rate integration rules recognize and take account of this reality.

Specifically, because nationwide carriers will, by definition, have higher average costs than regional carriers who serve only low cost areas, rigid rate averaging and rate

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<sup>53</sup> See Further Notice of Proposed Rulemaking, Policy and Rules Concerning Rates for Dominant Carriers, 3 FCC Rcd. 3195, 3452 (1988) (noting that AT&T and other IXCs historically engaged in rate averaging "primarily because they have strong economic incentives to average their rates"); Notice of Proposed Rulemaking, Competition in the Interstate Interexchange Marketplace, 5 FCC Rcd. 2627, 2649 (1990).

<sup>54</sup> The NPRM (¶ 53) correctly assumes that LECs generally will be regionally-focused competitors and provide interexchange services predominantly to customers in their own local service territories -- as has historically been the case for the interexchange affiliates of LECs such as SNET and Rochester Telephone.

integration requirements would force nationwide carriers to develop averaged nationwide rates that reflect those costs. The resulting higher rates would make nationwide carriers uncompetitive in low cost areas and reduce competition for the large numbers of consumers who live in such areas.<sup>55</sup> This places nationwide IXCs (and customers) in a Hobson's choice: either the carriers must abandon high cost areas in order to compete effectively against regional IXCs in low cost areas, or abandon low cost areas and charge higher prices to customers in rural and high cost areas. Either way, each group of customers faces less competition and higher prices.<sup>56</sup>

Further, not only would uncompromising rate averaging and rate integration rules drive up the costs and prices of carriers that serve high cost areas, they would also provide strong disincentives for low cost/low price carriers to expand their

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<sup>55</sup> For example, the average access costs per minute (originating and terminating) in some LEC areas are as much as 0.8 cents per minute lower than the nationwide average. Thus, LEC interexchange carriers serving those areas have up to a 1.6 cent per minute cost advantage over nationwide carriers, even if they are equally efficient in all other aspects of their business. This equates to about a 10% cost differential, giving the regional carriers a substantial market advantage over nationwide carriers.

<sup>56</sup> This would be especially true if the Commission continues to deaverage access prices (see, e.g., Memorandum Opinion and Order, NYNEX Tel. Co. Petition for Waiver, Transition Plan to Preserve Universal Serv. in a Competitive Env't, 10 FCC Rcd. 7445 (1995)). The impacts of deaveraged access rates are felt in both originating and terminating access costs. Today, for example, some of AT&T's nodal services rates (which include transport and terminating, but not originating, access charges), are less than the access charges AT&T incurs to terminate calls in certain areas. Because of this disparity, other IXCs sometimes resell AT&T's service when terminating calls to such areas, because it is cheaper than carrying the call to those areas and purchasing terminating access from the LEC.

operations into rural and high cost areas. Low cost carriers could not charge prices that reflect the actual costs of entering such areas unless they also raised prices in low cost areas. No economically rational carrier, however, would choose to reduce its competitiveness in its existing serving areas. Indeed, the distorted economics resulting from rigid rate averaging and rate integration rules are more likely to cause carriers to abandon any efforts to serve the comparatively smaller number of consumers who live in rural and high cost areas. This would turn the statute on its head, driving nationwide carriers from low cost areas, leading to ever-increasing prices for consumers in rural and high cost areas (and eventually low cost areas as well), and virtually guaranteeing that all consumers will experience less competition and higher prices than today.

Fortunately, no such result is required -- or, indeed, authorized -- by the 1996 Act. To the contrary, it is clear that Congress only intended § 254(g) to codify the Commission's existing policies on rate averaging and rate integration. Congress directed the Commission to implement § 254(g) through rules, and Congress fully anticipated that the Commission would consider both the pro-competitive goals of the 1996 Act<sup>57</sup> and the Commission's broad

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<sup>57</sup> The NPRM (§ 1), quoting from the Senate Conference Report, recognizes that the 1996 Act "seeks 'to provide for a pro-competitive, de-regulatory national policy framework' designed to make available to all Americans advanced telecommunications and information technologies and services 'by opening all telecommunications markets to competition.'"

forbearance authority in developing those rules.<sup>58</sup> Accordingly, the unqualified rules proposed in the NPRM should be substantially revised.

As the report on the Senate bill preceding the 1996 Act expressly states, in enacting the rate averaging provision Congress "simply incorporate[d] in the Communications Act the existing practice of geographic rate averaging and rate integration for interexchange, or long distance, telecommunications rates."<sup>59</sup> The conference report for the final version of the bill similarly states that § 254(g) "is intended to incorporate the [Commission's] policies of rate averaging and rate integration," and that Congress "intend[s] that the Commission, where appropriate, should continue

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<sup>58</sup> The 1996 Act requires the Commission to forbear from applying any provision of the Communications Act that meets the test of new Section 10. Section 10 (47 U.S.C. § 160) provides that

The Commission shall forbear from applying any regulation or any provision of this Act to a telecommunications carrier or telecommunications services in any or some of its or their geographic markets if the Commission determines that: (1) enforcement of such . . . provision is not necessary to ensure that the charges, practices, classifications or regulations by, for, or in connection with that . . . telecommunications service are just and reasonable and are not unjustly or unreasonable discriminatory; (2) enforcement of such . . . provision is not necessary for the protection of consumers; and (3) forbearance from applying such provision . . . is consistent with the public interest.

<sup>59</sup> H.R. Rep. No. 458, Joint Explanatory Statement of the Comm. of Conference, 104th Cong., 2d Sess. 129 (1996) ("Joint Explanatory Statement") (emphasis added). The NPRM (¶ 68 n.153) acknowledges that the text of Section 254(g) contains only minor modifications from this earlier Senate provision.

to authorize exceptions using its forbearance authority under Section 10."<sup>60</sup>

This flexibility is further confirmed by Conference Committee changes in the bill. The original Senate and House bills each mandated a specific statutory rule regarding geographic rate averaging.<sup>61</sup> In the Conference Committee's final bill, however, the provision was changed from a mandatory prescription of a Congressionally-defined rule to a requirement that the Commission adopt rules to implement rate averaging. In sum, the Commission has significant authority and flexibility to create rate averaging and rate integration rules that are compatible with the basic pro-competitive policies underlying the 1996 Act.

Accordingly, AT&T urges the Commission to:

- (1) clarify that IXCs may continue to (a) assess surcharges to recover state-specific gross receipts taxes, (b) use geographically-specific promotions, and (c) offer point-to-point private line rates as well as Tariff 12, contract tariff and other high end business services offerings; in the alternative, the Commission should forbear from applying rate averaging and rate integration requirements to such practices and offerings;
- (2) forbear from applying rate averaging and rate integration requirements to nondominant carriers' services, except

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<sup>60</sup> Joint Explanatory Statement at 132.

<sup>61</sup> See S. 652, § 253(g), 141 Cong. Rec. S8575 (daily ed. June 16, 1995); H.R. 1555, § 248(e), 141 Cong. Rec. H9983 (daily ed. Oct. 12, 1995).

possibly for a single, tariffed rate schedule that every carrier would offer to all residential customers;

(3) affirm that a competitive necessity justification can justify any pricing action by an IXC that could otherwise violate the Commission's rate averaging or rate integration requirements; and

(4) assure that rules regarding intrastate rate averaging are not inconsistent with rules for interstate services.

Foremost, however, the rate averaging provisions of the Act (and the rules adopted by the Commission thereunder) must be interpreted in accordance with the broader pro-competition policies that are the Act's primary goal. In this context, it is manifest that one of the principal cost factors that gives rise to the averaging concern -- access charges imposed on interexchange carriers -- is also among the most formidable obstacles to local competition. The Act thus contemplates and requires that the access charge mechanism be completely overhauled, so that subsidies are removed and prices are driven to efficient, forward-looking cost-based levels. After this occurs, of course, access prices will be far lower and more uniform than they are today, and a reasonable averaging policy should impose fewer burdens and anomalies. Until access reform is complete, however, it is particularly important that interexchange carriers not be doubly penalized, first by having to pay inflated prices for monopoly access services, and second by being forbidden efficiently to reflect those costs in competitive pricing. For this reason, the Commission should, at a minimum, defer or waive the effectiveness

of its rate averaging rules, to make them effective concurrently with access reform.

**A. The Commission Should Confirm That Existing Pro-Competitive Practices Which Allow Deaveraging May Continue.**

Because Section 254(g) is only intended to incorporate existing Commission policies, the Commission should confirm that the 1996 Act does not proscribe existing pro-competitive practices which allow rate deaveraging in certain circumstances. These include, inter alia, state-specific gross receipts tax surcharges, geographically-limited promotions, geographically-specific private line rates, and Tariff 12, contract tariff and comparable services.

Each of these currently-allowed practices serves a pro-competitive purpose and is independently justified. For example, current Commission practice properly allows carriers to apply gross receipts tax surcharges to customers in states which impose such taxes (costs) on interstate carriers. That is because ratepayers in the subject states are the direct and sole beneficiaries of the state tax policies, and the costs imposed by such policies should not be borne by other customers who receive no benefit from such taxes.<sup>62</sup> This rationale is unchanged by the passage of the 1996 Act, and rates plainly should be considered net of such state-

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<sup>62</sup> See Memorandum Opinion and Order, Connecticut Office of Consumer Counsel v. AT&T Communications, 4 FCC Rcd. 8130, 8132 (1989), aff'd sub nom. Connecticut Office of Consumer Counsel v. FCC, 915 F.2d 75 (2d Cir. 1990) (rejecting claim that such charges create geographic deaveraging and finding no unreasonable discrimination in the application of such charges).

specific surcharges for purposes of determining compliance with rate averaging and rate integration requirements.

Promotions, of course, are universally accepted marketing practices commonly used throughout the telecommunications industry and in most other competitive businesses. Similarly, AT&T and its competitors offer geographically-specific pricing for private line services.<sup>63</sup> Geographically-targeted promotions can increase rivalry in the market in specific ways, such as introducing a service in a new area or spurring localized interest in particular services.<sup>64</sup> Even more important in light of the new competitive landscape created by the 1996 Act, such promotions and geographically-specific pricing for private line services enable national carriers to respond to competition from regional carriers.<sup>65</sup> The benefits of these pro-competitive activities, which offer lower prices to consumers, should not be restricted by rigid national rate

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<sup>63</sup> See, e.g., WilTel Tariff F.C.C. No. 4, Section IV.16; Sprint Tariff F.C.C. No. 8, Section 3.1; MCI Tariff F.C.C. No. 8, Table A.201, Tariff F.C.C. No. 1, Appendix A, Option No. 815; Tariff F.C.C. No. 12, Sections 3.703 and 3.763; AT&T F.C.C. Tariff. No. 9. AT&T is unaware of any objections to such rates.

<sup>64</sup> See, e.g., Sprint F.C.C. Tariff No. 1, Sections 6.58 and 6.86; MCI Tariff F.C.C. No. 1, Section C.10 (Option Q.S. promotions and 1-800-COLLECT promotion); AT&T F.C.C. Tariff No. 1, Sections 8.1.1.688, 739 and 774 and F.C.C. Tariff No. 27, Sections 21.1.1.1.B.4-7 and 39 (Consumer Long Distance promotions); AT&T F.C.C. Tariff No. 1, Section 8.1.1.924 (Calling Card promotion) and Sections 8.1.1.43 and 8.1.1.331 (Collect call promotions); AT&T F.C.C. Tariff No. 27, Sections 21.1.1.B.28 and 21.1.1.B.40 (Calling Card promotion).

<sup>65</sup> See, e.g., AT&T Tariff F.C.C. No. 1, Section 8.1.1.688, F.C.C. Tariff No. 27, Sections 21.1.1.A.26, 21.1.1.A.97 (Consumer Long Distance promotions); Section 8.1.1.975 (UNIPLAN promotion), 8.1.1.967 (MultiQuest promotion).

averaging or rate integration requirements which could preclude their use.

Customers also greatly benefit from Tariff 12, contract tariff and other similar high-end business services. Competition for the customers of these services -- the largest and most sophisticated telecommunications customers -- is intense, and these services allow carriers to provide telecommunications packages tailored to customers' needs at the lowest possible competitive prices. That is why the Commission has previously found that both Tariff 12 and contract tariff services serve its pro-competition objectives.

In all events, the criteria of Section 10 are satisfied with respect to each of these existing pro-competitive practices and would therefore require that the Commission exercise forbearance with respect to any such practice deemed inconsistent with general rate averaging and rate integration requirements.<sup>66</sup> Gross receipts tax surcharges are merely passthroughs to a State's residents of the taxes their State government has elected to impose for their benefit. Any rule that did not allow such passthroughs would provide States with a perverse incentive to impose their tax burdens on residents of other States -- a result that would plainly be contrary to the public interest.

Enforcement of a strict rate averaging requirement is not necessary in the case of geographically-specific promotions, because temporary price changes do not have any significant impact

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<sup>66</sup> As noted above, the NPRM (§ 17) recognizes that Section 10 requires forbearance if the statutory criteria are met.

on the market as a whole. In particular, there should be no concern that such activities would allow nondominant carriers to discriminate unreasonably or to charge unjust or unreasonable prices.<sup>67</sup> The whole purpose of promotions is to offer consumers lower prices. Thus, restrictions on such pricing actions would more likely injure than protect consumers. Finally, the market effects of such promotions -- increased competition and downward pressures on prices -- demonstrate that forbearance would be in the public interest.

Similarly, the Commission's longstanding support of private line, Tariff 12 and contract tariff offerings demonstrates the reasonableness of those offerings and the appropriateness of forbearance, if the Commission should determine that such a justification is required. Many facilities-based suppliers are vying for customers' business, and the Commission has found that no carrier dominates the provision of such services.<sup>68</sup> In these circumstances, the existing nondominant suppliers of such services could not sustain unreasonable practices, prices or discrimination. Moreover, the purchasers of such services are a relatively small group of the largest and most sophisticated corporate telecommunications users. Enforcement of the rate averaging requirement is particularly unnecessary to protect these customers.

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<sup>67</sup> See NPRM, ¶ 28 (reaffirming the Commission's 15-year old conclusion that "firms lacking market power simply cannot rationally price their services in ways which, or impose terms and conditions which, contravene Sections 201(b) and 202(a) of the Act") (citation omitted).

<sup>68</sup> See, e.g., AT&T Nondominance Order, ¶¶ 45-50, 57-60.

Indeed, forbearance in the case of Tariff 12 services is expressly contemplated in the Conference Report,<sup>69</sup> and any other position with respect to such high end business services could require the renegotiation of literally thousands of detailed commercial contracts, which would be directly contrary to congressional intent that Section 254(g) would not require the renegotiation of any contracts for telecommunications services.<sup>70</sup>

**B. The Commission Should Forbear From Applying Rate Averaging And Rate Integration Requirements To Non-Dominant Carriers' Services.**

The NPRM (§ 28) acknowledges that nondominant carriers lack power to discriminate unreasonably and (§ 19) tentatively concludes that all three of the statutory forbearance criteria are met with respect to such carriers' tariffed offerings. For essentially the same reasons, forbearance from the geographic averaging requirement for nondominant carriers' services also is warranted and would not harm consumers.

Nevertheless, in order to provide a baseline of averaged rates available to all consumers, the Commission could, if it deems appropriate, have all IXCs file at least one tariffed schedule of averaged rates that would be available to residential customers on a nationwide basis. Competition in the interexchange market, combined with ongoing Commission oversight, will ensure that rates are just, reasonable and not unreasonably discriminatory. This

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<sup>69</sup> Joint Explanatory Statement at 132.

<sup>70</sup> Joint Explanatory Statement at 132 ("the conferees do not intend that this subsection would require the renegotiation of existing contracts for the provision of telecommunications services").

approach will serve the public interest by promoting the overarching pro-competitive purposes of the Act, avoiding the market distorting impacts of inflexible rate averaging and rate integration rules, and also protecting the specific interests that are reflected in Section 254(g).

**C. The Commission Should Confirm That Competitive Necessity Will Justify Any Pricing Action That Might Otherwise Conflict With Rate Averaging Or Rate Integration Policies.**

Marketplace events requiring prompt competitive response occur continuously in the interexchange market. In particular, as regionally-focused carriers, including the SNET and GTE companies that are actively pursuing customers now, expand their competitive entry, national carriers face increasing pressures to respond quickly to meet the needs of customers in specific geographic areas. Thus, the Commission should reaffirm that carriers may take any pricing action required by competitive necessity. See NPRM, ¶ 69 ("competitive conditions or other circumstances . . . could justify Commission forbearance").

Specifically, the Commission should find that forbearance of geographic rate averaging or rate integration requirements is appropriate under the following conditions:

- a. There is effective competition for the service for which forbearance is sought in the relevant geographic area; and
- b. either
  - (i) The carrier's price is offered to meet a competitive offer to the affected customers, or
  - (ii) External factors influence the costs of providing the service in that area (e.g., access costs, taxes, regulatorily-imposed subsidies); such external factors result in total costs that are

different from the nationwide average; and the proposed rate differential is not greater than the external cost differences; and

- c. The proposed rate is at or above the appropriate measure of incremental cost.

These standards reflect existing Commission decisions and practices regarding cost justification and competitive necessity, which routinely have been used to support differences in rates for like services. The Commission should affirm their applicability against any future claim that a carrier has not complied with rate averaging or rate integration rules.<sup>71</sup>

Forbearance pursuant to these guidelines will promote competition by allowing carriers to respond to competitors' offers, as they may currently.<sup>72</sup> It will also allow carriers to make reasonable price adjustments to account for the differing impacts that access and other externally-imposed costs have on nationwide and regional carriers.<sup>73</sup> In addition, it will reduce the market

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<sup>71</sup> The NPRM correctly recognizes that nondominant interexchange carriers' tariffs are presumptively lawful and subject to one day notice requirements, and that reduced tariffing is likely. These rules are specifically designed to foster prompt competitive responses. The NPRM (§§ 70, 78) further recognizes that "it would not be in the public interest to attempt to enforce geographic rate averaging" and "rate integration requirements through the tariff process," and that these requirements should principally be enforced through complaint proceedings. Accordingly, there should be no pre-effectiveness tariff review, and the forbearance guidelines proposed above should be available as defenses in any complaint proceeding alleging that a carrier has violated Commission rate averaging or rate integration requirements.

<sup>72</sup> See, e.g., Report and Order, Private Line Rate Structure and Volume Discount Practices, 97 F.C.C.2d 923, 948 (1984).

<sup>73</sup> See, e.g., Memorandum Opinion and Order on Reconsideration, Competition in the Interexchange Marketplace, 10 FCC Rcd. 4562, 4567 (1995).

distortions of rate averaging that discourage entry into high cost areas.

**D. The Commission Should Assure That Rules Regarding Intrastate Rate Averaging Are Not Inconsistent With The Rules For Interstate Services.**

AT&T generally supports the Commission's conclusion (NPRM, ¶ 68) that Section 254(g) only preempts state rate averaging laws or rules to the extent they are inconsistent with the rules adopted in this proceeding. In particular, consistent with the language of the Act, states should not be prohibited from applying rate averaging requirements on a less than statewide basis.<sup>74</sup> The Commission should make clear, however, that States may not apply rate averaging requirements in ways that would distort competition; rather, any State rules must be narrowly focused and consistent with the Act's underlying purpose and the Commission's rules.

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<sup>74</sup> Thus, for example, States should not prohibit carriers from establishing multiple contiguous "rate zones" that associate urban and rural areas which have logical relationships with each other.

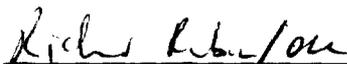
**CONCLUSION**

For the reasons set forth above, AT&T urges the Commission to (1) retain its existing single national interexchange services market definition, (2) impose more stringent separation requirements on LECs' provision of out-of-region interexchange services, and (3) adopt reasonable and flexible rate averaging and rate integration rules that are compatible with the pro-competition goals of the Act.

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