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Before the
Federal Communications Commission
Washington, D.C. 20554

FEDERAL COMMUNICATIONS COMMISSION
OFFICE OF SECRETARY

In the Matter of:

Policy and Rules Concerning the
Interstate, Interexchange, Marketplace

Implementation of Section 254(g) of the
Communications Act of 1934, as Amended

To: The Commission

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) CC Docket No. 96-61
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COMMENTS OF THE SOUTHERN NEW ENGLAND TELEPHONE COMPANY

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SUMMARY

In these comments, The Southern New England Telephone Company ("SNET") asks that the FCC revise its regulatory policies in four specific respects in response to the agency's Notice in this proceeding, and SNET explains why each of these four revisions is appropriate.

- In Part I of its comments, SNET urges the Commission to permit a small LEC such as SNET to provide interstate communications service under non-dominant regulation to customers located outside the area where it provides telephone exchange service ("out-of-region interstate service"). Non-dominant regulation would replace the FCC's present policy of regulating a small LEC's out-of-region interstate offerings under the much more burdensome dominant carrier regime.
- In Part II, SNET asks that the Commission specifically propose in its forthcoming Notice to apply non-dominant regulation to any non-access interstate service provided by a small LEC such as SNET to customers located within that LEC's exchange service area. SNET also requests that the Commission issue that Notice promptly.
- In Part III, SNET urges the Commission to promptly issue an order which amends the agency's LEC price cap regulatory policies in the manner proposed by the agency in its Second Notice issued more than seven months ago in the LEC price cap performance review docket.
- In Part IV, SNET asks the agency to hold that interstate toll free directory assistance ("toll free DA") is a separate interstate service market. It also requests that the agency regulate AT&T's interstate toll free DA service under dominant carrier regulation until structural barriers that prevent more than one company from providing interstate toll free DA are eliminated.

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This is the first rulemaking proceeding under the Commission's new statutory "regulatory forbearance" authority.^{1/} A major purpose of this first forbearance proceeding is to decide whether to eliminate certain regulatory requirements the agency presently applies to LECs.

Two significant market trends make it increasingly important that the Commission reduce regulation of small LECs such as SNET so that they may compete efficiently in the telecommunications market. The first is the rapidly growing tendency of telecommunications vendors to expand their product lines in order to meet the desire of consumers for one-stop shopping. The second -- partially caused by the first -- is the increasing pace of corporate consolidations within the telecommunications industry.

SNET's experience provides a good illustration of these phenomena. In Connecticut, where SNET provides telephone service,

^{1/} See Pub. L. No. 104-104 at §401, 110 Stat. 56, 128 (1996), adding Section 10(a) to the Communications Act of 1934.

the Department of Public Utility Control ("DPUC") has certified the nation's two largest interstate carriers (and several smaller ones) to provide all types of local and in-state long distance service throughout Connecticut. Teleport Communications Group, a company controlled by three of Connecticut's four largest cable TV operators -- TCI, Comcast, and Cox -- likewise has been certified to provide a full array of local and long distance telephone services throughout Connecticut in combination with cable service provided by its cable TV owners. Moreover, Cablevision Corp., the state's second largest cable operator, has applied for a certificate to provide local telephone service to its cable subscribers and expects to obtain a certificate shortly. In fact, both Cablevision and TCI have upgraded their Connecticut cable TV networks in order to provide local and long distance telephone service, and TCI has begun to test market its telephony offering.^{2/}

SNET's own experience illustrates the inefficiencies that regulatory policies cause. Of most relevance to the present proceeding, the FCC's dominant/non-dominant carrier dichotomy imposes inefficiencies on SNET's provision of a full array of local and long distance telephony services. This is because that policy requires SNET to provide interstate service either under dominant regulation or through a different corporation in order to take advantage of non-dominant regulation. SNET's huge one-stop shopping competitors need not suffer these inefficiencies since the

^{2/} The DPUC has certified eight companies to provide facilities-based exchange service in Connecticut, and it has certified more than 100 carriers to provide in-state toll service.

dominant/non-dominant dichotomy does not apply to them. Moreover, SNET's ability to keep the very largest users of its exchange facilities from bypassing its exchange network is hindered by outdated FCC regulations which require SNET to levy uniform exchange access rates regardless of market conditions. These regulations do not apply to any of SNET's competitors in the one-stop shopping market.

In this proceeding, the Commission has the opportunity to begin removing the outdated regulatory requirements that impose inefficiencies on small LECs in competing in the new one-stop-shopping market against the much larger companies with whom they now must compete in order to remain viable.

DISCUSSION

I. Small LECs Like SNET Should Be Allowed to Provide Out-of-Region Interstate Service Under Non-Dominant Regulation Since the Benefit of Regulating These Small LEC Services Under Dominant Regulation Now Is Clearly Outweighed by the Cost

The Commission recognizes in its Notice that the time has come to review its 1983 decision to regulate a LEC's non-access interstate telecommunications service under dominant carrier regulation unless the LEC provides its interstate offerings through a different entity than the one providing exchange and exchange access service.^{3/} In that 13-year-old order, the FCC held that it would reg-

^{3/} See Notice at ¶56-63, requesting comment on whether to revise the agency's decision in Policy and Rules Concerning Rates for Competitive Common Carrier Services, Fourth Report and Order, 95 F.C.C. 2d 554, 576-79 (1983), clarified, Fifth Report and Order, 98 F.C.C. 2d 1191, 1198-99 (1984). In those orders, the Commission held that it would regulate a LEC's interstate non-access service (continued...)

ulate a LEC's interstate service under dominant regulation if offered directly through the LEC because it concluded that the benefit outweighed the cost under circumstances existing then. The agency recognized that the choice it offered LECs (providing interstate service through the LEC under dominant regulation or through a different entity under non-dominant regulation) imposed costs on consumers by preventing the LEC from operating at optimal economic efficiency.^{4/} It found that these costs are particularly severe for smaller LECs like SNET.^{5/} Nonetheless, the Commission concluded that in the competitive and regulatory environment of the mid-1980's, the benefit outweighed this cost. The agency found that the choice it provided (dominant regulation if service is offered by the LEC and non-dominant regulation if service is offered by a non-LEC affiliate) could be beneficial to the Commission by providing a regulatory tool to keep a LEC from competing unfairly in the interstate service market by leveraging -- into that market -- its control over the telephone exchange facilities upon which many interstate service providers depend. It felt that such leveraging could take one of two forms: the LEC might unfairly subsidize its interstate service by misallocating interstate service costs to its exchange access service upon which nearly all

^{3/} (...continued)
under dominant regulation unless the LEC offers the interstate service through a different entity than the one providing access and exchange service.

^{4/} Fifth Report and Order, supra, 98 F.C.C. 2d at 1199.

^{5/} Id., 98 F.C.C. 2d at 1198 n.23.

interstate carriers depend in order to originate and terminate interstate traffic, or the LEC might unfairly discriminate against other interstate carriers by providing access service that is inferior to the access service it gave itself.^{6/}

Rather than using the present proceeding to examine the cost and benefit of applying dominant regulation to all LEC-provided interstate services in today's environment, the Commission instead has chosen to divide its review into two parts. In the present proceeding, it asks whether the benefit of dominant regulation of interstate services offered directly by a LEC continues to outweigh cost when a LEC provides interstate service to customers located outside the area where the LEC provides telephone exchange service ("out-of-region interstate service").^{7/} The Commission says it will consider later in a separate rulemaking proceeding whether the benefit of applying dominant regulation to a LEC's non-access interstate service offerings to customers inside the area where it provides telephone exchange service ("in-region interstate service") still outweighs the cost.^{8/}

Even if the benefit of regulating either the out-of-region or in-region interstate offerings of some LECs still outweighed the cost, it plainly does not in the case of SNET because SNET's core

^{6/} Fifth Report and Order, supra, 98 F.C.C. 2d at 1204 (leveraging by allocating costs); Fourth Report and Order, supra, 95 F.C.C. 2d at 576 (leveraging by providing exchange access on discriminatory terms).

^{7/} Notice at ¶¶61-62.

^{8/} Id. at ¶53 n.122.

telephony markets -- including local exchange service -- are more open to competition than the core markets of most other LECs. Even AT&T has stated that "Connecticut is one of the first states in the nation working to adopt widespread local competition for phone service."^{2/}

Because of the unique circumstances applicable to SNET, SNET's parent company has petitioned the FCC requesting authority for SNET to provide both in-region and out-of-region interstate service under non-dominant regulation.^{10/} That petition is before the Commission, and the agency should grant it expeditiously regardless of the outcome of either the present rulemaking proceeding or the one which will follow.

While the Commission should grant non-dominant regulatory treatment to SNET by granting its pending petition, the agency should apply non-dominant regulatory treatment to the out-of-region interstate offerings of all small LECs in response to the present Notice since the benefit of dominant regulation in that situation is plainly outweighed by the cost. Below, we first show that little benefit results from regulating the out-of-region interstate offerings of small LECs under dominant regulation. Then, we demonstrate that the cost of dominant regulation is especially severe when applied to small LECs like SNET.

^{2/} See Att. No. 1. See also notes 20 and 24, infra.

^{10/} See Pet. of So. New Eng. Telecomm. Corp. for Declaratory Ruling, CCB Pol. 96-03 (filed Jan. 17, 1996).

A. The Benefit Obtained by Regulating a Small LEC's Out-of-Region Interstate Offerings Is Inconsequential

Dominant regulation of a small LEC's out-of-region interstate service produces little benefit for four reasons. Each is discussed below.

1. A Small LEC Cannot Leverage Market Power In Exchange Service Into the Interstate Service Market When Providing Out-of-Region Interstate Service Since An Insignificant Amount of Its Interstate Traffic Would Use Its Exchange Facilities

First, a small LEC providing out-of-region interstate service could not harm interstate competition in the area where it provides interstate service by leveraging any exchange market power since only a small amount of the LEC's interstate traffic would use its exchange facilities. The theory of the FCC's 1983 decision that a LEC providing interstate service might have an ability without dominant regulation to leverage its exchange market power into the interstate market is valid, at best, only if a significant percentage of the LEC's interstate traffic uses that LEC's exchange access service. In that case, the theory holds that the LEC might allocate costs to its access service which should have been allocated to its interstate offering, thereby enabling the LEC unfairly to provide interstate service below cost. But that theory is inapplicable if a small LEC like SNET provides interstate service to customers outside of its telephone exchange area. In that case, an insignificant amount of the LEC's interstate traffic would use that LEC's exchange service since none of the LEC's interstate

traffic would originate on its exchange facilities as explained above, and only a small amount would terminate on its exchange facilities.

Assume, for example, that SNET offered interstate service in one or more states where it does not provide the telephone exchange service which is the theoretical source of its leveraging power. In that case, none of SNET's interstate traffic would originate on SNET's telephone exchange facilities as explained above, and only about 1.25 percent of its interstate traffic could be expected to terminate on its exchange facilities.^{11/} This means, in turn, that just one-fourth of one percent (0.25%) of SNET's interstate service revenue would be attributable to payments for use of SNET's own exchange network since roughly 20 percent of a carrier's total interstate service revenues are paid to LECs for terminating access.^{12/} A LEC cannot possibly harm interstate service competition in the area where it provides interstate service by leveraging any power in the telephone exchange market when the portion of its

^{11/} This figure is calculated based on the reasonable assumption that SNET's exchange facilities would be used to terminate a percentage of its out-of-region interstate traffic equal to the number of SNET exchange access lines as a percentage of the total number of U.S. access lines. As of December 1, 1994, SNET had 1.97 million of the nation's 156.8 million access lines (i.e., 1.25 percent of all access lines). See USTA, Phone Facts 1995 at 9-10.

^{12/} If 20% of SNET's interstate revenues were attributable to payments for terminating access, just 0.25% of its revenues would be attributable to exchange access payments for use of SNET's exchange access facilities given that only 1.25% of its interstate traffic would use these facilities as explained in n.10 above. (20% X 1.25% = 0.25%).

interstate service revenues attributable to use of its exchange facilities is so small.

2. Numerous FCC Regulatory Policies Implemented In the Last Several Years Have Substantially Reduced a LEC's Market Power In the Telephone Exchange Market In Any Event

Numerous FCC regulatory policies adopted in the last several years further reduce the theoretical benefit of applying dominant-regulation to a small LEC's out-of-region interstate offerings. First, the agency significantly lessened a LEC's ability to leverage any remaining exchange market power by revamping its cost accounting rules in 1986. The 1986 rules established a uniform accounting system and a uniform set of cost allocation principles for use by all Tier 1 LEC's (including SNET) and required these LECs to develop a cost accounting manual establishing procedures for allocating costs based on these allocation principles.^{13/} Unlike in 1983, moreover, independent auditors now must attest every year that each LEC's accounting books conform with all applicable FCC regulations, including the agency's 1986 rules.^{14/} Commission auditors also review these independent audits.^{15/} And

^{13/} Joint Cost Order, 2 FCC Rcd. 1298 (1986), recon. 2 FCC Rec. 6283 (1987), further recon. 3 FCC Rcd. 6701 (1988), aff'd sub nom. Southwestern Bell corp. v. FCC, 896 F.2d 1378 (D.C. Cir. 1990).

^{14/} Computer III Remand Proceedings: Bell Operating Co. Safeguards and Tier I Local Exch. Co. Safeguards, Report and Order, 6 FCC Rcd. 7571, 7593, vacated in part and remanded, Calif. v. FCC, 39 F. 3d 919 (9th Cir. 1994). See also Joint Cost Order, supra, 2 FCC Rcd. at 1329-33.

^{15/} Computer III Remand Proceedings, supra, 6 FCC Rcd. at 7593.

the agency uses ARMIS, an automated data storage and analysis system that did not exist in 1983, to track a LEC's accounts over time and to compare the accounts of different LECs. This too helps the agency detect efforts to leverage telephone exchange market power through cost misallocations.^{16/}

The FCC also has significantly lessened a LEC's incentive to leverage any exchange market power by changing the way it regulates the price LECs charge interstate carriers for exchange access service. Under the "rate-of-return" regulatory regime that existed in 1983, a LEC's allowable return on investment was based on its reported costs. A LEC that misallocated costs from non-access service to exchange access service could have increased the price charged for access service by whatever amount was required to recover misallocated costs. In 1990, however, the agency substituted "price cap" regulation for rate-of-return regulation.^{17/} Today, price cap regulation is used to control the access service prices charged by LECs serving almost 95 percent of the nation's population, including SNET. Both the Commission and the courts have found that price cap regulation significantly reduces the

^{16/} Id., 6 FCC Rcd. at 7593-94. See also U.S. v. West. Elec. Co., 993 F. 2d 1572, 1580 (D.C. Cir. 1993) (the existence of many LECs increases the number of benchmarks that can be used by regulators to detect discrimination).

^{17/} Policy and Rules Concerning Rates for Dominant Carriers, Second Report and Order, 5 FCC Rcd. 6786 (1990), recon., 6 FCC Rcd. 2637 (1991), aff'd. sub nom. Nat. Rural Teleph. Ass'n v. FCC, 988 F.2d 174 (D.C. Cir. 1993). See also LEC Price Cap Performance Review for Local Exchange Carriers, First Report and Order, 10 FCC Rcd. 8961 (1995), aff'd. Bell Atlantic Corp. v. FCC, No. 95-1217 (D.C. Cir. March 29, 1995).

incentive a LEC otherwise might have to misallocate costs since misallocation reduces the LEC's earnings rather than permitting it to charge higher prices for the access service to which costs were misallocated.^{18/}

FCC regulations promulgated in the past several years also reduce any theoretical risk that a LEC will provide interstate access on discriminatory terms. In 1985, the agency established rules by which LECs would be required, over a transition period, to provide switched access service to all interstate carriers on equal terms.^{19/} This transition is now complete. Each Tier 1 LEC now offers interstate equal access arrangements to all interstate carriers in all (or nearly all) of that LEC's end offices.^{20/}

^{18/} See, e.g., Policy and Rules Concerning Rates for Dominant Carriers, Notice of Proposed Rulemaking, 2 FCC Rcd. 5208, 5213 (1987) (price caps "substantially decrease incentives to shift costs from more to less competitive service offerings" and "reduce, if not eliminate, any perverse incentive to inflate rate bases"); Policy and Rules Concerning Rates for Dominant Carriers, supra, 5 FCC Rcd. at 6792 (price caps "mitigate misallocation as a regulatory concern"); id., 5 FCC Rcd. at 6791 (price cap regulation "defeats any LEC attempt to finance a predatory rate level by contemporaneously increasing rates for other services"); U.S. v. West. Elec. Co., supra, 993 F.2d at 1580 ("the FCC move in the direction of price cap regulation . . . reduces . . . [the LEC's incentive] to shift costs . . . [to exchange access services] because the increase in costs for the [access service] . . . does not automatically cause an increase in the legal rate ceiling").

^{19/} MTS and WATS Market Structure, Report and Order, 100 F.C.C.2d 860, 875 (1985).

^{20/} Industry Analysis Division, FCC, Trends in Telephone Service (Feb. 1995). SNET provides equal access for interstate calls in all of its nearly 140 end offices. Many state public utility commissions have implemented similar equal access requirements for in-state interLATA calls as well. The Connecticut DPUC has gone even further by mandating equal access for all intraLATA toll calls. At present, SNET provides equal access for intraLATA
(continued...)

More recently, the Commission has made discriminatory provision of exchange access even more difficult by promulgating its expanded interconnection rules.^{21/} The Commission has held that these new requirements further "improve [its] ability to scrutinize filed rates to prevent . . . discrimination."^{22/}

3. The Telecommunications Act of 1996 Requires the Commission, by August 8, to Adopt Whatever Additional Regulations Are Necessary to Facilitate Competition In All Important LEC Markets

A LEC's ability and incentive to leverage whatever market power it has in the exchange market is further reduced by the Telecommunications Act of 1996. First, that Act explicitly bars enforcement, effective upon enactment, of any "statute or regulation or other . . . requirement . . . [that] may prohibit or have the effect of prohibiting the ability of any entity to provide any

^{20/} (...continued)
toll calls in half of its end offices, and by the end of this year the company will provide equal access arrangements for intraLATA toll calls in all of its end offices.

^{21/} Expanded Interconnection with Local Tel. Co. Facilities, Report and Order, 7 FCC Rcd 7369 (1992), recon., 8 FCC Rcd 127 (1992), vacated in part and remanded sub nom. Bell Atlantic Tel. Co. v. FCC, 24 F.3d 1441 (D.C. Cir. 1994), recon., 8 FCC Rcd 7341 (1993), proceeding after remand, 9 FCC Rcd 5154 (1994) (adopting expanded interconnection rules governing provision of special access). See also Expanded Interconn. with Local Telephone Company Facilities, Second Report and Order, 8 FCC Rcd 7374 (1993), vacated in part and remanded sub nom. Bell Atlantic Tel. Co. v. FCC, 1995 U.S. App. LEXIS 12180 (D.C. Cir. Apr. 17, 1995), proceeding after remand, 9 FCC Rcd 5154 (1994) (adopting expanded interconnection rules governing provision of switched access).

^{22/} See Expanded Interconn. with Local Tel. Co. Facilities, supra., 8 FCC Rcd at 7368.

interstate or intrastate telecommunications service."^{23/} No longer may any government regulatory policy directly or indirectly protect LECs from competition in any service market.

But the 1996 Act did even more than eliminate any previously existing regulatory policy that had the effect of prohibiting competition by any entity in any core LEC service market. It also added two new provisions to the Communications Act -- Sections 251 and 252 -- which affirmatively require that the FCC adopt whatever additional regulations are necessary to affirmatively promote competition in each of these product markets. And it instructs the agency to adopt these regulations by no later than August 8 of this year.^{24/}

^{23/} Pub. L. No. 104-104, supra, at §101(a) adding new Sec. 253(a) to Commun. Act of 1934.

^{24/} See Pub. L. No. 104-104, supra, at §101(a), adding new Sections 251 and 252 to the Commun. Act of 1934. New Sections 251 and 252 require that the regulations adopted by August 8 are sufficient to ensure that a LEC (a) provides telephone number portability; (b) provides dialing parity and nondiscriminatory access to telephone numbers, operator services, directory assistance and directory listings to all competing carriers; (c) provides interconnecting carriers with reciprocal compensation arrangements; (d) provides competitors with reasonable access to the LEC's poles, ducts, and rights of way; (e) permits competitors to interconnect on nondiscriminatory terms with the LEC's network at any technically feasible point; (f) provides competitors with unbundled network elements on nondiscriminatory terms at any technically feasible point; (g) offers competitors for resale at wholesale rates any telecommunications service it provides end users at retail; (h) provides competitors with reasonable notice of changes in the information necessary to transmit and route services which use the LEC's exchange network; and (i) provides competitors with the opportunity to colocate their equipment with comparable LEC equipment on LEC premises. As measured by these criteria, the exchange service market in Connecticut already is fully open to competitive entry due to state regulations already in place there. Thus, as explained fully in SNET's petition requesting authority to provide
(continued...)

4. Marketplace Realities, Including Industry Consolidation and Product-Line Expansion, Also Reduce A Small LEC's Incentive to Leverage Any Exchange Market Power It May Have

Marketplace realities reduce a small LEC's incentive to leverage exchange market power as well. First, industry leaders in the interstate service market would have a substantial ability to withstand any attempt by a small LEC to leverage exchange market power since they all are much larger than any small LEC. For example, 1995 revenues of SNET and its affiliates were less than three percent of AT&T's 1995 revenues,^{25/} were just 12 percent of MCI's 1995 revenues,^{26/} were just over 14 percent of Sprint's 1995 revenues,^{27/} and were just 50 percent of WorldCom's 1995 revenues.^{28/} Combined, these four carriers have more than 95 percent of the

^{24/} (...continued)
any non-access interstate service under non-dominant regulation (see n.10, supra), DPUC regulations already require that SNET provide number portability, dialing parity, reciprocal compensation, unbundled access to exchange facilities, and a right to resell its exchange service.

^{25/} See AT&T Annual Report to Shareholders at 2 (reporting that AT&T's 1995 revenues were \$79.6 billion).

^{26/} Electronic Media (Feb. 5, 1996) (reporting that MCI's 1995 revenues were nearly \$15.3 billion).

^{27/} See Sprint Annual Report to Shareholders (reporting that Sprint's 1995 revenues were nearly \$12.8 billion).

^{28/} See WorldCom Form 10-K for year ending December 31, 1995 (reporting that WorldCom's 1995 revenues were \$3.64 billion. Moreover, WorldCom's 1996 revenues may increase dramatically since it has signed agreements within the last three months alone to carry interstate traffic for Ameritech, Southwestern Bell Mobile Systems, and GTE. Id. at 5-6.

interstate service market. This significant size difference gives incumbent interstate carriers the ability to withstand any attempt by a small LEC to leverage exchange market power into the interstate service market since a large company providing interstate service can economically justify spending far more on advertising than a smaller company and can spread the cost of providing interstate service over a much larger base of costs. The greater ability of a large interstate service competitor to withstand any theoretical leveraging also results from its established interstate service brand. By contrast, a small LEC would enter the out-of-region interstate market with no market share and little (or no) name recognition.^{29/}

The growing trend toward product line expansion in the telecommunications industry reduces a small LEC's incentive to leverage market power into the interstate service market even against smaller interstate service competitors. This is because a full-service company inherently has a greater ability to withstand leveraging than a company providing interstate service alone since a full service company can spread its fixed costs over a wider array of offerings. The Commission's proposal in the proceeding to permit all non-dominant carriers to bundle CPE with their inter-

^{29/} Small LECs also are at a disadvantage vis-a-vis their much larger interstate service competitors because of the manner in which they must enter the market. A small LEC must provide interstate service either as a reseller or by deploying an interstate transmission network from scratch. Neither option is conducive to effective leveraging of exchange market power.

state offerings illustrates this point.^{30/} SNET supports that proposal, and its adoption will make it even more difficult for small LECs to leverage any exchange market power into the interstate market since it will give incumbent interstate carriers a larger base of products and services from which to counteract any attempted leveraging.

B. The Cost that Results from Regulating a Small LEC's Out-of-Region Interstate Offerings Under Dominant Regulation Is Greater than the Cost that Results from Regulating a Large LEC's Out-of-Region Offerings Under Dominant Regulation

The Commission not only should recognize that dominant regulation of a small LEC's out-of-region interstate service produces only a marginal benefit (at best), it also should balance this marginal benefit against the fact that the cost which results from applying dominant regulation to smaller LECs is greater than the cost which results from applying dominant regulation to larger LECs. The Commission frequently exempts smaller LECs from the obligation to comply with specific regulatory requirements because of the relatively higher cost that would result from forced compliance with the subject regulation. For example, in its seminal Computer II orders the agency exempted all companies owning LECs other than the seven large Bell companies from a requirement that enhanced services be provided through an affiliate other than the company's LEC. It took the action because of the relatively higher

^{30/} Notice at ¶88.

cost that would result from imposing this requirement on the smaller LECs.^{31/}

Congress likewise has recognized that smaller LECs should not have to comply with specific regulatory obligations because of the relatively higher cost of compliance. For example, new Section 251(f)(2) of the Communications Act authorizes regulators to exempt any LEC with fewer than two percent of the nation's subscriber lines from mandatory compliance with any requirement imposed by new Sections 251(b) or 251(c) if the cost of forced compliance is unreasonable.

II. The Commission Should Promptly Issue a Notice Proposing to Regulate a Small LEC's In-Region Interstate Service Under Non-Dominant Regulation Since the Cost of Dominant Regulation Outweighs the Benefit

Not only should the Commission issue an order in this proceeding permitting small LECs to provide out-of-region interstate service under nondominant regulation, it also should explicitly propose in its forthcoming Notice of Proposed Rulemaking to permit the same small LECs to provide in-region interstate service under non-dominant regulation. And the agency should issue that Notice promptly so that it can end this unnecessary regulation more quickly than would be possible if it delayed issuance of the Notice.

The benefit obtained from regulating a small LEC's in-region interstate service has been significantly attenuated because of the new regulatory controls described in Part I(A)(2) above which the

^{31/} See Computer II, First Recon. Order, 84 F.C.C. 2d 50, 72-75 (1980).

Commission has adopted in the past several years. Amendments to the Communications Act described in Part I(A)(3) also have reduced the benefit. Marketplace developments described in Part I(A)(4) have reduced the benefit as well by reducing a small LEC's incentive to exploit any remaining market power. Moreover, the cost that results from regulating a small LEC's in-region interstate offerings under dominant regulation also is higher than the cost that results from imposing dominant regulation on the in-region interstate offerings of larger LECs as explained in Part I(B).

III. The Commission Should Promptly Adopt the Revisions In Its LEC Access Charge Rules that It Proposed More Than Seven Months Ago, and It Should Promptly Initiate a Proceeding to Reform the Access Charge Rate Structure

The FCC's access charge rules compound the unfair competitive harm that results from the Commission policy to regulate a small LEC's interstate service under dominant regulation. While the price cap rules give LECs a modest amount of flexibility to price interstate exchange access services in order to meet the greatly increased competitive threat of bypass that the 1996 Telecommunications Act creates, in many respects they still unfairly constrain LECs from the pricing flexibility necessary to meet this competition. More than seven months ago, the FCC recognized this fact, and it proposed to revise its access charge rules in a variety of ways to increase a LEC's access pricing flexibility.^{32/} The record in that proceeding is complete. The Commission should

^{32/} Second Further Notice of Proposed Rulemaking, Price Cap Performance Review for Local Exchange Carriers, 60 Fed. Reg. 49539 (1995).

promptly issue an order amending its access charge rules in the manner proposed by the Second Notice. In addition, the FCC long ago recognized that the access charge rate structure required by the Part 69 rules needs to be reformed in order to provide LECs with additional pricing flexibility. The agency also should quickly initiate a proceeding to accomplish those needed reforms.

IV. Interstate Toll Free Directory Assistance Should Be Treated As a Separate Interstate Service Market, and AT&T's Interstate Toll Free Directory Assistance Service Should Be Regulated Under Dominant Regulation Until Structural Barriers that Prevent Competition Are Eliminated

The Commission also should treat interstate toll free directory assistance ("toll free DA") as a separate interstate service market. In its Notice, the Commission proposed to treat all interstate services as part of a single product market except for a particular service or group of services for which there is no close substitute.^{33/} Under this test, interstate toll free DA plainly is a separate product market since there is no close substitute for the service. No other telecommunications service offers consumers the ability to obtain directory information about interstate toll free numbers. While consumers also may obtain some interstate toll free numbers through printed directories rather than by using toll free DA, printed directories are a supplement to interstate toll free DA rather than a substitute for that service since the provider of interstate toll free DA controls access to the toll free numbers listed in these directories.

^{33/} Notice at ¶41.

Not only should the Commission hold that interstate toll free DA is a separate interstate service market, it also should regulate AT&T's provision of interstate toll free DA under dominant regulation since AT&T is the only company providing interstate toll free DA due to structural barriers that make competitive entry impossible. Indeed, the Commission held last year that AT&T has monopoly power in providing interstate toll free DA.^{34/} It reiterated this finding earlier this year and promised to consider ways to remove the structural barriers that preclude competition in interstate toll free DA.^{35/} SNET has proposed a specific way in which competition can exist in the interstate toll free DA market, and it petitioned the Commission to issue an order implementing SNET's plan nearly one year ago.^{36/} The Commission should promptly grant SNET's petition. Until structural barriers to competition are eliminated, the agency also should regulate AT&T's interstate DA service under dominant regulation.

CONCLUSION

The Commission should (1) permit all small LECs, including SNET, to provide out-of-region interstate service under non-dominant regulation; (2) promptly issue a Notice proposing to permit the same small LECs to provide in-region interstate service

^{34/} Revisions to Price Cap Rules for AT&T, 76 Rad. Reg. (P&F) 2d 1375, 1382 (1995).

^{35/} Toll Free Service Access Codes, DA 96-69 at ¶57 (rel. Jan. 25, 1996).

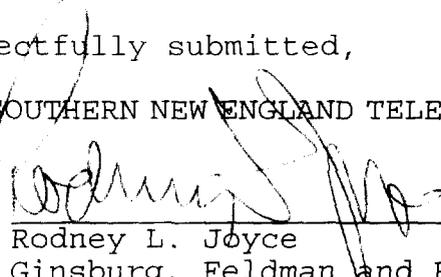
^{36/} See "Pet. of The So. New Eng. Tel. Co. for Declaratory Ruling", DA-1062 (filed May 8, 1995).

under non-dominant regulation; (3) promptly complete action in response to its Second Further Notice in the LEC Price Cap Performance Review proceeding; and (4) hold that interstate toll free directory assistance is a separate interstate service market and regulate AT&T's interstate toll free directory assistance service under dominant regulation until structural barriers that make competition impossible are removed.

Respectfully submitted,

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