

ORIGINAL

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

RECEIVED

MAY - 3 1996

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 )

CC Docket No. 96-61

DOCKET FILE COPY ORIGINAL

REPLY COMMENTS

MCI TELECOMMUNICATIONS CORPORATION

Donald J. Elardo  
Frank W. Krogh  
Mary J. Sisak

1801 Pennsylvania Avenue, N.W.  
Washington, D.C. 20006  
(202) 887-2006

Its Attorneys

Dated: May 3, 1996

No. of Copies rec'd      
List ABCDE      
*dfb*

## SUMMARY

Most commenters agree with the Commission's proposed approach toward defining the market for interstate, interexchange services, as it amply allows for evaluation, at an appropriate time, of the likely effects of Bell Operating Company (BOC) entry into in-region markets.

With regard to BOC and other Local Exchange Carrier (LEC) provision of "out-of-region" interstate, interexchange services, the record amply supports continuation of the Competitive Carrier requirement that LECs be required to provide such services through separate affiliates if they wish such services to regulated as non-dominant. BOCs, however, should be made subject to a more stringent standard, namely, that their out-of-region interexchange offerings be made available only through separate affiliates and, then, only pursuant to policies and rules applicable to dominant carriers.

Finally, with respect to the questions of geographic rate averaging and rate integration, substantial concerns are expressed on the record as to how both these important policy objectives can be met. MCI continues to believe that, as in the past, they can co-exist. Serious consideration should be given to the proposal that all interstate, interexchange carriers file tariffed rate schedules that establish averaged rates on a nationwide basis. This approach would address and resolve a number of problems while, at the same time, it would furnish carriers with the flexibility they need to compete in the marketplace, especially against regional carriers.

**TABLE OF CONTENTS**

I. RELEVANT PRODUCT AND GEOGRAPHIC MARKETS . . . . . 1

II. SEPARATION REQUIREMENTS FOR OUT-OF-REGION SERVICES . . . . . 2

    A. The Telecommunications Act of 1996 Does Not Affect  
        the Commission's Power to Regulate BOC  
        Interexchange Services . . . . . 3

    B. The Initial Comments Confirm the LECs' and BOCs'  
        Continuing Market Power in Out-of-Region  
        Interexchange Services . . . . . 3

    C. The Initial Comments Confirm That the Separate  
        Affiliate Requirements Should be Strengthened and  
        That BOC Out-of-Region Interexchange Affiliates  
        Should be Subject to Dominant Carrier Regulation . . . . . 13

III. GEOGRAPHIC RATE AVERAGING AND RATE INTEGRATION . . . . . 19

    CONCLUSION . . . . . 25

**ATTACHMENT**

## **REPLY COMMENTS**

MCI Telecommunications Corporation (MCI) respectfully submits these reply comments in connection with the Commission's "Notice of Proposed Rulemaking" (FCC 96-123), released March 25, 1996. Therein, the Commission sought comment on a number of matters concerning the state of competition in the interstate, interexchange marketplace and the recent, significant modifications made to the Communications Act of 1934.<sup>1</sup>

The "first phase" of this proceeding involves the definition of relevant product and geographic markets, the provision of "out-of-region" interstate, interexchange services by Local Exchange Carriers (LECs), including the Bell Operating Companies (BOCs), and issues relating to geographic rate averaging and rate integration. Initial comments were filed by approximately fifty parties on or about April 19, 1996.<sup>2</sup>

### **I. RELEVANT PRODUCT AND GEOGRAPHIC MARKETS**

By and large, the commenters do not have major disagreements with the Commission's proposed approach to defining the market for interstate, interexchange services. A few commenters focus primarily on an entirely separate question -- whether a BOC or independent LEC can exercise market power with respect to the provision of interstate, interexchange services in areas where it provides local access services.<sup>3</sup> However, the Commission

---

<sup>1</sup> Telecommunications Act of 1996, Pub. L. No. 104-104, 110 Stat. 56 (1996) (hereinafter referred to as "the new law" or the "1996 Act").

<sup>2</sup> All references herein to these comments shall be to the filing party in abbreviated fashion and any page citation(s).

<sup>3</sup> E.g., BellSouth at 15-20; Pacific at 5-8; and US West at 3-10.

expressly decided not to resolve this issue in this proceeding.<sup>4</sup> Most commenters accept this decision.<sup>5</sup>

As the NPRM intended, the proposed standards for product and geographic market definition do not prejudge the question of regulatory treatment of in-region interstate services provided by the BOCs. The BOCs' ability to exercise market power in the interstate, interexchange market does not depend on whether that market is broadly or narrowly defined.<sup>6</sup> The Commission's proposed guidelines for market definition allow for consideration of special circumstances, such as control over an essential input, and with the qualification described in MCI's initial comments, the guidelines establish a reasonable analytical framework for assessment of market power.

## II. SEPARATION REQUIREMENTS FOR OUT-OF-REGION SERVICES

The initial comments confirm that the BOCs and other LECs continue to possess overwhelming local bottleneck power and the ability to project that power into out-of-region interexchange services. They also demonstrate that such power and ability

---

<sup>4</sup> NPRM at para. 53, n.122.

<sup>5</sup> E.g., SBC Communications at 5 ("The Commission need not evaluate in advance the market power of a potential class of participants in the interstate, interexchange market.") (footnote omitted).

<sup>6</sup> The danger of BOC entry results from their monopoly power over local exchange and exchange access services. See AT&T at 6-8. None of the incumbent LECs submitting comments seriously disputes the fact that they currently control these bottlenecks. These bottlenecks give the BOCs power over price and output in the interexchange market -- regardless of their initial share of the interexchange market, any lack of brand recognition outside their regions, interexchange rate averaging policies, or regulations that prohibit price and non-price discrimination in theory, but not in practice. See discussion in part II(B), infra.

require that LECs continue to provide any interexchange services, including out-of-region services, through separate affiliates as a condition of nondominant regulatory treatment for such services, that BOCs be compelled to provide out-of-region interexchange services through separate affiliates, and that such BOC affiliates be regulated as dominant carriers.

A. The Telecommunications Act of 1996 Does Not Affect the Commission's Power to Regulate BOC Interexchange Services

Recycling the procedural arguments they made in the BOC Out-of-Region proceeding,<sup>7</sup> some of the BOCs claim that the 1996 Act precludes any Commission-imposed separate affiliate requirement, or any other requirements, for BOC out-of-region interexchange services, since Congress omitted any such restrictions for those services.<sup>8</sup> As MCI explained in its Reply Comments in the BOC Out-of-Region proceeding, a copy of which is attached hereto, nothing could be further from the truth. MCI refers the Commission to pages 1-4 of its attached BOC Out-of-Region Reply Comments for a full rebuttal of the BOCs' statutory authority arguments.

B. The Initial Comments Confirm the LECs' and BOCs' Continuing Market Power in Out-of-Region Interexchange Services

As in the BOC Out-of-Region proceeding, most of the LECs and BOCs do not strongly contest the one issue that is dispositive of their market power in out-of-region interexchange services, namely, their continuing local exchange bottleneck control, which

---

<sup>7</sup> Bell Operating Company Provision of Out-of-Region Interstate, Interexchange Services, CC Docket No. 96-21.

<sup>8</sup> See, e.g., BellSouth at 24-25.

is discussed in MCI's and others' initial comments.<sup>9</sup> They instead fall back on the claim that, for a variety of reasons, their local bottleneck control cannot be exercised in out-of-region interexchange services.

Some local carriers do suggest, however, that their bottleneck control is not as strong as it was and that substantial local exchange and access competition is just around the corner. US West, for example, states that "local exchange market power has been declining," citing "the development of wireless technology and existing wireline competition," with no factual elaboration or statistical support.<sup>10</sup> Various local carriers argue that "local competition will develop quickly," pointing to the Commission's expanded interconnection requirements, the interconnection, unbundling and other requirements of Sections 251, 252 and 271 of the 1996 Act and various interexchange carriers' and other providers' announced plans to enter the local exchange and access markets.<sup>11</sup> The Southern New England Telephone Company (SNET) adds that "the exchange service market in Connecticut already is fully open to competitive entry due to state regulations already in place there."<sup>12</sup>

In fact, however, it is going to take some time for the requirements in the 1996 Act to be implemented in regulations and

---

<sup>9</sup> See, e.g., MCI at 13-15.

<sup>10</sup> US West at 4, n.7.

<sup>11</sup> GTE at 10. See also, e.g., BellSouth at 18, n.43; US West at 4, n.7; Ameritech at 7-8; SNET at 12-13.

<sup>12</sup> SNET at 13 n.24.

for those regulations and the comparable intrastate regulations to bring about the significant local exchange and access competition that now is only in the planning stages. Nynex admits as much in stating that the local carriers' bottleneck control "will eventually be a moot point, because the [1996 Act] will promote competition in the access market."<sup>13</sup> Similarly, Ameritech asserts that competitive access providers and others "are poised ... to enter the local exchange marketplace."<sup>14</sup> As for the implementation of parallel intrastate policies, MCI has demonstrated, in its comments on SNET's request for nondominant treatment for its interexchange services, SNET's failure to carry out the pro-competitive policies established by the Connecticut Department of Public Utility Control (DPUC) that were cited by SNET as evidence of competitive conditions. SNET's uncooperative approach in Connecticut confirms the LECs' continuing reluctance to give up any local bottleneck power.<sup>15</sup>

Similarly, as stated by Frontier Corporation, which provides both local exchange and interexchange services, the BOCs now "are dominant providers of access, local and intraLATA services" in their service regions,<sup>16</sup> and "even if the Bell companies were to embrace fully the Act's goal of opening the local exchange to

---

<sup>13</sup> Nynex at 7 (emphasis added).

<sup>14</sup> Ameritech at 12 (Emphasis added).

<sup>15</sup> See Comments of MCI Telecommunications Corporation at 18-25, Petition Requesting that Any Interstate Non-Access Service Provided by Southern New England Telecommunications Corporation Be Subject to Non-Dominant Carrier Regulation, CCB Pol. 96-03 (filed Feb. 26, 1996), incorporated herein by reference.

<sup>16</sup> Frontier at 4.

competition, it will take years for significant local exchange competition actually to develop.”<sup>17</sup> Thus, it would not be prudent before the fact to assume that local exchange and access competition will spring forth almost immediately upon promulgation of the regulations implementing the 1996 Act and parallel intrastate requirements and to remove safeguards prematurely. Instead, the Commission should carefully review the effectiveness of the yet-to-be issued regulations implementing the 1996 Act after they have been in effect for a reasonable period of time and should consider removing any requirements based on the local carriers’ bottleneck power only when it is clear that actual significant local competition has loosened the local bottleneck to such an extent that there is no longer any risk of abuse.

Given the local bottleneck control that still exists and will continue to exist for the foreseeable future, the local carriers argue that their local dominance is irrelevant to their market power in out-of-region interexchange services, citing their low market shares in interexchange services and the presence of large, well-established competitors as conclusive proof of their lack of market power.<sup>18</sup> As MCI and others explain in their initial comments, however, the Commission has correctly looked primarily to local exchange market power in analyzing local carriers’ interexchange market power, and that

---

<sup>17</sup> Id. at 5.

<sup>18</sup> See, e.g., BellSouth at 16-17; US West at 4-9; Ameritech at 3-7.

factor has always overshadowed such facts as the local carriers' interexchange market shares.<sup>19</sup>

US West inadvertently stumbles into the truth on this point when it asserts that "over-reliance on market share can cause erroneous evaluations of market power."<sup>20</sup> As long as other interexchange carriers (IXCs) continue to be dependent on the local carriers for access to the vast bulk of telephone subscribers, local dominance will continue to be the primary factor in assessing the local carriers' market power in interexchange services. The local carriers complain that this approach is different from the approach recently taken in declaring AT&T nondominant,<sup>21</sup> but there is, of course, no inconsistency. Since AT&T has no local bottleneck power, its dominance in interexchange services could only be measured by such factors as market share and elasticity of supply.

Moreover, MCI and others demonstrated in their initial comments how a local carrier can discriminate within region against IXCs competing on a nationwide basis so as to advantage the local carrier's out-of-region interexchange services, particularly as to out-of-region calls that terminate in-region.<sup>22</sup> Ameritech attempts to minimize this issue by asserting that "almost 90% of the calls of an out-of-region competitor will

---

<sup>19</sup> See, e.g., MCI at 19-20 & nn. 31-32.

<sup>20</sup> US West at 4.

<sup>21</sup> See, e.g., BellSouth at 16.

<sup>22</sup> See MCI at 15-17.

be handled completely outside the BOC's network."<sup>23</sup> That percentage, however, is more like 80-85% for the typical BOC and, for the BOCs that are merging (assuming the mergers pass regulatory and Department of Justice scrutiny), probably only 60-70%. Furthermore, access discrimination affecting just 10%, or less, of a nationwide IXC's traffic is more than enough disruption and expense to do significant harm to the IXC's overall operations and to disadvantage that IXC vis-a-vis the local carrier's out-of-region interexchange services.

The local carriers also take an overly narrow view of the types of injuries that a local carrier can inflict on its out-of-region interexchange rivals. Although the clearest form of discrimination would be unequal terminating access for its own and competitive providers' out-of-region traffic, the local carriers fail to acknowledge that a much wider range of abuses is possible. Since some of the "independent IXCs" competing against a local carrier's out-of-region services operate on a nationwide basis, they provide services within the local carrier's region, thereby affording the local carrier tremendous leverage against them. A local carrier thus could do serious damage to its out-of-region interexchange competitors through its provision of inferior access for outbound, as well as inbound, interexchange traffic. Such tactics could injure its competitors' services and nationwide reputations and raise their costs. For a BOC not yet providing in-region interexchange services, such tactics would

---

<sup>23</sup> Ameritech at 7.

not even appear to be discriminatory, since the BOC would not be using its own originating access services.

Thus, for example, SBC Communications argues against the likelihood of access discrimination by stating that "[a] BOC cannot easily or economically identify calls that originate with its interexchange competitors in markets in which the BOC operates as an interexchange carrier from calls originating in markets in which it does not."<sup>24</sup> The problem with that response is that a BOC does not have to make such fine distinctions in order to disadvantage its out-of-region competitors; all it has to do is identify all interexchange traffic carried by its competitors that either originates or terminates within region and burden that traffic with inferior access.

Similarly, SNET misses the point when it states that "none of SNET's [out-of-region] interstate traffic would originate on SNET's telephone exchange facilities ... and only about 1.25 percent of its interstate traffic could be expected to terminate on its exchange facilities."<sup>25</sup> How much of SNET's own interexchange traffic is originated or terminated in-region is not the only issue, though. It is also necessary to consider the origination and termination of the traffic of other IXCs that also compete with SNET's out-of-region services in the interexchange market, because that is the traffic that the local carrier can burden with inferior or overpriced access.

---

<sup>24</sup> SBC Communications at 7.

<sup>25</sup> SNET at 8.

The local carriers assert, however, that local dominance nevertheless cannot be exercised in out-of-region interexchange services for a variety of reasons, such as the geographical separation of the out-of-region services from the local services, price cap regulation, cost allocation rules and other accounting regulations and the equal access requirements.<sup>26</sup> The United States Telephone Association (USTA) also points out that no one local carrier controls all of the essential facilities it needs to provide interexchange service and that local carriers are as dependent as IXCs on other local carriers for access.<sup>27</sup>

Some local carriers argue that the existence of large IXC competitors makes any anti-competitive conduct, especially predatory pricing, utterly futile and that the local carriers could never drive the independent IXCs out of business.<sup>28</sup> Others argue that the local carriers have no interexchange market power because they could not raise interexchange rates by restricting output.<sup>29</sup> They also argue that the supposed implausibility of carrying out access discrimination, as well as the ease of detection of unequal access charges and other forms of access discrimination, negate any possibility of creating an advantage for the local carrier's own interexchange services.<sup>30</sup>

---

<sup>26</sup> See, e.g., Bell Atlantic at 3-4; BellSouth at 19-20, 24; USTA at 10-11.

<sup>27</sup> See USTA at 11-12.

<sup>28</sup> See Bell Atlantic at 4; BellSouth at 18.

<sup>29</sup> See BellSouth at 17-18.

<sup>30</sup> See e.g., Bell Atlantic at 4-5; BellSouth at 21-22; Ameritech at 7; SBC Communications at 7.

MCI has addressed most of these issues at pages 9-12 of the attached Reply Comments and incorporates that discussion, which is equally applicable to LEC out-of-region interexchange services, by reference. MCI especially wishes to emphasize that even "pure" price cap regulation does not necessarily curb incentives to cross-subsidize. Whether or not the local carrier's monopoly rates can be raised to absorb additional costs under price cap regulation, the conferring of monopoly-derived benefits on the local carrier's interexchange services at less than their true economic value unfairly subsidizes those services. Thus, cross-subsidization through the conferring of monopoly benefits on the local carrier's interexchange operations can be carried out without raising monopoly rates.

As discussed in the attached Reply Comments, the local carriers can also discriminate in a variety of ways that take advantage of their local monopolies. They are in an especially strong position vis-a-vis multi-state customers using their local exchange services, who can be pressured into taking their out-of-region interexchange services. As AT&T points out, there are also a variety of terminating access pricing strategies that could be designed to appear neutral but would, in fact, favor the local carrier's own out-of-region interexchange services.<sup>31</sup> Most of these discriminatory techniques would not be affected by current equal access requirements or by the interconnection requirements of the 1996 Act, which will not bring about significant local competition for some time in any event. Thus,

---

<sup>31</sup> AT&T at 25, n.45.

local carriers would not have to be concerned about losing access customers in response to their access discrimination, as some of the local carriers claim.<sup>32</sup>

The attached Reply Comments also explain that the misuse of market power to raise rivals' costs injures competition, irrespective of the ability or lack of ability to drive those rivals from the market.<sup>33</sup> As long as the local carriers are in a position to raise the IXCs' costs, they will do so. That the local carriers might pose little danger of "charging excessively high rates" for out-of-region interexchange services,<sup>34</sup> at least in the short run, thus is irrelevant.

This situation is not analogous, as Nynex suggests, to one in which a competitive product, such as steel, happens to be an input for another, such as automobiles.<sup>35</sup> It would be analogous, however, if steel were a monopoly, as in the late Nineteenth Century, and the steel monopoly also produced automobiles. The steel monopoly in that situation would certainly be dominant in the automobile market, notwithstanding the presence of the "big three" auto makers.

---

<sup>32</sup> See BellSouth at 22.

<sup>33</sup> See Ball Memorial Hospital, Inc. v. Mutual Hospital Insurance, Inc., 784 F.2d 1325, 1339 (7th Cir. 1986). The cases cited in note 20 on page 8 of US West's Comments are not to the contrary. In their particular contexts, these cases consider whether a firm can exercise power in the relevant market, and raising rivals' costs constitutes an exercise of market power affecting price and output even if other firms that are equally or more efficient are not driven from the market.

<sup>34</sup> USTA at 8. See also, Pacific Telesis at 7 & n.13

<sup>35</sup> Nynex at 11, n.22.

It also does not matter that, outside their own regions, local carriers are dependent on the incumbent local carrier in each service area for access. Local carriers still have a tremendous advantage over IXCs arising from their bottleneck control and the ability deriving therefrom to inflict cost increases on IXCs. They are not likely to "equalize" such burdens by discriminating against other local carriers providing out-of-region interexchange services, due to their parallel interests, leaving independent IXCs as the only likely targets of such discrimination. Indeed, there appears to be a tacit understanding among the local carriers not to compete with each other in local exchange and access services. They clearly have the same incentive not to jeopardize the current system of inflated access charges. The local carriers' partial dependence on other local carriers thus is largely illusory and is irrelevant to an analysis of their interexchange market power.

C. The Initial Comments Confirm That the Separate Affiliate Requirements Should be Strengthened and That BOC Out-of-Region Interexchange Affiliates Should be Subject to Dominant Carrier Regulation

The local carriers complain that the separate affiliate requirements and dominant carrier regulation are too burdensome and inhibit the development of competition by hobbling them unfairly. They argue that the interexchange and local exchange markets are more competitive than they were when the Competitive Carrier<sup>36</sup> separation requirements were first established and stress that dominant carrier regulation creates inefficiencies by

---

<sup>36</sup> The full citation to the Competitive Carrier proceeding is set out in footnote 5 of MCI's initial comments.

delaying competitive responses to new offerings.<sup>37</sup> USTA also claims that the separation requirements and dominant carrier regulation do nothing to prevent cross-subsidies and discrimination and that other regulations are more than adequate to address such concerns. USTA argues that such regulation of only one category of interexchange service provider creates a competitive imbalance and that the separation requirements inhibit the trend toward one-stop shopping.<sup>38</sup>

The short answer to these arguments is that Pacific Telesis supports separate affiliate requirements for all BOC and LEC interexchange services, within-region and out-of-region. Its primary reason for this position is competitive equity; it wants to ensure that all local carrier interexchange services compete on an even footing. Wherever local carriers compete against each other in interexchange services, one might be providing such service within-region, and the rest will be operating out-of-region. Since the BOCs' in-region services will be subject to such a requirement (albeit considerably more stringent than the Competitive Carrier requirements),<sup>39</sup> its competitors should also.

Sprint also "assure[s] the Commission, first hand, that these [separation] requirements have hardly proven to be 'unduly burdensome.'"<sup>40</sup> In fact, Sprint states, from its own experience, that a local carrier will not be inconvenienced by these

---

<sup>37</sup> See, e.g., BellSouth at 20; Nynex at 12-13; Ameritech at 11-12.

<sup>38</sup> USTA at 8-13.

<sup>39</sup> Pacific Telesis at 8-10.

<sup>40</sup> Sprint at 8.

requirements if it is treating its own interexchange operations the same way it treats others. Moreover, "[t]hese requirements are certainly the best, and perhaps the only, reliable tool that the Commission has at hand for this purpose."

It is true that the interexchange market is more competitive than it was at the time of Competitive Carrier, but the central issue here is the nature of the local exchange and access markets, and, as explained in MCI's and others' initial comments, the local carriers are still overwhelmingly dominant in those markets. It is also true, as USTA claims, that separation requirements and dominant carrier regulation do not necessarily prevent all cross-subsidies and anti-competitive conduct, but they certainly provide a useful first layer of protection by making such activities more difficult and visible.<sup>41</sup> MCI and other parties have also explained in their initial comments the failure of other regulations to provide the necessary safeguards.<sup>42</sup> As for USTA's one-stop shopping point, there is nothing that prevents a local carrier from making its separate affiliate the "retail" one-stop outlet for all services. The separate affiliate could resell local and other services it purchased from the local exchange provider, which would make such local network services available to all other customers on the same terms and conditions.

---

<sup>41</sup> See MCI at 21-22, discussing Competitive Carrier rationale for separate affiliate requirements; Telecommunications Resellers Association at 20-22.

<sup>42</sup> See MCI at 22-25.

The independent LECs maintain, however, that the same analysis does not apply to them, since they either are too small to exercise any leverage in the interexchange market or do not control sufficiently large contiguous service areas to do so, and that the separate affiliate condition for nondominant treatment for interexchange services should be eliminated for LECs, or at least small LECs. They point out that the Commission has applied a lesser degree of regulation to LECs than to the BOCs in other contexts and that the 1996 Act also draws a distinction between small LECs and other local carriers.<sup>43</sup>

Some of these points cut both ways. For example, GTE asserts that it serves primarily suburban and rural areas, but local facilities-based competition is unlikely to develop as rapidly there as in urban areas, thereby prolonging GTE's bottleneck control. SNET states that it is too small -- having only 1.25% of the access lines in the United States<sup>44</sup> -- to disrupt the interexchange market, but MCI demonstrated in its comments on SNET's request for nondominant treatment for its interexchange services that, in fact, the market served by SNET is quite significant.<sup>45</sup>

Moreover, as explained above, SNET has delayed implementation of the DPUC competition policies, thereby postponing the day when it can demonstrate the existence of significant local competition. Thus, to the extent that SNET is

---

<sup>43</sup> Frontier at 6-8; SNET at 16-18; GTE at 7-13.

<sup>44</sup> SNET at 8, n.11.

<sup>45</sup> See MCI Comments cited in n. 15, supra, at 4-5.

representative of the smaller LECs and that "SNET's core telephony markets -- including local exchange service -- are more open to competition than the core markets of most other LECs," as SNET claims,<sup>46</sup> the LECs still possess local bottleneck control that can be used to exert significant leverage in the out-of-region interexchange market and will continue to do so for the foreseeable future.

The independent LECs are correct, however, that the BOCs are capable of much more harm. Accordingly, while MCI has recommended that the Competitive Carrier separation requirements be maintained as a condition for nondominant treatment for all LEC interexchange services, including out-of-region services, it has advocated that those requirements be strengthened and made mandatory for BOC out-of-region interexchange services and that BOC out-of-region affiliates be subject to dominant carrier regulation.<sup>47</sup> MCI supports the proposals of other parties to strengthen the separation rules, at least for the BOCs, by requiring complete physical, operational and administrative separation of the BOC out-of-region affiliates from the local exchange operations, including a prohibition of joint marketing and the sharing of customer proprietary network information and

---

<sup>46</sup> SNET at 5-6. It should be noted that the Common Carrier Bureau's Spring 1996 Common Carrier Competition Report shows that switched local service competition has begun in portions of only seven states -- not including Connecticut. Report No. CC96-9 (released April 10, 1996) at 3-4.

<sup>47</sup> See MCI at 20-26; MCI Comments at 10-17, BOC Out-of-Region proceeding (filed March 13, 1996), incorporated herein by reference.

other confidential information.<sup>48</sup> These strengthened requirements are necessary to restrain the more subtle forms of cross-subsidization and anti-competitive conduct discussed above. See also pages 12-15 of the appended Reply Comments.

MCI would modify its initial position in one respect under one condition -- that the Commission ultimately decides to require mandatory detariffing for all nondominant interexchange carriers, including mass-market services. In that event, MCI has pointed out in its "Phase II" comments in this proceeding that competitors and the public would lose out on some of the benefits of tariffing mass-market services. It would be arbitrary for the Commission to require that nondominant interexchange carriers forgo the benefits of tariffing mass-market services while their dominant competitors -- the local carriers providing out-of-region interexchange services -- retained those benefits. Thus, for both LECs providing unseparated interexchange services and BOCs providing out-of-region interexchange services, mass-market interexchange offerings should be detariffed if nondominant IXCs are required to detariff such offerings. Unseparated LEC and all BOC interexchange offerings to large and medium-sized customers, however, should continue to be subject to all of the current tariffing requirements in any event.

MCI's request for tariffing equality for mass-market services does not in any way reflect a diminished need for dominant carrier regulation for unseparated LEC and all BOC interexchange services. Consistent with the Commission's

---

<sup>48</sup> See Public Utilities Commission of Ohio at 3-4; Telecommunications Resellers Association at 22-24; CompTel at 4-5.

detariffing proposal, local carriers should be required to keep price lists for all detariffed mass-market offerings, and should file such price lists with sufficient cost support for each offering to allow the Commission to assure itself that such mass-market rates conform to price cap or rate-of-return regulation, whichever is applicable to the carrier. The cost support filed with the local carrier price lists should be comparable to that submitted with local carrier tariffs. Only by maintaining dominant carrier regulation of dominant carriers, while preventing the misuse of such regulation as a shield against nondominant competitors, can the Commission ensure a level playing field for all interexchange services.

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

Positions taken by parties on this issue reveal deep-seated concerns and, in some cases, misunderstandings that go to the very heart of the new law and Congressional intent. As MCI noted in its Comments, there is potential conflict between the rate-averaging and rate integration requirements, on one hand, and competition, on the other hand. This conflict must be removed, or at least minimized, if the public interest is to be served.

The Telecommunications Resellers Association correctly states that Congress did not intend, in enacting Section 254(g), "to restructure the entire telecommunications services environment;"<sup>49</sup> rather, it "intended to codify the manner in which the Commission has incorporated geographic rate averaging and rate integration into its current regulatory scheme." *Id.* In

---

<sup>49</sup> Telecommunications Resellers Association at 27.

other words, Congress intended merely to codify existing Commission policy, not expand it.<sup>50</sup>

In the same vein, AT&T states that "[t]he rigid and inflexible application of rate averaging and rate integration requirements" would be injurious to competition.<sup>51</sup> And, as necessary, it urges that the Commission exercise its forbearance authority to assure that the rate averaging and integration "requirements" do not interfere with competition.<sup>52</sup> MCI hopes that such an undertaking will be unnecessary and urges the Commission to recognize that there can be "peaceful coexistence" between these two important policy objectives, such that all consumers will be able to acquire service at affordable rates while, at the same time, carriers will be able to compete effectively in the marketplace.<sup>53</sup>

---

<sup>50</sup> See, also, AT&T at 31-33. ("... [I]t is clear that Congress only intended § 254(g) to codify the Commission's existing policies on rate averaging and rate integration." (Emphasis in original))

<sup>51</sup> AT&T at 28.

<sup>52</sup> Id at 28. See also, Sprint at 14, 25. The 1996 Act expressly directs the Commission to adopt rules providing for rate averaging and rate integration, but it also allows for the Commission to forbear from enforcing them. It seems clear to MCI that, should such rules be found irreconcilable with the national economic policy of competition, the Commission could satisfy the requirements necessary to forbear from enforcing them.

<sup>53</sup> But see, Rural Telephone Coalition at 11, which suggests that increased or added interexchange competition will result in greater deaveraging, and USTA at 6, which states that "market incentives tend to encourage the type of geographic deaveraging prohibited by the 1996 Act." These observations are troubling. As some commenters indicate (e.g., Sprint at 10), the perfect environment for fully averaged rates is one characterized by monopoly, which is precisely the market environment the 1996 Act is intended to cure.

The tension between geographic rate averaging and rate integration in a competitive environment is addressed in numerous comments. As correctly recognized by the General Services Administration, "[r]ate averaging is a form of cross-subsidy" that might work if, in a competitive environment, "all competitors are ubiquitous."<sup>54</sup> However, not all competitors are, or plan to be, ubiquitous,<sup>55</sup> and even those who could be are seeking to escape the requirement.<sup>56</sup>

Furthermore, as several commenters indicate, rate-averaging will have anti-competitive effects if it is imposed without appropriate consideration being given to competitive conditions or circumstances. Thus, BellSouth contends that the Commission should forbear from imposing rate averaging and rate integration requirements "with respect to offerings made in response to

---

<sup>54</sup> General Services Administration at 5. The GSA notes that MCI and Sprint have incurred substantial costs to reach most of the exchanges in the nation through their own facilities.

<sup>55</sup> Cable & Wireless at 1-7. Cable & Wireless argues for less than ubiquity, presumably to avoid serving in low-use/high-cost areas, and it further seeks to maintain deaveraging as between services using its own facilities and those using facilities obtained from others. It cites cost differences as the basis for justifying the latter approach. (*Id.* at 6)

MCI has no quarrel with a carrier's choosing to engage in business on a regional basis or, certainly, to price its services based on cost. The quarrel would arise if MCI were obliged to establish rates on a nationwide basis (in competition with a regional carrier) and average into those rates disparate costs over which it had no control, e.g., LEC access charges.

<sup>56</sup> MFS Communications at 2, 8-10. MFS unabashedly asks that the Commission forbear from applying the rate averaging requirement to carriers that possess less than five percent of the access lines in the interexchange market. The reasons offered in support of its position -- "their customer bases are more modest" and "their service provision is limited to a few select geographic areas" -- are unpersuasive. As MCI indicated in its Comments (at 28), any geographic averaging requirement "should apply to all providers" of service. (Emphasis in original)

competitive conditions in particular geographic markets,"<sup>57</sup> and LDDS WorldCom speaks of a "'special circumstances' test" that would allow the Commission to forbear from applying rate averaging requirements "in situations dictated by competitive necessity."<sup>58</sup> And, the Pennsylvania Office of Consumer Advocate argues for recognition of volume discount plans offered by carriers.<sup>59</sup> MCI concurs with these positions, which implicitly suggest that geographic rate averaging and competition can continue to co-exist as they have in the past.

As noted by MCI in its Comments, varying costs, especially those over which a carrier has no control, such as exchange access costs that eat up nearly half of each interstate, interexchange carrier's revenues, dramatically impact rate averaging. As the America's Carriers Telecommunications Association indicates, "interexchange carriers cannot be made to average their rates if their underlying costs are not also required to be averaged and therefore uniform"<sup>60</sup> -- a position shared by Frontier when it indicates "that the level of access

---

<sup>57</sup> BellSouth at 5.

<sup>58</sup> LDDS WorldCom at 14.

<sup>59</sup> Pennsylvania Office of Consumer Advocate at 7, n.4. See, also, Frontier at 9. ("Nor is there any reason for the Commission to proscribe ... special pricing packages and practices.")

<sup>60</sup> America's Carriers Telecommunication Association at 8. And, as AT&T correctly notes (at 30, n.56), the trend appears to be running in the opposite direction, as the Commission appears inclined toward deaveraging access prices. See, e.g., Memorandum Opinion and Order, NYNEX Tel. Cos. Petition for Waiver, Transition Plan to Preserve Universal Service in a Competitive Environment, 10 FCC Rcd 7445 (1995).