of fair interpretation, statutes will be construed to defeat administrative orders that raise substantial constitutional questions." Bell Atlantic Tel. Cos. v. FCC, 24 F.3d 1441, 1445 (D.C. Cir. 1994); see also, Rust v. Sullivan, 500 U.S. 173, 190-91 (1991). Indeed, where property rights are implicated, a fair reading of the statute must provide a "clear warrant" for the agency's authority to take property. Bell Atlantic, 24 F.3d at 1446. The 1996 Act provides no such warrant and is more naturally read to preclude the Commission from establishing below-cost rates.

(g) A reasonable profit means a positive profit, not just a return on capital. Profit is the excess of the firm's total revenues over the firm's total costs, taking into account all costs, including the cost of capital. The cost of money to purchase capital assets is a necessary component of incremental costs, joint and common costs, and embedded costs. A firm that merely recovers all those costs, including the cost of capital, has not earned a positive profit. Without the potential for a positive profit, investors would have no incentive to risk their capital in building new plants and facilities, and the public interest would suffer because consumers would be deprived of the benefits of such facilities. Hausman Aff. ¶¶ 12-13.

(3) Rate Levels.

(a) LRIC-Based Pricing Methodology. For the reasons given above, the Commission should not set a ceiling on prices for interconnection and unbundling that does not allow the LECs to recover the incremental, joint and common, and embedded costs of their networks, as well as a reasonable profit. It follows that two cost measures on which the Commission has sought comment, LRIC (long-run incremental cost) and TSLRIC (total service long-run incremental cost), cannot appropriately serve as rates for network elements or interconnection. LRIC could serve as a price floor only in the context of voluntary price negotiations or when pricing in response to competition. LRIC cannot be mandated by a state commission or the FCC because it does not allow recovery of total costs.

(i) LRIC. LRIC is the long-run cost of providing a specified additional quantity of a LEC's service or, alternatively, the amount a carrier saves by dropping that incremental quantity of service. LRIC does not account for the fixed or underlying costs of providing the service on the network. These fixed or "lumpy" costs of providing the service are incurred regardless of whether a few customers more or less are served. Thus, a price set at LRIC would not even cover the costs of the particular service and would make no contribution to the joint costs of facilities shared with other services, the common costs of the network as a whole, or embedded costs. Hausman Aff. ¶¶ 10-13.

The Commission has itself recognized that LRIC is an inappropriate standard for mandated prices because such rates "will not recover the total costs of the network." Notice of Proposed Rulemaking, Interconnection Between Local Exchange Carriers and Commercial Mobile Radio Service Providers, CC Docket 95-185, ¶ 48 (released Jan. 11, 1996) ("LEC-CMRS Interconnection Notice"). See also Special Access Interconnection Order, 7 FCC Rcd at 7429 n.291 ("it would not be reasonable to require the LECs to base [expanded interconnection] charges on the direct costs of those services, with no loadings for overhead costs"). If LECs can only charge entrants incremental costs, they must recover the fixed costs elsewhere, such as through increases in retail rates. But because the entrants do not have to bear the fixed costs, they can undercut any retail price increases made by the LECs and take the LECs' customers. This distortion deters entrants from making efficient investments in facilities and deters the LECs from developing new services. Thus, LRIC alone cannot be the basis for legally and economically sound pricing of interconnection or unbundled network elements.

LRIC may be useful as a price floor, however, to prevent anticompetitive or predatory pricing. As competition increases, LECs will need to respond to the prices set by new entrants who have built their networks from scratch, using the latest technology, and are not burdened by the LEC's historical costs. As long as prices are set above LRIC, the LECs will still be able to compete for this business and make a contribution to their embedded costs. Thus, a price floor set at LRIC gives LECs the flexibility to respond to competitive conditions, while still ensuring that the marginal costs of the service in question are covered so that the LEC's prices are not predatory. Hausman Aff. ¶ 13.

(ii) TSLRIC. TSLRIC captures the costs that would be saved by the LEC if it did not provide the entire service in question. Accordingly, TSLRIC may capture the "lumpy" costs of providing a particular service. That is to say, TSLRIC includes service-specific fixed costs (non-volume-sensitive costs), while LRIC typically holds these costs separate from volume-sensitive costs. But if a service uses facilities that support other services, TSLRIC will still not cover joint and common costs or embedded costs, much less provide for a reasonable profit. Hausman Aff. ¶¶ 10-11.

Prices set at TSLRIC would therefore be inconsistent with the Act's requirement that the LECs be permitted to recover their total costs plus a reasonable profit. Prices set at TSLRIC would also distort the LECs' technology decisions. When a LEC can use the same facilities to support several distinct services, economies of scope are realized. Inputs can be shared instead of being installed separately for each service. Shared costs and facilities lower total costs for the firm by lowering the TSLRIC for each individual service that shares the joint facilities. If firms know that they can recover the costs of those shared facilities (which costs, as shown above, are not captured in TSLRIC), then they have incentive to seek efficient, shared technologies. On the other hand, if joint costs are not recovered because prices are constrained to TSLRIC, the firm's incentive is to find technologies with low shared costs but higher incremental costs. Such technologies are less efficient, but if a firm is required to operate under these constraints, they are a rational response if the firm is to recover its costs. Hausman Aff. ¶ 11.

(iii) The MCI and AT&T Models. The ex parte models presented to the Commission that advocate TSLRIC as a rate constraint are unrealistic and incorrect. In particular, the Hatfield model of TSLRIC pricing, submitted on behalf of MCI, would lead to massive under-recovery. As an initial matter, the study assumes that LECs provide services to entrants "in the ways the best available technology allows."[40] But a network is not rebuilt at each point in time to take advantage of improved technology. Instead, it is built bit by bit over time and encompasses multiple generations of technology. Although each investment decision may have been efficient and foresighted when made, the resulting network will not be identical to the one that could be built today if it were reconstructed under the best forward looking technology available.

As the Commission has explained, "where technological developments are reducing the costs of providing service, setting the price of discrete services equal to the forward-looking LRIC of each service is not likely to recover the historical, embedded costs of the network."[41] The Hatfield study wrongly suggests that "existing infrastructure . . . is irrelevant" and that the embedded costs of such infrastructure should not be recovered. Firms have

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[40]Hatfield Assocs., Inc., The Cost of Basic Network Elements: Theory, Modeling and Policy Implications at 16 (Mar. 29, 1996) ("Hatfield study")

[41]Notice of Proposed Rulemaking, Interconnection Between Local Exchange Carriers and Commercial Mobile Radio Service Providers, CC Docket No. 95-185, FCC No. 95-505, ¶ 48 (released Jan. 11, 1996).

incurred substantial costs in building existing infrastructure and should not be saddled with ex-post regulatory revisions that bar prices that recover those legitimate costs.

A rule that always reduces rates to the level achievable under the latest technology, as the Hatfield study recommends, will provide firms with strong incentives to underinvest and thereby cause losses in productive efficiency. Hausman Aff. ¶¶ 11-12. It will also be confiscatory and will produce an uncompensated taking of LECs' property. This is particularly important for small and mid-size companies that are still regulated under a rate-of-return regime. Those costs cannot suddenly and simply be ignored.

The Hatfield study acknowledges that its estimate of the total economic cost of unbundled network elements amounts to only 44% of the LECs' existing revenue requirements (at 35). The study furthermore concedes that the embedded costs of past investments not captured by TSLRIC amount to over $17 billion -- at least 20% of current revenue requirements -- and acknowledges that the model does not capture all of the LECs' actual overhead expenses (at 36, 43). These gaps indicate that TSLRIC-based prices will fail to capture anything close to total costs. The study glibly tries to explain away the gap with the unsupported assertion that the LECs are inefficient and with nonspecific collateral attacks on the Commission's policies and the past decisions of more than 50 regulatory agencies in thousands of proceedings. Such vague, after-the-fact attacks supply no basis for preventing the LECs from recovering the embedded costs and overhead expenses of operating their networks.[42]

AT&T's proposal has similar flaws. AT&T acknowledges that "TSLRIC pricing of services that share fixed facilities may, under some circumstances, result in large-scale under-recovery of facilities costs." AT&T Ex Parte submission at 50 (FCC Mar. 21, 1996). AT&T accordingly proposes using the TSLRIC of adding an element or facility to the network instead of a service. Id. at 47-50. To the extent an element or facility supports multiple services, TSLRIC of that element or facility may capture more joint costs than TSLRIC calculated on a service basis. Nonetheless, AT&T does not dispute that its version of TSLRIC still leads to underrecovery of common and historical costs. Id. at 50.

In short, neither LRIC nor TSLRIC can provide an adequate level for prices set by the Commission. Rather, LRIC can serve only as a floor for rational, cost-based pricing. LRIC cannot be mandated. Even using LRIC as a floor, moreover, the Commission should not itself attempt to quantify LRIC for interconnection and unbundled network elements. Trying to establish LRIC for services across LECs based on a single cost study would fail to capture

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[42]The Supreme Court has traditionally held that a utility should be compensated "for all prudent investments at their actual cost when made (their "historical" cost) irrespective of whether individual investments are deemed necessary or beneficial in hindsight"). Duquesne Light Co. v. Barasch, 488 U.S. at 309; see also Missouri ex rel. Southwestern Bell Tel. Co. v. Public Serv. Comm'n, 262 U.S. 276, 291 (1923). See also Daniel F. Spulber, Regulation and Markets 610 (1989) ("Perhaps the most important aspect of the regulatory bargain is the ability of regulators, customers, and the regulated firm to make commitments both to pricing policies and to irreversible investments").

differences in cost structures among firms or geographic regions and would lead to a contentious battle over which study to use. Such a straightjacket would be particularly hard on rural LECs and, in some instances, LECs eligible for the two percent waiver process under Section 251(f). Their costs vary markedly and are likely to be substantially higher. Thus, a ceiling approach is inappropriate for these LECs.

(b) Rate Proxies.

Given the administrative difficulty of establishing rate guidelines based on formulas, the Commission has asked for comment on the alternative of setting rates by proxy. Proxies may, indeed, be a feasible way to establish presumptively valid rates for some unbundled elements. But the Commission needs to proceed with great care here in defining the elements and establishing the proxies to avoid arbitrage by interexchange carriers seeking to avoid paying access charges prior to general access charge reform. It is important, moreover, that any proxies not be established as rate ceilings; at most, they can serve to indicate levels below which rates will be presumptively valid and above which they must be further justified. Placing a rigid, proxy-based cap on rates will lead to undercompensation in some instances, depriving LECs of their legitimate right to cost recovery. It will also deprive state commissions of the regulatory flexibility guaranteed to them by the new Act and by Section 2(b) of the 1934 Act, which was not amended by Congress and which deprives the Commission of jurisdiction to set rates for intrastate services.

Paragraph 139 of the NPRM suggests using interstate access charges, less CCLC and RIC, to measure certain rates. But the Commission has misconstrued the unbundling process if it believes that interstate switched access is an adequate proxy for all unbundled elements priced under Section 252(d)(1). In particular, unbundled local switching (i.e., the port concept described above) includes different functionalities from the switching component of interstate switched access. As a proxy for unbundled local switching, the Commission would have to combine a number of elements from existing state and federal tariffs, with appropriate adjustments.

Switched access charges could be a proxy, if at all, only for the transport and termination of traffic under Section 252(d)(2). As explained below (pp. 58-66, infra), interexchange carriers should not, must not, be permitted to buy network unbundled elements as a substitute for access. Otherwise, interexchange carriers will have a strong incentive to avoid access charges by buying unbundled network elements and reconstructing access, particularly if both CCLC and RIC are excluded from the proxies for those unbundled elements.

CCLC and RIC reflect genuine costs incurred by LECs. Currently, these charges are born by interexchange carriers in the switched access charges they pay to LECs. If those charges are excluded from the rates paid by new entrants for unbundled elements, and the unbundled elements could be reconstructed to replace access, then a significant danger of arbitrage would be created.

To avoid such arbitrage and treat all providers equally, the Commission should eventually move to a system in which all interconnectors -- IXCs, CMRS providers, CLECs, ESPs, etc. -- pay common prices for common services. But such a result will require a completion of access charge reform and a new model for ensuring universal service. Ideally, the Commission would complete those reforms at the same time that it completes this rulemaking. Since that appears impractical, however, the Commission has a fundamental choice to make in the meanwhile. It must either include CCLC and RIC in the prices paid by new entrants or it must rigidly police the boundaries between interexchange access and unbundled network elements. If it eschews the former but neglects the latter, then the LECs will be left with a huge shortfall as IXCs game the system to avoid paying access charges. Moreover, the IXCs, having gained their advantage through arbitrage, will then have little incentive to cooperate with access charge reform and universal service reform. What the Commission should do, in the meanwhile, is restrict the use of unbundled elements to the loops and ports and various forms of dedicated transport needed to provide local service, not including anything corresponding to switched access for interexchange carriers. Switched access should be a proxy only for reciprocal compensation for the transport and termination of local traffic under Section 252(d)(2). And even that proxy should include both CCLC and RIC until the Commission has completed its work on access reform and universal service.

With respect to true unbundled elements, the special access tariff for a voice grade local channel may, in at least some instances, provide a potentially useful proxy for an unbundled local loop.[43] An unbundled loop does not terminate at the LEC switch. Rather, it is provisioned and maintained in a manner that is more analogous to a special access dedicated line than to a regular switched exchange line. As far as the LEC's network is concerned, this is a non-switched facility. In appropriate circumstances, pricing of dedicated, nonswitched facilities at the current special access tariff has a number of advantages, such as preventing tariff shopping and permitting competitors to choose loops other than 2 wire voice grade channels.

Again, however, any such proxies have to be handled with care. Local loop costs will vary widely from area to area depending on population density and other factors. Indeed, some rural areas have monthly local loop costs approaching $100.[44] A grave threat

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[43]Alternatively, the Commission has acknowledged (NPRM ¶ 141) that CCLC and SLC together recover about 25% of local loop costs. Proxies for unbundled loops could therefore be based on a multiple of the CCLC plus the SLC.

[44]Comments of the United States Telephone Association, Federal-State Joint Board on Universal Service, CC Docket No. 96-45 (filed Apr. 12, 1996).

to universal service would be posed if the Commission established too low or too rigid a proxy for local loop costs.[45]

The Commission must also recognize that some unbundled elements (such as databases) have no counterparts in access charges. Here, the Commission should either eschew proxies altogether or, again, look to existing state and federal tariffs for appropriate analogues for these elements.

Special pricing rules are appropriate for rural LECs and those LECs that are eligible for the waiver process specified under Section 251(f). For some of these LECs it would be especially logical and expedient to use current access charges, including flat-rated elements, to derive interim prices for interconnection and unbundled elements where possible. This would serve several purposes. First, interconnection arrangements could be quickly negotiated since existing prices (i.e., access charges) would be in place. Small and mid-size incumbent LECs could otherwise be burdened with producing cost studies that could bog down the

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[45]The September 1995 Benchmark Cost Model (BCM) submitted to the Commission (for CC Docket No. 80-286) by MCI, NYNEX, Sprint and U.S. West does not provide an appropriate proxy for local loop costs. The BCM model was designed only to identify "high cost areas," not to provide an accurate estimate of the costs to serve each Census Block Group included in the model. The Hatfield version of that model is even more inappropriate because it is based on an idealized, optimal network that simply doesn't exist. It does not capture embedded costs and therefore has nothing to do with the real costs of LEC networks. The BCM model does, however, reinforce the fact that costs will differ substantially, census group by census group, depending on population densities.

interconnection negotiation process.[46] Second, migration in interconnection pricing would automatically track with changes in the access pricing regime. Finally, the cost recovery contemplated by the 1996 Act is largely incorporated within current access prices.

(c) Other Issues.

USTA has already explained in detail why LECs should be permitted to include their embedded costs in the total costs to be recovered in charges for interconnection and unbundled elements. See supra pp. 40-43. The Commission seeks comment on the "empirical magnitude" of the embedded costs that would not be recouped if a solely forward-looking pricing methodology were used. A variety of estimates have been placed on these costs, ranging from $13 billion to as much as $18.4 billion. See, e.g., Mike Mills, Phone Firms Seek Higher Local Rates, Washington Post, A1 (May 7, 1996) ($13 billion); Hatfield study at 36 ($17.65 billion); AT&T, MCI, LDDS, WorldCom, Comtel, Interconnection, Unbundling and Access: Creating FullService Competition Under the Telecommunications Act of 1996 at 3 (Mar. 1996) ($18.4 billion).

Whatever the actual amount, these are perfectly legitimate embedded costs. They have been properly incurred pursuant to regulatory oversight, and regulators must permit them to be

[46]Administrative convenience looms large for small and mid-size LECs since the volumes of interconnecting traffic and the demand for unbundled elements from such LECs is likely to be low, particularly at first, as new entrants target the larger and more lucrative urban areas. However, the option of producing cost studies should be left to their discretion.

recouped. Indeed, if the Commission does not permit the LECs to recover a proportionate share of such amounts in charges for interconnection and unbundling, the embedded costs attributable to those services will have to be recouped elsewhere. This would throw large amounts of costs onto the states and create pressure to raise local rates to permit full cost recovery by the LECs.

The Commission would thus place itself in an extremely vulnerable legal and political position if it does not permit the recovery of embedded costs under Sections 251 and 252. After supplanting the states' authority to determine just and reasonable rates under those sections, the Commission would then set rates that force the states to make up the shortfall elsewhere. If anything, those who purchase interconnection and unbundled access from the incumbent providers of last resort should make a contribution to universal service (along with paying the total costs of what they are buying), see § 254(b)(4); such carriers certainly should not themselves obtain a subsidy (by paying less than total costs) which detracts from universal service by forcing an increase in local rates.

(4) Rate structures.

Within the rate-setting guidelines established by the Commission, the particular structure of rates should be left to private negotiation and state review. The Commission should not prescribe restrictive rules narrowly specifying the structure of rates for particular network elements. Among other things, such rules might interfere with the ability of parties to tailor interconnection packages to particular entrants' needs. As a general principle, the Commission's proposal that costs be recovered in the manner in which they are incurred (¶ 150) is sound. Shared facilities (such as unbundled elements and transport and termination of calls) are more reasonably priced on a usage-sensitive basis, whereas dedicated facilities (such as interconnection and dedicated transport) will be priced at a flat monthly rate. The Commission should not go beyond establishing general presumptions based on those principles.[47]

(5) Discrimination.

Sections 251(c)(2) and 252(d)(1) prohibit LECs from providing interconnection and unbundling on discriminatory terms and conditions. These provisions should be read to prevent only "unreasonable discrimination." Differences in the treatment of different carriers will sometimes be dictated by different circumstances. Indeed, treating unlike carriers alike could itself be said to be discriminatory. The word "discrimination," standing alone, implies some standard of reasonable differences in measuring the treatment of different companies.[48]

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[47]Currently, some usage sensitive charges (notably CCLC) are designed to cover a portion of NTS local loop costs. As already discussed, the Commission cannot eliminate such charges until it engages in comprehensive access charge reform in keeping with whatever framework for universal service it establishes.

[48]See, e.g., Black's Law Dictionary 553 (4th ed. 1968) (emphasis added) (defining "discrimination," with reference to common carriers, as "[a] carrier's failure to treat all alike under substantially similar circumstances").

There is no reason to believe that Congress intended to depart from well-established principles under the 1934 Act making unlawful only unjust or unreasonable discrimination. Thus, for example, the Commission's regulations implementing the nondiscrimination requirement should not prevent differences in terms such as volume discounts.[49] Such discounts must, of course, be offered on nondiscriminatory terms to all interconnecting entrants that are similarly situated with respect to their volume demands. As the Commission has frequently recognized elsewhere, volume discounts benefit consumers so long as the terms are generally available to all competing entrants.

(6) <u>Relationship to Existing State Regulation and Agreements</u>.

Section 251(d)(3) expressly bars the Commission from supplanting state regulations that are consistent with the Act's requirements. That provision makes clear that, while the Commission has authority to implement general guidelines, the specific details of interconnection and network element pricing must be left to state discretion. The Commission should interpret Section 251(d)(3) as a clear limitation on intrusion by the Commission into state policies or rate determinations.

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[49]Different terms could also be driven, for example, by the different costs of serving urban and rural interconnectors. Or, they might be driven by the necessity to respond to competitive pressures for a particular service in a particular area.

e. <u>IX, CMRS, and Non-Competing Neighboring LECS</u>

(1) <u>Interexchange Services</u>.

The <u>NPRM</u> is correct that interexchange carriers are "telecommunications carriers" under the 1996 Act, and as such, are clearly entitled to seek interconnection and access to unbundled network elements under Sections 251(c)(2) and (c)(3), respectively. The <u>NPRM</u> is also correct, however, that Section 251 imposes certain limits on the purposes for which requesting telecommunications carriers, including interexchange carriers, may request interconnection or access to unbundled network elements under the Act. <u>See</u> <u>NPRM</u> ¶ 160.

Specifically, in the months leading up to the release of the <u>NPRM</u>, the long distance industry has claimed that the language of Section 251 permits IXCs to circumvent the Commission's present access charge regime, either directly under the interconnection requirement of subsection (c)(2), or indirectly by claiming that subsection (c)(3) allows them to "reconstruct" access by piecing together network elements. IXCs further claim that these elements should be priced at incremental cost. None of these positions is sound, and they would have disastrous public interest consequences. Moreover, USTA has shown above that pricing of unbundled elements cannot be mandated at incremental cost.

First, the interexchange carriers claim that because they are "telecommunications carriers," Section 251(c)(2)'s interconnection requirement applies to the incumbent LEC's provision of interexchange access services. Thus, the IXCs claim that they may bypass the Commission's current access charge requirements and negotiate new access rates that are subject only to state review.

This position simply lacks any sound legal or policy foundation. Section 251(c) plainly contemplates the existence of an emerging facilities-based competitor seeking to offer its own local exchange or exchange access services. Thus, Section 251(c)(2) imposes an obligation upon incumbent LECs to provide requesting carriers with interconnection -- i.e., a physical link between the incumbent LEC network facilities and equipment and the competing provider's network facilities and equipment -- where the request is for "the transmission and routing of telephone exchange service and exchange access."

As the NPRM recognizes, "telephone exchange service" and "exchange access" are both defined terms under the 1934 or the 1996 Acts,[50] and neither term encompasses the provision of interexchange service. Indeed, the definition of "exchange access" calls for the "offering" of access to telephone exchange services or facilities. See 1996 Act § 3(16) (emphasis added). By contrast, as the NPRM observes, an interexchange carrier requesting interconnection to originate or terminate a toll call would be receiving access services, not offering them. Thus, the NPRM (at

[50]"Telephone exchange service" is defined in the 1934 Act to mean "service within a telephone exchange, or within a connected system of telephone exchanges within the same exchange area operated to furnish to subscribers intercommunicating service of the character ordinarily furnished by a single exchange," or "comparable service[s]." 1934 Act § 153(r). "Exchange access" is defined to mean "the offering of access to telephone exchange services or facilities for the purpose of the origination or termination of telephone toll services." 1996 Act § 3(16).

¶ 161) is correct in its conclusion that the obligation to provide interconnection under subsection (c)(2) does not apply to telecommunications carriers requesting such interconnection for the purpose of originating or terminating interexchange traffic.

The correctness of this conclusion is buttressed by other Sections of the Act and by sound public policy. In Section 251(i), for example, Congress expressly mandated that nothing in Section 251 "shall be construed to limit or otherwise affect the Commission's authority under Section 201," i.e., the jurisdictional basis on which interexchange carriers have long been entitled to interconnect for the purpose of originating and terminating interexchange traffic. Congress would not have acted to expressly preserve Commission jurisdiction over interstate access charges if, as the IXCs claim, Section 251 transfers regulation of access charges from the Commission to the states. In addition, the Commission's conclusion is also consistent with Section 251(g), which requires local carriers to continue to provide exchange access service to interexchange carriers under the Commission's existing rules, including those governing "receipt of compensation," until such rules are expressly superseded. This provision is further evidence that Section 251 does not automatically displace the Commission's access charge regime.[51]

[51]It is also widely acknowledged that access charge pricing has profound implications for universal service. Had Congress truly intended to direct changes to the access charge regime within the six months mandated for implementation of Section 251, it would not have granted the Joint Board created under Section 254 one year to make recommendations to the Commission with respect to universal service.

As a fallback to their position on access charges under subsection (c)(2), the IXCs have also claimed that Section 251(c)(3) permits long distance providers with no local exchange facilities of their own to buy network elements from the incumbent LEC and to combine them solely to provide access to themselves, without any requirement of offering local exchange or exchange access competition. This interpretation of the Act would once again allow them to circumvent the Commission's access charge regime.

The 1996 Act does not allow the interexchange carriers to accomplish indirectly through subsection (c)(3) what they cannot accomplish directly under subsection (c)(2). While it is true that Section 251(c)(3) allows requesting carriers access to unbundled network elements for the provision of a "telecommunications service," it does not follow that IXCs may request access to unbundled network elements _solely_ for purposes of originating and terminating interexchange toll traffic without also intending to provide local exchange and exchange access services.[52]

The reason is that subsections (c)(2) and (c)(3), which define the duties of incumbent LECs in negotiations with interconnectors, only make sense if they are interpreted as co-extensive obligations. Under Section 251(c)(3), an incumbent LEC must provide nondiscriminatory "access" to an unbundled network element

[52] Moreover, the IXC must be a legitimate local exchange provider. It cannot simply set up a local exchange affiliate whose exclusive (or almost exclusive) function is to provide access to the IXC.

at any technically feasible "point." The only way a carrier can obtain "access" to a "point" is by interconnecting its own facilities to those of the incumbent, and under subsection (c)(2), an interconnecting carrier must be using its facilities to compete in the provision of local telephone or exchange access service -- not interexchange service. The language of Section 251(c)(3) expressly contemplates an emerging facilities-based carrier that intends to offer its own local exchange and exchange access service by physically interconnecting its facilities with those of the incumbent LEC.[53]

An incumbent LEC is not obligated to provide access to unbundled elements solely to allow IXCs to originate and terminate interexchange traffic. As the __NPRM__ suggests, this view is fully consistent with the Act's definition of "network element" as a facility or function, as opposed to a jurisdictionally distinct

[53]The legislative history confirms that subsections (c)(2) and (c)(3) should be read together to permit new entrants to connect their local exchange network facilities with those of the incumbent, and to supplement their own facilities with access to incumbent network elements. The Senate, for example, noted that the provision requiring access to "network elements" clarifies the "different types of interconnection" that are required. S. Rep. No. 23 at 19. Furthermore, the Joint Explanatory Statement observes that "it is unlikely that competitors will have a fully redundant network in place when they initially offer local service, because the investment necessary is so significant. __Some__ facilities and capabilities (__e.g.__, central office switching) will likely need to be obtained from the incumbent local exchange carrier as network elements pursuant to new section 251." Joint Explanatory Statement at 148 (emphasis added). Given this legislative history, the most reasonable reading of Section 251(c)(3) is that the provision allows new entrants to combine one or more network elements obtained from the local exchange incumbents with some of their own local exchange facilities to provide a competing facilities-based service.

"service."[54] Furthermore, as the NPRM acknowledges, a contrary reading of Section 251(c)(3) would re-introduce all of the adverse legal and policy consequences that would flow from interpreting the Act to allow IXCs to bypass access charges under subsection (c)(2). Such an interpretation simply cannot be squared with Congressional intent or the pro-competitive goals of the 1996 Act.

Finally, the Commission seeks comment on whether a carrier may request cost-based interconnection under section 251(c)(2) solely for the purpose of offering competitive access services, or whether the requesting carrier must also offer telephone exchange services. Section 251(c)(2)(A) is clear on this point. It states that a carrier requesting interconnection must use that interconnection "for the transmission and routing of telephone exchange service and exchange access." The word "and" is used, not "or." Thus, Congress's choice of words plainly indicates that requesting carriers must provide both exchange service and exchange access, not just one or the other.

A requirement that the requesting carrier provide both kinds of services is in keeping with the Act's purpose of encouraging full, facilities-based local competition. It also prevents an interexchange carrier from evading the Commission's access charge regime by forming (or buying) an affiliate for the sole purpose of

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[54]NPRM at ¶ 164. Thus, an incumbent LEC's statutory obligation to provide access to network elements would extend only to providing exclusive access to an entire loop, in which case the IXC could not, as a practical matter, purchase such access without having won over the local customer associated with the loop and providing that telephone exchange service to that customer. Id.

providing exchange access to itself. As the Commission recognizes, NPRM ¶ 162, a contrary interpretation of the Act would permit interexchange carriers to accomplish indirectly that which the Act bars them from doing directly: i.e., obtaining interconnection under section 251(c)(2) solely for the purpose of receiving exchange access and thereby evading the current access charge regime.[55]

Because access reform is not mandated by the 1996 Act, the Commission is not bound by the pricing standards set forth in Section 251(d). Thus, in designing a transition from the present subsidy-based system, the Commission can adopt its own transition mechanisms, taking into account universal service and other goals. However, the fact that neither Section 251(c)(2) nor 251(c)(3) requires the Commission to circumvent the present access charge scheme does not mean that access charge reform is unimportant or that access charges bear no relationship to the pricing standards found in Section 251. To the contrary, the Section 251 pricing

[55]Competitive access providers ("CAPs") will not be harmed by an interpretation that restricts interconnection under Section 251(c)(2) to full-service local entrants. To the extent that CAPs wish to provide only exchange access service, they are fully protected by the Commission's existing Expanded Interconnection Rules. To the extent that they want to combine exchange and exchange access service, they can seek interconnection under Section 251(c)(2). If the Commission nonetheless decides to include all CAPs within a uniform interconnection regime under Section 251(c)(2), it should adopt strict regulations excluding interexchange carriers or their affiliates from seeking interconnection under Section 251(c)(2) solely for the purpose of providing exchange access. Absence of such a safeguard would permit interexchange carriers to make an end-run around the Act and access regulations, and would fundamentally undermine the Act's competitive goals.

issues are crucial because even though Section 251(c)(2) or (c)(3) do not apply to interstate access, the possibilities for arbitrage are still tremendous. It may prove to be difficult to police the abuse of the unbundled rate elements by the interexchange and other competitive carriers. The solution is access charge reform and movement towards the goal of pricing the local loop so that, in the end, it is irrelevant who connects to it. USTA urges the Commission to commence the process of access reform as soon as possible.

(2) CMRS.

There can be no genuine question that CMRS requests for interconnection fall within the scope of Section 251(c)(2).[56] CMRS providers are "requesting telecommunications providers" that seek interconnection from incumbent LECs for the purpose of providing "telephone exchange service and exchange access" within the LECs' service area. As the Commission has correctly noted, see NPRM ¶ 168, CMRS services are within the definition of "telecommunication services" in Section 153(46) of the 1934 Act, and CMRS providers are within the definition of "telecommunications carrier[s]" in Section 153(44). CMRS providers also offer "telephone exchange service" as defined in Section 153(47).[57] Thus,

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[56]See Comments of the United States Telephone Association, Interconnection Between Local Exchange Carriers and Commercial Mobile Radio Service Providers, CC Dkt. No. 95-185 (filed Mar. 4, 1994) ("USTA Comments").

[57]The one possible exception is for one-way paging. Section 153(47) defines "telephone exchange service" in terms of an "intercommunicating service of the character ordinarily furnished by a single exchange." One-way paging, unlike other CMRS services, is not intercommunicating.

CMRS-LEC interconnection agreements fall within the coverage of Section 251(c)(2).[58]

The suggestion that Section 332(c) somehow trumps section 251 for LEC-CMRS interconnection has been refuted elsewhere.[59] USTA notes here only that, even if it were possible for the Commission to establish a separate interconnection regime for CMRS under Section 332(c), it would be inadvisable to do so. The Commission should not be playing favorites among telecommunications carriers based on the technology they use. Interconnection charges for CMRS that are lower than for wireline technologies would constitute a straightforward subsidy to CMRS, which would distort market choices by producers and consumers alike. Hausman Aff. ¶¶ 19-20. That would create the exact opposite of the level playing field for local exchange competition that Congress intended to create.

(3) Non-competing Neighboring LECs.

Agreements between incumbent LECS and non-competing neighboring LECs fail to satisfy the plain language of Section 251(c) because they are not agreements between an "incumbent LEC" and a "requesting telecommunication carrier" for the purpose of providing "telephone exchange service and exchange access" in the local service area of the other party. Rather, the agreements

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[58]Because such interconnection arrangements govern the terms for the "transport and termination of telecommunications" between a LEC and a CMRS provider in the LEC's local service area, they also fit within Section 251(b)(5).

[59]See Letter from Michael K. Kellogg to William F. Caton, Ex Parte Communication, CC Dkt. No. 95-185 (Mar. 13, 1996); Letter from Michael K. Kellogg to William F. Caton, Ex Parte Communication, CC Dkt. No. 95-185 (Feb. 26, 1996).