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FEDERAL COMMUNICATIONS COMMISSION
Washington, D.C. 20554

MAY 24 1996

FEDERAL COMMUNICATIONS COMMISSION
OFFICE OF SECRETARY

In the Matter of)
)
Policy and Rules Concerning the)
Interstate, Interexchange Marketplace) CC Docket No. 96-61
)
Implementation of Section 254(g) of the)
Communications Act of 1934, as amended)

To: The Commission

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REPLY COMMENTS OF CONSUMER ELECTRONICS RETAILERS COALITION

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SUMMARY

From the American consumers' perspective, the antibundling rule has been an unqualified success, and one of the Commission's most successful policy initiatives. It has permitted CPE users to obtain innovative, state-of-the-art equipment from a large number of suppliers at reasonable, market-driven prices. This fact alone speaks for retention, not elimination, of the rule.

Supporters of the proposal to amend the rule offer only one alleged benefit: allowing carriers to offer packages of CPE and service to customers. Carriers, however, can already offer such "one-stop-shopping" under the current rule. Thus, "packaging" CPE and service is not the issue; rather, the issue is whether carriers should be permitted to require customers to purchase a package, and whether carriers should be permitted to offer "discounts" on CPE by subsidizing the cost of the CPE with revenues from service.

Even the majority of the supporters of the amendment acknowledge the potential for abuse created by allowing such activity. They therefore offer suggestions for attempting to prevent such abuse. Rather than eliminating a successful rule and then trying to prevent the potential for abuse caused by such elimination, the Commission should simply retain the rule in its present form.

The reasons against amending the rule are compelling:

- it would decrease consumer choice by forcing consumers to choose among carrier-determined

service/CPE packages rather than being able to purchase the combination of CPE and service that bests meets their needs at a price they are willing to pay;

- it would allow the development of proprietary CPE making it difficult for customers to switch carriers;
- it would diminish the vitality of the CPE marketplace; and
- it is fundamentally at odds with the Telecommunications Act of 1996.

If the Commission does amend the rule to allow bundling, Section 202(a) of the Communications Act mandates that the Commission require carriers also to offer separately, unbundled services on a nondiscriminatory basis. Carriers cannot be permitted to discriminate against those customers who elect not to use the carrier-provided CPE. Carriers also must be required to disclose all interface specifications using existing industry guidelines and procedures.

The record in this proceeding does not justify amendment of the rule. Given that fact and the radical regulatory changes occurring in the telecommunications industry today, the Commission should defer consideration of any amendment of the antibundling rule at this time.

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To: The Commission

REPLY COMMENTS

The Consumer Electronics Retailers Coalition (the "Coalition"),^{1/} hereby files Reply Comments on the Commission's Notice of Proposed Rulemaking (NPRM) in the captioned proceeding.^{2/}

I. THE COMMISSION SHOULD NOT AMEND § 64.702(e) TO ALLOW NONDOMINANT INTEREXCHANGE CARRIERS TO BUNDLE CPE WITH INTERSTATE, INTEREXCHANGE SERVICES

A. Introduction

In its Comments, the Coalition explained why Section 64.702(e) of its Rules -- the "antibundling rule" -- should not be amended to allow nondominant interexchange carriers to bundle CPE with interstate, interexchange services. Comments

^{1/} The members of the Coalition are major retailers of consumer electronics products in the United States, and their trade associations. They include Best Buy, Circuit City, Dayton Hudson, Montgomery Ward, Sears, Tandy, the International Mass Retail Association, the North American Retail Dealers Association, and the National Retail Federation.

^{2/} NPRM released March 25, 1996, FCC 96-123.

filed by other parties underscore why the rule should not be amended.

The comments demonstrate that from the consumer's perspective, the antibundling rule has been an unqualified success, and one of the Commission's most successful policy initiatives.^{3/} ITAA, for example, explains that the rule has allowed its member companies to obtain "innovative, state-of-the-art equipment from a large number of suppliers at reasonable, market-driven prices."^{4/}

Some proponents of bundling argue that the antibundling rule should be repealed precisely because of its success in encouraging a competitive CPE marketplace.^{5/} The fact that the rule has helped to create the competitive CPE marketplace that the Commission intended, however, is a reason to retain the rule, not to repeal it.^{6/} As shown in the Coalition's Comments and herein, repeal of the rule would lead to a reduction in CPE competition, turning back the clock to the period when a few suppliers provided CPE to carriers and there was little consumer choice as to CPE features, functions or price.

^{3/} Comments of the Information Technology Association of America ("ITAA") at 3; Comments of Independent Data Communications Manufacturers Association ("IDCMA") at 2; Comments of MCI Telecommunications Corporation at 22.

^{4/} ITAA at 2.

^{5/} See, e.g., Comments of Excel Telecommunications, Inc. at 5.

^{6/} See ITAA at 3; IDCMA at 12.

Supporters of the Commission's proposal offer only one alleged benefit from repeal of the rule: it would allow carriers to offer packages of CPE and service to customers. As the Coalition and others showed, however, such "one-stop shopping" is already both permitted and existing under the current rule. Therefore, no amendment of the rule is necessary to achieve this benefit.

Even supporters of the proposed amendment recognize the dangers inherent in permitting bundling, and offer suggestions for attempting to prevent the occurrence of abuse should bundling be permitted. Rather than eliminate a highly successful rule and trying to prevent abuse resulting from such elimination, the Commission should simply retain the rule in its present form.

B. The Commission's Focus On The Potential For Antitrust Violations Is Misplaced

The justification proffered by the Commission for amendment of the rule is that the potential for anticompetitive activity or "tying" is not as great now as it was at the time of adoption of the rule.²¹ The Commission's focus on the precise legal definition of "tying" and whether the rule is necessary to prevent antitrust violations is misplaced. As the Coalition and others demonstrated, that was not the sole reason, or even the primary reason, for the

²¹ NPRM 99 87-88.

adoption of the rule, and it is not reason enough for its repeal.^{8/}

The Coalition agrees with ACTA that the Commission's analysis cannot end with whether there is a potential for unlawful tying.^{9/} Rather, regardless of whether certain behavior passes muster under the antitrust laws, the Commission must also determine whether it is in the public interest.^{10/} As shown in the Coalition's Comments and herein, bundling reduces consumer choice and is contrary to the public interest.

C. Carriers Today Can Offer "One-Stop Shopping" Consistent With The Antibundling Rule

Supporters of the Commission's proposal argue that repeal of the antibundling rule is necessary because carriers must have the ability to offer packages of CPE and service in order to provide consumers with what they want. For instance, API contends that bundling is necessary because

^{8/} See Comments of the Coalition at 3-6; IDCMA at 3-4.

^{9/} Comments of America's Carriers Telecommunications Association ("ACTA") at 17.

^{10/} Even if an antitrust analysis were sufficient grounds for repeal of the rule, the Commission has not engaged in such an analysis. It simply proclaims that the risk of anticompetitive activity has been reduced because "nondominant" firms lack market power. This is not enough. Rather, "the Commission must conduct a fact-specific assessment of the realities of the marketplace" since "[f]irms lacking market power have nonetheless been found to have the ability to engage in tying." IDCMA at 34. If the Commission is going to justify its action on antitrust grounds, then it must perform a true antitrust analysis, which it has not done.

"constraints on a carrier's ability to offer both equipment and service impedes the ability to obtain an integrated telecommunications package."^{11/} GTE supports the proposal because it allows "one-stop shopping."^{12/} Sprint believes that repeal of the rule is warranted because "many consumers seek to reduce their transaction costs by requesting that Sprint provide both the communications services and equipment in a bundled package."^{13/}

But, as shown by the Coalition and others, such "packaging" is permitted under the rule as it stands today. US WEST explains that the rule does not interfere with the ability of any carrier, dominant or nondominant, to market packages of services including CPE and basic transmission service.^{14/} Carriers can (and do) offer one-stop shopping under the present rule, so long as the charges for each are separately stated and the equipment is not subsidized from charges for service.^{15/} Thus, the argument that repeal of the rule is necessary to "reduce transaction costs" is simply wrong. As ITAA explains, the antibundling rule disadvantages

^{11/} Comments of the American Petroleum Institute ("API") at 15.

^{12/} Comments of GTE Service Corporation at 10.

^{13/} Comments of Sprint Corporation at 28. See also Comments of the Telecommunications Resellers Association ("TRA") at 40-41; Comments of SBC Communications Inc. at 7.

^{14/} US WEST, Inc. Comments at 7.

^{15/} Coalition at 8-9. See also IDCMA at 12.

no one since it does not deny consumers the benefits of one-stop shopping, nor does it preclude a carrier from providing CPE.^{16/}

The only incentive for elimination of the rule is the opportunity to offer "discounted" or "free" CPE, which, in reality, is subsidized by higher service rates. This desire to subsidize CPE is implied, though never expressly stated, by those who support modification of the rule. For example, Excel argues that only by eliminating the rule would carriers be able to offer "attractive" service/equipment packages to customers.^{17/} AT&T similarly argues that the antibundling rule "foreclose[es] the ability of providers to create and offer packages of services and CPE, which can provide consumers with value, efficiencies and pricing solutions that they demand."^{18/}

While such subsidized bundles may appear attractive to customers on the surface, the costs of bundling ultimately are passed through to consumers in the form of higher service charges. Bundling does not lower the total cost to consumers, since a carrier that provides a discount on CPE to purchasers of a package must still recover the cost of both components of the package. If costs are not recovered on CPE, then they must be recovered through higher service

^{16/} ITAA at 4.

^{17/} Excel at 5.

^{18/} Comments of AT&T Corp. at 26.

charges.^{19/} Further economic inefficiencies are inevitable because consumers would not know the cost or price of the constituent elements that they are buying as a package.

Bell Atlantic argues that allowing bundling in the cellular marketplace has resulted in growth in the cellular industry and increased competition among cellular providers.^{20/} However, bundling in the cellular market grew out of very different conditions that are not present in the interexchange market. Indeed, the FCC based its decision to permit cellular bundling "on the unique conditions in the cellular market today"^{21/} Those conditions were described as a highly competitive cellular CPE marketplace featuring numerous manufacturers, retailers and other vendors and a desire to promote cellular subscribership and efficient spectrum utilization. By contrast, there is no public policy justification today for promoting interexchange usage, no issue of spectrum utilization and nothing approaching a vigorously competitive market for services and equipment yet to be devised.

Moreover, most cellular CPE is sold by independent retailers who also act as agents for the cellular carriers in their market; these retailers commonly offer equipment

^{19/} See IDCMA 38-39.

^{20/} Comments of Bell Atlantic at 6.

^{21/} Bundling of Cellular Customer Premises Equipment and Cellular Service, 7 FCC Rcd 4028 (1992).

produced by several competing manufacturers. The bundling the Commission allowed, therefore, was by independent retailers assembling packages that combined customer-selected CPE with transmission service.^{22/} In the interexchange market, however, the point of sale typically occurs not with the independent CPE retailer, but with the carrier, who can choose which CPE to provide to its customers.^{23/} Thus, whatever the Commission believes the benefits of cellular bundling have been, the conditions under which that bundling was permitted are different in crucial respects from the conditions present in the interexchange market.

D. Bundling Decreases Consumer Choice

Bundling inevitably leads to a reduction in consumer choice. First, customers are forced to choose among carrier-determined service/CPE packages, none of which may represent the customer's ideal.^{24/} Second, since bundling allows the development of proprietary CPE, customers will have difficulty switching carriers, and may be unable to use the same CPE to access services provided by different carriers.^{25/}

As MCI correctly observes, "the true cost of CPE is hidden in a bundle, thus depriving consumers of the ability

^{22/} See IDCMA at 40.

^{23/} IDCMA at 40-41.

^{24/} See Coalition at 5-6.

^{25/} See, e.g., US WEST at 8.

to make independent decisions based on features and price. In addition, bundling locks customers into a vendor and perhaps even a technology, thus diminishing the vitality of marketplace competition. This is especially true when the technology is proprietary to the supplier or when the total cost of the equipment is high relative to the transmission component."^{26/} Under the Commission's proposal, an IXC could make transmission service available only to customers that agreed to obtain carrier-provided CPE; an IXC might also provide transmission service at a lower price to customers that agreed to obtain carrier-provided CPE.^{27/} US WEST observes that (in either case) this would significantly impact the interconnection framework envisioned by the 1996 Act, which grants interconnection rights to carriers, but not to the end users.^{28/}

Moreover, were the Commission to adopt its proposal, carriers would inevitably seek to partner with a small number of CPE vendors. Those that are without carrier alliances would inevitably exit the market because they would lack the ability to use the carrier's basic service revenue to cross-

^{26/} MCI at 24 n.38. As the PaPUC explains, "Competitive choices are only good for consumers if they understand their choices at a level which allows them to exercise wise purchasing decisions." PaPUC at 13. Bundling CPE and service eliminates the ability of consumers to understand what their true choices are.

^{27/} IDCMA at 14; US WEST at 8.

^{28/} US WEST at 8.

subsidize their CPE offerings. Thus, the success or failure of any individual CPE provider would not turn on its ingenuity, customer care, or product quality, but instead on its ability to "cooperate" with carriers in creating discounted packages.^{29/}

In such a situation, the vendors allied with the carriers would be dependent on their carrier-patrons rather than end-user customers. "As a result, they would be unlikely to have the incentive or ability to develop equipment that competes 'intermodally' against network-based facilities or services."^{30/} Carriers could also manipulate their interface and other operating specifications to induce such cooperation and further limit competition.^{31/}

Thus, instead of the current CPE market in which a large number of manufacturers compete to sell equipment to end-users, "a new oligopoly/oligopsony market would arise in which a handful of manufacturers would sell equipment to a few carrier-purchasers."^{32/}

API argues nevertheless that such bundling is necessary to meet the needs of large, sophisticated companies, and that the bundling prohibition hinders such companies' efforts "to

^{29/} See IDCMA at 19-20; ITAA at 5-6.

^{30/} IDCMA at 20.

^{31/} ITAA at 5-6.

^{32/} IDCMA at 37-38.

obtain innovative system-wide telecommunications solutions."^{33/} API contends that a service/equipment package purchased from a carrier offers: "(1) a single point of responsibility, control and billing for all services and facilities; (2) cost savings due to volume purchases and long-term commitments; and (3) timely access to and the flexibility to implement new services and technologies."^{34/}

API does not explain why unsubsidized packages, which can today be offered by carriers, do not meet these needs. But even if they do not, the Commission should think carefully before taking an action which would primarily benefit the largest, most sophisticated customers to the detriment of other interexchange customers.

API seeks to convince the Commission that opponents to the proposal are those who, "rather than operate in a fully competitive market, . . . would prefer to operate in a market distorted by regulatory constraints."^{35/} But, in fact, it is the antibundling rule that prevents market distortions. As ITAA explains, the antibundling rule places CPE providers on a level playing field.^{36/} Some carriers, and large customers such as API, want to tip that field to their advantage. While API argues that bundling opponents "brandish" the

^{33/} API at 14.

^{34/} API at 15-16.

^{35/} API at 13.

^{36/} ITAA at 4.

antibundling rule "as a regulatory shield against competition,"^{37/} it is wide-open manufacturing and retail competition that the Coalition is trying to preserve and promote -- competition that will wither if the Commission adopts its proposal.

E. The Commission's Proposal Is At Odds With The Telecommunications Act Of 1996

The proposal to allow bundling is contrary to the concern expressed by Congress in the Telecommunications Act of 1996 about the anticompetitive effects of bundling, especially for independent manufacturers and vendors.^{38/} IDCMA echoes this theme, and explains, "The Commission proposal to retreat from its long-standing unbundling policy reflects a disturbing disregard for the clear policy choices made by Congress" in the 1996 Act.^{39/}

The only bundling supporter arguing against this position is API, which merely asserts that the bundling proposal "is envisioned by the 1996 Act, which clearly enunciated a 'pro-competitive, de-regulatory national policy framework.'^{40/} The Coalition agrees with API's characterization of the 1996 Act as pro-competitive and de-regulatory, but observes that Congress chose to pursue those

^{37/} API at 12.

^{38/} Coalition at 11-12.

^{39/} IDCMA at 20-21.

^{40/} API at 13.

pro-competitive policies by extending the antibundling rule to video CPE in newly enacted Section 629(a) of the Communications Act.^{41/} Thus, API's argument serves merely to support the Coalition's point that the best way to promote competition is to ensure a viable CPE market through retention of the antibundling rule.

F. The Proposed Amendment Would Inevitably Result In Wholesale Repeal Of The Rule

If the Commission adopts its proposed "amendment" of the antibundling rule, it would soon lead to wholesale repeal of the rule, since the Commission could not justify for long having such a rule in place for IXCs and not for LECs, or for interexchange services, and not for the local exchange services of the same carrier.^{42/}

The comments filed by other parties bear this out. Bell Atlantic, NYNEX, SBC, and USTA all make the case that the Commission could not justify repeal of the rule for the IXCs and not the LECs.^{43/}

Further, AT&T argues that IXCs should be permitted to bundle interexchange with enhanced services, while MCI assumes that the proposed amendment would allow bundling of transmission with enhanced services as well as CPE or "any

^{41/} See Coalition at 11; IDCMA at 20.

^{42/} Coalition at 11-12; see also IDCMA at 23.

^{43/} See Comments of NYNEX at 6; Bell Atlantic at 5; SBC at 7; Comments of United States Telephone Association ("USTA") at 3-4.

other product or service that the carrier chooses to include in a bundle."^{44/}

These comments demonstrate the slippery slope that the Commission is proposing to start down with its amendment of the antibundling rule. The Commission cannot view its proposal as an isolated action, since once it takes this step evisceration of the rule is inevitable. For this reason alone, the Commission should not take the step it is proposing today based on the record before it.

II. IF THE COMMISSION AMENDS § 64.702(e) IT ALSO MUST REQUIRE INTEREXCHANGE CARRIERS TO CONTINUE TO OFFER SEPARATELY, UNBUNDLED SERVICES ON A NONDISCRIMINATORY BASIS AND TO DISCLOSE CARRIER INTERFACES

The Coalition's comments showed that, in the event the Commission amends the rule to allow nondominant interexchange carriers to bundle service and equipment, it also must require carriers offering bundled packages to continue to offer separately, unbundled, unsubsidized interstate, interexchange services on a nondiscriminatory basis. All bills and marketing materials should separately state the price being paid for the transmission service and the price being paid for the equipment.

The vast majority even of those parties supporting the proposal to allow bundling recognize the dangers inherent in allowing carriers to offer only bundled packages, and thus

^{44/} AT&T at 28; MCI at 22-23 n.33.

urge the Commission to require carriers that bundle to offer separately, unbundled services on a non-discriminatory basis.

GTE explains that requiring carriers to make the service component of the package available on an unbundled basis "gives consumers the ability to determine whether to purchase the bundled service or create their own packages," thus "encourag[ing] competition in the CPE market."^{45/} NYNEX similarly says that requiring carriers to offer both unbundled and bundled services "will provide customers with a choice of equipment vendors for CPE," and will "further advance the Commission's pro-competitive policies in the equipment marketplace."^{46/} The PaPUC, which points out the competitive abuses it has encountered in situations where bundling is permitted, suggests that, "at a bare minimum, the Commission must require carriers to offer unbundled service offerings along with any bundled service offerings which are permitted."^{47/}

The Commission, however, must go farther than simply requiring the offering of unbundled services; it must also require that the unbundled components be offered on nondiscriminatory terms. USTA explains that requiring carriers to offer separately unbundled services on a nondiscriminatory basis would increase consumer choice by

^{45/} GTE at 11.

^{46/} NYNEX at 7.

^{47/} PaPUC at 12 (emphasis in original).

"preserving opportunities for competitors to utilize their own equipment to provide competitive services and CPE/service packages through resale, or to provide resold services to customers who already have their own CPE."^{48/} LDDS adds that such a requirement is necessary to prevent anticompetitive activities by carriers.^{49/}

Section 202(a) of the Communications Act, in fact, requires such a nondiscriminatory unbundling provision.^{50/}

"Nondiscrimination" means that a carrier cannot be permitted to offer stand-alone transmission service at the same price at which it offers a service/CPE package, since under such terms the customer that does not take the CPE is paying a higher charge for the same service. This constitutes unjust and unreasonable discrimination in violation of the Communications Act.

MCI correctly states that the practical effect of assuming consumers will benefit from "packages" is that many consumers will end up paying for a product they do not really want, and will accordingly be made to pay more for the product they really want.^{51/} MCI therefore suggests that if the Commission allows bundling, it also require that carriers

^{48/} USTA at 4. See also Comments of Pacific Telesis Group at 11; TRA at 41-42; US WEST at 9.

^{49/} LDDS Worldcom, Inc. at 18-19.

^{50/} See IDCMA at 39-40.

^{51/} MCI at 25.

"grant credits to any consumer equal to the value of any unwanted, bundled equipment so that consumers would be in a position to purchase their equipment-of-choice."^{52/}

The Coalition also agrees with those parties urging that not only must carriers offer services on an unbundled basis, but carriers also should be required to use public interfaces for their services and to give adequate public notice of any changes in those interfaces. "Such requirements would strike an appropriate balance between the policy goals of maximizing customer choice and preserving competition in the CPE market."^{53/} NYNEX and US WEST similarly state that carriers should be required to disclose all interface specifications using existing industry guidelines and procedures.^{54/}

Such a disclosure requirement is necessary because by denying the necessary technical information to unaffiliated manufacturers, carriers could preclude competition in the market for CPE competitive with that provided in the bundle. US WEST agrees that this would have potentially serious consequences in the CPE market, and also notes the vulnerability of the end users, who actually use the CPE, and

^{52/} MCI at 26 n.40.

^{53/} Comments of the Ad Hoc Telecommunications Users Committee ("Ad Hoc") at 12-13.

^{54/} NYNEX at 7; US WEST at 8.

who, unlike carriers, have no interconnection rights under the 1996 Act.^{55/}

AT&T and Compaq alone oppose an unbundling requirement. AT&T asserts that the abundance of service and product providers will ensure that customers desiring unbundled service and CPE options will still have those options available, because if one provider does not offer unbundled components, its competitors will. There is thus no need, AT&T argues, for requiring carriers that bundle to also offer separately, unbundled services.^{56/}

First, the Commission cannot take for granted that "if one provider does not offer unbundled components, its competitors will." In many areas of the country, consumers have a very limited choice of service providers from which to choose.

More importantly, AT&T's argument sidesteps the fact that providing service on an unbundled, nondiscriminatory basis is required by Section 202(a) of the Communications Act, as shown above. Complying with the nondiscrimination requirements of the Act is not a choice that carriers are free to make depending on the marketplace. If carriers are permitted to bundle CPE with service, then they must also provide service on an unbundled, nondiscriminatory basis.

^{55/} US WEST at 8.

^{56/} AT&T at 27. See also Compaq Computer Corporation at 4-5.

CONCLUSION

The record in this proceeding shows the dangers of the Commission's proposed amendment of the antibundling rule, while demonstrating no benefits. The Commission therefore cannot justify adopting its proposal on the record before it. For the reasons stated above and in the Coalition's Comments, the Commission should not amend Section 64.702(e) of its rules to allow nondominant interexchange carriers to bundle CPE with interexchange service.

Respectfully submitted,



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I, Marjorie Schroeder, hereby certify that on this 24th day of May, 1996, I caused a copy of the attached Reply Comments of the Consumer Electronics Retailers Coalition to be served by first-class mail, postage pre-paid to the following:

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