

**BEFORE THE
FEDERAL COMMUNICATIONS COMMISSION
WASHINGTON, D.C. 20554**

RECEIVED

AUG 30 1996

In the Matter of)
)
Implementation of the Non-Accounting)
Safeguards of Sections 271 and 272 of the)
Communications Act of 1934, as amended:)
)
and)
)
Regulatory Treatment of LEC Provision)
of Interexchange Services Originating in the)
LEC's Local Exchange Area)

CC Dkt No. 96-149

DOCKET FILE COPY ORIGINAL

**REPLY COMMENTS OF THE
UNITED STATES TELEPHONE ASSOCIATION**

Mary McDermott
Linda Kent
Charles D. Cosson
Keith Townsend

United States Telephone Association
1401 H Street, N.W., Suite 600
Washington, D.C. 20005
(202) 326-7247

August 30, 1996

No. of Copies rec'd
List ABCDE

027

TABLE OF CONTENTS

EXECUTIVE SUMMARY	i
I. INTRODUCTION	1
II. SCOPE OF THE COMMISSION'S AUTHORITY [¶¶ 19-30]	2
III. SEPARATE AFFILIATE ISSUES [¶¶ 55-64]	3
A. Independent Operations	6
B. Sharing of Administrative Services	8
C. Competitive Exchange and Exchange Access Services Provided by a BOC	10
IV. NONDISCRIMINATION SAFEGUARDS: SECTION 272 [¶¶ 65-89]	10
A. Nondiscrimination in Section 272(c) [¶¶ 72-79]	11
B. Nondiscrimination Requirements of Section 272(e) [¶¶ 80-89]	13
V. JOINT MARKETING PROVISIONS OF SECTIONS 271 AND 272 [¶¶ 90-93]	14
VI. OTHER ISSUES	16
A. Definition of InterLATA Information Services [¶¶ 41-47]	16
B. Internet Services are Information Services [¶¶ 41-47]	17
C. Previously Authorized Services [¶¶ 38-39]	18
D. Incidental Services [¶¶ 36-38]	18
VII. ENFORCEMENT OF SECTIONS 271 AND 272 [¶¶ 94-107]	18
A. Mechanisms to Facilitate Enforcement of the Separate Affiliate and Nondiscrimination Safeguards of Sections 271 and 272 [¶¶ 94-96]	19
B. The Section 271(d)(6) Complaint Process [¶¶ 97-107]	20

VIII. BOC In-Region InterLATA Offerings Should be Classified as Non-Dominant [¶¶ 108-162]. 23

A. Market Definition 24

 1. Product Market. 24

 2. Geographic Market. 24

B. Pseudo-Economic Arguments About Leveraging Are Unpersuasive and Irrelevant. 25

 1. Raising Rivals' Costs. 26

 2. Cost Misallocation. 29

EXECUTIVE SUMMARY

Rather than focusing on the promotion and protection of competition, most of the commenters in this proceeding have focused instead on the promotion and protection of their own narrow interests. But the plain language of Sections 271 and 272, and the intent behind them, are unmistakable. In those two Sections, Congress carefully balanced the supposed risks from BOC participation in interLATA markets against the competitive and consumer benefits it would bring. The result is a finely-tuned, detailed statute that addresses the supposed risks and imposes safeguards appropriate to each. Accordingly, there is no reason for the Commission to revisit Congress' judgment or to supplement Congress' safeguards with additional restrictions. Moreover, there is every reason for the Commission to avoid such a course. The imposition of additional burdens is not only contrary to Congressional intent, but also anticompetitive and detrimental to public welfare. By over-burdening the BOCs with regulatory requirements, the Commission would render them less competitive, forcing consumers to endure higher prices and inferior service.

For example, Section 272(b) (which governs BOC provision of interLATA telecommunications and information services), provides that the BOC and its interLATA affiliate must "operate independently." Several commenters have attempted to broaden this phrase to preclude competitively beneficial interactions well beyond the activities specified in Sections 272(b)(2)-(5). But the same term is used in Section 274 as well, where it could not possibly have such a broad meaning. It is thus clear that the "independent" operation requirement was not meant to include a facilities bar, or prohibitions against BOC provision of hiring, training, installation, maintenance, or research and development services for its affiliate. Nor is there any basis for reading the term as precluding BOCs from sharing in-house or outside administrative services with their affiliates. The commenters urging such a course have presented no credible evidence why such a restriction is necessary. And the proposed restrictions would be inconsistent

with Commission precedent, will raise BOC costs, create economic inefficiency, and decrease competition.

USTA also urges the Commission to reject the calls of several commenters that have suggested that a BOC cannot establish a separate competitive exchange and exchange access affiliate, independent of the BOC. Nothing in the 1996 Act prohibits such a result, nor is it in the public interest to restrain competition by prohibiting the creation of such an affiliate.

Nor does the record demonstrate the need for the Commission to impose additional regulatory requirements on the BOCs to ensure they comply with the non-discrimination safeguards of Section 272. Congress expressly adopted a biennial audit requirement and enhanced complaint process to ensure that a BOC does not engage in anti-competitive behavior. Similarly unnecessary are the draconian complaint processes, schedules, and burden shifting schemes proposed by the commenters under Section 271(b)(6). Such proposals are unnecessary, unfair, unwise, and unlawful. Instead, the Commission's usual even-handed processes are more than adequate, so long as proceedings are handled on an expedited schedule.

The Commission should also resist the IXCs' attempt to end-run Congress' joint marketing parity policy. Specifically, the Commission should reject the IXCs' attempts to expand the scope of the joint marketing activities permitted to them, while restricting the BOCs' joint marketing activities. Parity means that the BOCs and IXCs should be able to engage in similar joint marketing activities once the statutory preconditions have been met -- not that IXCs should have special advantages.

Finally, there can be no dispute that BOC interLATA affiliates should be treated as non-dominant carriers. Almost everyone agrees that the proper product market includes all interexchange services, and that the geographic market is national (for the purposes of the dominance/non-dominance inquiry). In such a market, the BOC interLATA affiliates will start

with no market share. Nor can the BOCs "leverage" control over exchange services into power in interLATA markets. They have not "leveraged" that control into power in any other downstream markets, and the Commission's regulations -- non-discrimination safeguards, accounting rules, and price caps -- as well as an increasingly competitive marketplace preclude any such attempt. No commenter has presented any credible evidence to the contrary.

**BEFORE THE
FEDERAL COMMUNICATIONS COMMISSION
WASHINGTON, D.C. 20554**

In the Matter of)	
)	
Implementation of the Non-Accounting)	
Safeguards of Sections 271 and 272 of the)	
Communications Act of 1934, as amended:)	CC Dkt No. 96-149
)	
and)	
)	
Regulatory Treatment of LEC Provision)	
of Interexchange Services Originating in the)	
LEC's Local Exchange Area)	

**REPLY COMMENTS OF THE
UNITED STATES TELEPHONE ASSOCIATION**

I. INTRODUCTION

Not surprisingly, the comments in this proceeding fall into the same predictable pattern as the comments in other proceedings under the 1996 Telecommunications Act. Rather than seeking to bring the benefits of a fully competitive marketplace to consumers, most comments reflect the narrow interests of their authors. Under the guise of seeking protection from discrimination and cross-subsidization, incumbent interexchange carriers ask the Commission to impose restrictions on BOC activities so onerous as to render the BOCs non-competitive. *See, e.g.*, AT&T Comments; MCI Comments; LDDS WorldCom Comments ("LDDS"). Using similar arguments, information service providers seek to impose additional burdens on the BOCs even though such burdens are nowhere contemplated by the Act. *See, e.g.*, Information Technology Ass'n ("ITAA"); Indep. Data Comm. Mfrs. Ass'n ("IDCMA").

As the D.C. Circuit has pointed out, the clamorings of such obvious interest groups are entitled to little weight. *See United States v. FCC*, 652 F.2d 72, 97 (D.C. Cir. 1980) (*en banc*) (AT&T's "protestations in favor of vigorous competition ring hollow" when "the immediate result

of [an AT&T victory] would be to block the entry into the industry of a strong and technologically innovative competitor."). Instead, what matters here is Congress' plan -- and the public interest that Congress' plan is designed to serve.

That plan and Congress' intent are clear from the plain language of Sections 271 and 272 themselves. In those two Sections, Congress carefully balanced the supposed risks from BOC participation in interLATA markets against the competitive benefits it would bring. The result is a finely-tuned, detailed statute that addresses the supposed risks and imposes safeguards appropriate to each. See ITAA at 2 (statute is detailed and should be enforced as written). Accordingly, there is no reason for the Commission to revisit Congress' judgment or to supplement Congress' safeguards with additional restrictions. Moreover, there is every reason for the Commission to avoid such a course. The imposition of additional burdens is not only contrary to Congressional intent, but also anticompetitive and detrimental to public welfare. By over-burdening the BOCs with regulatory requirements, the Commission would render them uncompetitive, depriving consumers of the great benefits that additional competition would bring.

II. SCOPE OF THE COMMISSION'S AUTHORITY [¶¶ 19-30]

Although almost all of the commenters agree that the statute by its terms addresses both interstate and intrastate traffic, the commenters spar over the extent to which the FCC or state commissions have jurisdiction over (and therefore should pass rules concerning) intrastate traffic. Compare Telephone Resellers Ass'n at 5-6 ("TRA") (urging the Commission to issue rules concerning interstate and intrastate service), with People of the State of California and the CPUC at 2-8 (urging the Commission to restrict its rules to interstate services). They thus implicitly recognize a distinction that Congress itself recognized in the Telecommunications Act -- the difference between the enactment of a statute that governs an issue and the grant of authority to the Commission. See 47 U.S.C. § 152(b) ("nothing in this [Act] shall be construed to apply or

to give the Commission jurisdiction with respect to" intrastate services and facilities (emphasis added)).

The various comments, however, fail to address an antecedent question -- whether there is any reason for the Commission or any other body to supplement the statute *in any way*. As explained above and in the USTA's opening comments (at 2-6), the Commission has neither reason nor authority to impose restrictions on BOC interstate activity beyond those contemplated in the statute itself. It follows a fortiori that there is even less reason -- and still no authority -- for the Commission to impose additional regulatory burdens on purely intrastate traffic.

Instead, the rules of the road for interstate and intrastate traffic alike are provided by the statute itself. In great detail, Sections 271 and 272 set out what BOCs must do, and what protections are appropriate, when BOCs enter interLATA markets (interstate and intrastate) inside of their regions. Neither the states nor the Commission have authority to provide different or additional rules.

III. SEPARATE AFFILIATE ISSUES [¶¶ 55-64]

Section 272(b) requires that a BOC, to the extent it engages in manufacturing activities, originates certain interLATA telecommunications services, or provides interLATA information services, to do so through a separate affiliate that meets five separation requirements. At the outset, it is important to place these separation restrictions in context. Congress established them as transition measures for a limited amount of time (three or four years) while competition develops in the exchange and exchange access markets. 47 U.S.C. § 272(f). Nothing in the record does or can dispute this simple fact.

The five separation requirements do not require the Commission to adopt new interpretations of each of the requirements because the language of each requirement is drawn directly from the Commission's existing Competitive Carrier, Computer II and Computer III regulatory regimes.

Had Congress wanted to place more onerous restrictions on the BOCs' provision of services from these separate affiliates, as some commenters have suggested, it certainly could have done so. Indeed, the fact that Congress adopted extensive separation requirements for BOC provision of electronic publishing services (Section 274) and manufacturing services (Section 273) demonstrates Congress' intent not to place similar extensive restrictions on the separate affiliates required by Section 272. The Commission must reject the IXCs' and other commenters' attempt to end-run Congressional intent by having the Commission place additional restrictions on BOC separate affiliates.

In addition to not adding new and unnecessary regulatory burdens on the BOCs and their separate affiliates, it is critical that the Commission review Section 272's requirements in the context of the sea-change in the telecommunications market structure that the 1996 Act recognizes, embraces and accelerates. The BOCs' competitors have urged the Commission to saddle the BOCs with outdated, inefficient and unnecessary regulations based on some perverted vision of a "Computer II -- plus" maximum separation policy. While this may enhance their own competitive positions during the transitional period when the separate affiliate requirements are in place, it will do nothing for competition or the public interest. Indeed, as Professor Hausman explains in his attached Statement, the separation proposals made in the NPRM and endorsed by the IXCs "will likely lead to decreased innovation and fewer new services." Hausman Reply Aff. ¶ 15. The Commission should reject the IXCs' pleas to eviscerate Congress' intent in this area.

In fact, to the extent that Section 272(b)'s separation requirements require further interpretation, which USTA believes they do not, they must be interpreted as being less rigorous than the requirements promulgated in the Computer II proceeding. At the time of Computer II, the BOCs were not under the extensive interconnection duty to which they are now subject under Section 251. Indeed, the threshold for creating separate interexchange telecommunications and

information services affiliates is when a BOC meets the extensive factors enumerated in Section 271(c)(2)(B)'s competitive checklist -- a rigorous and unprecedented demonstration that the local BOC network is open to competition. As a result, the hypothetical possibility of BOC incentives to engage in discriminatory and improper cross-subsidization activities that drove the creation of the Computer II structural separation requirements are dramatically reduced by Section 251's interconnection requirements.

Moreover, the need for "maximum separation" has been eliminated in light of the Commission's use of price caps to regulate the BOCs. As USTA noted in its comments, "existing price caps regulation eliminates a BOC's incentive to misallocate costs." USTA at 45. Because cost increases on the BOCs' side of the ledger do not automatically trigger price increases for consumers, there is no reward for shifting costs from unregulated to regulated activities. As a result of the interconnection duties and price cap regulation, the separate affiliate requirements need not be, and therefore should not be, interpreted as rigorously as when they were first promulgated.

Furthermore, the Commission expressly rejected the Computer II maximum separation regime suggested by the IXCs when it adopted the Computer III nonstructural safeguards ten years ago. The Commission recognized that there are economies of integration (derived from more efficient production and lower transaction costs) that outweigh any potential diseconomies stemming from hypothetical abuses of underlying market power. See Final Decision, Section 64.702 of the Commission's Rules and Regulations (Third Computer Inquiry), 104 F.C.C.2d 958, 1008 (1986). And as Professor Hausman explains, the economic evidence has already demonstrated that Computer II maximum separation requirements led to consumer welfare losses in the billions of dollars. Hausman Reply Aff. ¶ 14. It would be wholly inappropriate for the

Commission now to revert to a regime it has thoroughly rejected when the plain language of the 1996 Act does not require, and indeed does not allow, it to do so.

USTA believes that its opening comments already have addressed the great majority of the hypertechnical and incorrect interpretations of Section 272(b). Instead, in this section, USTA will concentrate its reply comments on two aspects of the separate affiliate requirements that it believes are the most important -- the requirement that the BOC affiliate operate independently from the BOC (Section 272(b)(1)), and the requirement that the BOC affiliate have separate officers, directors and employees from the BOC (Section 272(b)(3)).

A. Independent Operations

It is utterly unnecessary for the Commission to promulgate additional rules and requirements that interpret the first separate affiliate standard, which requires the BOC affiliate to "operate independently" from the BOC. 47 U.S.C. § 272(b)(1). As USTA and other BOCs noted in their comments, Congress specifically borrowed the "operate independently" language from the Commission's rules governing BOC provision of enhanced services (47 C.F.R. § 64.702(c)(2)) and cellular services (47 C.F.R. § 22.903(b)). See e.g., USTA at 19-20, Bell Atlantic at 4.

In particular, both sets of rules governing a BOC's separate affiliate offering of enhanced services and cellular services requires the BOC and its affiliate to "operate independently." Despite the IXC's statutory construction arguments that the Commission must add a new interpretation to define what exactly "independent operations" are (AT&T at 19; MCI at 23; Sprint at 23), the Commission, in both the enhanced services and cellular contexts, did not interpret the phrase "operate independently" to mean anything more than what was enumerated in each of the rule's following subsections (e.g., 47 C.F.R. § 64.702(c)(1) and (c)(3)-(5); 47 C.F.R. § 22.903(b)(1)-(3)). Both subsections stand by themselves and do not permit the FCC to

adopt the vast number of restrictions that the IXCs and other BOC competitors suggest. See AT&T at 20; MCI at 24-27.

Had Congress wanted to include the list of prohibitions on operations suggested by the IXCs (prohibitions on joint ownership and use of any transmission facilities, switching facilities or other property, sharing of physical space, restrictions on joint research development and prohibition on joint hiring and training of personnel), it could easily have done so. In Section 274(b), for example, Congress expressly and explicitly adopted a number of these same prohibitions on a BOC affiliate's provision of electronic publishing services. The fact that Congress did not specifically add these requirements to Section 272(b) should make it clear that it is inappropriate for the Commission to do so now. As the Yellow Pages Publishers Association noted, "[a]dditional requirements would overregulate when Congress chose not to do so, and only harm the ability [for the BOCs and their affiliates] to efficiently offer services to the public." Yellow Pages Publishers Ass'n at 8.

More specifically, had Congress wanted a facilities bar for separate affiliates governed by Section 272 (as suggested by MCI at 23), it would have adopted one as it did in Section 274(b)(5)(B). The commenters' professed fears that the interLATA affiliate will have discriminatory access to basic transmission facilities and enjoy reduced costs through cost misallocations are unfounded. MCI at 25; AT&T at 20-22. First, Sections 272(c) and (e) obligate the BOCs to treat affiliated entities and unaffiliated entities even-handedly. As discussed below in Section IV, the non-discrimination safeguards in Sections 272(c) and (e) provide the necessary and sufficient protection for competitive access to a BOC's basic transmission facilities. Second, as Professor Hausman indicates, the Commission's experience with price caps demonstrates that the BOCs now have no incentive to misallocate costs because there is no reward (i.e., higher prices for its services) from misallocating their costs in the manner in which

MCI has suggested. Hausman Reply Aff. ¶ 19. In fact, MCI's proposal for a separate facilities bar will impose a penalty on the BOCs in terms of decreased efficiency that will lead to higher costs for the BOCs and higher prices for consumers. *Id.* ¶ 18.

Thus, it is clear that Congress' use of the term "operate independently" do not require anything more than what Congress adopted in Section 272(b)(2)-(5). It is equally clear that in order to harmonize the interpretation of the words "operate independently" across Sections 272 and 274, it cannot mean those additional restrictions that are included in Section 274(b), but not included in Section 272(b) (*i.e.*, a facilities bar, or prohibitions against BOC provision of hiring, training, purchasing, installation, maintenance, or research and development services for the separate affiliate).¹

B. Sharing of Administrative Services

Section 272(b)(3) requires the BOC and its affiliates to have separate officers, directors and employees. As USTA and the BOCs noted in their comments, it is completely inconsistent with Commission precedent for the Commission now to interpret this language as prohibiting the sharing of in-house services on a cost reimbursable basis as is currently allowed under the Commission's Computer II rules. *See e.g.*, NYNEX at 24; U S West at 22.

AT&T, and to an extent the other IXCs, have urged the Commission to prohibit the sharing of in-house and outside services, even on a cost reimbursable basis, because of alleged fears of improper cross-subsidization. The "opportunity for misallocation of costs" is the only excuse some commenters use to suggest prohibiting sharing of in-house services. AT&T at 24-25; MCI at 27-28. These opponents present no credible evidence that there remains any incentive for the BOCs to cross-subsidize their competitive service offerings with the increasingly competitive

¹Even if the term "operate independently" had an independent meaning, which it does not, USTA believes that nothing in the record would justify the a priori regulatory straightjacket suggested by the commenters.

offering of exchange and exchange access services. Indeed, AT&T has gone so far as to suggest that the BOCs and their affiliates cannot share out-sourced services because of these same unjustified fears of cost misallocation. AT&T at 25.

The commenters continue to voice the same discredited arguments they have been using for years in an attempt to prevent the BOCs from offering enhanced services and CPE on a competitive basis. As a result, these arguments have since lost any semblance of credibility. The simple fact is that federal price cap regulation has eliminated the incentives the BOCs may have had to cross-subsidize any competitive offering with exchange and exchange access services. As Professor Hausman illustrates, Sprint and others discuss the problem of "misallocation of costs" between the BOC interLATA affiliate and the BOC, but they never explain how a problem can arise in the absence of rate of return regulation. Hausman Reply Aff. ¶ 19. Indeed, Professor Hausman concludes that Sprint's recommended prohibition on sharing would raise the BOCs' costs, create economic inefficiency and decrease competition. Id.

Similarly, USTA opposes AT&T's suggestion that BOCs not be permitted to form a third entity (i.e. one that is neither a successor of a BOC nor an affiliate subject to Section 272) to perform administrative services for the BOC and any of its Section 272 affiliates for three reasons. AT&T at 25. First, the plain language of Section 272(a) prohibits a BOC and its Section 272 affiliates from offering of intraLATA and interLATA telecommunications or information services on an integrated basis. The 1996 Act does not in any way prohibit a BOC from structuring its business to provide administrative services from a third entity to both the BOC and its Section 272 affiliates. Nor does the 1996 Act preclude a BOC from determining the most efficient way to provide administrative services to its subsidiaries. Second, as Professor Hausman indicates, the costs in terms of lost efficiency to the BOCs and to consumers associated with a BOC's separate provision of administrative services outweigh any potential benefits.

Hausman Reply Aff. ¶ 20. And third, as the Commission noted in the NPRM, the Computer II rules clearly permit a BOC and its affiliate to share administrative services on a cost reimbursable basis. NPRM ¶ 62. For these reasons, the Commission should reject AT&T's suggestion.

C. Competitive Exchange and Exchange Access Services Provided by a BOC

Contrary to the suggestions of certain IXCs and competitive access providers, the 1996 Act does not prohibit a BOC from offering competitive exchange or exchange access facilities from separate facilities not jointly owned with the BOC. See e.g., AT&T at 17-18, Teleport Comm. Group at 3 ("TCG"). If a newly-created separate BOC affiliate develops its own network that provides additional competitive entry, then the underlying goals of the 1996 Act for increased facilities-based competition will have been met. The goals of the 1996 Act also will be met if the newly-created separate affiliate resells the BOC's exchange and exchange access services. As the Commission has recognized:

Resale will be an important entry strategy for many new entrants, especially in the short term when they are building their own facilities. Further, in some areas and for some new entrants, we expect that the resale option will remain an important entry strategy over the longer term.

First Report and Order, Implementation of the Local Competition Provisions in the Telecommunications Act of 1996, CC Dkt. No. 96-98, FCC No. 96-325, ¶ 907 (FCC Aug. 8, 1996) ("Local Competition Order"). Moreover, if a separate BOC affiliate resells a BOC's exchange and exchange access services under Section 251(c)(4), it must offer those services to other new entrants on competitive and non-discriminatory terms. Thus, the 1996 Act clearly envisions the use of resale as means to stimulate additional competition in the exchange and exchange access markets.

IV. NONDISCRIMINATION SAFEGUARDS: SECTION 272 [¶¶ 65-89]

The record demonstrates that Sections 272(c) and (e) set forth two broad nondiscrimination safeguards that apply to a BOC's dealings with its separate affiliates and with other nonaffiliated

entities providing the same services. The requirements of Section 272(c) sunset after the three or four year transition periods as do Sections 272(e)(2) and (4) because they necessarily involve the BOCs offering their services through separate affiliates. Notwithstanding the plain inapplicability of Sections 272(e)(2) and (4) to a BOC's operations after the sunset periods, AT&T has suggested that Section 272(f)'s requirement that subsection (e) continue to apply after the sunset period requires that the BOCs continue to use separate affiliates to provide information and interexchange services. AT&T at 30, n.29. AT&T is virtually alone among the commenters and has fabricated this argument out of thin air. There is neither a basis in the 1996 Act nor in the legislative history for suggesting that Congress intended to require the BOCs to continue to use separate affiliates to offer interLATA telecommunications and information services after the sunset period. The Commission should reject this suggestion.

USTA supports Sprint's view that the Commission's existing nondiscrimination requirements embodied in Section 201 and 202 of the Act obviate the need for new nonaccounting, nondiscrimination rules pursuant to Section 272. In particular, Sprint commented that:

[t]he new nondiscrimination requirements in Section 271(c)(1) and 272(e) augment the Commission's existing nondiscrimination provisions. There would not appear any reason for the Commission to describe any nonaccounting, nondiscrimination rules to implement these sections.

Sprint at 38. This view is consistent with USTA's comments that the language of Section 272's nondiscrimination requirements are plain on their face and do not require additional Commission interpretation. USTA at 25-26.

A. Nondiscrimination in Section 272(c) [¶¶ 72-79]

Section 272(c) requires that a BOC not discriminate between itself or its affiliate(s) and any other entity in the provision or procurement of goods, services, facilities, and information, or in the establishment of standards. Contrary to the IXCs' comments, this section does not impose additional requirements on the BOCs to provide "identical outcomes." AT&T at 31; MCI at 31;

Sprint at 36. Section 272(c) only requires a BOC to provide even-handed treatment of nonaffiliated entities compared to the treatment of affiliated entities. Requiring BOCs to provide additional services or functions to requesting carriers that a BOC does not provide its own affiliates would be completely beyond the scope of the plain language of Section 272(c).

Contrary to MCI's suggestion, the language of Section 272(c) is easily distinguishable from the language Congress used to impose functional equivalency or identical outcomes in the nondiscrimination requirement of Section 251(c)(2)(C). MCI at 32. Section 251(c)(2)(C) requires a BOC to provide interconnection to any requesting carrier "that is at least equal in quality to that provided by the local exchange carrier to itself or to any" affiliate. The Commission interpreted this language to impose a functional equivalency requirement on the BOCs. That is, if asked to do so, the BOCs must provide a higher quality interconnection than they provide to themselves or to affiliates to enable new entrants to compete with incumbent LECs. Local Competition Order ¶ 225.

While USTA does not agree with this interpretation of Section 251(c)(2)(C), even if it were correct, a similar interpretation in Section 272(c) would be erroneous. The plain language of Section 251(c)(2)(C) requires interconnection that "is at least equal in quality." Section 272(c) only prohibits BOC discrimination against unaffiliated providers, and does not use the "at least equal in quality" language. Thus, MCI's interpretation is unwarranted and clearly not contemplated by the plain language of Section 272(c). The suggestion that Section 272(c) requires functional equivalency or identical outcomes should be rejected.

IXCs have also suggested that the Commission oversee and involve itself in the standard setting process for telecommunications networks to ensure that the BOCs do not create standards that favor the BOCs' affiliates and disadvantage their competitors. See AT&T at 35. Such a requirement is not needed. In an era of open telecommunications markets, BOCs are potential

competitors of other BOCs and, thus, have no incentive to collaborate with the other BOCs to discriminate against potential competitors, which by definition may include themselves. As a result, the existence of the BOCs as competitors to the other BOCs will provide an additional "competitive check" and ensure nondiscriminatory standard setting processes. The Commission need not involve itself in setting network standards.

B. Nondiscrimination Requirements of Section 272(e) [¶¶ 80-89]

Some commenters suggest that the Commission impose new regulatory burdens on the BOCs to ensure that they comply with the nondiscrimination safeguards of Section 272(e). For example, AT&T has suggested that the Commission extend the access, reporting, disclosure and CPNI requirements of Computer III and ONA to BOC provision of exchange and exchange access services and adopt new regulatory reporting and disclosure requirements on BOC provision of these services. AT&T at 35-47.

These suggestions are unwarranted and contradict the deregulatory thrust of the 1996 Act. In Section 272(d), Congress expressly adopted a biennial audit requirement to determine whether a BOC and its affiliates have complied with the requirements of Section 272, and in particular the separate accounting requirements under subsection (b). In addition, Congress enhanced the Commission's existing complaint processes under Sections 206-209 of the Communications Act by adding a new complaint process under Section 271(d)(6)(A). Congress has deemed these to be effective deterrents to ensure that the requirements of Section 272 have been met. The Commission should not promulgate additional burdensome requirements that do not further the public interest.

One particularly egregious example of IXC overreaching is MCI's suggestion on Section 272(e)(3)'s imputation requirement. MCI at 44. MCI has suggested that the Commission not only require a BOC to charge its affiliates an amount for access that is no less than the amount

charged to any unaffiliated interexchange carrier, but also that the Commission review a BOC's interLATA telecommunications or information services affiliates' books and accounts to ensure that the affiliate's "rates or earnings cover its access and all other costs." *Id.* This requirement is totally unnecessary. As USTA has pointed out above, and Professor Hausman has confirmed, the BOCs simply have no incentive to improperly cross-subsidize their interLATA telecommunications or information service offerings from their exchange and exchange access business. Moreover, the BOCs will already be complying with, and paying for, a Federal/State biennial audit and thus, there is no need for the Commission to perform another review that even MCI has suggested "would be extremely difficult, uncertain and time-consuming." *Id.* To do otherwise would be to return to the days when the Commission used rate-of-return regulation to determine whether a BOC's prices were just and reasonable. The Commission should not adopt such an onerous and inefficient regulatory requirement that will have no public interest benefits.

V. JOINT MARKETING PROVISIONS OF SECTIONS 271 AND 272 [¶¶ 90-93]

There is substantial support in the record for BOCs and their affiliates to jointly market exchange and exchange access services and interLATA services, as long as during the transitional three- or four-year time period in which separate affiliates are required, joint marketing occurs on an arm's length basis as required by Section 272(b)(5). *See e.g.*, BellSouth at 9-10; Bell Atlantic at 9; MCI at 48. As BellSouth noted, "[t]hese joint marketing provisions are an integral part of the Congressionally-established scheme for eliminating barriers to entry into the local and long-distance markets." BellSouth at 9.

Congress, in adopting the joint marketing provisions of Sections 271 and 272, noted that the ability to bundle telecommunications, information and cable services into a single package to create "one-stop-shopping" is a significant competitive marketing tool. USTA at 27. *See* Hausman Reply Aff. ¶ 22. As a result, Congress adopted the restrictions on joint marketing by

BOCs and IXC's in Sections 271 and 272 "to provide for parity among competing industry sectors." S. Rep. No. 652, 104th Cong., 1st Sess. 23 (1995).

In the face of Congress' strong desire to ensure joint marketing parity among competing industries, the large IXC's have attempted to redefine the very meaning of "parity" to refer to those activities during the relevant restricted time periods in which the BOC's cannot engage, but those in which the IXC's can. For example, AT&T, MCI and Sprint erroneously argue that the IXC's can jointly market within a single, fully-integrated company, their long-distance services with a local service that is provided through the purchase of unbundled elements from the incumbent LEC under Section 251(c)(3). AT&T at 53; MCI at 46; Sprint at 48. As USTA noted before, the "purchase of unbundled network elements from a BOC is the equivalent to reselling a BOC's local exchange services." USTA at 29. See also NYNEX at 13-14. Because IXC's may serve customers through the purchase of LEC network elements and/or resale of LEC services, as Ameritech noted, the IXC's could completely evade the intent of Section 271(e) by serving just one customer through the purchase of unbundled elements and the rest through resale. Ameritech at 50.

To further compound this attempted end-run around Congress' joint marketing parity policy, the IXC's have attempted to expand the scope of permissible activities that they can engage in (before BOC's provide interLATA services in a state), while *simultaneously* narrowing the scope of joint marketing opportunities for the BOC's (during the three years of mandatory structural separation). For example, MCI has argued that Section 271(e) permits the IXC's, during the period of restricted joint marketing, to advertise the availability of both interLATA and local exchange services, making these services available from a single source, and to provide bundling discounts for the purchase of both products, but that Section 272(g)(2) does not permit the BOC's to do the same during the period in which the BOC's must offer interLATA telecommunications

services via a separate affiliate. MCI at 46. This interpretation is contrary to Congress' parity policy. There will be no parity if BOC affiliates are not allowed to engage in the same activities that the IXC's were able to engage in during the time period that IXC's were prohibited from joint marketing. Indeed, MCI's reasoning that the IXC should be able to engage in these activities, but that the BOC's cannot, because Congress did not intend to impose unnecessary costs on IXC's, is equally applicable to the BOC's. *Id.* at 47.

The Commission would further tilt an uneven playing field by adopting anti-competitive suggestions as Time Warner's request that a BOC be prohibited from engaging in national or regional advertising "until and unless regional relief has been justified by the RBOC in every one of its states." Time Warner at 24-25. Such suggestions are unsupported by either the statute or Congressional intent and the Commission should reject them.

Finally, USTA also opposes two additional "extra-statute" restrictions proposed by AT&T. First, AT&T has suggested that a BOC be required to announce the availability and terms of any joint marketing arrangement at least three months prior to implementing it. AT&T at 55. Second, and equally without merit, is the suggestion that a BOC be required to make marketing opportunities for its services equally available to unaffiliated carriers. *Id.* at 56. Nothing in the language of the 1996 Act requires such anticompetitive and burdensome results. As Professor Hausman demonstrates, such requirements would do little more than decrease the efficiency benefits that the BOC's can pass on to their customers in terms of lower prices. Hausman Reply Aff. ¶ 23.

VI. OTHER ISSUES

A. Definition of InterLATA Information Services [¶¶ 41-47]

USTA suggested in its comments that an interLATA information service is one that contains an interLATA transmission component provided by the BOC in direct association with the

provision of the service. An information service that cannot be accessed across LATA boundaries, provides service only within a given LATA, or does not use an interLATA telecommunications component provided by the BOC is not an interLATA information service under the 1996 Act. USTA at 14. MCI has taken the contrary view that if a BOC selects the interLATA component, that qualifies that service as an interLATA information service subject to Section 272. MCI at 17. USTA disagrees with this definition because if a BOC does not provide the interLATA telecommunication component, it will be purchasing the interLATA service from an IXC. As a result, by definition, the purchase of this service does not raise cross-subsidy and discrimination concerns that could arguably arise if the BOC provided the interLATA telecommunications component itself. Only those information services that include an interLATA telecommunications component provided by the BOC should be included in the definition of interLATA information services subject to Section 272.

B. Internet Services are Information Services [¶¶ 41-47]

MFS uses its comments to insist that Internet access services are interLATA information services that must be provided through a separate subsidiary under Section 272 and cannot be provided until the BOC has been authorized to provide interexchange services pursuant to Section 271. As discussed above, the determining factor in deciding whether an information service is an interLATA information service is whether, in the BOC's offering of the service, the BOC also provides the underlying interLATA transmission component. Thus, to the extent that a BOC provides Internet access services, if the BOC does not provide the underlying interLATA transmission component, the BOC's offering will not be an interLATA information service subject to Section 272.

C. Previously Authorized Services [¶¶ 38-39]

There is wide support in the comments for USTA's interpretation of the previously authorized services portion of Section 272(a)(2)(B)(iii). See e.g., U S West at 16-17; MCI at 8-9. In particular, the plain language of the statute requires that previously authorized interLATA services be exempt from the one-year transition period requirements in Section 272(h).

D. Incidental Services [¶¶ 36-38]

In its comments, USTA noted that incidental interLATA services described in paragraphs (1)-(3), (5) and (6) of Section 271(g) are exempt from the separate affiliate requirements of Section 272. USTA at 10-11. Despite the clear language of this section, MCI and some others insist that the Commission require that these enumerated incidental services be offered through a separate affiliate that complies with the Competitive Carrier separate affiliate requirements. MCI at 10-11. As USTA noted in its comments, because these services are incidental, they do not raise the competitive issues or any specific harms that require the Commission to develop additional safeguards. Even the MFJ Court recognized that the competitive concerns that led Congress to adopt separate affiliate requirements were not present when the BOCs offered the named interLATA incidental services. USTA at 11. The Commission likewise should reject MCI's arguments here.

VII. ENFORCEMENT OF SECTIONS 271 AND 272 [¶¶ 94-107]

In an almost universal chorus, the interexchange carriers and other potential competitors to the BOCs ask the Commission to establish a system of enforcement so burdensome and punitive as to be utterly absurd. Ignoring the administrative burden on the Commission and the loss of efficiency that ultimately hurts consumers, they argue in favor of onerous reporting requirements. See, e.g., AT&T at 37 (requiring detailed reports showing each instance of affiliate service and each instance of service to non-affiliate); TRA at 19 (arguing that all affiliate transactions must

be filed with the Commission and made available for public inspection); TCG at 22-23 (quarterly reporting of all service rendered to affiliate and to competitors). Ignoring fundamental principles of due process, they ask the Commission to presume that the BOCs are guilty of misconduct and require BOCs to prove their innocence. See, e.g., TCG at 22-23; AT&T at 53. And, ignoring the statutory language, they urge the Commission to adjudicate under Section 271(d)(6) (and its 90-day time deadlines) any assertion of BOC misconduct -- even though Section 271(d)(6) expressly limits itself to addressing allegations that a BOC has ceased to satisfy the conditions for entry into in-region, interLATA services. See, e.g., Time Warner at 38; LDDS at 30. None of these radical suggestions are appropriate -- and many of them are wholly unlawful.

A. Mechanisms to Facilitate Enforcement of the Separate Affiliate and Nondiscrimination Safeguards of Sections 271 and 272 [¶¶ 94-96]

Contrary to the assertions of the interexchange carriers, there is no reason for the Commission to impose additional disclosure requirements beyond those expressly articulated in Section 272 itself. See MCI at 50-51; AT&T at 37-38. Under Section 272, BOCs must reduce all affiliate transactions to writing and make them available to the public and submit biennial audits concerning compliance with accounting, structural separation, and nondiscrimination requirements. There is no requirement that the BOCs file with the Commission detailed reports concerning non-affiliate transactions, nor should there be. Sophisticated competitors like AT&T, MCI and Sprint will be able to detect and protest any suspected discrimination in service, while Section 272's express requirements ensure that the Commission has enforcement information at its disposal. See USTA at 31-33. Because Congress already has specified the type of reporting that is necessary to eliminate the potential for anticompetitive conduct, no further regulation is required.

Notwithstanding the statute's clear language and Congress' obvious intent, AT&T argues that not even the disclosures required by Computer III are sufficient. Instead, AT&T suggests that