RECEIVED

SEP 27 1996

FEDERAL COMMUNICATIONS COMMISSION
OFFICE OF SECRETARY

FEDERAL COMMUNICATIONS COMMISSION
Washington, D.C. 20554

In the Matter of	)	
	)	
Section 257 Proceeding to Identify and Eliminate Market Entry Barriers for Small Businesses	)	**GN Docket No. 96-113**
	)	
	)	

To: The Commission

DOCKET FILE COPY ORIGINAL

COMMENTS OF THE
COMPETITIVE TELECOMMUNICATIONS ASSOCIATION

The Competitive Telecommunications Association ("CompTel") offers the following comments in response to the Commission's Notice of Inquiry in the above-captioned matter.

INTRODUCTION

CompTel is the principal industry association of competitive telecommunications carriers. Included among the CompTel membership are companies ranging in size from several billion dollars in annual revenues to those realizing less than one million dollars per year. Of nearly 200 carrier members, only 12 have revenues exceeding $100 million. And while $100 million in revenues is large in some industries, it is less than three-tenths of one percent of the largest long-distance carrier and less than one percent of any Regional Bell Operating Company ("RBOC") or GTE. Thus, CompTel's membership includes dozens of smaller carriers which have an interest in FCC rules and policies pertaining to small business.

Owing in large part to the pro-competitive federal and state regulatory policies, the marketplace trend over the last 20 years has clearly been in the direction of lowering barriers to entry. For example, in 1974 a new long-distance entrant would have to construct, operate and maintain its own microwave, cable or satellite network

No. of Copies rec'd 0+6
List A B C D E

By 1980, resale was possible so long as the carrier could purchase and operate its own switch. By 1988, the availability of local exchange carrier ("LEC") billing allowed even smaller carriers to specialize in operator service calling, without the need for large marketing budgets or staff. And by 1990, switchless resale became possible, eliminating even the expense and technical burden of buying and operating a switch. A carrier could operate simply by purchasing bulk services and reselling them. Around 1992, this evolution took another step, when prepaid calling cards allowed the purchase and resale of long-distance service on an individual call basis. A single individual with no knowledge of engineering could become a telecommunications carrier. This signified the removal of nearly all technical barriers to market entry. As discussed below, however, other barriers remain.

I. Marketplace Characteristics

CompTel is in the process of compiling data on telecommunications carriers that offer interexchange service in the United States. While this information will be published in its complete form within the next few months, certain preliminary findings from this survey may prove helpful to the Commission in this investigation.

First, CompTel has identified approximately 750 entities within the U.S. that offer interexchange telecommunications services. Of these, approximately 225 responded to the CompTel survey. Several initial results of this survey are relevant to this proceeding.

A. Most Carriers Are Small Businesses

The Commission's recent Report and Order in CC Docket Nos. 96-128 and 91-35 ("Payphone Compensation Order")[1] identified 22 carriers with annual interexchange revenues of more than $100 million. Obviously, then, the approximately 728 remaining carriers have less than $100 million in annual gross revenues.

The 225 respondents to the CompTel survey included all of the 22 carriers with $100 million or greater yearly revenues except AT&T, Alascom, Midcom Communications and Tel-Save. The survey showed the following.

Annual Revenues	Carriers	Average Employees
$0-10 million	117 (52%)	28
$10-25 million	40 (18%)	75
$25-100 million	44 (21%)	159
$100-500 million	12 (6%)	649
over $500 million	6 (3%)	19,833

While this data finds 70 percent of carriers have less than $25 million in annual revenues, in fact the proportion undoubtedly is much higher. The Commission's own statistics indicate that there are 22 carriers with more than $100 million in revenue, and CompTel's survey includes 18 of them. Thus, of the 525 carriers not responding to the survey, four have revenues over $100 million and 521 are smaller. If skewed at all, then, the survey results

[1] *Implementation of the Pay Telephone Reclassification and Compensation Provisions of the Telecommunications Act of 1996*, CC Docket Nos. 96-128 and 91-35, FCC 96-388 (released September 20, 1996).

actually understate the proportion of small carriers in the marketplace.

These figures confirm that small telecommunications carriers are numerous and growing. Perhaps more importantly, they provide a degree of entrepreneurial spirit and creativity that brings many public benefits. These small companies often are the first to identify and exploit a new opportunity or market trend as they struggle to find a marketplace niche. The result is a vibrancy and consumer responsiveness that would be lacking in a market closed to entrepreneurs and new entrants. It is this public benefit which merits the Commission's attention and enactment of policies to ensure its continuation.

II. Obstacles To Market Entry

Small carriers still face many hurdles in entering the telecommunications market. In general, these can be placed into one of three categories: (1) access to capital; (2) regulatory requirements; and (3) dependence on suppliers who also are competitors.

A. Access To Capital

As a rule, bigger companies have better borrowing power. Because of their size, they are able to arrange financing from equipment manufacturers and financial institutions more easily, at better interest rates, and on more favorable terms and conditions.

In contrast, small companies often are subject to high deposit requirements and installation charges when purchasing equipment. They routinely are overlooked by larger companies in

forming strategic alliances, because of the erroneous view that they bring nothing to the table. And in financing transactions, their corporate officers often are required to forego the protection of corporate status. It is not uncommon for small business owners to be required to waive personal liability limitations, pledge their family homes, or sign personal guarantees.[2]

In other contexts, the Commission has sought to assist small businesses in overcoming their disadvantage in the financial markets. For example, in spectrum auctions the Commission has created special eligibility requirements and financing programs for small businesses. And for many years, the Commission administered a tax certificate policy which encouraged the sale of broadcast properties to minorities and women.

While CompTel has no specific proposals at this time to supplement or expand these policies, it believes the concept is sound and should be explored in this investigation. The Commission should solicit ideas from any interested party to devise ways to assist small telecommunications businesses in obtaining access to capital and credit. Further, as described below, the FCC should be increasingly aware of the financial burdens imposed on small telecommunications businesses by regulatory policies and requirements.

---

[2] See Statement of Kathryn L. Haycock, President and CEO, Call America, presented to Federal Communications Commission Forum on Small Business Market Entry Barriers, September 24, 1996.

B. Regulatory Policies

Regulatory policies often can exacerbate the problem of access to capital and credit for smaller companies. For example, in 1986 Ameritech proposed a system for operator assisted calling known as "billed party preference" ("BPP"). This system would require that all operator handling functions for operator assisted interexchange services be performed by the local exchange carrier. After ascertaining which carrier served the billed party's home telephone, the LEC would route the call to that IXC for transmission. This system would eliminate entirely those companies specializing in operator services, and close the door to future entrants. While this proposal has never been adopted by the Commission, it has been the subject of public comment on at least three occasions and as recently as this year the Commission declined to announce a final end to its consideration of BPP.[3]

For 10 years now, the FCC has allowed this threat to overhang the operator services marketplace. Every operator service provider ("OSP") financial placement document, whether public or private, must disclose the possibility that BPP will be enacted and, within three years thereafter, eliminate the marketplace. Similar questions must be discussed with lenders and prospective investors. The result is that all capital invested must be capable of full recovery within a three-year span, lest the BPP guillotine be dropped on the OSP marketplace. The cost of capital for a small OSP, then, is far higher than for AT&T, the main competitor.

---

[3] *Billed Party Preference for InterLATA 0+ Calls*, CC Docket No. 92-77, Second Further Notice of Proposed Rulemaking, FCC 96-253 (released June 6, 1996).

To compound matters, the Commission added a new threat this summer. Without any sort of cost analysis, the Commission proposed to limit OSP rates to 115 percent of the average rate for the "big three" IXCs (AT&T, MCI and Sprint).[4] Again, the cost of capital for OSPs was driven upward by a regulatory proposal.

The Commission's pending proposal to impose a rate ceiling on the charges of small operator service companies also represents a potential regulatory policy that is particularly harmful to small businesses. As discussed above, operator services provide an easier method of initial entry into the interexchange business. As a result, the marketplace is populated with many small OSPs.

These companies compete with large carriers by offering commissions and other services (e.g., billing and collection of property surcharges) to aggregators who choose the presubscribed carrier to serve public telephones. The pending proposal, if adopted, would require that OSPs charge no more than 115 percent of the rates of an average of the "big three," including any property surcharge, unless they play a consumer warning at the beginning of each call. This proposal has the practical effect of (1) banning the collection of property charges by OSPs, (2) mandating a rate structure identical to the "big three," and (3) limiting commission payments to a minimal amount. In combination, these items will present barriers to entry for small OSPs which will make start-up nearly impossible.

Another example of a regulatory policy which harms small businesses can be found in the Commission's denial of a petition

---

[4] Id.

filed by Time Machine Inc.[5] There, the Commission declined to grant Time Machine's plea for FCC preemption of state regulation of prepaid calling cards. The consequence of this ruling was that prudent prepaid calling card companies must obtain certification for intrastate interexchange calling and file and maintain a tariff in every state that regulates interexchange service (about 40). Unlike 1+ or 0+ resellers who can limit the states in which they originate traffic (and thus limit their need for state certification) to one or a few states, the portability of prepaid calling cards gives them the potential to originate intrastate calling from anywhere. The requirement for state authorization adds several months of delay and tens of thousands of dollars in expense to the cost of entry into the marketplace. Ironically, this burden afflicts only new entrants because the larger, pre-existing carriers already have intrastate certification and need only amend their tariffs.[6]

If the Commission had granted Time Machine's Petition, those regulatory delays and expenses would have been removed. Because the Petition was denied, the public utility commission ("PUC") requirements stand today as a barrier to entry.

A third example of burdensome regulatory policies creating barriers for small businesses can be found in the Commission's

---

[5] *Time Machine, Inc.*, 11 FCC Rcd 1186 (1995).

[6] Fortunately, in its recent Local Competition Order the Commission adopted national rules and guidelines to reduce the regulatory barriers to entry by small businesses into the local services marketplace. *Implementation of the Local Competition Provisions in the Telecommunications Act of 1996*, CC Docket No. 96-98, First Report and Order, FCC 96-325 (released August 8, 1996). CompTel wholeheartedly supports this approach.

Payphone Compensation Order released last week.[7] There, the FCC required all carriers that receive calls from payphones to develop tracking systems for 800-based access code calls originated at payphones, or to contract with some other carrier for tracking, to facilitate the payment of compensation to payphone owners beginning October 1, 1997. On that date, start-up prepaid calling card companies must have invested in the equipment necessary to identify 800-based access code calls originated from payphones, or contracted with a carrier who has, so that they may prepare a bill to send to themselves on behalf of Bell Atlantic and the other RBOCs. And then they must pay the compensation amount to the RBOCs.[8]

Until this Commission decision, prepaid calling cards presented the interexchange market entry strategy with the lowest hurdles. The vast expense of the tracking requirement, however, undoubtedly will greatly increase the cost of becoming a carrier in this fashion. Moreover, small carriers must provide their customers with a travel card service to compete successfully with the larger companies. These travel cards typically rely on 800-based origination. Under the new regime, carriers must track (or contract for tracking) these calls to identify which come from payphones, then identify the payphone owner and process payment.

---

[7] See note 1, supra.

[8] The Commission's stated rationale for this assignment of tracking responsibility is that the carriers receiving the calls are the beneficiaries of the calls. It is difficult to understand, however, how the carriers can be viewed as the beneficiaries of the tracking and billing system. In this perspective, because a Buyer is the beneficiary of a purchase, the Seller should be relieved of the burden of measuring and billing for its product. CompTel is aware of no instance where a marketplace has developed in this manner.

This system promises to impose financial, administrative and technical burdens on small carriers which impair them disproportionately.

Often new opportunities or developments are identified first by entrepreneurs who are less experienced and sophisticated about regulatory nuances than large established carriers. While CompTel would never advocate a Commission failure to enforce its own rules or to ignore consumer interests, the FCC should be careful to craft its policies in new areas precisely. An overbroad or heavy-handed approach to problem-solving can impair or destroy the creative entrepreneurial spirit which small businesses bring to telecommunications.

Another regulatory burden which impacts smaller carriers more than larger ones is the jurisdictional division of responsibility among regulators. While the FCC has essentially deregulated small carriers (basically an international Section 214 authorization and a tariff are all that is required), many of the states have not. Nearly 40 states require certification and tariffs, and some (e.g., New Mexico) still require hearings even on routine applications. As local competition develops, city and municipal governments often present additional barriers and requirements as well. It is common, for example, for an applicant for a local franchise to be asked to pay an initial application fee equal to one or two percent of estimated annual revenues and five percent of revenues on an on-going basis as a franchise fee, plus agree to provide free services to schools, hospitals and other local government locations. Nearly always, these demands far exceed the

requirements imposed on the existing LECs. Whether justified or not, the task of monitoring and compliance with so many different regulations can be extremely cumbersome for smaller companies. The mere fact that there are dozens of different regulations is a serious obstacle to small carriers. A single set of nationwide guidelines set by the FCC is often the most effective way to lower regulatory barriers to entry for small carriers.

C. Competitive Considerations

A third category of barriers to entry for small telecommunications carriers is the dependence of many such companies on their competitors for services. Small carriers will face numerous such entry barriers as they seek to add local services to their menu of offerings. New, competitive providers who enter the local service market under the market opening provisions of the 1996 Act face the same bottleneck disadvantages that the long distance industry has labored under since divestiture. For the foreseeable future, new entrants will be forced to rely on incumbent LECs' ("ILECs") facilities and services for origination and termination of their customers' local traffic. With the ILEC as a direct competitor, the potential for anticompetitive abuse remains enormous.

The establishment of fair, reasonable wholesale rates for the resale of ILEC retail services is essential. Indeed, the only practical opportunity for small companies to be able to provide local and long-distance services to their customers for the foreseeable future may be through an economically rational resale regime. If a carrier wishes to resell an ILEC's existing retail

services, it must be permitted to do so at prices which are discounted by the cost of all services and functions assumed by the reseller. The FCC's new local competition rules will play a pivotal role in ensuring that all carriers, including resellers, have an opportunity to serve their customers in a competitive environment.

Another example can be found in the fact that Bell Companies soon will be empowered to become involved in the selection of the interLATA carrier to serve their public payphones. The likely outcome of this development is that the opportunities to serve those payphones as the presubscribed carrier will be reduced substantially. The RBOCs have many incentives to discriminate and few to choose small carriers (unless they choose a single one which they can purchase at a later date).

Similarly, small carriers are dependent upon the ILECs for billing and collection services. Again, as the Bell Companies themselves enter the long-distance business, they will have incentives to stop providing billing and collection services for smaller competitors.

These competitive barriers to entry may only be reduced, in the short run, by continued FCC vigilance against discrimination and other anticompetitive conduct. To maximize the benefits of this process for small carriers, the Commission should consider ways to make the invocation of FCC enforcement processes as easy as possible. For example, the existing system is more costly, unwieldy and time-consuming than is acceptable for many small carriers unless the issue is one of survival. The Commission

should explore ways to expedite the formal complaint process and to make alternative dispute resolution more effective. These actions could enable small carriers to enforce their legal rights quicker and with less expense.

CONCLUSION

Small carriers provide a level of innovation and vibrancy to the marketplace that cannot be matched by larger companies. This is the essence and the genius of the free enterprise system. In a fast-moving industry like telecommunications, these traits are particularly important, especially in identifying and implementing new consumer produces and services. The Commission should do whatever it can to nurture small businesses and to make the environment as friendly as possible for them.

Respectfully submitted,

THE COMPETITIVE TELECOMMUNICATIONS ASSOCIATION

By: Danny E. Adams

Danny E. Adams
Kelley Drye & Warren, LLP
1200 Nineteenth St., N.W.
Suite 500
Washington, D.C. 20036
(202) 955-9600

Genevieve Morelli
Carol Ann Bischoff
Competitive Telecommunications Association
1140 Connecticut Avenue, N.W.
Suite 220
Washington, D.C. 20036

September 27, 1996