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

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Federal Communications Commission
Office of Secretary

In the Matter of	)	
	)	
Implementation of the Non-Accounting Safeguards of Sections 271 and 272 of the Communications Act of 1934, as amended	)	CC Docket No. 96-149
	)	
Implementation of the Telecommunications Act of 1996: Accounting Safeguards Under the Telecommunications Act of 1996	)	CC Docket No. 96-150

CONSOLIDATED PETITION FOR RECONSIDERATION

Pursuant to 47 C.F.R. § 1.429(a), Cox Communications, Inc. ("Cox"), by its attorneys, hereby submits its *Consolidated Petition for Reconsideration* of the Commission's *Orders* in the above-captioned proceedings.[1/] Despite the Commission's recognition in other contexts of the continued need to restrain the Bell Operating Companies ("BOCs") from market abuses in an era of emerging competition, the *Orders* fail to adopt safeguards that will act to check anticompetitive BOC behavior in certain emerging or competitive markets.

The Commission has taken an inappropriately constricted and minimalist approach to implementing the 1996 Act's required competitive safeguards. Adequate oversight of potentially

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1/ As an emerging facilities-based carrier of wireline and wireless telecommunications services, Cox is an interested party in these two proceedings within the meaning of 47 C.F.R. § 1.429(a). Cox has submitted a consolidated *Petition for Reconsideration* because of the interrelated nature of the competitive safeguards issues involved in the two above-captioned *Orders*. *See Implementation of the Non-Accounting Safeguards of Sections 271 and 272 of the Communications Act of 1934, as amended,* First Report and Order and Further Notice of Proposed Rulemaking, CC Docket No. 96-149, FCC 96-489 (released December 24, 1996) ("*Non-Accounting Safeguards Order*"); *Implementation of the Telecommunications Act of 1996: Accounting Safeguards Under the Telecommunications Act of 1996*, Report and Order, CC Docket No. 96-150, FCC 96-490 (released December 24, 1996) ("*Accounting Safeguards Order*"); (collectively the "*Orders*").

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huge BOC investments in competitive services will be critical during the next few years as new entrants struggle to become established against the incumbent BOCs. The minor changes the Commission has made to its pre-existing accounting and non-accounting safeguards are not responsive to the 1996 Act's stated concern that BOCs can make use of market power to thwart competition, nor do they address the changing nature of BOC investment in non-regulated businesses that will inevitably over time share substantial common costs with regulated BOC activities. At the very least the Commission must make clear on reconsideration that neither of the *Orders* should prejudice the outcomes of pending rulemakings to establish vital competitive safeguards for BOC in-region participation in CMRS or video services.

I. EXISTING NONSTRUCTURAL SAFEGUARDS ARE NOT SUFFICIENT TO PROTECT TELEPHONE EXCHANGE RATEPAYERS AND COMPETITION

Sections 271 and 272 of the 1996 Act set forth minimum safeguards required by Congress for BOC entry into certain new market segments. Pursuant to its implementation of these Sections in the *Non-Accounting Safeguards Order*, the Commission asked what safeguards it should adopt for "incidental interLATA services" such as interLATA commercial mobile radio services ("CMRS") and video programming.[2/]

Section 271(h) directs the Commission to ensure that BOC provision of incidental interLATA services "will not adversely affect telephone exchange service ratepayers or competition in any telecommunications market." The *Non-Accounting Safeguards Order* fails to implement this requirement. Despite explicit findings in other dockets that additional safeguards

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2/ *See Implementation of the Non-Accounting Safeguards of Sections 271 and 272 of the Communications Act of 1934, as amended,* Notice of Proposed Rulemaking, CC Docket No. 96-149, FCC 96-308 (released July 18, 1996) at ¶ 37.

are required for the provision of BOC in-region CMRS and video services, the *Non-Accounting Safeguards Order* concludes that the Commission need take no action beyond confirming the application of its existing accounting safeguards.[3] No consideration is given to contemporaneous Commission findings that, despite the existing accounting safeguards, incumbent local exchange carriers ("LECs") continue to abuse their market power.

The Commission last August tentatively concluded that existing safeguards on incumbent LEC in-region CMRS are insufficient to prevent the LECs from abusing their position of control over interconnection to the public switched network.[4] In the *Non-Accounting Safeguards Order* the Commission inexplicably proclaims that existing nonstructural safeguards are sufficient.[5] These incompatible positions must be reconciled in favor of effective safeguards. There is record evidence of LEC market power abuses in both the wireline and wireless markets, especially where a BOC is permitted to integrate regulated monopoly and competitive services.[6] Whenever monopoly and competitive services are integrated, Cox's consistent view is that

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3/ *Non-Accounting Safeguards Order* at ¶ 97.

4/ *See Amendment of the Commission's Rules to Establish Competitive Service Safeguards for Local Exchange Carrier Provision of Commercial Mobile Radio Services*, Notice of Proposed Rulemaking, Order on Remand, and Waiver Order, WT Docket No. 96-162, FCC 96-319 (released August 13, 1996) at ¶ 34 ("*CMRS Safeguards Notice*").

5/ *Non-Accounting Safeguards Order* at ¶ 97.

6/ *See Amendment of the Commission's Rules to Establish Competitive Service Safeguards for Local Exchange Carrier Provision of Commercial Mobile Radio Services,* Reply Comments of Cox Communications, Inc., WT Docket No. 96-162 (filed October 24, 1996).

structural separation should be the preferred approach. In any event, enhanced accounting, CPNI and joint marketing rules are necessary to protect the opportunity for competition.[7/]

The Commission also acknowledged last spring that current Part 64 rules are inadequate to regulate substantial anticipated LEC investment in common plant for non-regulated activities such as video programming.[8/] The Commission now concludes that Part 64, along with Part 32 and price caps, will protect ratepayers from cross-subsidies. The *Non-Accounting Safeguards Order* neglects to account for the pending *Cost Allocation* proceeding or address the arguments made by Cox and others in response to the *Cost Allocation Notice* that support the Commission's tentative conclusions that price caps and the current affiliate transaction and cost allocation rules are insufficient to protect against cross subsidization.

The Commission has recognized in other proceedings the shortcomings of a price cap system that allows price cap LECs to choose and switch annually between different sharing options.[9/] Even if a LEC elects the price cap no-sharing option in one year, it still has the incentive to systematically misallocate costs to regulated services to reduce regulated earnings and avoid sharing obligations in future years. Indeed, recent press reports show that systematic cost misallocation is more than just a theory — the BOCs continue to face fines from state

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7/ *Id.* at 7-9.

8/ *See Allocation of Costs Associated with Local Exchange Carrier Provision of Video Programming Services,* Notice of Proposed Rulemaking, CC Docket No. 96-112, FCC No. 96-214 (released May 10, 1996) at ¶¶ 16-21 ("*Cost Allocation Notice*").

9/ *See, e.g., In the Matter of Access Charge Reform*, Notice of Proposed Rulemaking, Third Report and Order, and Notice of Inquiry, CC Docket No. 96-262, CC Docket No. 94-1, FCC 96-488 (released December 24, 1996). *See also Allocation of Costs Associated with Local Exchange Carrier Provision of Video Programming Services,* Reply Comments of Cox Communications, Inc., CC Docket No. 96-112 (filed June 12, 1996) at 2-3.

regulators because of instances that come to light of anticompetitive cross subsidization.[10] The Commission recognized in the *Cost Allocation Notice* that current rules were not designed to accommodate an incumbent LEC's use of the same network facilities to provide competitive and noncompetitive offerings. The Commission has yet to resolve the "basic problem addressed in [that] proceeding [of] how to allocate common costs between the nonregulated offerings that will be introduced by incumbent local exchange carriers and the regulated services they already offer."[11]

The Commission has failed to resolve these issues in the *Non-Accounting Safeguards Order.* On reconsideration the Commission must clearly state that, whatever regime it determines should apply to Section 272 affiliates to protect against cross-subsidies, it is not sufficient to protect competition where a BOC integrates operations that share common costs. At a minimum, the Commission must confirm that its determinations in these proceedings do not supersede the critical work the Commission must still complete in its *CMRS Safeguards* and *Cost Allocation* notices.

10/ NYNEX, for example, will pay more than $100 million in fines under the terms of a settlement between it and the New York Public Service Commission due in large part to impermissible affiliate transactions. Linda Haugsted, *Cross-Allocation Behind $100M Nynex Fine*, MULTICHANNEL NEWS, February 17, 1997, at 28. In fact, the $100 million was a compromise amount that reduced the administrative law judge recommendation for a $300 million fine. Ameritech is also under scrutiny in Illinois for improperly funding cable projects with telephone ratepayer money. *Id.*

11/ *Cost Allocation Notice* at ¶ 2.

II. PART 64 RULES DO NOT PROVIDE INTERESTED PARTIES WITH THE DATA NECESSARY TO DETECT CROSS SUBSIDIZATION

The Commission acknowledged in the *Accounting Safeguards Order* that the 1996 Act likely will increase the scope of BOC non-regulated activities because they may now provide, on an integrated basis, previously prohibited services.[12/] When the Commission developed the Part 64 rules ten years ago, BOC service offerings now allowed by the 1996 Act were not contemplated. However, without explanation, the *Accounting Safeguards Order* proclaims that the cost allocation rules were designed to accommodate the growth of the new non-regulated BOC activities now allowed.[13/]

The Part 64 cost allocation rules were developed in 1986 when BOC non-regulated activity was limited. The rules on non-regulated costs were intended to "keep regulated common carriers from using the revenues from their regulated services to subsidize nonregulated enterprises and . . . ensure that ratepayers receive their appropriate share of the benefits arising from the offering of regulated and nonregulated services on a structurally unseparated basis."[14/] The accounting reports pursuant to Part 64 may have been adequate when BOCs had limited unregulated businesses not earning high revenues as a portion of total BOC revenues. Those accounting reports no longer are adequate where business circumstances have changed.

Abbreviated accounting treatment is not appropriate in this new era, particularly when the cost of requiring separate reporting for discrete non-regulated business activity is *de minimis*

12/ *Accounting Safeguards Order* at ¶ 26.

13/ *Accounting Safeguards Order* at ¶ 26. As recently as 1994, all BOC non-regulated services put together accounted for less than 1 percent of total BOC plant. *See* FCC ARMIS Report 43-01, September 30, 1994.

14/ *Report and Order*, 2 FCC Rcd 1298, 1307 (1987).

and the information is undoubtedly collected by the BOCs for their own internal accountability. The summary of costs required under current Part 64 cost accounting rules provides virtually no information about investments grouped together under non-regulated.[15] Without further detail it is impossible to identify service-specific costs and match them to regulated costs. Further, because these rules require allocation of costs only between common carrier and non-common carrier services using a carrier's own forecast of relative use, there is no way to know that costs are in fact reasonably allocated. The Commission and third parties reviewing the filings have no meaningful way to challenge a carrier's unreasonable forecast. Finally, even assuming the Commission modifies Part 64 to require that BOCs break out CMRS, video and other non-regulated costs from monopoly landline and other investments, the Commission currently has a patently inadequate policy directing BOC determinations of what constitutes a CMRS or video cost as opposed to a telephone cost for purposes of assessing common costs. As the LECs showed in their excursions into video dialtone, they have every intention of loading common costs onto telephony ratepayers.[16]

15/ *See, e.g., Amendment of the Commission's Rules to Establish Competitive Service Safeguards for Local Exchange Carrier Provision of Commercial Mobile Radio Services,* Comments of Cox Communications, Inc., WT Docket No. 162 (filed October 3, 1996) at 5-7.

16/ In Omaha, Nebraska, the Commission has apparently let U S West allocate all of the common costs associated with its video dialtone "trial" — a figure approaching $35 million — to telephone ratepayers. *See U S West Telephone Company Files Revisions To Its Cost Allocation Manual Reflecting The Change of its Video Dialtone Trial To A Cable System,* Comments of Cox Communications, Inc., AAD 96-82 (filed August 30, 1996) at 2. This agenda is not unique to U S West. Cox demonstrated during the Dover tariff investigation that Bell Atlantic intended to allocate its video dialtone costs to ratepayers, employees and customer/competitors rather than to shareholders. *See Bell Atlantic Telephone Companies Revisions to Tariff F.C.C. No. 10, Rates, Terms, and Regulations for Video Dialtone Service in Dover Township, New Jersey,* Opposition to the Bell Atlantic Direct Case filed by Cox Enterprises, Inc., Transmittal Nos. 741,

(continued...)

If the Commission fails to adopt rules that require BOCs to provide cost information that distinguishes between different non-regulated activities, detection of cross subsidization will be virtually impossible because a single lump sum result for all non-regulated activities can mask serious over or under-reporting problems. Disclosure requirements must be imposed on all BOC affiliates involved with non-regulated activities to avoid corporate structures that otherwise would allow BOCs to camouflage their true costs of entering competitive businesses.[17/]

It is critical that the Commission establish specific guidelines for the cost allocation of non-regulated BOC activities. The question of what is or is not a regulated cost should not be answered by the BOCs alone because the BOCs retain significant incentives to misallocate their costs to regulated operations. Moreover, federal and state regulators must have access to sufficient financial data to make informed decisions on what costs properly should be included in the telephone rate base.

The *Accounting Safeguards Order* appears to assume that, because Section 272 provides for separate subsidiaries for some competitive BOC businesses, significant regulated and non-regulated common costs will not be incurred. This is plainly not the case for those competitive services where separate subsidiaries have not yet been required. It would not be the case even with separate subsidiaries for those services such as video programming and CMRS where the aggregate value of common costs is likely to be immense.

16/ (...continued)
786, CC Docket No. 95-145 (filed November 30, 1995) at 4-12. The Commission never ruled on the lawfulness of the Dover tariff.

17/ The BOCs have a history of using corporate structures to avoid regulatory obligations. For example, some, such as BellSouth, have shifted directory operations to "unregulated" subsidiaries to shield Yellow Pages revenues from state regulators.

The Commission must adopt rules sufficient to detect and deter BOC abuse.[18] The current cost allocation rules are insufficient as long as rules have not been adopted pursuant to the *Cost Allocation Notice.* If, however, the Commission does not choose to impose meaningful oversight on Section 272 affiliates on reconsideration here, the Commission must not indirectly use its findings in the *Accounting Safeguards Order* to determine the outcome of the pending *CMRS Safeguards* and *Cost Allocation* notices.

III. THE *ORDERS* VIOLATE THE 1996 ACT AND CONFLICT WITH PRIOR COMMISSION FINDINGS

Section 254(k) requires the Commission to ensure that carriers not "use services that are not competitive to subsidize services that are subject to competition." Unless the Commission adopts appropriate non-accounting safeguards, and requires BOCs to disclose all costs and revenues associated with CMRS and video services in their ARMIS reports on a line-item basis, cross subsidization will not be detectable and the Commission will fail to meet the mandates of Section 254(k).

The Commission has based its failure to adopt enhanced safeguards on the fallacious assertion that current rules were designed with the BOC Section 272 non-regulated activities in mind. The Commission's own findings as to BOC CMRS and video activities suggest that the Commission must reconsider its decision not to adopt sufficient accounting and non-accounting safeguards. At the very least, the Commission must confirm that its decision on Section 272

18/ *See, e.g., Accounting Safeguards Order* at ¶ 20 ("MCI asserts that we must adopt safeguards stricter than our existing accounting safeguards to account for the increased opportunities for BOCs to enter new lines of nonregulated businesses. . . . In particular, MCI suggests that we adopt a rule requiring carriers to maintain a complete audit trail of all cost allocations and affiliate transactions.").

safeguards does not apply to integrated in-region BOC operations where the potential for cross-subsidies on common costs is enormous.

Respectfully submitted,

COX COMMUNICATIONS, INC.

Christina H. Burrow

Werner K. Hartenberger
Laura H. Phillips
Christina H. Burrow

Its Attorneys

DOW, LOHNES & ALBERTSON, PLLC
1200 New Hampshire Avenue, N.W.
Suite 800
Washington, D.C. 20036
(202) 776-2000

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