Cost Proxy Model Criteria

U S WEST Criteria	Staff Analysis Criteria	Joint Board Criteria	BCPM Meets Joint Board Criteria
The proxy cost model should accurately reflect the elements which it purports to reflect.			✔ BCPM is completely documented, user friendly, and easily verifiable. All model equations and logic are clearly stated and described. Underlying data is specifically documented and validated by actual experience in installing state-of-the-art networks and technology.
The proxy cost model and its application to the targeting of high-cost support to specific geographic areas should assure the continued provision of affordable basic telephone service and encourage the efficient evolution of local competition.			✔ The BCPM has the ability to target support to a CBG and will have the ability to target to smaller geographic areas in the next phase of the model. ✔ The network designed by the BCPM provides sufficient network distribution to provide high quality, affordable service.
	Use of forward looking economic cost as a basis for pricing.		✖ Proxy cost models <u>should not</u> be used to develop forward looking economic cost as a <u>basis for pricing</u>.

Cost Proxy Model Criteria

U S WEST Criteria	Staff Analysis Criteria	Joint Board Criteria	BCPM Meets Joint Board Criteria
	Ability to measure costs relating to a narrowband network.		✔ The network designed by the BCPM is the least cost method of providing telephone service.
	Use of proxy models for multiple objectives.		✔ The use of a single model for multipurpose calls for more complexity in the model. ✔ The BCPM could be refined to perform multiple functions, in fact work is in progress to allow multiple capabilities.

ATTACHMENT B

Before the
FEDERAL COMMUNICATIONS COMMISSION
Washington, DC 20554

RECEIVED

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FEDERAL COMMUNICATIONS COMMISSION
OFFICE OF SECRETARY

In the Matter of	)	
	)	
Implementation of the Local Competition Provisions in the Telecommunications Act of 1996	)))	CC Docket No. 96-98

PETITION FOR ORDER DIRECTING THAT DISCOVERY BE PERMITTED

U S WEST, Inc. ("U S WEST"), hereby petitions the Federal Communications Commission ("Commission") to enter an order directing that AT&T Corp. ("AT&T") and MCI Telecommunications Corporation ("MCI") make available for discovery, review and copying all documents related to the so-called "Hatfield Models" (including any variations of those Models) submitted in various configurations in the instant docket. Specifically, U S WEST requests that the Commission direct that MCI and AT&T permit review of the Models themselves and any and all inputs to those Models, and to respond to interrogatories according to the schedule set forth herein. In support hereof, the following is submitted.

In their submissions in this docket, AT&T and MCI have relied heavily on something called the "Hatfield Models."[1] These "Models," which purport to

[1] See AT&T's Comments, filed herein May 16, 1996 at 51-54 and attached Affidavit of William J. Baumol, Janusz A. Ordover, and Robert D. Willig at 15-20 ("AT&T Comments"); MCI's Comments, filed herein May 16, 1996 at iii, 59-70 and Attachment 1.

Before the
FEDERAL COMMUNICATIONS COMMISSION
Washington, DC 20554

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	)	
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demonstrate what local exchange carrier ("LEC") total service long run incremental costs ("TSLRIC") are for network elements, form the primary basis for the demands of AT&T and MCI that incumbent LEC prices for network elements be set at rates which U S WEST claims are clearly unreasonable and confiscatory. So heavily do AT&T and MCI rely on these "Models" that AT&T actually suggests that the "Models" be used as establishing a presumptively valid pricing and costing standard in all interconnection negotiations.[2]

Unfortunately for those trying to analyze what AT&T and MCI are up to in this docket, the Hatfield Models remain a secret. AT&T and MCI have repeatedly refused to divulge either the inputs used in the Hatfield Models or the algorithms which the Models use to process the unknown information. In other words, the actual functioning of the Hatfield Models is a complete mystery. In the one case in which U S WEST personnel obtained a brief ability to look at an actual Model (in a recent state proceeding in Utah), U S WEST's representative was required to sign a non-disclosure agreement agreeing not to use the information received during his examination in any other regulatory proceeding -- an agreement which precludes U S WEST's representative from divulging what was learned about the Model to anyone working on the instant proceeding before the Commission. To make matters worse, AT&T and MCI have apparently developed a new Hatfield Model for

[2] AT&T Comments at 54.

the purpose of their reply comments in the instant docket, one which is different in undisclosed ways from the earlier Models.[3]

AT&T's and MCI's refusal to make the Hatfield Models public would make a mockery of any proceedings in which they were used. There has never been a legitimate reason for AT&T's and MCI's reluctance to make the Models public -- indeed, one excuse, that certain publicly available Bell Communications Research ("Bellcore") information used in the Models was "copyrighted" and thus not subject to photocopying -- is a transparent sham. The Hatfield Models do not deal with AT&T's or MCI's confidential or proprietary business plans -- they deal with a methodology by which AT&T and MCI seek to obtain regulatory pricing of incumbent LEC services below the cost of providing those services. Reliance on secret data in the Hatfield Models by the Commission to support any conclusion in the instant docket would clearly countermand the dictates of the Administrative Procedure Act.[4] As no less a scholar of the statutory prohibitions against agency reliance on secret documents than MCI commented in another context:

> Unfortunately, by denying MCI access to unredacted cost support information and imposing on intervenors a nondisclosure agreement for access merely to redacted information, the Commission has violated its obligations under the Communications Act, the Administrative Procedure Act (APA) and Constitutional Due Process protections.[5]

---

[3] AT&T's Reply Comments, filed herein May 30, 1996 at Appendix D; MCI's Reply Comments, filed herein May 30, 1996 at 8-11.

[4] See Home Box Office v. FCC, 567 F.2d 9, 51-59 (D.C. Cir.), cert. denied, 434 U.S. 829 (1977); U.S. Lines v. FMC, 584 F.2d 519, 535, 539-42 (D.C. Cir. 1978).

[5] MCI's Opposition to Direct Case, CC Docket No. 94-128, filed May 11, 1995, at 26-27 (footnotes omitted).

MCI made this statement in an attempt to obtain access to U S WEST's confidential information about U S WEST's own internal operations and prices. Here the Hatfield Models relate to U S WEST's prices and costs (or Hatfield's fantasization of those costs) -- and even so AT&T and MCI refuse to make either the Models or the inputs fed into the Models available for review in the course of this docket.

We recognize that the Commission's discovery rules do not apply in the context of a rulemaking or other non-adjudicatory proceeding.[6] Nevertheless, the Commission has clear authority under its inherent powers to order that discovery proceed in a non-adjudicatory proceeding whenever justice so requires.[7] In this case a simple order directing that AT&T and MCI disclose the underlying Hatfield Models and the input data utilized in running the Models (obviously all Models need to be disclosed because of the possibility that corrections to earlier versions of the Models have exacerbated, rather than corrected, defects in the earlier versions), and answer simple interrogatories about the Models according to an expedited time schedule, should suffice to protect U S WEST's due process rights and ensure that the Commission obtains the information necessary upon which to render a reasoned decision. U S WEST will be ready to serve such interrogatories within four days of receiving the Models and the input information. A reasonable time for AT&T and

---

[6] See AT&T, 62 FCC 2d 35, 37 ¶ 6 (1976).

[7] See ITT World Communications Inc., 82 FCC 2d 282, 290 n.12 (1980); Offshore Telephone Company, 68 FCC 2d 63, 65-66 ¶ 8 (1978); AT&T Company, 73 FCC 2d 689, 694 n.12 (1979).

CERTIFICATE OF SERVICE

I, Kelseau Powe, Jr., do hereby certify that on this 10th day of July, 1996, I have caused a copy of the foregoing **SUPPLEMENT TO PETITION FOR ORDER DIRECTING THAT DISCOVERY BE PERMITTED** to be served via first-class United States Mail, postage prepaid, upon the persons listed on the attached service list.

Kelseau Powe, Jr.

***Via Hand-Delivery**

(CC9698G.COS/BM/lh)
Phase I

ATTACHMENT C

Before the
FEDERAL COMMUNICATIONS COMMISSION
Washington, DC 20554

AFFIDAVIT OF GLENN H. BROWN

I, Glenn H. Brown, hereby state the following information is true and correct to the best of my knowledge, information and belief.

1. I am Executive Director, Public Policy, U S WEST, Inc.

2. My address is Suite 700, 1020 19th Street, N.W., Washington, DC 20036

3. In December of 1996, I participated in a panel discussion at an industry conference. Also on this panel was Mr. Richard Clark, Division Manager of AT&T Corp. During the question and answer session Mr. Clark was asked whether AT&T was pricing its competitive services at TELRIC. His answer was that in competitive procurement cases for the provision of wholesale interLATA services to RBOCs, deals were being proposed at around 1.5 cents per minute which was about the TELRIC for interLATA service.

I hereby declare under penalty of perjury that the foregoing is true and correct to the best of my knowledge and belief.

Dated: February 18, 1997

Glenn H. Brown

Subscribed and sworn to before me this 18th day of February, 1996, by Glenn H. Brown.

My commission expires:
8-30-2000

Patrice D. LaBadie
Notary Public

PATRICE D. LaBADIE
NOTARY
PUBLIC
STATE OF COLORADO

ATTACHMENT D

The Optimization Problem Used to Determine Network Fill Factors

The best way to think of the optimization problem is to look at one "reinforcement" cycle. When cable is initially installed, whether it be feeder, distribution or transmission, the planner must decide how to accommodate growth in the demand for pairs along the route. There are two options available; 1) Place enough capacity to accommodate growth until the cable reaches the end of its life and must be replaced, or; 2) Reinforce the route periodically by installing additional capacity, initially installing only enough capacity to accommodate growth until reinforcement. The decision between these two options depends on the useful life of the cable, the cost of installation, the cost of cable, the cost of money and the rate of growth of demand.

Think of making this decision at the time of initial installation. You have paid a contractor to make the installation whether it be a trench or poles and now you must decide whether to put in enough pairs to cover growth [1]until some possible reinforcement or until the cable must be replaced. In either case the cost of one cycle, from the time of having a trench available until the same condition in the next cycle will be:

$$C = c(Ne^{\gamma t} - 1) + Ie^{-rt}$$

Where:

C = Total cost.
γ = Rate of growth including breakage.
c = Cost of adding one pair to a sheath.
I = Cost of installation, i.e. opening, installation and closing a trench.
r = Cost of money.
t = Time in years to reinforcement or replacement.

The first term on the left hand side is the cost, in current dollars, of adding sufficient pairs to the cable to accommodate growth for t years. The second term is the present value of the cost of installation t years in the future. That is, the amount of money that would have to be invested at a rate of interest r, to yield I dollars in t years. Note that the first term is increasing in t because the number of pairs increases the longer reinforcement is delayed. The second term is decreasing in t because the longer the investment has to accumulate interest, the smaller the required investment

Figure 1 presents the path of each of these costs and their sum as the time to reinforcement is increased. Clearly the lowest cost in this case occurs at t=T*, indicating that the least cost design includes installation of $Ne^{\lambda T^*}$ pairs and reinforcement every T* years.[2]. The initial or design fill factor will be:

$$F_D = \frac{N}{Ne^{\gamma T^*}} \text{ or simply } \frac{1}{e^{\gamma T^*}}$$

[1] Growth is assumed to include breakage.
[2] This assumes T* is less than ½ of the life of the cable.

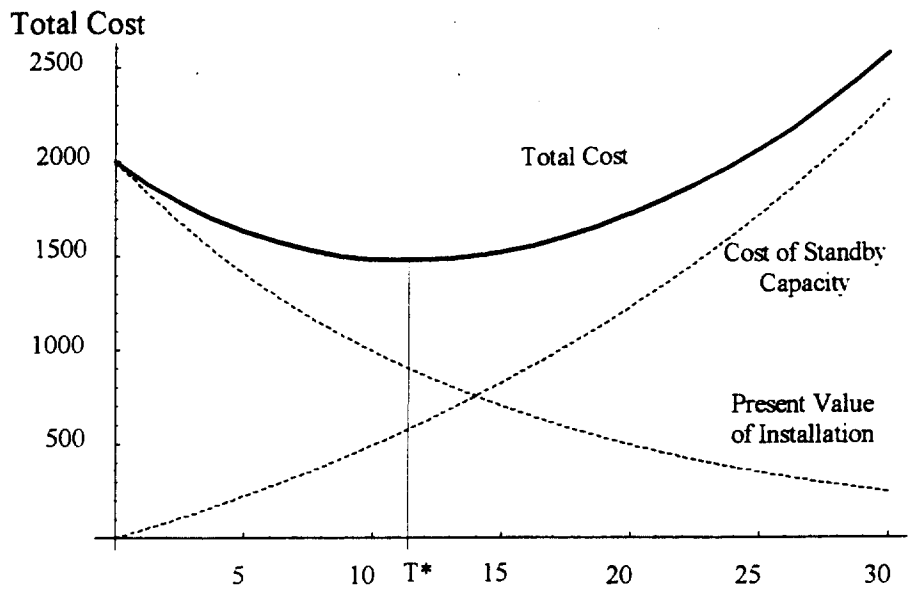


Figure 1

Although the horizontal axis used in Figure 1 is time, it is clear that by applying the above relationship between time and fill factor, the axis could easily be converted to initial fill factor.

Figure 2 shows the effect of changing growth rate. The increase in the amount of standby that must be installed results in a reduction of the optimal time to reinforcement from T^* to T^{**}.

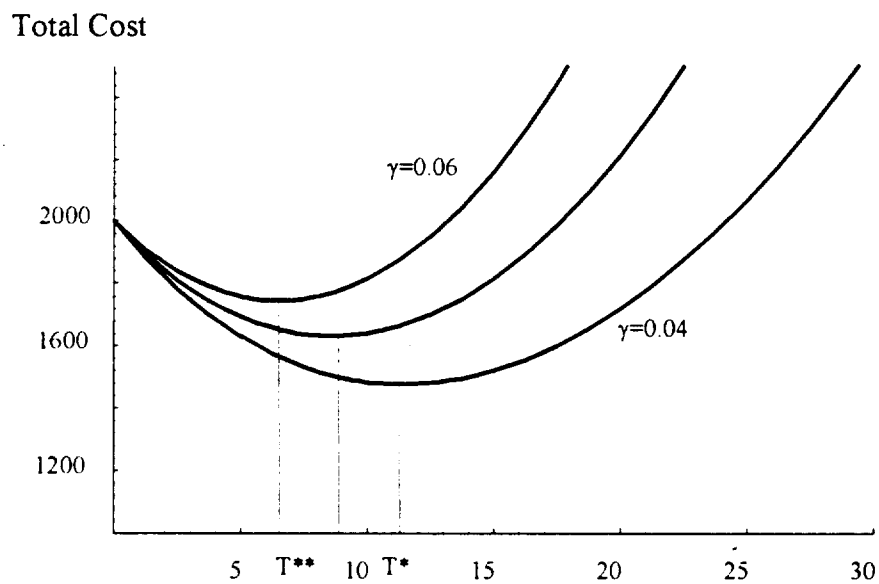


Figure 2

Figure 3 shows the effect of changes in the installation cost. Clearly, an increase in installation cost increases the optimal time to reinforcement. In the same way, reducing cable costs will increase the optimal time to reinforcement by reducing the cost of waiting to reinforce. Which brings us to consideration of the extreme case where T^* is greater than the useful life of the cable,

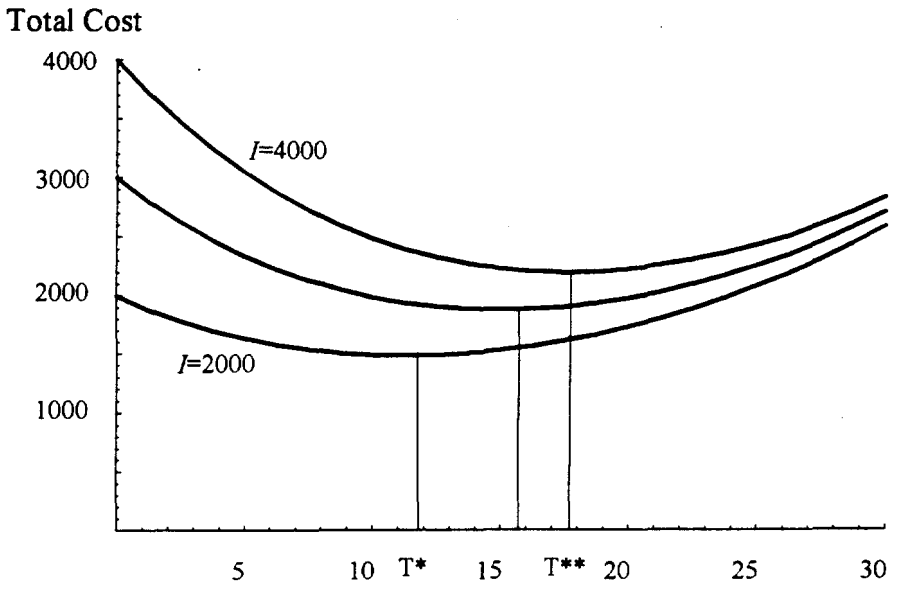


Figure 3

the typical condition in distribution plant. In this case the cable is simply designed with sufficient standby capacity to accommodate growth over the entire useful life of the cable.

The cost of installation is not the only cost that must be considered. Other costs result from the possibility of "premature" exhaustion of the cable. If growth were completely deterministic, the designer would simply have to plan for development as described above and as long as reinforcements were done on schedule the cable would never exhaust. Unfortunately, growth is not deterministic, it varies over geographic area and also over time. The increased usage of the Internet has certainly resulted in temporal variation in growth as subscribers add second lines to accommodate this usage. If the distribution of growth is know then this variation can be accounted for in the design. The simplest case to develop is that in which the cable will not be reinforced, but provided with sufficient capacity to accommodate growth over its entire useful life. In that case the total cost can be written as:

$$C = c(Ne^{\hat{\gamma}T_R} - 1) + PXe^{-rT_R}$$

Where:

C = Total cost.

N = Number of active pairs at installation.

$\hat{\gamma}$ = Design growth rate.

X = Cost of premature exhaustion of the cable.

P = Probability of premature exhaustion.

Assuming that the distribution of growth rates can be described as a normal distribution with a mean of $\bar{\gamma}$ and a variance of σ_γ the probability of exhausting the cable can be calculated as $1 - \Phi(\bar{\gamma}, \sigma_\gamma, \hat{\gamma})$.[3] The optimal design will assume the level of growth that minimizes the total

[3] $\Phi(\bar{\gamma}, \sigma_\gamma, \hat{\gamma})$ represents the probability of finding a value of growth less than $\hat{\gamma}$ in the distribution of growth rates.

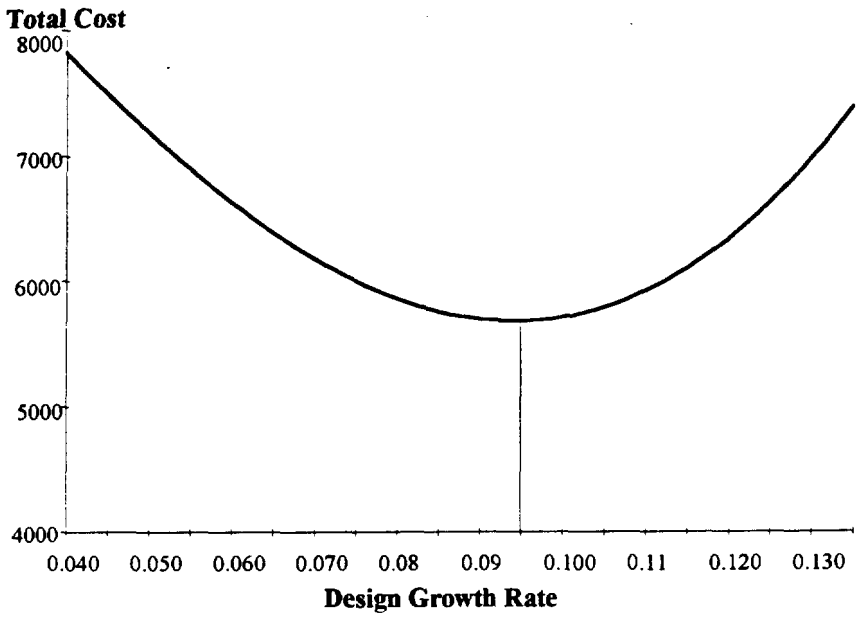


Figure 4

cost. Figure 4 shows the total cost curve with a minimum at $\hat{\gamma}$ =9.5% or a design fill factor of 0.24[4]. Note that although the horizontal axis show is design growth, it can easily be expressed as fill factor using the relationship:

$$F = \frac{N}{Ne^{\hat{\gamma}T_R}} \text{ or } \frac{1}{e^{\hat{\gamma}T_R}}$$

The designer is therefore choosing an optimal fill factor, that which minimizes the total cost including both capital cost and the additional maintenance and service cost associated with premature exhaustion of the cable.

[4] Assuming a useful life of 15 years.

The Fallacy of Reducing Cost By Increasing Fill Factor

Figure 5 illustrates the effect on cost of increasing design fill factor. C^*_S is reduced to C'_S but C^*_X is increased to C'_X, yielding a total cost larger than C^*. However, if I assume that

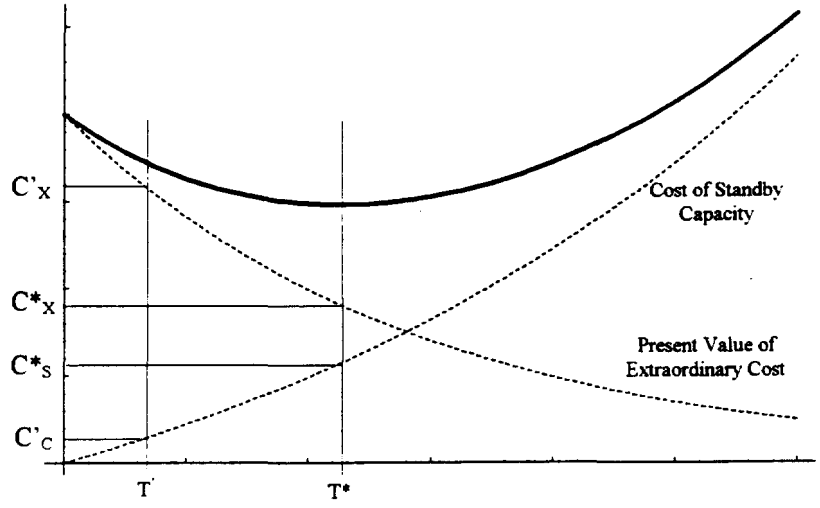


Figure 5

increasing the design fill factor effects only C_S then the change will result in an apparent total cost of $C'_S + C^*_X$ which must be less than C^*. The fallacy is obvious in this context, but when buried in a model, detecting such a fallacy is not nearly so straightforward.

Application Considerations

There are a number of reasons why not all pairs in a cable can be connected to a subscriber. First of all there is some requirement for "administrative" pairs to be used for testing and other administrative activities. More important are the requirements for replacement of pairs which are broken or otherwise become unserviceable and finally standby capacity to provide for growth as new housing or business units are added to an area or existing customers take additional lines. Because of differences in the cost structure and specificity of distribution and feeder plant, the there are differences in the way in which each of these requirements for standby capacity is met.

Distribution Plant

Distribution plant includes the facilities required to connect the customer's premises to the Serving Area Interface (SAI). One of the important characteristics of distribution plant is that the cost of reinforcement, installation of additional cable, or rearrangement of existing cable is very high relative to the cost of the cable itself. This is true even though the initial installation cost may be minimal, as in new residential areas where it may be possible to place cable in developer provided trenches. Initial installation is usually done before obstacles such as lawns, gardens, patios fences and often even streets and sidewalks have been placed. Once these obstacles are in place, the cost of placement reflects the extreme effort and cost required to avoid or replace them. In determining the optimal amount of standby capacity to include in a design, the designer must weigh the cost of additional capacity against the present value of the cost of any

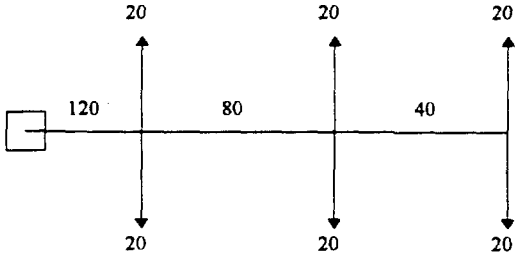
modifications, additions or penalties that might result from a lack of capacity. If the expected discounted cost resulting from exhausting the facility is greater than the cost of the additional capacity, then the least cost design will include installation of the additional capacity at initial installation. Obviously, the higher the cost of modification of the plant, the more cost effective it will be to provide sufficient capacity in order to avoid required plant modifications and penalties.

The effect of growth

One of the major difficulties in providing for growth in distribution is the customer specificity of distribution plant. For example, an average growth of 4% over 15 years would require that about twice as many pairs be available in the distribution than required at initial installation. Unfortunately those additional pairs may be required in a concentrated location such as a home converted to a business or multifamily occupancy or simply a single customer who requires several additional lines. Consider a two pair design in which all of the pairs designed to serve ten households are terminated in a common pedestal. There will initially be 20 pair available and only 10 used. If these ten households exhibit "average" growth each of the 20 pair will be in use after 15 years. That is not to say that every household will be using two pair, only that the total pairs used by the 10 households adds up to 20. Figure 5 depicts such a distribution design. Clearly, if any ten household cluster exhibits greater than average growth, something that by definition occurs 50 percent of the time, some rearrangement of the plant must be done to provide additional pairs to that location. The only way to eliminate the need for rearrangement is to provide additional pairs, over and above those required to cover "average" growth, to each pedestal.

The probability that a particular group of households will exhibit above average growth depends not only on the average growth but on the distribution of growth. If growth rate in all of the groups is very close to the average growth rate, i.e. a low variance, the probability that a group will exhibit twice the average growth will be small. However, as the variance of the growth increases, the probability that an individual group of households will exhibit such a level of growth increases substantially. The number of standby pairs provided at each group is therefore dependent upon the variance of growth as well as its mean.

Figure 6



The effect of breakage or maintenance requirements

Breakage, like growth, does not necessarily occur uniformly over the area served by the plant. Even a very small percentage of pair loss due to breakage will lead to the requirement of

additional standby pairs at each pedestal. To do otherwise would increase the probability that a costly rearrangement or reinforcement would be required.

The effect of service standards

Service standards such as a maximum allowable time to provide requested service have an effect similar to that of a very high cost of installation or rearrangement. If there is not sufficient capacity available to immediately provide service, a rearrangement or reinforcement of plant must be ordered. Unless the modification to plant can be accomplished within the allotted time, penalties may ensue, effectively increasing further the cost of the modification. The effect on customer satisfaction is also properly included in the cost resulting from the inability to serve.

Usage effects, business versus residential

The ability of businesses to utilize PBX equipment to concentrate calls can increase the variability of growth in a distribution area which serves business premises. A building that houses several small businesses, each with one or two active lines, can easily be converted to use by a single firm which might have the same number of lines but chooses to serve them through a PBX. A business might also exhibit steady growth in the lines it requires and at some point convert to a PBX, system immediately reducing the number of lines it requires. In either case the result would be that the number of active lines is reduced even though the apparent usage of each line would increase. Since this process can also occur in the opposite direction, it may be necessary to provide sufficient capacity to serve a much higher number of lines than required for the original occupant of a building.

Density effects

The density of a distribution area affects the feasibility of providing common termination for distribution pairs. If an area is very sparsely populated, perhaps only five houses will have their drops terminated at a common pedestal. Above average growth in lines required by any of the five will result in a much higher probability that providing the additional pairs will require rearrangement or reinforcement. Thus less dense areas may require a higher percentage of standby capacity, i.e. a lower fill factor.

Feeder

Feeder plant, consisting of the main arteries between the end office and the SAI, differs from distribution in several fundamental ways. First of all it consists primarily of underground rather than buried cable, making reinforcement much less expensive. Underground cable, placed in conduit which allows easy reinforcement by simple pulling additional cable into an existing duct, is cost effective in feeder because of the concentration of routes as they converge on the central office. Feeder plant may also include pair gain facilities which allow multiple transmission channels on either copper or fiber. These differences result in different optimal solutions to accommodate the need for spare capacity. The least cost time between reinforcements is determined, as described above, by the relative cost of cable and installation as well as the growth rate and the cost of capital. The trade-off is between installing a large amount of standby which allows a longer period between reinforcements and providing a small amount of standby and reinforcing more often. Note that the fill factor, the occupied number of pairs divided by the available number of pair, is the result of an economic optimization process. Since there is variability in growth, the actual time between reinforcements may be somewhat longer or shorter than the designed period. By monitoring the actual percent of the available pairs used,

reinforcement can be initiated when the feeder reaches "objective" fill. Allowing the fill of a feeder to increase beyond "objective" level increases the risk that the cable will exhaust before the additional cable can be installed.

The optimal level of "objective" fill is determined by the mean rate and variability of growth and the lead time required between initiation of reinforcement and availability of the additional facilities. The mean growth rate determines mean time between achieving objective fill and exhaustion of the cable. The variance of the growth rate is important in determining the probability that actual growth will exceed the mean and thus exhaust the cable in and unexpectedly short time. With knowledge of these variables planners choose an appropriate probability of unexpected exhaustion and an associated level for the objective fill. Notice that this objective fill level may vary with growth rates and may require adjustment where there are seasonal restrictions on installation of cable.

Variability of growth relative to distribution

The growth in feeder plant, since it combines several serving areas, is the total of the growth in those serving areas. The mean growth rate of the feeder will be the weighted average of the mean rates of the serving areas covered by the section of plant. The variance of the feeder growth rate will depend not only on the variance of the individual serving areas but also on the correlation between the growth rates. Unless the variance in growth in the serving areas in uncorrelated, i.e. the variation in growth in the areas is not related, the variation of growth in the feeder will be the same as in the areas served.

Conclusion

The design of loop plant is the result of rational economic decisions which attempt to minimize the life cycle cost of the plant. The inclusion of what appears to be excess capacity is usually simply the most cost effective way to provide reliable and timely service to subscribers. It has been shown above that the amount of standby capacity built into the network is depends not only on the growth in the network but also the variation in that growth. The variation is especially significant where the provider has an obligation to serve. Other factors affecting the decision are the cost of cable, the cost of money and the cost of installation. To the extent that these may all differ across states, differences in design fill factors are not unexpected. The above is not meant to be a manual on engineering loop plant, there are a myriad of practical details left undressed. It may, however, provide the reader with a sufficient understanding of nature of the decisions that are made in designing an efficient loop plant.

CERTIFICATE OF SERVICE

I, Kelseau Powe, Jr., do hereby certify that on this 18th day of February, 1997, I have caused a copy of the foregoing **COMMENTS OF U S WEST, INC.** to be served via hand-delivery upon the persons listed on the attached service list.

Kelseau Powe, Jr.

(CC9645H.COS/BM-KF/lh)

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2100 M Street, N.W.
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MCI to respond to such interrogatories would be seven days. U S WEST would then commit to filing its response to the Hatfield Models within ten days after receiving proper responses to these interrogatories.[8]

We realize that the interconnection docket is, as a matter of statutory necessity, on an extremely fast track. Thus, U S WEST commits to moving as quickly as possible in reviewing the information received pursuant to this request (and will not seek additional time unless AT&T and MCI refuse to cooperate in discovery). We also realize that U S WEST is allotted only ten pages for ex parte presentations -- although, as neither AT&T nor MCI apparently counted the Hatfield exhibits to their filings as counting towards their page limits, we assume that rebuttals to the Hatfield exhibits would likewise not count towards the ten page ex parte limit. These procedural hurdles are formidable. However, the Hatfield Models, and the AT&T and MCI pricing and costing arguments which are derived from those Models, represent a direct threat to the Constitutional property rights of incumbent LECs, to the continued viability of the nation's telecommunications infrastructure, and to the development of true competition under the Telecommunications Act of 1996. To rely on these Models for any purpose without permitting the very minimal discovery requested in this Petition would serve to deprive the Commission of critical information which it needs if it is to make a reasoned and supportable decision in this proceeding. Failure to grant

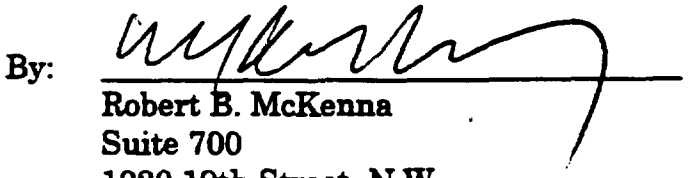
[8] If AT&T and MCI were to choose to attempt to obstruct proper discovery in these matters, additional time would be necessary. All additional filings on discovery would also need to be on an expedited basis.

this clearly necessary discovery would also serve to poison the entire docket and any rules which came out of it.[9]

Wherefore, U S WEST respectfully requests that AT&T and MCI be required to submit the Hatfield Models to discovery under the terms and conditions set forth herein.

Respectfully submitted,

U S WEST, INC.

By: 

Robert B. McKenna
Suite 700
1020 19th Street, N.W.
Washington, DC 20036
(303) 672-2861

Its Attorney

Of Counsel,
Dan L. Poole

June 13, 1996

[9] The legal points made in this Petition apply to any economic models the Commission might have to rely on in this proceeding -- including internal models developed by the Commission. All such models should be made public sufficiently in advance of the Commission's decision in the interconnection docket to permit meaningful public comment (and consideration of such comment by the Commission).

CERTIFICATE OF SERVICE

I, Kelseau Powe, Jr., do hereby certify that on this 13th day of June, 1996, I have caused a copy of the foregoing **PETITION FOR ORDER DIRECTING THAT DISCOVERY BE PERMITTED** to be served via first-class United States Mail, postage prepaid, upon the persons listed on the attached service list.

Kelseau Powe, Jr.

*Via Hand-Delivery

(CC9698E.COS/BM/lh)
Phase I