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January 28, 1998

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FEDERAL COMMUNICATIONS COMMISSION
OFFICE OF THE SECRETARY

Magalie Roman Salas
Secretary
Federal Communications Commission
1919 M Street, NW, Room 222
Washington, D.C. 20554

Re: Ex parte presentation, IB Dkt. No. 97-142

Dear Ms. Salas:

This is a supplement to the ex parte presentation on January 23, 1998, between Stan Moore and Gina Harrison representing SBC Communications, Inc. (SBC), Jerry Hausman of MIT, and Carl Frank of Wiley, Rein & Fielding made a presentation to Douglas W. Webbink, Chief Economist, Mark Uretsky and Adam Krinsky of the International Bureau; Donald K. Stockdale, Jr., Associate Bureau Chief of the Common Carrier Bureau; and Patrick DeGraba, Deputy Chief Economist of the Office of Plans and Policies to discuss grooming of inbound international telecommunications traffic. In addition to the document depicting the economic efficiencies of grooming, we also presented the attached bullet points.

Sincerely,

Gina Harrison

Attachment
cc: Douglas W. Webbink
Mark Uretsky
Adam Krinsky
Donald K. Stockdale, Jr.
Patrick DeGraba

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GROOMING
January 23, 1998

Definition: Grooming is the geographic allocation of proportionate return traffic.

FCC Treatment and Background:

- Grooming with non-dominant carriers is permitted under the FCC rules; Commission should amend its *Foreign Participation Order* rules to make this clear, in accordance with SBC's Petition for Reconsideration.
- Grooming is being done even now.
- Grooming is not just a BOC-only issue; If grooming is a special concession, it should be applied uniformly to any carrier seeking geographic enrichment of inbound traffic, not just BOCs.

Public Interest: Grooming is good for carriers and consumers, and is not a zero sum game.

- Grooming reduces costs for carriers, permitting lower prices for outbound international long distance.
- Grooming does not rob from one carrier to pay another; rather, grooming taps unused "consumer surplus."
- Grooming leads to lower prices for consumers.

To: Carl Frank
From: J Hausman
Re: Dominance presentation
Date: December 17, 1996

In Figure 1 I depict the usual "monopoly problem". I assume constant marginal cost (MC) and the first best solution is price equals MC. Now of course because of significant fixed cost, a telecom cannot charge MC and survive. Thus, p_2 is the price at which the firm earns its cost of capital. If the price is set at the monopolist level, p_3, then the loss to the economy is the triangle which I have cross hatched. This loss in economic efficiency is always a triangle, because the rectangle is gained by the company's shareholders, although income distribution issues do arise.

In Figure 2 I now consider the grooming problem. The marginal cost decreases from MC_1 to MC_2 so the rectangle is a real savings to the US economy. This cost savings is why grooming is not a zero sum game with people in Nebraska. The cost to people in Nebraska doesn't change, but we save costs which is real resource savings to the economy. Now if the price didn't change from p_2 before we still have a gain in productive economic efficiency, which is almost greater than a gain in allocative economic efficiency. However, since we expect Pacific to capture part of the cost decrease, it will lower its price to p_4 which also causes a gain in allocative economic efficiency. Thus, grooming is good in both types of economic efficiency. It cannot be correctly characterized as "whipsawing" because grooming causes a real gain in economic efficiency to the US economy and also will lead to lower prices for consumers.

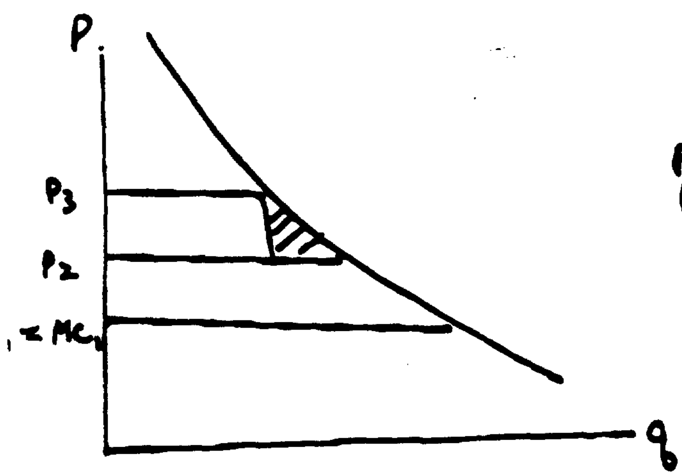

Figure 1

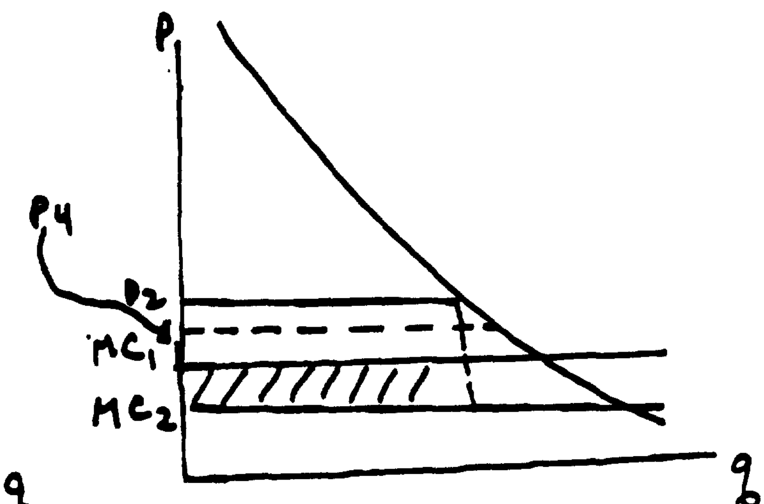

Figure 2