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Before the
FEDERAL COMMUNICATIONS COMMISSION
Washington, DC 20554

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FEDERAL COMMUNICATIONS COMMISSION
OFFICE OF THE SECRETARY

In the Matter of	)	
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	)	
Rules and Policies on Foreign Participation in the U.S. Telecommunications Market	)	IB Docket No. 97-142
	)	
	)	

REPLY TO COMMENTS AND OPPOSITIONS

MCI Telecommunications Corporation ("MCI"), pursuant to Section 1.429(g) of the Commission's Rules, hereby replies to the Comments and Oppositions filed in response to the Petitions for Reconsideration of the Commission's Report and Order in this proceeding.[1]

I. Introduction and Background

On February 10, 1998, ten parties, including MCI, filed Comments or Oppositions in response to Petitions for Reconsideration of the *Foreign Participation Order*.[2] MCI herein responds to the Comments or Oppositions of Ameritech, Cable & Wireless, GTE, SBC, Sprint, and Telefonica regarding MCI's Petition for Reconsideration.[3]

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[1] *Rules and Policies on Foreign Participation*, IB Docket No. 97-142, Report and Order, FCC 97-398 (rel. Nov. 26, 1997) ("*Foreign Participation Order*" or "*Order*").

[2] Comments were filed by Ameritech, AT&T Corp. ("AT&T"), Cable and Wireless plc and Cable & Wireless, Inc. ("Cable & Wireless"), GTE Service Corporation ("GTE"), MCI Telecommunications Corporation ("MCI"), SBC Communications, Inc. ("SBC"), Sprint Communications Company, L.P. ("Sprint"), Societe Internationale de Telecommunications Aeronautiques ("SITA"), Telefonica Internacional de Espana, S.A. ("Telefonica"), and Telecommunications Resellers Association ("TRA").

[3] MCI opposes Cable & Wireless' suggestion in its Comments that any foreign-affiliated carrier that complies with the Commission's structural separation safeguards should not be subject to the

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In its Petition, MCI requested that upon reconsideration the Commission should:

(1) impose a benchmark condition on the switched resale authorizations of foreign-affiliated carriers or, at the very least, not grant such authorizations unless their foreign affiliates commit to achieve proportionate annual reductions in their settlement rates with U.S. carriers during the transition to the benchmark;

(2) clarify that it will act swiftly to impose the benchmark condition on any authorized switched reseller that cannot rebut credible evidence of its efforts to distort competition in the U.S. international services market; and

(3) require all foreign-affiliated switched resellers to include in their quarterly traffic and revenue reports filed with the Commission traffic and revenue information about originating and terminating traffic of the foreign affiliate in addition to their own information, and to file copies of all contracts and arrangements with any other carrier relating to services and traffic on affiliated routes.

II. Additional Conditions are Necessary for Switched Resale Entry

A. Failure to Adopt a Benchmark Condition for Foreign-Affiliated Switched Resellers Will Undermine the Benchmarks Order

In its Petition, MCI argued that the failure to impose a benchmark condition on switched resellers would undermine the *Benchmarks Order*.[4] Cable & Wireless disagrees in its Comments, claiming that application of the benchmark condition is not intended to enforce benchmarks, but to prevent competitive distortion.[5] Cable & Wireless is mistaken. While it is correct that the Commission is concerned about competitive distortion in the U.S. international

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reporting requirements for dominant foreign-affiliated carriers. *See* Cable & Wireless Comments at 9-10. Not only does this suggestion lack substantive merit, but Cable & Wireless seeks an entirely new dominant carrier rule that it should have raised on reconsideration. Cable & Wireless' attempt to have the Commission consider a late-filed reconsideration should therefore be rejected.

[4] *See* MCI Petition at 3-4, citing *International Settlement Rates*, IB Docket No. 96-261, Report and Order, FCC 97-280 (rel. Aug. 18, 1997) ("*Benchmarks Order*"), *recon. pending, appeal filed, Cable & Wireless et al. v. FCC*, No. 97-1612 (D.C. Cir. Filed Sept. 26, 1997).

[5] Cable & Wireless Comments at 3-4. *See also* GTE Comments at 7.

market, it is also the case that one of the Commission's primary objectives is to reduce the tremendous subsidy that U.S. carriers and, by extension, their customers must pay to foreign carriers through excessive accounting rates.

Progress towards the benchmark settlement rates will be retarded and, as MCI stated in its Petition, the Commission's objective of lowering accounting rates will be undermined if foreign-affiliated switched resellers are permitted to enter into the U.S. international services market without first being required to lower accounting rates to the applicable benchmarks. Foreign carriers will have every incentive to enter the U.S. market through switched resale while simultaneously taking unfair advantage of U.S. carriers and consumers by maintaining excessive accounting rates. The Commission should recognize that the marginal benefit to be gained by allowing foreign-affiliated carriers with market power into the U.S. market is far outweighed by the significant anticompetitive harm that U.S. consumers and carriers will suffer due to excessive accounting rates.

B. Anticompetitive Pricing in the United States by Foreign-Affiliated Switched Resellers Would be Very Difficult to Detect

Several parties argue in their Comments that the Commission should not grant MCI's Petition because foreign-affiliated switched resellers would have neither the ability nor the incentive to attempt to distort competition in the United States.[6] Commenters also disagree with MCI that the underlying costs of switched resellers are difficult to discern and that detecting below cost pricing is therefore difficult. They argue, for example, that the Commission is capable of evaluating complex wholesale costs and that the spot market for wholesale minutes

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[6] *See, e.g.*, Cable & Wireless Comments at 2-3, SBC Opposition at 4.

can demonstrate pricing "patterns."[7] These arguments ignore the fact that foreign-affiliated switched resellers have substantially the same incentive and ability to distort competition in the U.S. market as facilities-based affiliates of foreign carriers, and that such distortion would be very difficult to detect.

First, as MCI demonstrated in its Petition, so long as a foreign carrier controls an essential cost input in the U.S. market -- accounting rates -- its affiliated U.S. reseller can use the subsidies from the excessive accounting rates to distort competition in the United States.[8] Second, these parties fail to address the fundamental flaw in the Commission's reasoning in the Order -- even "trends" or "patterns" of below-cost pricing will be nearly impossible to monitor because most wholesale minutes are purchased pursuant to complex private arrangements that often involve term commitments and volume discounts. Sprint, for example, does not demonstrate how the Commission would apply its experience in evaluating complex average costs to the switched resale situation. Cable & Wireless' suggestion that MCI should have information about wholesale costs as a provider of wholesale services is irrelevant because MCI's wholesale contracts are complex and vary depending on the circumstances -- precisely why it is nearly impossible to determine an average wholesale price and why safeguards are necessary.

Moreover, none of the parties adequately respond to MCI's argument in its Petition that the Order is vague regarding how to determine a reseller's wholesale cost. For example, they do

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[7] Sprint Opposition at 2-3. Telefonica Comments at 5.

[8] *See* MCI Petition at 5.

not suggest whether average variable costs should be examined over a set period of time, or just at one specific point in time. They also do not sufficiently address MCI's concern that variable wholesale costs cannot be easily detected without indicating the inputs that should be measured to determine "cost." Contrary to the parties' arguments, a foreign-affiliated reseller could easily set its retail prices in an anticompetitive manner without detection because its costs would be obscured in the complicated and constantly changing resale market. It is therefore essential that the potential for competitive distortion be prevented by requiring switched resellers' foreign affiliates to offer settlement rates at benchmark.

Finally, Telefonica and Ameritech argue that, in addition to being unnecessary, application of the benchmark condition as suggested by MCI would be anticompetitive because it would have the effect of prohibiting entry by foreign-affiliated carriers in, or causing existing carriers to exit from, the U.S. international services market.[9] However, these parties fail to recognize that the marginal benefit to be gained by permitting foreign-affiliated switched resellers to serve the U.S. market is far outweighed by the anticompetitive harm U.S. consumers and carriers will suffer if such entry is permitted without necessary safeguards.

C. The Potential Threat of Traffic Distortion Must Be Addressed by Strengthened Conditions on Foreign-Affiliated Switched Resellers

Cable & Wireless, SBC and Ameritech oppose MCI's request that the Commission strengthen its conditions to address traffic distortion in the U.S. international services market.[10]

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[9] Ameritech Opposition at 4. Telefonica Comments at 6.

[10] For example, Cable & Wireless argues that the Commission has already considered and rejected the requirement that switched resellers file copies of all contracts with any other carrier and that MCI provides no justification for changing that finding. Cable & Wireless Comments at 6. *See also* Ameritech Opposition at 5-6.

In its Petition MCI urged the Commission to go beyond its quarterly traffic and revenue reporting requirement by requiring all foreign-affiliated switched resellers to include in their quarterly reports traffic and revenue information about originating and terminating traffic of the foreign affiliate in addition to their own information, and to file copies of all contracts and arrangements with any other carrier relating to services and traffic on affiliated routes.[11]

As MCI explained in its Petition, traffic distortion can be extremely difficult to detect on a route. Merely requiring switched resellers to file quarterly traffic and revenue reports will not provide the Commission or competitors with enough information to determine whether distortion is occurring on a particular route. Making available copies of the contracts and arrangements of switched resellers with all other carriers on affiliated routes is necessary to enable competitors or the Commission to determine whether switched resellers have special arrangements to exploit traffic flows with their affiliates but not with other carriers. A contract filing requirement will also serve as a deterrent to attempting traffic distortion schemes.[12]

Ameritech and Cable & Wireless also oppose MCI's requested clarification of its enforcement process. They argue that Commission has already stated that it will impose the benchmark condition where it detects attempts to engage in anticompetitive behavior, and that

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[11] MCI Petition at 8-9.

[12] Cable & Wireless also claims that the Commission has no jurisdiction to require foreign carriers to disclose information, and cannot be assured that the U.S. carrier could in any event compel its affiliate to provide such information. Cable & Wireless Comments at 6. MCI, however, urged the Commission to require U.S.-authorized switched resellers to submit information about traffic and revenues of their foreign affiliates. The Commission clearly has jurisdiction to apply conditions to a U.S. carrier's authorization as necessary to further the public interest in the United States. Any confidentiality concerns regarding such information could be addressed through non-disclosure agreements.

MCI does not justify the need for such a clarification.[13] Contrary to Ameritech's claim, MCI provided justification when it stated in its Petition that adopting a clear standard with specific timeframes will discourage carriers from attempting such traffic distorting practices before they occur.[14] In addition, although MCI believes that a hard and fast definition for "credible evidence" is unnecessary, it submits that such a definition should include any evidence that would lead a reasonable person with expertise in international telecommunications to conclude that a carrier is attempting to engage in traffic distortion.[15] Contrary to the claims of Ameritech and Cable & Wireless, a clarified enforcement procedure is therefore necessary to prevent attempts to distort traffic between the United States and foreign points before they occur.

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[13] Cable & Wireless Comments at 6. Ameritech Opposition at 6. Ameritech also argues that MCI did not define what it means by "credible evidence." *Id.*

[14] MCI Petition at 8.

[15] The Commission need not act on every complaint through the formal complaint process pursuant to Section 208 of the Communications Act. Thus, SBC's argument that Section 208 already serves as an effective complaint mechanism is irrelevant.

III. Conclusion

For the reasons set forth herein, MCI submits that the arguments made in response to MCI's Petition for Reconsideration by Ameritech, Cable & Wireless, GTE, SBC, Sprint, and Telefonica should be rejected, and that the Commission should expeditiously grant MCI's Petition for Reconsideration.

Respectfully submitted,

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February 20, 1998

CERTIFICATE OF SERVICE

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