

Before the
FEDERAL COMMUNICATIONS COMMISSION
Washington, DC

In the matter of)
)
LCI Petition for Declaratory Ruling)
Concerning Bell Operating Company Entry)
Into In-Region Long Distance Markets)
)

CC Docket No.

98-5
FEDERAL COMMUNICATIONS COMMISSION
OFFICE OF THE SECRETARY

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BELL ATLANTIC COMMENTS

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BELL ATLANTIC¹ COMMENTS

Introduction and Summary

LCI's so-called "Fast Track" proposal for long distance entry is a back door attempt to have the Commission rewrite the Telecommunications Act of 1996, and is designed to slow (rather than accelerate) the entry of new competitors into the long distance business. The Commission, however, cannot change the steps Bell Operating Companies ("BOCs") must take under the Act to enter the long distance market. Congress prescribed the requirements for long distance entry and prohibited the Commission from changing them.

Moreover, there is no legal or policy basis for the Commission to force Bell Operating Companies to separate and divest their local intrastate telephone operations or to dictate the corporate structure they must use to offer those services. Requiring a

¹ The Bell Atlantic telephone companies ("Bell Atlantic") are Bell Atlantic-Delaware, Inc.; Bell Atlantic-Maryland, Inc.; Bell Atlantic-New Jersey, Inc.; Bell Atlantic-Pennsylvania, Inc.; Bell Atlantic-Virginia, Inc.; Bell Atlantic-Washington, D.C., Inc.; Bell Atlantic-West Virginia, Inc., New York Telephone Company and New England Telephone and Telegraph Company

structural change in the way Bell Operating Companies provide local telephone services would add an unnecessary level of confusion for customers that are already struggling to understand the changes now taking place in the telecommunications industry. It would also violate the Fifth Amendment by leaving the Bell Operating Companies with separate wholesale operations that are not financially viable.

I. LCI'S PETITION IS BASED ON A FALSE PREMISE.

LCI's stated reason for filing its petition – the failure of the Telecommunications Act to create local competition – is a myth. There is abundant evidence that the Act has opened local markets to competition. For example, Bell Atlantic has signed over 420 interconnection agreements under sections 251 and 252 of the Act, over 310 final agreements already have been approved by state commissions, and over 30 separate arbitration proceedings have been completed on the accelerated schedule required by the Act.

On the strength of these agreements, competitors are entering local markets in the states served by Bell Atlantic. Competitors have purchased over 267,000 interconnection trunks for use in exchanging telephone calls between their networks and Bell Atlantic's networks, are already exchanging over 1.5 billion minutes of traffic per month, and exchanged over 9.5 billion minutes of traffic during 1997. These traffic volumes equate to approximately 488,000 telephone lines that competitors are serving either wholly or partially over their own networks. In addition, competitors are serving over 232,000 lines by reselling services that they purchase from Bell Atlantic.

The entry of competitors in the New York local market is particularly striking. New York competitors have installed more than 20 local switches, connected them to Bell Atlantic's network with more than 130,000 interconnection trunks and are using them to exchange over 900 million minutes of traffic each month. These traffic volumes represent approximately 270,000 telephone lines that New York competitors are serving on their own networks. In addition, competitors have resold over 133,000 lines to residential and business customers in New York.

Competing local service providers that have invested billions of dollars in their own networks readily acknowledge the success of the Telecommunications Act.

According to Alex Mandl, CEO of Teligent and former president of AT&T:

“A group of smaller competitors have started to bring the benefits of competition . . . to key segments of the local communications market. These new competitors – including my company, Teligent – are accomplishing this goal by battling in the marketplace rather than in the courts and the regulatory agencies. Instead of arguing over the terms under which they will be allowed to use existing monopoly networks, the new competitors are building their own advanced, high-speed communications facilities that will give them direct access to their customers, bypassing the remnants of the old Bell system. . . . Already these ‘facilities-based’ carriers provide service over their own lines to more than 500,000 local telephone lines.”

A. Mandl, “Manager’s Journal: Telecom Competition Is Coming Sooner Than You Think,” The Wall Street Journal, p. A18 (Jan. 26, 1998). In fact, at a recent *en banc* presentation before the Commission, “CLECs painted a different picture of the local market than that portrayed by interexchange carriers (IXCs) – touting successes in both business and residential markets, through the use of resale and their own facilities.” Telecommunications Reports Daily, 1998 WL 6571143 (Jan. 29, 1998).

The Chairman of the Commission has also acknowledge the success of the Telecommunications Act:

“There are those, of course, who have already declared the 1996 Telecom Act to be a failure. The King is dead. Well, I say long live the King. Congress got it right: competition beats monopoly as the way to deliver the best telecom services to the American people. And the signs are that competition is indeed coming. We recently held a hearing at the FCC on the status of local telephone competition. And it was clear to anybody paying attention that the Act has successfully moved us in the right direction – toward greater competition.”

Remarks by William Kennard, Chairman of the Federal Communications Commission to the National Association of State Utility Consumer Advocates (Feb. 9, 1998). More recently, Chairman Kennard said “[w]e see competition in New York City, where over 20% of the business market is being served by carriers other than the incumbent Bell Company.” Remarks by William Kennard, Chairman of the Federal Communications Commission to Legg Mason Workshop (Mar. 12, 1998).

It is only the incumbent long distance companies, like LCI, that continue to chant their tired refrain about “barriers” to entry in the local market. LCI’s most recent petition is just another excuse for LCI’s unwillingness to compete in the local market. It is time for LCI and the other long distance carriers to acknowledge the ground rules Congress established for local competition and to begin competing under those rules. The Commission cannot and should not attempt to change those rules solely to benefit those carriers.

II. LCI'S "FAST TRACK" PROPOSAL IS CONTRARY TO THE TELECOMMUNICATIONS ACT.

LCI's "Fast Track" proposal, even though it is described as voluntary, is contrary to the Act because it purports to change the requirements for long distance entry.

To the extent that LCI's "Fast Track" proposal would impose a wholesale/retail separation requirement in addition to the existing Section 271 requirements for long distance entry, that proposal is contrary to the Act. Section 271(d)(4) expressly states that "[t]he Commission may not, by rule or otherwise, limit or extend the terms used in the competitive checklist set forth in subsection (c)(2)(B)." 47 U.S.C. § 271(d)(4).

Moreover, it is hard to understand how LCI's petition could create a "Fast Track" to accelerate long distance entry when it would impose an additional obligation to undertake a major divestiture on top of everything else that Section 271 requires.

Likewise, to the extent that LCI's "Fast Track" proposal purports to replace any existing Section 271 requirements with a wholesale/retail separation requirement for long distance entry, it is contrary to the Act. Congress wrote a specific fourteen point checklist that Bell Operating Companies must meet to qualify for long distance entry. The Commission may not rewrite the checklist requirements for long distance entry. *Id.*

Finally, if LCI is suggesting that the Commission write new structural safeguards for the Bell Operating Companies' long distance entry, that suggestion should be rejected. Congress has already addressed this issue and prescribed the structural safeguards that are necessary for long distance entry. Specifically, Section 272 requires that Bell Operating Companies offer long distance services through a structurally separate

subsidiary for a period of three years. 47 U.S.C. § 272. There is no need for this Commission to address this issue.

This is all the more true given that competition actually would be harmed in one significant respect if the Bell Operating Companies were deprived of the efficiencies they now realize by providing wholesale and retail services through a single corporation. If the Bell companies were denied the same efficiencies that their competitors were free to enjoy, then consumers inevitably would be denied much of the benefits that could be derived from efficient competition.

III. THERE IS NO PUBLIC POLICY REASON TO FORCE BELL OPERATING COMPANIES TO SEPARATE AND DIVEST THEIR RETAIL OPERATIONS FROM THEIR WHOLESALE OPERATIONS.

Under LCI's "Fast Track" proposal, Bell Operating Companies would be required to conduct all of their retail operations through a separate corporation and divest themselves of at least 40 percent of their ownership interests in that corporation. LCI Petition at 3, 14-17. In addition, the Bell Operating Companies' remaining wholesale corporations would be barred from offering retail services and would be constrained to offer only wholesale services "at cost." *Id.* at 10-11. These requirements would be contrary to the public interest and the law.

First, LCI's proposal would confuse and irritate the Bell Operating Companies' current local service customers. Every one of their customers would have to select another company for their local service or be allocated to another company, even if they didn't want to. No customers currently served by a Bell Operating Company would be able to continue receiving local service from the company that now serves them. This

required change of local service provider would inevitably generate confusion and dissatisfaction among consumers.

Second, by severely limiting the services the Bell Operating Companies' wholesale companies can offer and by capping their prices "at cost," it is hard to imagine how these corporations could remain financially viable. With no opportunity to offer services at profitable prices, there would be no incentive for anyone to invest in these companies. The public networks on which so many people now rely for all of their telecommunications needs would not be upgraded with newer technology and would inevitably deteriorate without the needed capital investments.

In fact, the pricing and line of business constraints LCI proposes for the Bell Operating Companies wholesale operations raise serious constitutional concerns. It is well settled that the Fifth Amendment requires a utility to be permitted to charge rates that will allow it to "maintain its financial integrity, to attract capital, and to compensate its investors for the risk [they have] assumed." *Duquesne Light Co. v. Barasch*, 488 U.S. 299, 310 (1989) (citing *FPC v. Hope Natural Gas Co.*, 320 U.S. 591, 605 (1944)). Under that standard "it is important that there be enough revenue not only for operating expenses, but also for . . . capital costs" which "include service on the debt and dividends on the stock." *Hope*, 320 U.S. at 603. By limiting the Bell Operating Companies to offering all services "at cost," LCI's proposal would violate the Fifth Amendment.

LCI's proposal would also violate the Fifth Amendment to the extent it sets all of the wholesale rates based on the forward-looking costs of a hypothetical, most efficient network. Nothing in *Hope* – or any other decision of the Supreme Court – even remotely suggests that rates may properly be based on the costs incurred by an imaginary utility.

On the contrary, in *Hope* the Court specifically upheld the federal commission's rejection of "conjectural and illusory" cost estimates. *Hope*, 320 U.S. at 597.

Third, the Commission does not have the authority to regulate how the Bell Operating Companies offer local intrastate telephone services. Section 2(b) of the Communications Act make clear that "nothing in this Act shall be construed to apply or to give the Commission jurisdiction with respect to (1) charges, classifications, practices, services, facilities, or regulations for or in connection with intrastate communication service by wire or radio of any carrier." 47 U.S.C. § 2(b). As a result, the Commission simply does not have jurisdiction to force the Bell Operating Companies to separate and divest their local intrastate telephone operations, to "freeze" their intrastate tariffs or to prohibit them from offering any intrastate services.

Finally, the Commission does not have any authority to require Bell Atlantic to divest any of its ownership interests in its local telephone operations. Bell Atlantic is entitled to provide local telephone services as an authorized line of business and to do so through a 100 percent ownership interest. The Commission cannot impose any ownership cap on Bell Atlantic's interest in any lawful business activity.

IV. THERE IS NO COMPETITIVE JUSTIFICATION FOR FORCING BELL OPERATING COMPANIES TO SEPARATE AND DIVEST THEIR RETAIL OPERATIONS FROM THEIR WHOLESALE OPERATIONS.

LCI argues that, because the Bell Operating Companies will be both a wholesale supplier and a retailer in a competitive market, that these two operations must be structurally separated to prevent discrimination. LCI Petition at 10, 12-13. But the Act already contains non-structural safeguards to prevent discrimination and these safeguards

have enabled the Bell Operating Companies to participate in many competitive markets as both retailer and wholesaler without inhibiting competition.

First, Bell Atlantic routinely has provided interLATA services in the northern New Jersey-New York and southern New Jersey-Philadelphia corridors for over ten years without structurally separating its retail and wholesale operations and without anticompetitive consequences. *See United States v. Western Elec. Co.*, 569 F. Supp. 990, 1018-19, 1023 (D.D.C. 1983). According to AT&T's own estimate, Bell Atlantic's prices are up to one-third lower than those of the Big Three interexchange carriers. AT&T Corp.'s Petition for Waiver and Request for Expedited Consideration, *AT&T Petition for Waiver of Section 64.1701 of the Commission's Rules*, CCB/CPD 96-26 Attachment A (FCC Oct. 23, 1996) ("AT&T Waiver Petition"). Yet, after twelve years, Bell Atlantic has not dominated the market — it has less than 20 percent of the corridor market. Declaration of Robert W. Crandall, ¶ 10, attached to Bell Atlantic Petition ("Petition"), DA 95-1666 (filed July 8, 1995); *see also*, Declaration of Robin A. Lewis-Ivy attached to Petition. When AT&T asked for permission to lower its own rates in the corridors, AT&T did not allege that Bell Atlantic has been leveraging its "bottleneck" over carrier access; rather, it complained that Bell Atlantic was undercutting AT&T's prices and that AT&T needed the ability to deaverage its rates to respond to the additional competition. AT&T Waiver Petition at 4-5. Similarly, other large incumbent local exchange carriers such as Rochester Telephone (now Frontier) have offered interLATA services for years without apparent anticompetitive effect.

Second, Bell Atlantic and other incumbent local exchange carriers have long been allowed to provide information services without structurally separating their retail and

wholesale operations, and the evidence shows that competition in these markets has been enhanced. If the Bell Operating Companies were able to inhibit competition in these markets, output would have dropped and prices would have risen. But, in fact, just the opposite has occurred. Since incumbent local exchange carriers began offering voice messaging services, the market has grown in size and prices have fallen. From 1990 to 1995, the incumbent local exchange carriers' participation in this market increased from zero to over six million subscribers, but their subscriber base collectively accounts for just over 15 percent of voice messaging service revenues nationally. *See Computer III: Further Remand Proceedings*, CC Docket No. 95-20, Comments of Bell Atlantic, at 8-9 (filed April 7, 1995); *see also* Jerry A. Hausman and Timothy Tardiff, *Benefits and Costs of Vertical Integration of Basic and Enhanced Telecommunications Services*, at 5 (April 6, 1995), attached to Comments of Bell Atlantic. At the same time, the monthly retail charge for voice messaging service has dropped from \$30 in 1990 to \$5-\$15 in 1995. *Id.*

Finally, since 1984, the Bell Operating Companies have been permitted to distribute customer premises equipment ("CPE") without separating their retail and wholesale operations, but have not impeded competition. Since BOCs were allowed into the CPE market, output has steadily grown and prices have fallen, and the Bell companies are dwarfed by major vendors such as Lucent, Nortel, and Siemens. *See* MMTA, 1998 MultiMedia Telecommunications Market Review and Forecast, 85-87 (detailing demand growth and price decreases for CPE markets); *id.* at 96, 102-104, 108 (listing leading suppliers in CPE submarkets). In fact, the U.S. Court of Appeals observed that the customer premises equipment market "has supported competition even though the BOCs"

theoretically “possess[] an incentive to discriminate in interconnection.” *U.S. v. Western Electric Co.*, 900 F.2d 283, 303 (D.C. Cir. 1990), *cert. denied*, 498 U.S. 911 (1990).

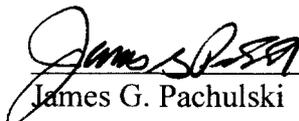
There is thus no competitive reason to require any Bell Operating Company to structurally separate its retail and wholesale local telephone operations before offering long distance services.

CONCLUSION

LCI is asking the Commission to do what it cannot. Congress has already prescribed the requirements for long distance entry by the Bell Operating Companies and directed the Commission not to change these requirements. Moreover, there is no policy or legal basis for the Commission to force the Bell Operating Companies to separate and divest their retail operations from their wholesale operations.

Respectfully submitted,

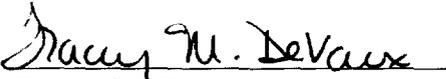
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Dated: March 23, 1998

CERTIFICATE OF SERVICE

I hereby certify that on this 23rd day of March, 1998 a copy of the foregoing "Bell Atlantic Comments" was sent by first class mail, postage prepaid, to the parties on the attached list.


Tracey M. DeVaux

* Via hand delivery.

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