

BELLSOUTH

W. W. (Whit) Jordan
Vice President-Federal Regulatory

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Suite 900
1133-21st Street, N.W.
Washington, D.C. 20036-3351
202 463-4114
Fax: 202 463-4198
Internet: jordan.whit@bsc.bls.com

September 3, 1998

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

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FEDERAL COMMUNICATIONS COMMISSION
OFFICE OF THE SECRETARY

RE: CC Docket Nos. 94-1, 96-45 and 96-262

Dear Ms. Salas:

Today, Ernest Bush and the undersigned, both representing BellSouth, met with Jim Casserly of Commissioner Ness's office, Kyle Dixon of Commissioner Powell's office, Kevin Martin of Commissioner Furchgott-Roth's office, Tom Power of Chairman Kennard's office, and Yog Varma, Jane Jackson, Rich Lerner and Katherine Schroeder of the Common Carrier Bureau. During these meetings, the attached materials regarding the above proceedings were discussed.

Please call me if you have any questions.

Yours truly,



W.W. Jordan
Vice President-Federal Regulatory

Attachments

CC: Jim Casserly
Tom Power
Rich Lerner

Kyle Dixon
Yog Varma
Katherine Schroeder

Kevin Martin
Jane Jackson

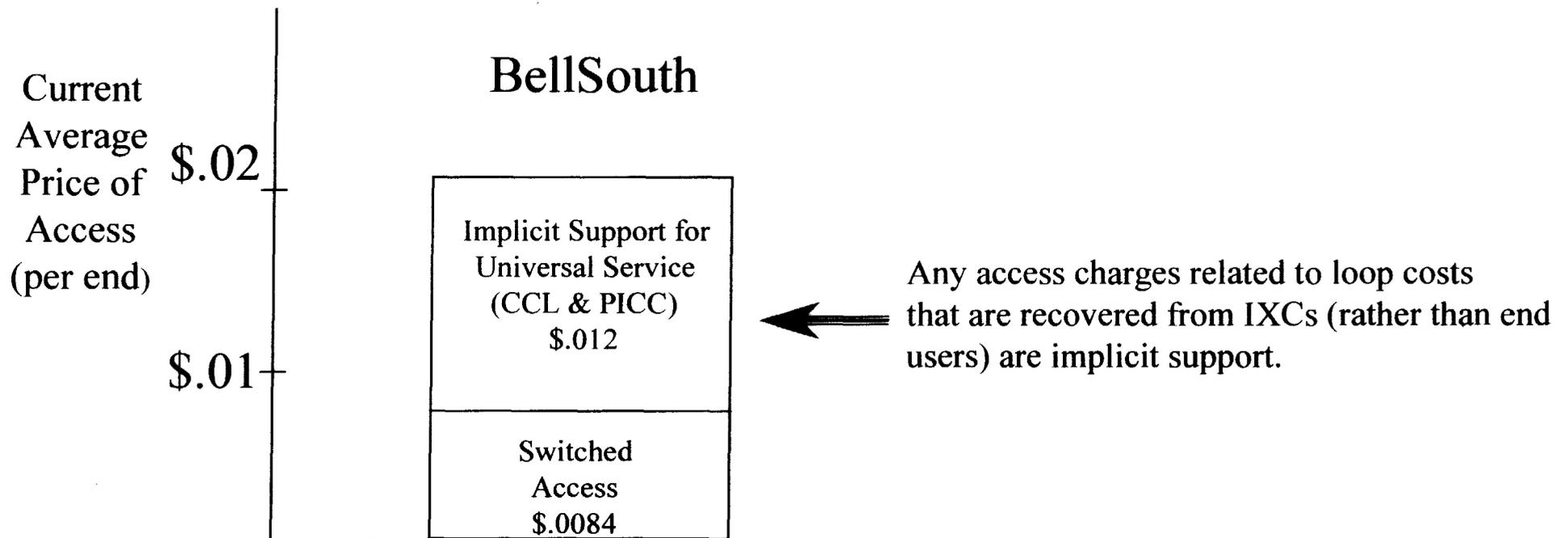
Access Reform - Next Steps

BellSouth Telecommunications
September 3, 1998

The FCC Issued a Comprehensive Order on Access Reform in 1997 and Circumstances Have Not Changed to Warrant a New Look

- Universal service remains to be dealt with before any look at access charges can commence.
- Competition is developing as envisioned by the Act.
- Price regulation is working as intended; any change to a more prescriptive approach could ultimately harm consumers.
- The changing environment calls for less regulation rather than more; pricing flexibility is long overdue.

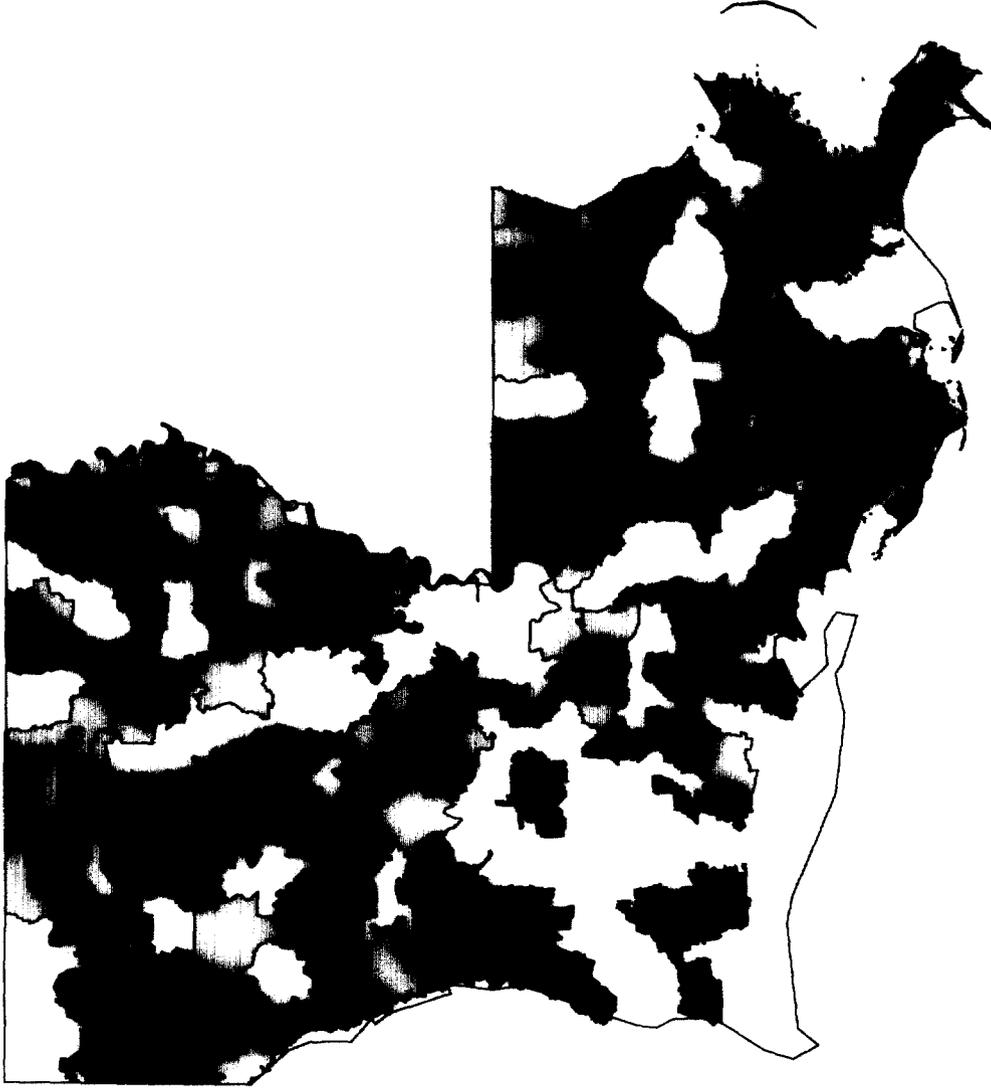
The Interrelationship Between Interstate Switched Access Service and Universal Service



Key Point:

Simply removing the implicit support for universal service that is built into access rates would allow rates to fall to less than a penny per minute for many large LECs.

Universal Service Fund - Cost per Line by Wire Center



LA Wire Centers - BellSouth
LPSC Order, HAI 5.0a

■	34 Wire Centers <\$25
■	67 Wire Centers >\$25 and <\$50
■	61 Wire Centers >\$50 and <\$75
□	28 Wire Centers >\$75 and <\$100
■	37 Wire Centers >\$100

It is Critical That Universal Service Support Be Maintained

- If the FCC allows the implicit support for universal service to be eroded/eliminated before implementing a sufficient and explicit fund, it will have:
 - ignored the mandate of Congress
 - set up a ‘no-win’ scenario for consumers
 - potential basic service rate increases
 - foreclosed competitive alternatives
 - declining infrastructure, especially in rural areas
 - reduced/eliminated LEC incentives to invest in universal service infrastructure; and
 - set up a scenario for increased investor risk and uncertainty.

Competition Is Developing At a Rapid Pace

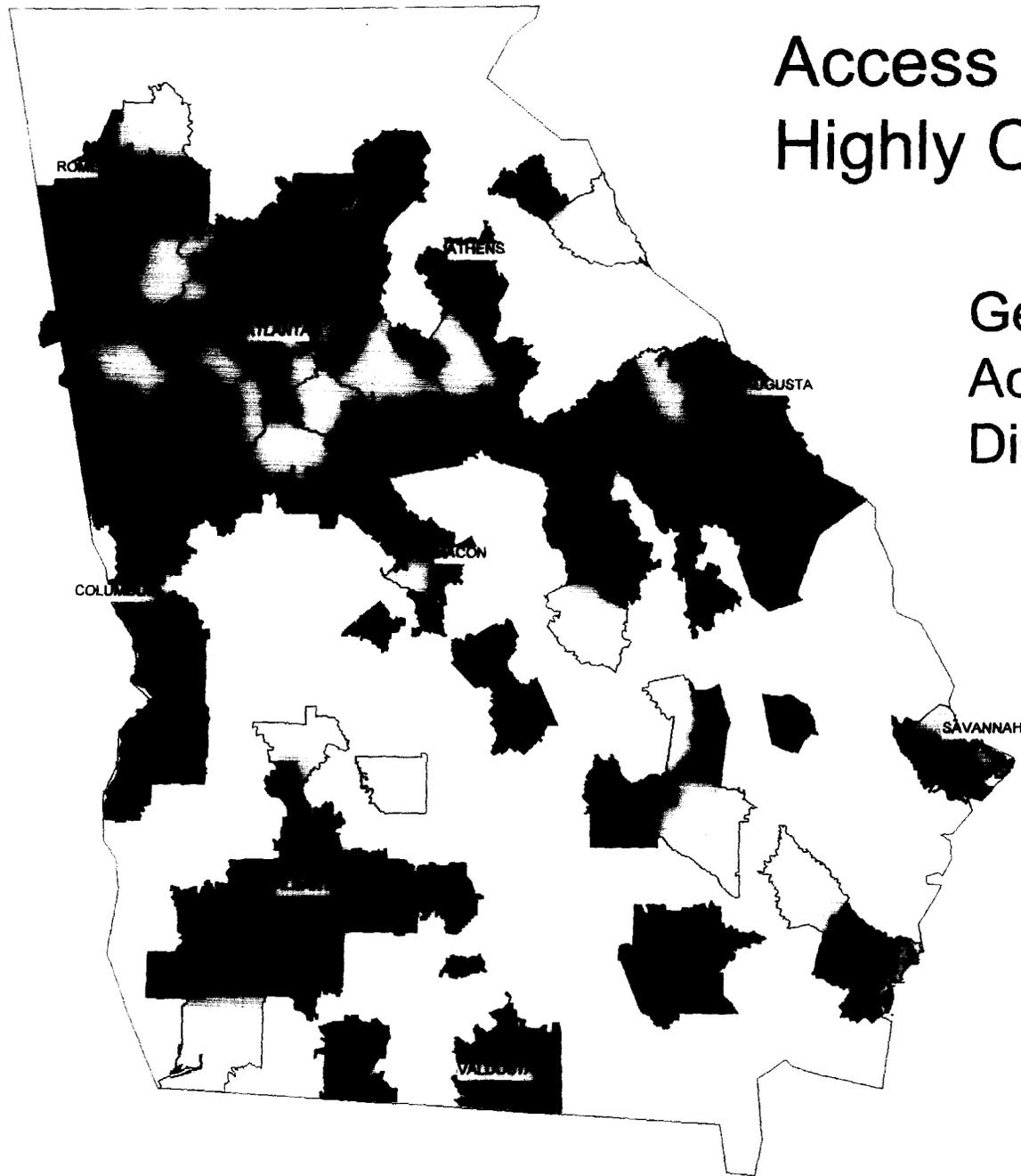
- Contrary to claims by IXC's, competition is developing at a rapid pace:
 - Numerous CAPs and CLECs are operational in first and second tier cities throughout BellSouth region and are capturing a growing share of BellSouth's revenue stream.
 - Competition is intense for high capacity services
 - BellSouth down to 66% market share in Atlanta, and 71% in South Florida (Source: Quality Strategies Analysis)
 - CLECs added more business lines in 1st Qtr, 1998 than did incumbent LECs.
 - Wireless service has begun to supplant wireline service.
 - Residential competition has begun in metro areas for high revenue customers.
 - E.g., MediaOne says it has 10% market share where it provides service in Atlanta (Business Week, July 6, 1998)
 - AT&T acquired TCG for \$11 B, and says that half the value of the merger will arise from avoidance of access charges.

**LOCAL COMPETITION SUMMARY REPORT: EO JULY, 1998 vs. EO MAY, 1997
BELLSOUTH REGION**

	EO July, 98	EO May, 97	Growth	% Growth
CLEC Certifications(Wireline)				
PSC Approved	751	304	447	147%
Pending	200	102	98	96%
Operational CLECs	156	98	58	59%
Resale Only	123	76	47	62%
Facility-based Only	0	0	0	0%
Both	33	22	11	50%
Operational CLEC/CAP Networks	150	98	52	53%
Networks w/ Switching Capability	106	41	65	159%
Networks Under Development	33	25	8	32%
Total Local Interconnection Trunks	197295	30246	167049	552%
CLEC-to-BST Trunks	85451	19360	66091	341%
BST-to-CLEC Trunks	111844	10886	100958	927%
Access and Transport	2781	716	2065	288%
Directory Assistance	1064	362	702	194%
Operator Services incl. Verification	840	174	666	383%
E911	821	166	655	395%
Intercept	56	14	42	300%
Collocated Interconnectors	33	20	13	65%
Collocation Arrangements	670	235	435	185%
Physical	341	57	284	498%
Virtual	329	178	151	85%
Wire Centers with Collocation	240	134	106	79%
CLEC NXX Codes Opened (w/PCS)	2103	488	1615	331%
Total Ported Numbers	85356	5555	79801	1437%
Ported Res. Lines	1949	28	1921	6861%
Ported Bus. Lines	83407	5527	77880	1409%
Total Unbundled Loops	23216	2653	20563	775%
Total Unbundled Ports	93	10	83	830%
Total Resold Lines	397914	49606	348308	702%
Resold Bus. Lines	176560	29208	147352	504%
Resold Res. Lines	219217	20398	198819	975%
Resold ISDN Lines	1606	NA	NA	NA
Resold Private Lines/Data CKTs	531	NA	NA	NA
Total Facility-Based Lines (estimated)	132699	NA	NA	NA
Facility-based Business	127753	NA	NA	NA
Facility-based Residential	4946	NA	NA	NA

Access Revenues Are Highly Concentrated

Georgia Access Revenue Distribution

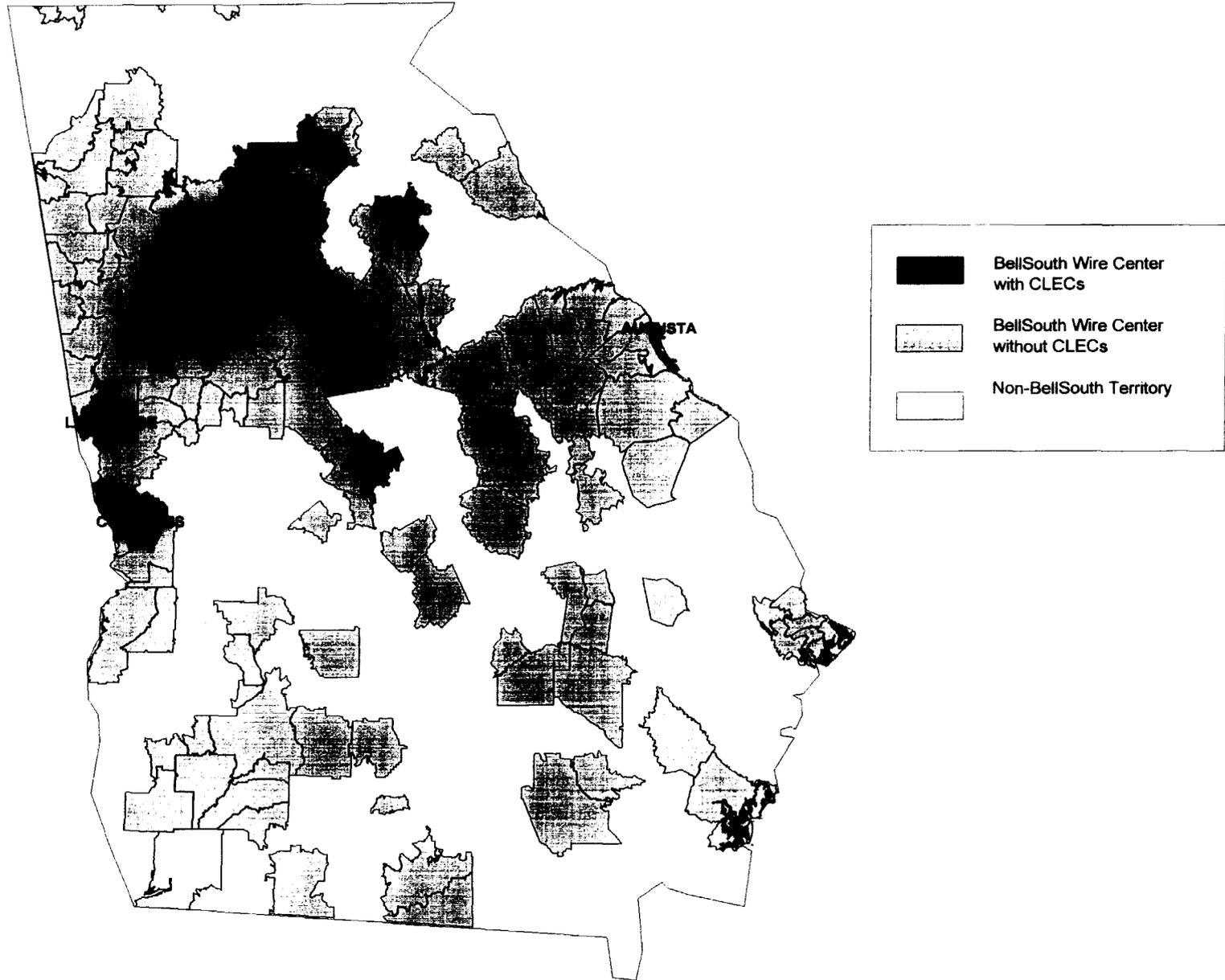


Distribution of Revenues (#WCTRs) (% of BST Area)

■	Top	30%	(8)	(1.3%)
■	Next	30%	(19)	(7.7%)
■	Next	25%	(35)	(20.6%)
□	Next	10%	(32)	(21.1%)
■	Bottom	5%	(84)	(49.3%)

Competitors Are Locating in High Revenue Wire Centers

(BellSouth Georgia Wire Centers with Colocation Companies)



Consumers Have Benefited from Price Regulation and Associated Market Based Approach

- USTA has estimated that access prices have fallen by \$11 B nationwide since 1991 under price regulation.
 - Access savings from BST's reductions amounts to \$2 B since 1991.

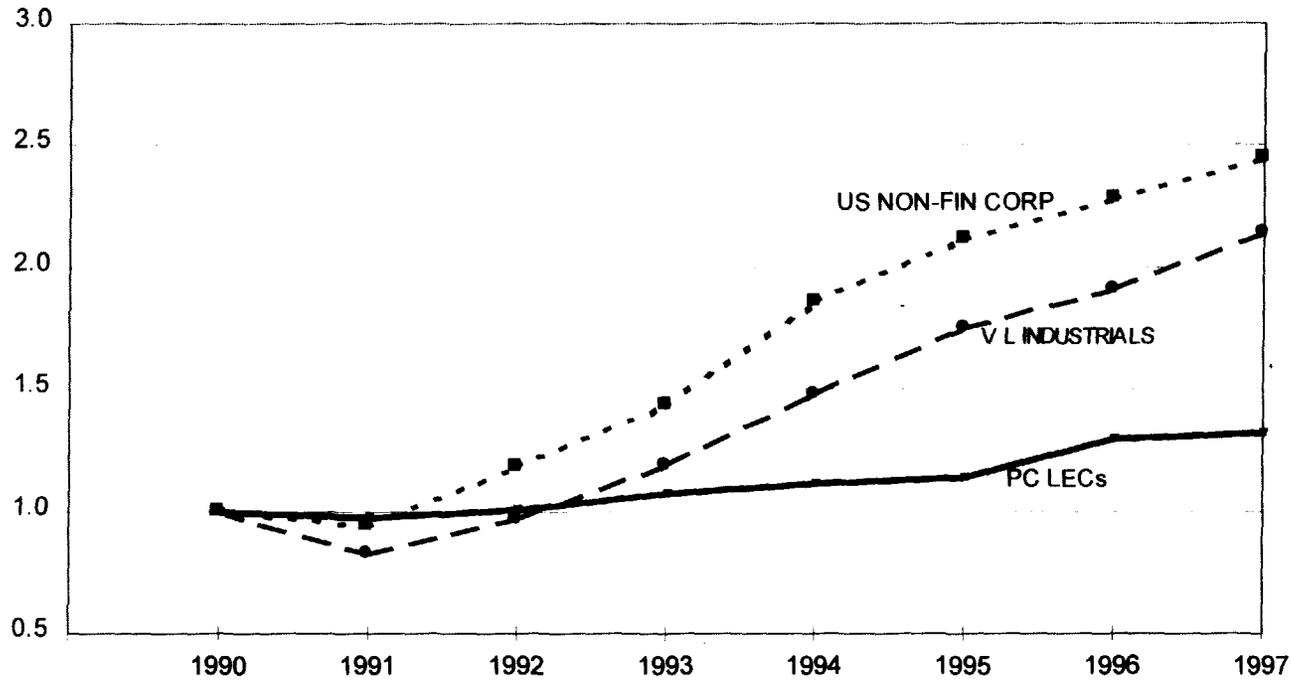
BST Rates

- 1991 composite rate per minute: \$.057
- 1998 current composite rate per minute: \$.040 (includes PICC \$)
- Investment in infrastructure continues
 - BellSouth invested \$3.5 B in the network in both 1996 and 1997.

Price Cap LEC Earnings Are Reasonable

- Price cap LEC returns are moderate compared to the very strong earnings growth at U.S. corporations overall.
- Price cap LEC returns are overstated by an estimated 200-300 basis points since they are not based on economic depreciation rates.
- All price cap LECs have lower ROE than AT&T.
 - AT&T's ROE on long distance service is 80%. (According to Janney, Montgomery and Scott Analysis, June 9, 1998.)
- Future interstate returns are already highly uncertain.
 - All companies have benefited from exceptional U.S. economy in mid/late 90's. Cooling off of economy could bode poorly for future ILEC productivity gains.
 - Price cap LECs have made substantial workforce cuts; continued cost cutting at '91-'97 rate is extremely unlikely.
 - 6.5% X-factor is not sustainable.

EARNINGS PERFORMANCE INDEXED FROM 1990
All US Non-fin. Corps., ValueLine Industrials,
Interstate Price Cap ILECs



The FCC Should Look to the States for More Flexible Price Regulation Plans

- Eight BellSouth states are under price regulation plans.
- State price regulation plans allow greater flexibility than FCC price cap plan.
 - Most states group services into three categories: Basic, Non-Basic and Interconnection. There are no subcategories, except in Florida.
 - Inflation formula productivity offset no greater than 4% in any state.
 - New service introduction rules are reasonable.
 - Existing services can be reclassified between service categories.
 - There are no rate structure requirements for services in any state price regulation plan. Majority of plans require switched access reductions to interstate level or by specified amounts.
- Contract Service Arrangements (CSAs) are not included in state price regulation plans. CSAs are effective in five states without Commission approval. CSAs are filed with and require Commission approval in three states. CSAs are filed as tariffs and approved by the TRA in Tennessee.
- Competition is disciplining prices in the states, as BST is unable to use all of the available headroom allowed by the plans.

What Should the FCC Do Regarding Access Charges?

- Implement universal service in an explicit and sufficient manner.
- Provide additional pricing flexibility to recognize the increased competitiveness of certain services in certain markets.
- Continue down the market based path to reform that is envisioned in the Telecommunications Act that was endorsed by the FCC in 1997 and affirmed by the 8th Circuit Court in 1998.
- Resist self serving calls by MCI and AT&T to unilaterally reduce access charges.
- In 1999, review the X-factor and lower it to a sustainable long-term level.
- Look to the Long Distance Market for price cuts.
 - Keep spotlight on IXC's to flow through July, 1998 access charge reductions.
 - Increase number of competitors in long distance market.