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Ms. Magalie Roman Salas
Secretary
Federal Communications Commission
445 Twelfth Street, SW, Room 204
Washington, DC 20554

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FEDERAL COMMUNICATIONS COMMISSION
OFFICE OF THE SECRETARY

Re: Ex Parte
Reform of the International Settlements Policy and Associated Filing Requirements – IB Docket 98-148
Regulation of International Accounting Rates – CC 90-337

Dear Ms. Salas:

Today, Judy Simonson, Larry Lafaro, Jim Talbot and I of AT&T and William Lehr on behalf of AT&T met with Diane Cornell and Bob McDonald of International Bureau and Pat DeGraba of the Office of Plans and Policy to discuss AT&T's positions in the above mentioned dockets. The attached document was distributed at the meeting.

Two copies of this Notice are being submitted to the Secretary of the Federal Communications Commission in accordance with Section 1.1206(a)(1) of the Commission's rules.

Respectfully submitted,

Douglas W Schoenberger

Attachment

cc: Diane Cornell
Bob McDonald
Pat DeGraba

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Recycled Paper

Reform of the International Settlements Policy, IB 98-148.

I. 25% Traffic Thresholds Are Arbitrary and Harm Competition.

The Commission should reject proposals by some carriers (a) to remove the ISP only for under-25 percent arrangements, or (b) to impose "no unreasonable discrimination" restrictions on above-25 percent arrangements.

- AT&T, in effect, would be regulated as dominant -- notwithstanding the Commission's 10/5/98 reaffirmation that AT&T has no market power.
    - 25 percent threshold would raise average unit costs of larger share carriers, but most of all of AT&T.

        -- *Almost half* of AT&T's traffic on 38 High Income benchmark routes would be restricted (*but only 22 percent of MCI WorldCom traffic on 32 routes. Sprint would be restricted on just 3 routes*).

    - "[R]estricting the competitiveness of the largest carrier only reduces competitive performance in the market." *AT&T International Non-Dominance Order*, 11 FCC Rcd. 17963, 17966 (1996).

- An arbitrary and unjustified burden on AT&T:
    - 25 percent threshold has no relationship to market power -- *see Foreign Participation Order* (no market power below 50 percent market share); *AT&T International Non-Dominance Order* (no market power at 59 percent).
    - "[L]acking market power, AT&T has no *a priori* economic advantage relative to other U.S. carriers that would allow it to negotiate uniquely favorable deals with the foreign incumbent." Reply Affidavit of Dr. William Lehr at 4-5.
    - Any concerns based on the continuing market power of *foreign* carriers should result in the retention of the ISP for *all* U.S. carriers -- not in the discriminatory application of the ISP to larger U.S. carriers, and particularly AT&T.

- Seeking to protect smaller carriers from competition by larger carriers is not reasoned decisionmaking. *Competitive Telecommunications Ass'n v. FCC*, 87 F.3d 522, 532 (D.C. Cir. 1996).

The NPRM proposes to allow secret under 25 percent flexibility arrangements that would encourage bypass and whipsaws and harm competition.

- Would result in more onerous and arbitrary regulatory treatment of AT&T:

  - AT&T required to reveal settlement rates on half its traffic; AT&T required to follow accounting rate modification or public notice procedures to change rates. Much lesser effect on other carriers (see above).

- New bypass and whipsaw opportunities for foreign dominant carriers not subject to effective competition:

  - Including incumbents in Mexico and the Philippines -- with prohibitions on ISR and settlement rates far above benchmarks.

    -- threshold test for flexibility (existence of multiple facilities-based competitors) would not prevent bypass or whipsaws.

  - Would encourage U.S.-inbound traffic termination with the lowest U.S. bidders -- raising outpayments, carrier costs and consumer prices, and reducing incentives to lower settlement rates.

  - New incentive for whipsaws to prevent or delay benchmark enforcement.

- *Potential 1999-2002 increase in U.S. outpayments if Telmex terminates all Mexico-U.S. traffic in secret flexibility arrangements at cost ($0.07): $500 million.*

- *Potential 1999-2002 increase in U.S. outpayments if PLDT terminates all Philippines-U.S. traffic in secret flexibility arrangements at cost: $110 million.*

- The Commission should:

  - Continue to review all flexibility arrangements as required by the *Flexibility Order* to ensure "no significant adverse impact on U.S. net settlement payments and resulting traffic volumes."

  - Remove the existing 25 percent flexibility threshold.

Removal of the ISP for <u>all</u> under-25 percent arrangements on WTO routes, as proposed by Sprint, would encourage even greater harm from bypass and whipsaws by the monopoly carriers that control the majority of WTO markets.

II. Best Practices Rates or Viable ISR Should Be Required for the Removal of the ISP with Foreign Dominant Carriers.

The recent *Sprint ISP Modification Order* (¶ 5) describes the dual purpose of the ISP:

- Traditional focus of the ISP was to prevent whipsawing.
- The ISP also focuses on the adverse effects of above-cost accounting rates.
- Both whipsawing and above-cost accounting rates are contrary to the public interest.

There is no basis to claims that the global telecommunications market is now sufficiently competitive to remove the ISP on a general basis.

- Virtually all countries maintain above-cost settlement rates.
- Only 20 (of 132) WTO Members will allow ISR with nondiscriminatory interconnection rates on 1/1/99.
  - These are Australia, Austria, Belgium, Canada, Denmark, Finland, France, Germany, Iceland, Italy, Japan, Korea, Luxembourg, Netherlands, New Zealand, Norway, Spain, Sweden, Switzerland and the UK.
  - *They account for just $770,000 (16 percent) of $4.7 billion total 1996 U.S. settlements outpayment to all 132 WTO member countries.*
  - Four additional WTO members allowing ISR (Chile, Guatemala, El Salvador, Hong Kong) have discriminatory interconnection rates and account for another $360,000 (8 percent) of the WTO outpayment.
- The fact that countries "represent[ing] 97 percent of total basic telecommunications service revenues" (SBC Reply, p. 9) have made *some* WTO commitments (e.g., in domestic services) has no relevance to the continuing need for the ISP to prevent whipsaws and to obtain cost-based settlement rates.

The threshold for the removal of the ISP should be whether viable ISR arrangements exist.

- Removing the ISP where ISR is *authorized by the Commission* would not prevent whipsaws and one-way bypass in closed and partially-competitive markets not allowing ISR.
  - Countries will qualify for ISR when 50 percent of traffic is settled at benchmarks without removing their prohibitions on ISR -- e.g., Israel and Singapore (1/1/1999 benchmark); Mexico (1/1/2000 benchmark).
- More than *the legal right to provide ISR in the foreign country* should be required.
  - Some countries allowing the legal right to provide ISR do not allow viable ISR arrangements (e.g., Chile).
- The second key requirement for viable ISR arrangements (and for the removal of the ISP) is *the availability of reasonable and nondiscriminatory terms and conditions for interconnection.*
  - ISR otherwise does not provide an effective alternative means of traffic termination.
- Approach is consistent with WTO requirements.
  - USTR has affirmed legitimacy of considering foreign market conditions in evaluating competitive effects.

Benchmark settlement rates are far above cost.

- Wide margin between \$0.15, \$0.19 and \$0.23 benchmark rates and cost (\$0.07 or less).
- *Sprint ISP Modification Order* (¶ 13) notes that \$0.19 benchmark "remains far above cost" and "encourage[s] carriers to negotiate lower rates."

Whipsaw and bypass risks remain at benchmark settlement rates.

- Removal of ISP at benchmark rates would lead to inbound bypass and whipsaws by foreign dominant carriers in closed and partially-competitive markets -- raising U.S. outpayments and keeping settlement rates at above-cost benchmark levels, rather than encouraging further reductions to cost.

    - Foreign carrier would engage in whipsaws to punish U.S. carriers seeking lower rates or refusing to pay unjust surcharges;

    - Foreign carrier would terminate U.S.-inbound traffic at cost and require U.S.-outbound traffic to be at benchmark rates, raising U.S. outpayments;

    - De-linking of inbound and outbound settlement rates reduces foreign carrier incentive to reduce settlement rates;

    - Existing ISR reporting safeguards are ineffective

        -- changes in the ratio of outbound to inbound "settled" traffic are no longer meaningful after removal of the ISP (after which there is no distinction between ISR and settled traffic).

- If High and Upper Middle Income remain at $0.15 and $0.19 benchmarks after 1999 and 2000, rather than moving down to cost ($0.07):

    - *U.S. outpayments 1999-2002 increase by $1.6 billion.*

- Additionally, if all U.S. inbound traffic is terminated at cost once High and Upper Middle Income benchmarks are met:

    - *U.S. outpayments 1999-2002 increase by a further $1.2 billion.*

The best practices rate is also a reasonable and viable threshold for the removal of the ISP.

- Reasonable surrogate for cost and already achieved by Sweden ($0.06) the UK ($0.06), Hong Kong ($0.06 from 1/1/99) and Norway ($0.08). The Netherlands ($0.095), Canada ($0.10), France and Germany ($0.105), Denmark and Italy ($0.11) approach this level.
  - Continuation of the ISP should be required for dominant foreign carriers maintaining higher rates to prevent whipsaws and encourage further reductions to cost.

III. BOC Inbound Geographic "Grooming" Should Be Prohibited Before Access Charges Are Lowered To Cost.

Above-cost access charges would allow the BOCs to make anticompetitive use of their domestic bottlenecks in diverting inbound traffic from other U.S. carriers.

- BOC access charges remain far above cost.
    - Average terminating access charges are five to six times higher than cost.
    - No competitive pressure to reduce access charges.

        -- Local exchange and exchange access competition remains negligible (*e.g.*, 1 percent or less of SBC access lines);

        -- Network element competition stymied by Eighth Circuit decisions and BOC intransigence.

- BOCs can offer lower termination charges than all other carriers for geographically "groomed" inbound traffic. Above-cost access charges would be intra-company transfer payments.
    - "BOC LD affiliates will compete for terminating traffic by offering lower prices, especially for lower cost traffic." (SBC Reply, p. 13.)

- BOC inbound-only geographically "groomed" termination would raise U.S. outpayments, consumer prices and IXC costs.
    - No U.S. consumer benefits from cheaper BOC inbound-only geographically "groomed" termination to foreign carriers.
    - By raising other carriers' costs, BOC inbound-only termination protects BOC local dominance and extends BOC market power to international services.

- No BOC competitive disadvantage from inbound grooming restrictions -- BOCs could still terminate non-geographically groomed international traffic.

    - Grooming restrictions would merely ensure a level playing field while access charges remain above-cost.

No effective safeguards against BOCs using above-cost access to lower termination prices.

- BOC control of exchange and exchange access facilities provides "the incentive and ability to engage in a price squeeze." *Access Charge Order* (¶ 278).

- Price squeezes unlikely "so long as an incumbent LEC is required to provide unbundled network elements quickly, at economic cost, and in adequate quantities." *Access Charge Order* (¶ 280).

    - Unbundled network elements still not available on these terms.

    - Changed circumstances have invalidated the key assumption underlying the Commission's "market based" approach to access reform -- that competitive local entry would reduce access charges to cost.

- Section 272 requirements would not prevent BOC use of above-cost access to lower termination charges below those offered by other carriers:

    - Section 272 nondiscrimination requirements apply only to BOCs *and do not cover services provided by BOC Section 272 affiliates.*

        -- fail to ensure that BOC Section 272 affiliate termination prices cover costs other than access.

    - Secrecy for under-25 percent flexibility arrangements (and/or lack of transparency for non-ISP arrangements) would impede monitoring of BOC Section 272 affiliate termination prices to foreign carriers.

- Section 272 requirements and *Competitive Carrier* separation rules do not apply to BOC out-of-region services. *LEC Regulatory Treatment Order* (¶¶ 210-11).

BOC carriage of all inbound-only international traffic outside the ISP should require in-region authority.

- Commission finding that international return traffic *generated by BOC out-of region international services* does not constitute in-region service was based, in part, on such traffic being "assigned . . . pursuant to the Commission's proportionate return policy." Order on Reconsideration, CC Docket 96-21 (Oct. 20, 1998), ¶ 10.

- BOC carriage of inbound-only non-ISP traffic would not result from neutral proportionate return principles but from active BOC underbidding of other U.S. carriers.
  - Such traffic would not be "return" traffic but inbound traffic resulting from direct BOC negotiation with foreign carriers.

- Inbound international traffic not generated by BOC out-of-region international services should not constitute an out-of-region service.