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Philip L. Verveer

July 2, 1999

EX PARTE

Ms. Magalie Roman Salas
Secretary
Federal Communications Commission
445 12th Street, S.W.
Washington, DC 20554

Re: CC Docket Nos. 98-262, 98-157, 98-227, 99-1, 99-65, and 99-24

Dear Ms. Salas:

On July 1, John Windhausen and Jonathan Askin from the Association of Local Telecommunications Services (ALTS); Dan Kelley of HAI Consulting; Gerry Salemme of Nextlink Communications, L.L.C.; Don Shepheard of Time Warner Telecommunications and I, as counsel to ALTS, met with Kathryn Brown, Chief of Staff for Chairman William Kennard, Dorothy Attwood, Legal Advisor to Chairman Kennard and Pat DeGraba, Office of Plans and Policy. We discussed the ILEC requests for forbearance from dominant carrier regulation for high capacity services. The attached outline summarizes the presentation.

An original and one copy of the letter is submitted herewith in accordance with Section 1.1206(b) of the Commission's rules.

Sincerely,

Philip L. Verveer

cc: Kathryn Brown
Pat DeGraba

Deregulation of Special Access Services -- Timing is Everything

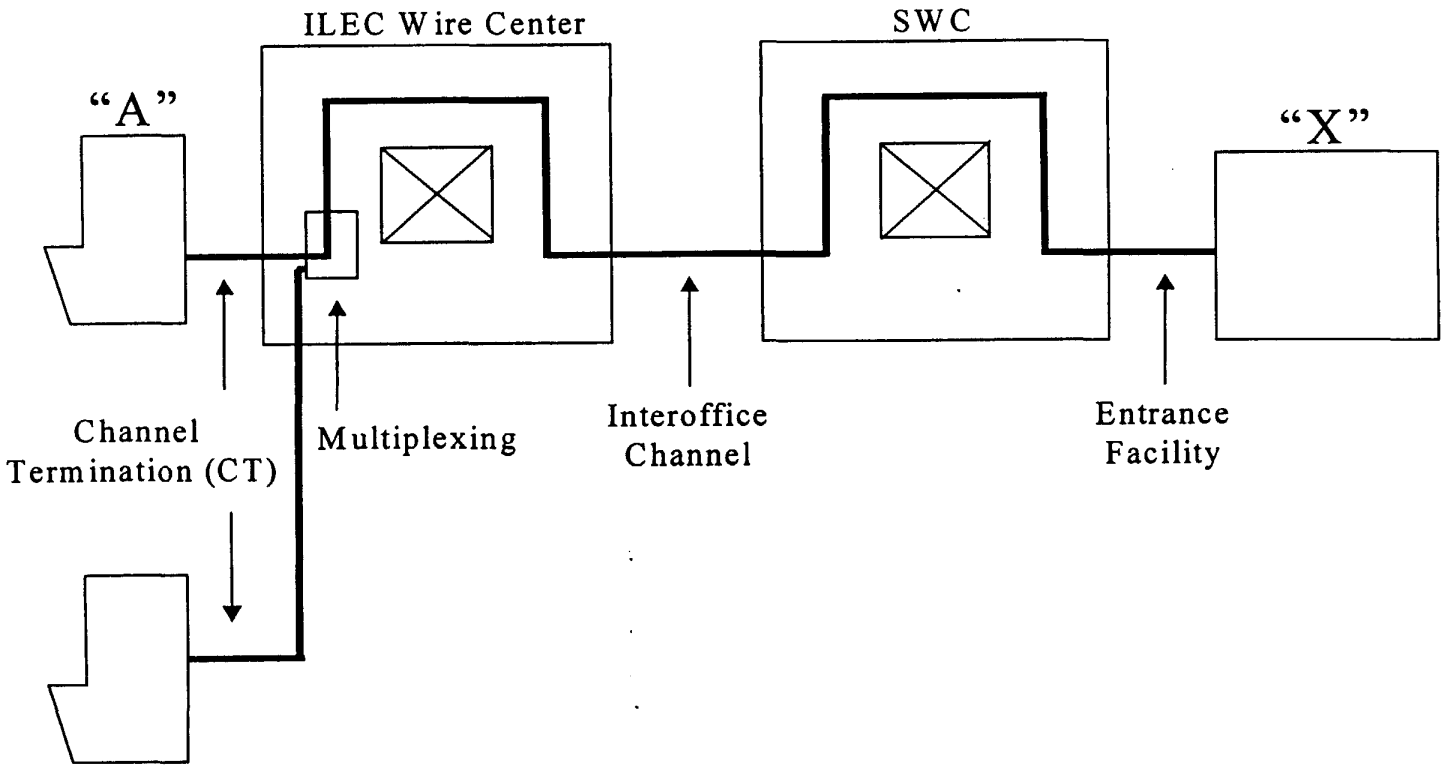
ALTS

July 1, 1999

Facts of the marketplace refute ILEC Claims of Competition

- ILEC marketshare estimates are misleading in forbearance filings
- ILEC filings ignore key linkage between sections 251/252 and Section 10 forbearance requests
- ILEC daily tactics continue to delay competition for all services INCLUDING special access

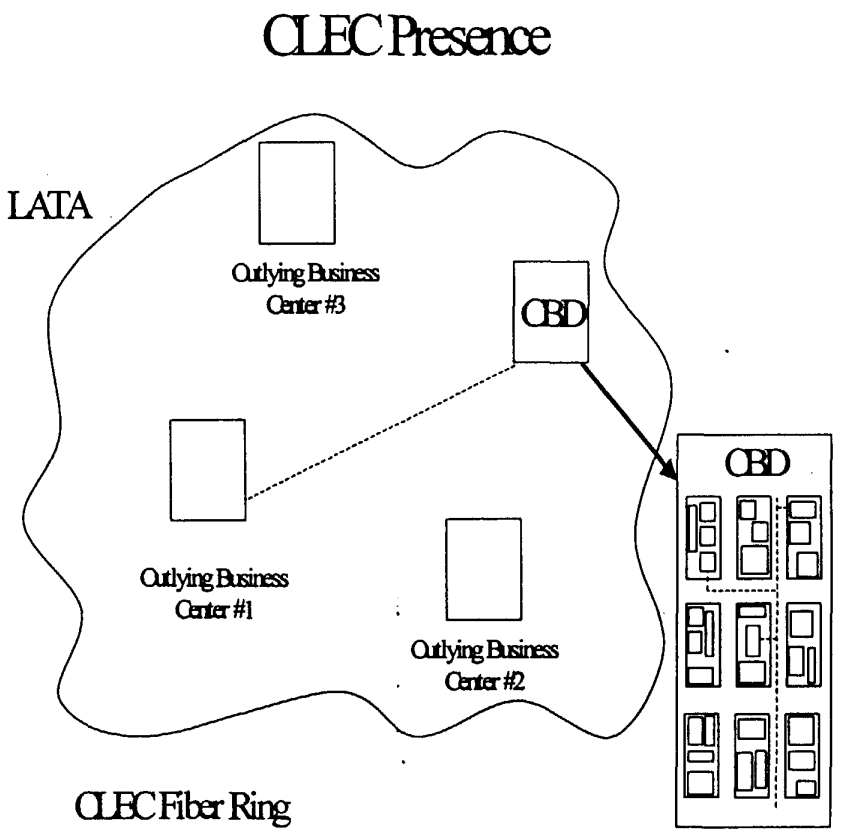
SPECIAL ACCESS



ILECs Retain Substantial Market Power

- In the provision of special access services
- In the provision of network components needed by CLECs to compete in the market for special access services
  - Access to collocation
  - Loops
  - Interoffice transport
- Even within the narrow service and geographic niches where CLEC competition is developing, ILECs retain substantial marketpower

CLEC Configuration



If the Commission grants the ILECs' forbearance petitions, this market power could be used to harm both consumers and competition.

- Where competitive alternatives are not available, prices could be raised.
- Where competitive alternatives are available, prices could be reduced in an anti-competitive manner.
- The net effect will be a reduction in consumer welfare because the prospects for competition will be reduced.

The potential for short-run predatory pricing cannot be ruled out:

- Modern economic analysis demonstrates that predatory pricing behavior can be profit maximizing under certain circumstances.
- Multi-market and network businesses allow dominant firms to signal rivals in order to discourage entry.
- The Department of Justice complaint against American Airlines shows that the antitrust authorities understand and disapprove of such predatory pricing behavior.

The Commission has recognized the danger of strategic anti-competitive pricing:

"If the incumbent is able to develop a reputation of aggressively competing via targeted bids with recent entrants by doing so in a handful of markets, it may be able to dissuade potential entrants from entering any of its other markets. Thus, the incumbent may protect its monopoly position in all of its markets by aggressively competing in markets where entry initially occurs."

In the Matter of CC Docket No. 97-158, Southwestern Bell Telephone Company Transmittal No. 2633 Tariff F.C.C. No. 73, Order Concluding Investigation and Denying Application For Review, rel. November 14, 1997.

The phased-in deregulation of the long distance market was successful.

- That experience can be used to inform Commission decisions regarding deregulation of local markets as well.
- AT&T was declared non-dominant in 1995 only after barriers to entry into the interLATA long distance business had been substantially removed.
- Competitors were no longer dependent on AT&T for facilities needed to compete.
- AT&T had surrendered almost 40 percent of market share and <u>all</u> customers had a choice of carriers.

Despite their market power, ILECs have already been given a great deal of regulatory flexibility:

- In 1980, tariffs were allowed to become effective only after a 90-day review period. Extensive cost support was required. Today, in many cases the tariff notice is 15 days or less and minimal cost support is required.

- Major tariff filings were regularly suspended and investigated. Today, tariffs are often allowed to go into effect with minimal dispute. Tariffs are frequently allowed to become effective even if the Commission finds that an investigation is warranted.

ILECs have been given substantial pricing flexibility

- The Commission has allowed significant rate realignment, allegedly made necessary by competition.
  - The pricing cross-over points between various speeds of service, e.g., voice grade & T1 and T1 & DS3 special access services, are dramatically different today than in years past.
  - Transport competition has led to a dramatic realignment of the rate structure.
  - Rates structures include substantial volume and term discounts.
- ILECs have not taken advantage of the flexibility they have been given.

Allowing the ILECs to engage in contract pricing, subject to retaining their tariffs, is not an adequate safeguard.

- Current price cap rules provide ILECs with substantial ability to alter terms and conditions in order to engage in discriminatory and predatory practices.
- The benefits of new services may be denied to tariff customers.

The ALTS Conclusion

- Contract pricing authority requires ubiquitous, or nearly ubiquitous, competition in the LATA including:
  - Actual collocation in 90% of the ILEC wire centers in the LATA
  - Competitive interoffice transport facilities extending to 90% of all offices in the LATA
  - Self-provisioning or use of unbundled loops covering 20% of total loops in the LATA
  - An efficient and smoothly operating process for provisioning collocation and unbundled network elements at reasonable prices