Before the
FEDERAL COMMUNICATIONS COMMISSION
Washington, D.C. 20554

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| Access Charge Reform | ) | CC Docket No. 96-262 |
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| Complete Detariffing for | ) | |
| Competitive Access Providers | ) | CC Docket No. 97-146 |
| and Competitive Local Exchange | ) | |

COMMENTS OF TDS METROCOM, INC.

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**COMMENTS OF TDS METROCOM, INC.**

TDS Metrocom, Inc. (TDS Metrocom or Metrocom), by its attorneys, submits these comments in response to the Commission's invitation for additional comments concerning Competitive Local Exchange Carrier (CLEC) access charges.[1]

**Introduction and Summary**

TDS Metrocom urges the Commission not to impose regulation on CLEC access charges that has never been shown to be necessary. Unfair and unlawful invalidation of CLEC's access charges would stifle the very competition and increased customer choices that Congress and the FCC are committed to fostering. TDS Metrocom's facilities-based residential and small or midsize market service would be particularly threatened. Instead, the Commission should reject ILEC cost-based assumptions of reasonableness for the charges of CLECs willing to enter these higher cost, more risky markets. CLEC revenue streams are already strained by other increased regulatory obligations and proposed compensation changes. The challenging carriers have not begun to show that CLEC charges above the local ILEC's charges are unreasonable; and the

1 Public Notice, DA 00-2751, CC Docket No. 96-262 (rel. Dec. 7, 2000).

Commission is well aware that CLECs face conditions that make their costs higher. Smaller CLEC markets and small incumbents' "edge out" CLEC operations must also attract higher penetrations than big-city and business-centered CLECs to maintain even their thin profit margins. Even in midsized and small cities the smaller available traffic volumes and customer base for a competitor result in higher costs. The law requires findings that carrier-initiated rates are unlawful and that Commission-set "reasonable" levels are just and reasonable. The facts do not support either determination, and no such findings can be made.

Any benchmark the FCC adopts must take into account the enormous disparities in market facts that govern CLECs in comparison to large incumbents. Thus, the Commission must create a sufficiently high benchmark to reflect CLECs' higher costs and a sufficiently broad exemption to preserve and foster competition and each customer's right to choose a local exchange and access provider. A rural exemption, while essential, is not adequate to accommodate the many competitive disadvantages and comparative diseconomies of scale that confront a CLEC newcomer in a former monopoly market served by a huge incumbent.

**TDS Metrocom Is Trying to Maintain and Expand its Small Market, Largely Residential, CLEC Service in an Increasingly Challenging Environment**

TDS Metrocom is a facilities-based CLEC, started in 1997, which provides service, with an emphasis on providing a choice in local exchange carriers to residential customers in small markets. It currently provides service in the cities of Madison, Green Bay, Appleton, Oshkosh, Racine and Kenosha, Wisconsin, and plans to begin service in several small and medium-sized Illinois and Michigan markets in the near future. None of the cities where TDS Metrocom provides service, except for Madison, has over 100,000 in population. Because of its emphasis on serving residential customers, who are less likely to attract competitive providers, fully a third of the total 60,000 lines TDS Metrocom serves are residential customers. This is a particular benefit to those markets because many CLECs do not serve any residential customers. Residential markets are a particular challenge for Metrocom because the costs of providing residential service are higher and margins are thinner, compared to the traditional CLEC entry model concentrating primarily or wholly on business customers. As a facilities-based carrier offering a competitive choice to both residential and business customers, TDS Metrocom's operations represent the kind of real and mature competition that the Commission has recognized the 1996 Act tried to allow carriers to evolve towards, using the section 251(c) interconnection methods.[2]

Unfortunately, just as competition by carriers such as Metrocom begins to take hold, the Commission and even Congress have been considering regulatory changes that threaten the still-nascent competition by local market entrants. If the largest incumbent succeed in persuading Congress and the Commission to eliminate reciprocal compensation, the loss of revenues will impair CLECs' ability to compete and to serve the more costly residential and smaller markets that TDS Metrocom has targeted. Even proposals for changes that will reduce revenues discourage CLECs from making or pursuing ambitious business plans that would otherwise benefit customers in their potential markets that lack a choice in carriers. In addition, although CLECs are not dominant carriers, the Commission nevertheless has imposed reporting conditions related to numbering, slamming, broadband deployment, universal service and, potentially, quality of service. Amid all of the regulatory requirements are regulation uncertainty surrounding CLECs, the CLECs must also comply with various state reporting requirements. Access regulation could be the proverbial straw that breaks the camel's back.

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[2] Section 257 Proceeding to Identify and Eliminate Market Entry Barriers for Small Businesses, FCC 97-164, GN Docket No. 96-113, 12 FCC Rcd 16802, n. 48 (1997).

Since Metrocom competes against the Ameritech operating companies, now owned by SBC, which have huge market shares and economies of scale, reporting requirements and other regulatory burdens weigh more heavily on the fledgling CLEC's smaller, necessarily leaner operations and must be recovered from a much smaller customer base. Increasingly tight financial markets also raise the cost of capital for CLECs, just at the time when they are trying to expand their operations and increase their market toe-hold.

At the same time, the second generation of interconnection agreements and related state proceedings reevaluating UNE prices, OSS requirements and other interconnection terms are raising prices for CLECs to interconnect with incumbents, coupled with increased regulatory uncertainty, further dampen the incentive and ability for CLECs to invest in expanded service, as well as their access to capital. Even successful, growing CLECs with business plans that are well-founded cannot avoid the pressure of regulatory changes and unknowns, and must divert resources from customer service and expansion to regulatory and legislative battles. The timing could not be worse for a Commission committed to fostering nationwide competition and customer choices to smother CLECs under access charge benchmarks that will expose them to revenue decreases or burdensome regulation even if there is some means to justify above-cap charges.

**The Interexchange Carriers Have Not Shown that CLEC Access Charges Are Unreasonable**

The Interexchange Carriers (IXCs) have been trying for years -- in regulatory proceedings and through self-help by denying statutorily-required interconnection or withholding access payments to many CLECs -- to force CLECs to lower their access charges to no higher than the charges of the incumbent local exchange carriers (ILECs) with which they compete, without ever showing that CLECs' current access charges are unjust or unreasonable. The

Commission has refused in the past to accept the underlying assumption that CLEC rates must be unreasonable if they exceed the charges of the ILEC in their service areas.[3] Now, although the Commission recognized in the Public Notice (p. 4) that costs for CLECs are likely to be higher given their start-up status, as well as their small and limited customer bases, and still without any showing that any CLEC charges are unreasonably high, the Commission is proposing to establish a benchmark for reasonable CLEC rates based on the ILEC's rates. It suggests a possible "rural exemption" to permit higher rates for some CLECs. While TDS Metrocom fully favors a rural exemption if the Commission sets a benchmark, it does not believe: (a) that the record supports any presumption that rates above the incumbent's are unreasonable and require the setting of a benchmark beyond which those rates will not be considered reasonable; or (b) that a benchmark and exemption tied to the ILEC's service area or the size of the CLEC in access lines adequately takes into account the thin markets and size disparity that necessarily confronts a CLEC trying to attract customers in an area where its ILEC competitor had, until recently, a monopoly to serve all customers in that area.

First, as earlier comments in this proceeding have demonstrated, sections 201(a) and 251(a) of the Communications Act require all interstate providers to interconnect with other carriers.[4] And, the regulatory framework for a non-dominant interconnecting carrier's access charges cannot be challenged by refusing interconnection, in violation of section 214(a), but must be challenged in a complaint proceeding pursuant to section 208 or damages action, where

[3] In the Matter of Sprint Communications Co. v. MGC Communications, Inc., File No. EB-00-MD-002, FCC 00-206, para. 6 (rel. June 9, 2000) (Sprint v. MGC).
[4] 47 U.S.C. Sections 201(a), 251(a).

the challenging carrier bears the burden of proving that the CLEC's rate is unreasonable.[5] Moreover, before the Commission can force a carrier to reduce rates, or charge below a prescribed benchmark, it must be able to find not only (1) that the existing rates are "in violation of any of the provisions of this Act," (i.e., in this case, are "unjust and unreasonable'), but also that the prescribed rates are "just and reasonable" under Section 205.[6] The Commission has not made any finding that carrier-initiated CLEC charges are unjust or unreasonable, let alone that rates based on each particular competing incumbent's charges would be "just and reasonable," since it is aware that CLEC costs are higher.

Consequently, the Commission should not be setting <u>any</u> benchmark in this proceeding, with or without a "rural exemption." It has not repudiated its earlier determination to treat CLECs as non-dominant carriers with respect to terminating or originating access.[7] Indeed, even if a complaint had been filed and the lawfulness of CLEC rates properly brought before it, the Commission should adhere to its duly established "presumption of lawfulness given to nondominant carrier rates and practices [that] is employed in the context of complaints alleging violations of sections 201(b) and 202(b), where the complaint must demonstrate that the defendant's rates and practices are 'unjust and unreasonable.' "[8] Until that showing has been made, the only lawful benchmark for CLEC access charges is the presumptively lawful rate set by the carrier.

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5 <u>Sprint v. MGC, para. 5</u>.

6 47 U.S.C. Section 205(a); <u>Sprint v. MGC</u>, para. 5 and note 16.

7 <u>Access Charge Reform, Price Cap Performance Review for Local Exchange Carriers, Transport Rate Structure and Pricing, End User Common Line Charges</u>, CC Docket Nos. 96-262, 94-1, 91-213, 95-72, First Report and Order, 12 FCC Rcd 15982, 16140-16141, p. 360-63 (1997) (determining that non-incumbent LECs should be treated as nondominant in their provision of terminating access); Local Competition Order, 11 FCC Rcd at 15981, p. 976 (stating that non-incumbent LECs, by definition, lack the market power possessed by incumbent LECs).

8 <u>See</u>, <u>Implementation of the Non-Accounting Safeguards of Sections 271 and 272 of the Communications Act of 1934, as amended</u>, FCC 96-489, CC Docket No. 96-149, 11 FCC Rcd 21, para. 351 (1996).

**Even If the Commission Could Lawfully Adopt a Benchmark, a "Rural" Exemption Would Not Go Far Enough**

TDS Metrocom wholeheartedly agrees that any benchmark would require an exemption for CLECs with costs and therefore rates above those of the ILEC with which they compete, but believes that a strictly rural exemption would be far too narrow. CLECs serving higher cost portions of the largest price cap carriers' areas, not only those serving in rural carriers' areas, plainly cannot be held to a standard for reasonable rates based on the costs for a giant incumbent LEC. Congress and the Commission have both recognized that both low-density rural and small or midsized carriers deserve to be differentiated from the largest, urban-centered carriers in tailoring appropriate regulation. For example, Section 251(f) exempts certain incumbent rural telephone companies from the most stringent interconnection requirements and provides for suspension or modification of those requirements for other incumbent groups with aggregated nationwide lines totaling less than 2% of the nation's total access lines. The Commission has also reduced regulation for midsized companies in recognition of their differences from the largest incumbent LECs.[9] The Conference Report on Section 251(f) reported the Senate report's conclusion that

> [t]he Senate intends that the Commission or a State shall, consistent with the protection of consumers and allowing for competition, use this authority to provide a level playing field, particularly when a company or carrier to which this subsection applies faces competition from a telecommunications carrier that is a large global or nationwide entity that has financial or technological resources that are significantly greater than the resources of the company or carrier.

[9] See, e.g., In the Matter of 1998 Biennial Regulatory Review -- Review of Accounting and Cost Allocation Requirements; United States Telephone Association Petition for Rulemaking; Implementation of the Telecommunications Act of 1996; Accounting Safeguards under the Telecommunications Act of 1996; Petition for Forbearance of the Independent Telephone & Telecommunications Alliance; Petition for Rulemaking to Amend Part 32 of the Commission's Rules, Uniform System of Accounts for Class A and Class B Telephone Companies, to Adopt the Accounting for Software Required by Statement of Position 98-1, CC Docket No. 98-81; ASD File No. 98-64; CC Docket No. 96-150; AAD File No. 98-43; RM-9341, FCC 99-106, 14 FCC Rcd 11396 (1999).

The position of the small CLEC seeking to compete with a BOC is equally precarious. Even if the CLEC needs to compete in a small city or residential area, rather than a purely "rural" area, its customer base will be far smaller and less densely packed than the incumbent's pervasive, former-monopoly customer base. Accordingly, any exemption must preserve and foster the gradually developing competition by smaller CLECs and the customer choices they bring to smaller urban and suburban markets, by accounting for the disparity in their size compared to the huge ILEC providers with which they must compete.

A benchmark based on the access charges of a large incumbent LEC is manifestly inappropriate for a small CLEC entrant in that large LEC's territory. Small CLECs are more closely comparable to small ILECs than to the massive RBOCs they are trying to challenge competitively. For example, TDS Metrocom's entire customer base in Wisconsin is 60,000, whereas SBC, which acquired Ameritech, has a customer base of more than 2.25 million lines in Wisconsin alone. SBC's customer base is, thus, more than 37 times Metrocom's subscribership, which is also split among many small Wisconsin cities and suburban residential areas. Hence, SBC has millions of subscribers and hundreds of millions of minutes over which to spread its costs, while Metrocom must recover its high costs of start-up and early years of operation from a comparatively tiny base of customers and minutes. Moreover, even when TDS Metrocom's service area is a metropolitan small market, it does not have the economies of scale that its competitor, SBC, enjoys because of its size and historical monopoly position. Beyond that, CLECs in no way can match the large incumbents' purchasing power for switching, plant and other equipment. CLECs' pricing must accommodate multiple large ILEC transport, trunking and switching charges, as well as having to absorb the transaction costs of negotiating arrangements, for example, for direct trunking, and dealing with the lack of such arrangements until they can be established. Indeed, since CLECs are faced with incumbent networks that are already in place and reflect the incumbent carrier's operating needs and design preferences, CLECs must pay the price for all traffic going through RBOC tandems, which increases their tandem switching and transport costs. CLECs may find themselves at a disadvantage even compared to similarly-sized rural and independent incumbents that have higher existing traffic flows and have already had the time to negotiate direct trunking arrangements.

The economic fact is that, while the location and population density of Metrocom's markets may not qualify them as "rural," the high costs of establishing local and access competition -- and especially residential customer choice -- are real and must be recovered in access charges if customer choice and competition are to take hold and survive as the 1996 Act intends. Only with an appropriate small-CLEC benchmark that recognizes these market realities can competition continue to take hold and grow (unless, of course, the Commission's preferable established policy of presuming non-dominant carriers' rates reasonable until shown otherwise prevails).

A fair and pro-competitive exemption must start from the premise, recognized in the Public Notice (para. 3) and Sprint v. MGC,[10] that CLEC rates that exceed the area's incumbent LEC's rates have not been shown and cannot be assumed to be unjust or unreasonable. Put another way, there is no basis for using the incumbent LEC's access charges as a benchmark for carriers with a short, non-monopoly history, different costs, challenges and economies and a different role to play in moving telecommunications markets from a sole source to a competitive environment. As newcomers, CLECs need pricing flexibility to keep their rates to end users competitive and recover their own costs – not the costs incurred by a company more than 37

[10] Sprint v. MGC, paras. 5-7.

times their size -- without becoming unprofitable. But if the Commission nevertheless chooses an incumbent-based benchmark for assuming reasonableness as if the presumption had been rebutted, it follows that the flawed benchmark must be accompanied by exceptions that provide relief for all the situations where the benchmark is ill-founded, not just in rural areas or for "rural telephone companies."

**Setting an Arbitrary Benchmark to Cap CLEC Access Charges Could Destroy the Emerging Competition in Second and Third Tier Markets and Doom Small LECs' "Edge-Out" Strategies**

Congress did not intend to foster competitive markets only in the densest, largest markets in the country. Second and Third Tier markets are a natural progression for competition as it moves from the highest volume markets and customers out toward smaller cities and residential areas. These markets in smaller cities typically lie in RBOC territory. They require the competitive entrant to take the risk of building up a sufficient customer base where costs are higher and there are fewer, less-concentrated potential customers, fewer business customers and lower traffic volumes to contest with the established incumbent than in major metropolitan areas where competition first appeared. This, again, increases the challenge of succeeding with fewer potential customers and minutes to share in the competitor's costs.

Such areas are likely to be served by smaller CLECs, which lack the resources and financing to compete in major metropolitan areas. In these smaller markets, building out a network costs nearly as much as in the major metropolitan areas, but the CLEC must achieve higher penetration to operate profitably or even stay afloat. Reducing CLEC access revenues and driving them to charge higher end user rates will thwart their efforts to make competition work.

With the large price cap carriers beginning to deaverage UNE rates, CLECs may also have to pay higher UNE rates to serve less populous small cities and residential areas. Added to their already higher costs as fledgling companies, the result of limiting their flexibility to charge current access rates is to squeeze these CLECs and the customers in smaller markets who depend on them for a competitive choice in local service providers. Residential margins are already particularly thin, and having to raise end user rates could quickly erode those thin margins.

While a rural exemption alone would not be an adequate safety valve for an arbitrary benchmark, a suitable exemption certainly must include rural CLECs. Small and typically rural ILECs have been contributing to the spread of competition and the choices of rural customers by expanding their service into neighboring large ILEC areas, particularly where the incumbent's service is inadequate, by means of a new CLEC. Often these are the areas that the largest LECs are selling off because it is less profitable than their business strategies permit. Often, too, the rural CLECs compete using UNEs and overbuilds to provide customers with improved service not available previously from the incumbent in Second Tier or smaller markets or in suburbs of markets where the city is served by larger CLECs. These companies face significant disadvantages from their comparatively small size, limited economies of scale, limited actual and potential customer base and limited traffic volumes. These market facts about competition with an ILEC in a rural market may result in even smaller margins than small city CLECs confront. These rural CLECs lack the size advantages not only of RBOCs and other large price cap companies, but also of smaller incumbents. Using the incumbent's access rates as a benchmark in these markets would effectively cap the CLECs at rates for much larger companies, denying them recovery of their higher access costs via appropriate access charges. It will be difficult, if not impossible, for such a CLEC to invest in a high quality network, pay for UNEs, price competitively and remain in business if the CLEC is robbed of its access pricing flexibility by a change in the Commission's rules. It would make a mockery of the 1996 Act's commitment to fostering competition to stifle these companies' innovations and incentives to expand, thereby smothering competition in less populated parts of the nation by companies with hands-on experience in serving rural customers' needs.

**The Commission Needs to Craft a Competition-Friendly CLEC Exemption**

Unless the Commission takes the most pro-competitive and equitable tack and declines both to set a benchmark for presuming CLEC access charges "just and reasonable" and to allow IXCs to use self help by denying interconnection or refusing payment of CLEC access charges, the Commission will need to fashion an adequately broad exemption to its benchmark to preserve the nascent competition and consumer choices in metropolitan and rural markets alike. While the exemption should cover all CLECs serving in rural, high cost, "rural telephone company," it should not be limited to those areas. As noted above, there are many factors that influence CLEC access costs and therefore rates, including the type of market being served, the size of the CLEC, and the amount of penetration in a market to name a few. It will be extremely difficult for the Commission to craft an exemption that does not arbitrarily penalize a CLEC that has one more customer than the threshold or 100 more minutes of use or serves a city with five too many people or density that is 1.5 persons per square miles too high. However, if the Commission determines a rate cap and an exemption are necessary, all of these factors must be taken into account.

There is ample precedent for distinctions among ILECs, such as the distinctions the Commission's rules makes between Tier 1 or Tier 2 carriers, or 2% and larger holding companies. One alternative that has been suggested would set revenue or access line thresholds for CLECs whose carrier-initiated charges would be deemed reasonable until shown otherwise in a complaint process (i.e., as contemplated in the Commission's policy for non-dominant carriers). However, the reasons that CLEC costs (and therefore charges) are typically higher than those of the large ILECs in whose markets the CLECs must compete turn not only on their absolute size but also on disparities in their customer bases, available economies of scale, market penetration and traffic volumes. TDS Metrocom urges the Commission not to overlook these disparities that justify the differences in charges.

Accordingly, the Commission should continue to follow its traditional non-dominant carrier presumption of validity, rebuttable in a complaint proceeding, to the access charges set by any CLEC unless and until it can design a benchmark that will allow all CLECs to recover their costs or an exception that can prevent any CLEC's carrier-initiated rates from being deemed unreasonable without the required factual showing in a complaint proceeding.

TDS Metrocom recognizes that there may some appropriate alternative approach to preserving competition in both metropolitan and rural markets and will consider the approaches that other parties may file. Our goal is simply to ensure that the hard-won competitive gains CLECs have made so far are not reversed by re-regulation tied to charges based on the costs of huge carriers with entirely different costs and market challenges.

Finally, although the Public Notice suggests (para. 5) a potential tie-in between a CLEC exemption and the universal service regime and support eligibility, the Commission should not mistake legitimate CLEC cost recovery of access costs with support or subsidy. The CLEC should be able to recover its costs, and may be called upon to justify its rates if they are successfully challenged in a complaint proceeding. But IXCs should not be able to veto either a CLEC's charges or a long distance customer's choice of access and local exchange provider. The Commission's longstanding "equal access" policy rests on the pro-competitive effects of allowing customers to choose their long distance carriers and, since the 1996 Act, their local exchange and exchange access provider. The costs of letting customers choose are appropriately costs both of those customers and of the IXCs that need their long distance traffic picked up and delivered to their long distance customers. Indeed, for the Commission to force CLECs to justify their rates in any case where they exceed the charges of the ILEC would erect an unlawful obstacle to the very competition the 1996 Act mandates via sections 251, 252, and 253.

**Conclusion**

Therefore, TDS Metrocom urges the Commission not to apply benchmarks based on the ILEC's access charges to any CLEC, in recognition of the manifest differences in the market facts that confront the ILEC and a CLEC in any market. If the Commission nevertheless adopts access charge benchmarks for CLECs, Metrocom urges a broad enough exemption to allow all carrier-initiated CLEC rates to prevail unless demonstrated not to be cost-based in a complaint proceeding. To be lawful, any such benchmark or exemption would have to take into account, at the very least, a CLEC's disparities in penetration, traffic and/or revenues compared to the ILEC it challenges and the less populous nature of certain markets. For CLECs that seek to serve small markets and residential customers, it is essential that the Commission not adopt a punitive benchmark based on ILEC costs and markets or too narrow an exemption. Such a mistake in resolving the issues here could destroy the development of competition, especially in residential markets, with their tiny margins.

Respectfully submitted,

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