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January 11, 2001

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FEDERAL COMMUNICATIONS COMMISSION
OFFICE OF THE SECRETARY

VIA COURIER

Magalie Roman Salas
Office of the Secretary
Federal Communications Commission
445 Twelfth Street, S.W.
Room TW-A325
Washington, D.C. 20554

Re: *In the Matter of Access Charge Reform, Price Cap Performance Review for Local Exchange Carriers, Interexchange Carrier Purchases of Switched Access Services Offered by Competitive Local Exchange Carriers*, CC Docket Nos. 96-262 and 94-1, and CCB/CPD File No. 98-63

Dear Ms. Salas:

Enclosed for filing in the above-referenced proceeding pursuant to the Commission's December 7, 2000 Public Notice Requesting Comments are an original, and eight paper copies, of the Comments of Focal Communications Corporation, RCN Telecom Services, Inc., and Winstar Communications, Inc.

Please date stamp and return the enclosed extra copy of this filing in the self-addressed, postage prepaid envelope provided. Should you have any questions concerning this filing, please do not hesitate to call us.

Respectfully submitted,

Harisha J. Bastiampillai

Enclosures

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FEDERAL COMMUNICATIONS COMMISSION
OFFICE OF THE SECRETARY

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

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	)	
Access Charge Reform	)	CC Docket No. 96-262
	)	
Price Cap Performance Review For Local Exchange Carriers	)	CC Docket No. 94-1
	)	
Interexchange Carrier Purchases of Switched Access Services Offered by Competitive Local Exchange Carriers	)	CCB/CPD File No. 98-63

COMMENTS OF

FOCAL COMMUNICATIONS CORPORATION, RCN TELECOM SERVICES, INC., AND WINSTAR COMMUNICATIONS, INC.

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January 11, 2001

SUMMARY

The buzzword in the telecommunications industry seems to be carrier compensation reform. In the area of access charges this has not been a new subject as the Federal Communications Commission has been for years trying to make ILEC access charges simpler, more cost based, and market driven. In its *CALLS Order*, the Commission noted its hope that by the end of the term of CALLS proposal, it will be able to deregulate price cap local exchange carriers ("LECs") to reflect competition. In fact, the Commission envisioned the *CALLS* proposal as a transition to economically rational competition.

Disregarding for the moment the merits of the *CALLS* proposal, it would be truly ironic that as the Commission holds out hope of deregulation and market-driven ILEC access rates, it attempts to "reform" CLEC access charges by imposing new regulations and divorcing the CLEC access charges from cost causation principles. The record has demonstrated that there is no need to impose new regulation on CLEC access charges. The vast majority of access charges assessed by CLECs are comparable to those of the ILECs, which is significant in and of itself given the higher costs CLECs face in providing such access. The marketplace is working in that it is providing for competitive CLEC access rates, and in the few cases, if any, where charges might be considered excessive, the Section 208 complaint process is available to address the issue and provide redress. IXCs who feel that charges are excessive have been availing themselves of the complaint process.

In short, the market for CLEC access charges is the market that the Commission should hope will evolve for ILEC charges. This proceeding presents the dilemma of "reform" of a process that is ostensibly working well. Any tinkering made in the name of positive regulation could end up effecting more damage than improvement. The local exchange market is still in the

nascent stages of competitive development. The first few years in the marketplace are difficult for any company, but companies battling entrenched monopolies face a tougher climb. To add "reform" into this mix in the form of curtailing CLEC access charges when there is insufficient indication of a problem would heighten these difficulties and undermine the pro-competitive goals of the Act. The record had demonstrated that CLECs are not gouging the market, but instead are charging competitive rates even in the face of higher costs. No "reform" of these rates is necessary, and any such reform could be very detrimental.

This is not to say no action needs to be taken on this issue. The threats of certain interexchange carriers to refuse to pay CLEC access charges or to refuse to interconnect with CLECs is cause for grave concern. If any action is taken by this Commission in regard to CLEC access rates, and if any benchmark is set, it should be done on the basis of ensuring that CLECs are able to collect their rightful charges and that their customers are able to make and receive long distance calls. Any benchmark set should provide a safe harbor for those CLECs whose rates are within the benchmark and a presumption of validity should attach to those rates within a reasonable range of the benchmark. Also an exemption to the benchmark should be provided for those CLECs providing service in rural and other high cost areas. Any benchmark should reflect the uncontroverted fact that CLECs face higher costs for providing access service than the ILECs in their operating areas.

The Commission should refrain from taking any action more invasive than what we propose in these Comments. Any further actions would tilt the regulatory balance and needlessly imperil CLEC interests. For instance, the record does not support detariffing of CLEC access charges. There is little indication of any problems created by tariffed CLEC access charges. Mandatory detariffing would impose substantial transactional costs on CLECs by forcing them to

negotiate individual contracts with hundreds of interexchange carriers. The CLECs would be in a markedly inferior bargaining position given the substantial resources of many IXCs and the need for CLECs to negotiate the contracts with all due speed. Detariffing would also place CLECs at a marked disadvantage vis-à-vis ILECs who would continue to enjoy all the efficiencies and protections of tariffs.

The Commission should also refrain from tying CLEC access charges to the ILEC access charges, particularly those of the large price cap ILECs. The ILEC access charge system is more complex than that of CLECs with many alternative methods of cost recovery. CLECs are dependent mainly on their per minute access charges for recovering their costs of providing access service, while ILECs have many different ways to allocate costs. The *CALLS Order* did not render ILEC access rates more comparable to CLEC access rates, and if anything, made the two rate systems more disparate. In addition, there are pending petitions for reconsideration of the *CALLS Order* challenging the lawfulness of the rates, so any use of the CALLS rates as a point of comparison or as a possible benchmark would be misplaced. Thus, any benchmark for CLEC access rates should be higher than the access rates for price cap ILECs, and perhaps more in line with the rates set by NECA. The record demonstrates that the costs of CLECs are more in line with those of the smaller ILECs who utilize the NECA tariffs than that of the ILECs.

The Commission should be lauded for its attempts to make the access charge system more rational, cost-based, and market driven. Reform is certainly needed in some areas, but the CLEC access charge system should serve more as a model for reform than a target of reform. The system works save for the refusal of some IXCs to pay the access charges or to interconnect with CLECs. The marketplace may not always produce perfect results, and invariably some

participants will feel aggrieved. If the Commission sifts through the rhetoric, however, it will see that the market is producing cost-based competitive CLEC access charge rates.

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COMMENTS OF
FOCAL COMMUNICATIONS CORPORATION,
RCN TELECOM SERVICES, INC. AND
WINSTAR COMMUNICATIONS, INC.

Focal Communications Corporation ("Focal"), RCN Telecom Services, Inc. ("RCN") and Winstar Communications, Inc. ("Winstar")(hereinafter collectively "Commenters") submit these comments in response to the Commission's request in the Public Notice dated December 7, 2000 in this proceeding for further comment on issues concerning whether the Commission should "reform the manner in which competitive local exchange carriers . . . may tariff the charges for the switched local exchange access service that they provide to inter-exchange carriers."

The Commenters are competitive local exchange carriers ("CLEC") currently operating throughout the United States. The Commenters provide competitive local exchange services to both residential and business customers in their operating territories and provide exchange access services to interexchange carriers ("IXCs") that provide long distance services to its local exchange service customers. The Commenters have committed significant resources to deploy

state-of-the-art network that facilitate both the provisioning of local telecommunications service and exchange access services.

Focal is a facilities-based provider of data and voice communications services, serving primarily traffic-intensive users of local services, value-added resellers, and Internet service providers in major markets nationwide. RCN is developing an integrated offering of local exchange and interexchange telephony, high speed Internet access, and video distribution, largely to residential customers. RCN is relying principally upon construction of its own state-of-the-art broadband fiber optic network. RCN offers originating and terminating access services in numerous markets, particularly in the northeastern corridor. Winstar is a publicly-held company which, among other things, develops, markets, and delivers local telecommunications and broadband services in the United States. Through its operating affiliates, Winstar provides facilities-based local telecommunications services on a point-to-point and point-to-multi-point basis principally using wireless, digital millimeter wave capacity.

I. A NEED FOR "REFORM" OF CLEC INTERSTATE ACCESS HAS NOT BEEN ESTABLISHED

The Commenters are concerned with the apparent assumption underlying the Commission's examination of whether, and how, it should "reform the manner in which competitive local exchange carriers . . . may tariff the charges for the switched local exchange access service that they provide to inter-exchange carriers" that there is a need for reform of CLEC interstate access charges. As explained elsewhere in these comments, most CLECs assess charges for access services are comparable to corresponding ILEC access rates,[1] and, that

[1] CC Docket No. 96-262, Initial Comments of RCN Telecom Services, Inc. at p. 2 (October 29, 1999)("RCN Comments"); CC Docket Nos. 96-262, 97-146, Comments of Winstar Communications, Inc. at p. 5 (July 12, 2000)("Winstar Detariffing Comments").

based on the higher costs they incur, CLECs would be justified in setting interstate access charges that are substantially higher than ILEC rates. The Commission has never made a finding that any CLEC access charge is unlawful, much less that there are substantial numbers of CLECs that have unlawfully high access charges. The information submitted by competitive carriers previously in this proceeding show, at most, that there may be a few "outliers" but that generally competitive carrier access charges fall within a relatively small range of the charges of the incumbents.[2]

The Commenters view the fact that the Commission at this late date has asked major IXCs to submit information about the access charges they pay to CLECs as accurately reflecting the fact that there is no record support for any finding that CLEC access charges on the whole are high or unreasonable. Thus, on the current record, there is no justification for a conclusion that the level of CLEC interstate access charges warrants regulation.

Moreover, to the extent there is any need to address the level of some CLEC interstate access charges, the Act and the Commission's rules already provide adequate mechanisms for doing so. To the extent an IXC believes that a CLEC's interstate access charges are unreasonable the IXC may seek relief by filing a complaint under Section 208 of the Act, the remedy intended for customers to challenge rates for interstate services.[3] Indeed, some IXCs have already used this process.[4]

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[2] CC Docket Nos. 96-262, 94-1, CCB/CPD File No. 98-63, Reply Comments of the Association for Local Telecommunications Services, Attachment A, Integrated Communications Corporation, *Interstate Switched Access Charges, A National Survey: A Public Policy Analysis of Interstate Switched Access Charges, Including a Survey of 1,435 Incumbent Local Exchange Carrier Tariffed Rates.* ("ICC Report")(October 29, 1999).

[3] RCN Comments at p. 7.

[4] *See, e.g., Sprint Communications Company, L.P. v. MGC Communications, Inc.*, File No. EB-00-MD-002 (2000)(The Commission denied Sprint's claim that exchange access rates charged by defendant were unjust and unreasonable and that Sprint failed to meet its burden by relying solely on the rates of defendant's incumbent competitors to establish a benchmark for reasonableness.)

However, while CLEC interstate access charges are not generally problematic, the interstate interexchange marketplace has been seriously disrupted by the fact that some IXCs are refusing to pay CLEC tariffed interstate access charges and are even threatening to refuse to complete calls to or from long distance customers. Rather than embark on new regulatory schemes to regulate CLEC interstate access charges, the Commission should enforce IXCs obligation to pay CLEC tariffed interstate access charges and make emphatically clear that IXCs must complete calls to and from CLEC customers.

Accordingly, The Commenters seriously question whether there is any need to reform regulation of CLEC interstate access charges, other than to take vigorous action concerning some IXCs' refusal to pay access charges and threats to not complete calls.

II. THE COMMISSION SHOULD PROCEED VERY CAUTIOUSLY

Assuming that the Commission determines that it needs to alter in any respect the current regulatory framework governing CLEC interstate access charges, Commenters urge the Commission to proceed very cautiously. CLECs are currently experiencing heightened marketplace difficulties.[5] The Commission should be sensitive to the fact that any regulatory actions that adversely affect CLEC interstate access revenue, or that are perceived as doing so, will only heighten these difficulties and undermine the pro-competitive goals of the Act. In addition, the types of regulatory reform that the Commission may be contemplating in this proceeding are highly problematic. The Commenters take this opportunity briefly to remind the Commission of these problematic aspects of "reform" of regulation of CLEC interstate access charges.

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[5] *See, e.g.* Small Phone Companies Losing Ground to Telecom Giants, CnetNews.com, http://news.cnet.com/news/0-1004-201-2932468-0.html?tag=st.ne.1004.ttext.sf, October 6, 2000.

Detariffing Would Impose Unacceptable Burdens on CLECs. It is possible that the Commission is contemplating that some form of mandatory detariffing of CLEC interstate access charges should play a role in amended regulations governing CLEC interstate access charges. For example, the Commission might impose mandatory detariffing on all CLEC interstate access charges, other than those eligible for the rural exemption, or impose detariffing only on CLECs charging above some benchmark rate, except for those eligible for the rural exemption. Other detariffing schemes are also possible.

In the absence of tariffs, a CLEC would need to individually negotiate interstate access charges with every IXC that might use the CLECs originating or terminating access services, *i.e.* the several hundred IXCs that might be providing long distance service to the CLEC's local service customers or that offer long distance service to virtually any subscriber nationwide that may be calling the CLEC's customer. Simply stated, it is not feasible for CLECs to set interstate access charges through negotiations with the hundreds of IXCs that may use a CLEC's access services. CLECs would need to devote significant time and resources, which are largely unavailable as a practical matter in the current business environment, to negotiating access charges with numerous IXCs.

As it is, CLECs currently struggle to devote adequate resources to their negotiations with ILECs for the interconnection agreements that are critical to their operations. Morevoer, the CLECs would be in an inferior bargaining position vis-à-vis interexchange carriers. Major IXCs possess tremendous resources, including financial resources and personnel to enter into protracted contract negotiations, and thus already have superior bargaining power over CLECs. This situation will be compounded by the fact that CLECs will be in critical need of establishing access service arrangements, thus, giving the IXCs an even more decisive negotiation advantage.

CLECs cannot realistically compete for customers if they are unable to offer customers the ability to receive calls from the millions of customers of any of the major IXCs. On the other hand, it would be far less problematic if AT&T were unable to offer its customers the ability to reach the far fewer customers of a CLEC.[6] Unlike the interconnection negotiation process established by the Act between CLECs and ILECs, there are no formal procedures or time lines in place for CLECs to arbitrate the rates and terms of an access contract.

Negotiating individual contracts with IXCs for access services will require much needed resources that could be more productively used to make the CLECs more competitive in the marketplace and ultimately result in lower prices for consumers. As CLEC operations begin to be able to take advantages of economies of scale and larger customer bases, which will lower the costs of providing access services, the market will witness further reductions in CLEC access charges.[7] Imposing the transactional costs that detariffing will bring will only increase CLEC costs and imperil competition in the local exchange marketplace.[8]

Moreover, in many cases where an IXC terminates calls to a CLEC the CLEC may have no relationship with the IXC in a detariffed environment. This would also be true for originating access services for IXCs offering "dial around" service. Detariffing would effectively compel CLECs to offer free interstate access services to these IXCs.

The detariffing of CLEC access services in any manner would also place CLECs at a significant competitive disadvantage vis-à-vis ILECs. ILECs would be allowed to continue to take advantage of the use of tariffs for access charges. In addition, ILECs would continue to enjoy the benefits of the filed tariff doctrine. Thus, while ILECs enjoy efficiencies of tariffing to

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6 Winstar Detariffing Comments at p. 8.
7 RCN Comments at p. 5.

set rates,[9] CLECs would be forced to incur substantial transactional costs and potential litigation costs in establishing and enforcing access service arrangements. Requiring CLECs to detariff, and denying them use of the filed tariff doctrine, while providing ILECs these advantages would be unfairly discriminatory and necessitate the rejection of mandatory detariffing of CLEC access charges.

Perhaps most tellingly, AT&T noted the competitive disadvantage that CLECs would experience under mandatory detariffing:

> Because ILECs will continue to exercise market power over access services for the foreseeable future, the Commission properly requires them to file tariffs for their access services. However, the existence of such tariffs means that the ILECs need not incur any costs to created switched access arrangements with any IXCs; rather they can rely on their tariffs to establish a clear, binding obligations on IXCs to pay access charges. The disadvantage faced by CLECs who are denied the option of filing tariffs is substantially compounded by the costs of and risks attributable to litigation with recalcitrant access customers concerning their obligation to comply with their access terms. The Commission should be especially reluctant to adopt any proposal that would provide the entrenched incumbents with an additional cost advantage over new entrants.[10]

As noted earlier in this proceeding:

> The effect of mandatory detariffing would be to have an extra weight applied to each CLEC that would limit its ability to expand its customer base, thereby protecting the considerable market share held by incumbent LECs. Given the Commission's pronounced pro-competitive objectives, it should not now institute a policy that hinders the growth of CLECs. In a competitive market, the merits of

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[8] Such an action will imperil the already precarious state of competition in the local exchange market in favor of the long distance market which is already very competitive.

[9] The Commenters understand the factors that led the Commission to seek detariffing and the elimination of the filed tariff doctrine in the interexchange market. Not one party in this proceeding has demonstrated the need for such action in regard to the access service market. For all their complaints, the IXCs have failed to show any excessive rates or abuse of the tariff system. In fact, IXCs have opposed mandatory detariffing in this proceeding and concede that the filed tariff doctrine is not a concern with respect to CLECs. Winstar Detariffing Comments at p. 12.

[10] Winstar Detariffing Comments at p. 9, *quoting,* AT&T Comments in CC Docket 97-146 (filed September 17, 1997) at p.6-7.

a CLEC's service offerings, rather than the scope of its negotiating resources, should determine whether that CLEC is successful.[11]

Accordingly, the Commission should not rely to any significant extent on mandatory detariffing in any "reform" of CLEC interstate access charges.

The Commission's Previous Experience Shows That Benchmark Regulation Is Very Burdensome. The Commission's only substantial experience with benchmark regulation was with rates for cable television service. [12] That experience shows that benchmark regulation is very burdensome for both regulated companies and the Commission. As with cable regulation, it would be necessary for the Commission to establish a methodology and form for converting rates of CLECs that choose not to have the same rate structure as that reflected in the benchmark rate so that it is possible to determine whether the CLEC is above or below the benchmark. To the best of our knowledge, the Commission has still not cleared the backlog of cable benchmark rate cases from 1992.

Even when utilizing the benchmark approach, the Commission recognized that since the benchmark methodology was based on industry-wide data, it may not reflect individual systems' costs of providing service. The Commission recognized that such an approach may not permit all cable operators to fully recover the costs of providing service and impede their ability to attract capital. The Commission, therefore, allowed cable operators to exceed the benchmark

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[11] CC Docket Nos. 96-262, 94-1, 98-157, CCB/CPD File No. 98-63, Comments of Focal Communications Corporation and Hyperion Telecommunications, Inc. d/b/a Adelphia Business Solutions at p. 17 (Oct. 29, 1999)("Focal/Adelphia Comments").

[12] The Commission's most extensive experience with benchmark regulation was regulation of rates for cable service under the 1992 Cable Act. *See Implementation of Sections of the Cable Television Consumer Protection and Competition Act of 1992 - Rate Regulation*, MM Docket No. 92-266, 8 FCC Rcd 5631 (1993). That experience shows that what was initially intended as a simple way of regulation turned about to be extremely complicated and burdensome.

rate if they could make the cost showings supporting the higher rate.[13] If a benchmark approach is utilized, such flexibility is warranted here.

Any Benchmark Must Guarantee CLEC Recovery. A possible benefit of a benchmark approach is that it could provide some assurance of payment by IXCs of CLEC rates that are at or below the benchmark. However, this will only be the case if the Commission explicitly establishes that requirement. To the extent the Commission determines that any regulation of CLEC interstate access charges is necessary, the Commenters urge the Commission adopt the least intrusive regulation possible. This regulation should be defined by the premise that the real problem is not excessive CLEC access charges, but the failure of IXCs to pay reasonable access charges. If the Commission otherwise satisfactorily resolves other problematic features of a benchmark approach, the Commission should provide that IXCs must pay any CLEC rates at or below the benchmark. If a CLEC is at, or within a reasonable range of the applicable benchmark, then that CLEC should be afforded a safe harbor against a Section 208 complaint and its rates should be presumed just and reasonable.[14] For those CLECs that exceed this reasonable deviation, they should be given the opportunity to demonstrate that their rates are in fact just and reasonable.

Any Benchmark Tied to ILEC Rates Must Accurately Determine the ILEC Rates Most CLECs do not utilize the complex rate structure that ILECs do, particularly that of price cap ILECs. Many CLECs have never assessed the subscriber line charges ("SLCs"), primary interexchange carrier charges ("PICCs"), and other flat non-traffic sensitive fees imposed by

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[13] CC Docket Nos. 96-262, 94-1, CCB/CPD File No. 98-63, Reply Comments of the Association for Local Telecommunications Services at pp. 25-26, fn. 64 (October 29, 1999)("ALTS Reply Comments").

[14] Focal/Adelphia Comments at pp. 9-15; RCN Comments at p. 13; CC Docket No. 96-262, 94-1, CCB/CPD File No. 98-63, and CC Docket No. 98-157, Comments of Winstar Communications, Inc. at p. 4 (October 29, 1999)("Winstar Comments").

ILECs. Thus, while many CLECs utilize simple per minute access charges, ILECs utilize a myriad of charges and methods of cost recovery. The *CALLS Order* somewhat reduced and simplified the number of charges, but as shall be shown below, merely allowed to ILECs to target their cost recovery to other revenue streams. Thus, any benchmark based on ILEC rates must ensure that all the applicable ILEC charges and cost recovery mechanisms for access related services are taken into account. If the Commission decides to employ ILEC rates in setting a benchmark rate for CLECs, the Commission must take into account both the flat and per-minute charges imposed by ILECs.

To What Rate Elements Would the Benchmark Apply? Obviously, it will be necessary for the Commission to establish to what rate elements the benchmark applies and to what rate elements it does not apply. For example, the Commission might establish that the benchmark applies to all traffic sensitive charges. It will be necessary for the Commission to specifically establish what charges and services are encompassed within traffic sensitive charges so that CLECs and IXCs will know what charges are entitled to the protection of the benchmark, whatever form that takes, and to which the IXC obligation to pay attaches. This will permit those CLECs that want to restructure their rates so that they can conform to the benchmark to do so. On the other hand, there may be CLECs whose rate structures do not precisely match the structure of the benchmark and prefer to keep their current rate structure. Any benchmark approach should permit CLECs to do so and should not formally, or as a practical matter, prescribe a rate structure for CLECs. In order to accommodate CLECs that do not want to revise their rate structure to conform to the benchmark, the Commission will need to identify a methodology by which they can convert their current rate structure for the limited purpose of making a benchmark comparison. Requiring CLECs to conform their rate structure to that

reflected in the benchmark, either directly, or as a practical matter, would also be very burdensome to CLECs.

Any Benchmark Approach Must Assure that IXCs Must Continue to Interconnect with CLECs. The Comments previously submitted in this proceeding establish that interexchange carriers are required to interconnect with *all* carriers (including CLECs) by the Communications Act of 1934, as amended. The Commenters will not reiterate the legal arguments that have been put forth by other commenters in this proceeding as to why interexchange carriers may not unilaterally refuse to deliver or accept access traffic from any local exchange carrier, except to state that a carrier that refuses to interconnect with or accept traffic from any local exchange carrier would violate Sections 201(a), 202(a), 203, 214, 251(a) and 214 of the Act. The CLEC Commenters note that the interexchange carriers have put forth no compelling arguments as to why the competitive carrier's interpretation of the Communications Act is incorrect. Unfortunately, however, the incidence of interexchange carrier refusal to pay tariffed rates appears to be increasing. AT&T has continued to threaten to accept or terminate calls from or to certain local exchange carriers. Focal has recently heard that AT&T is considering, or may have already implemented, a policy of not accepting additional primary interexchange carrier designations ("PICs") from Focal. Thus, any existing or future Focal customer seeking to change their long distance service to AT&T would be unable to do so. The Commission needs to preclude such practices of IXCs as violative of the Act for the reasons already detailed in the record of the proceeding.

Moreover, there is ample public policy reasons why the Commission should articulate, in the strongest language possible its policy that interexchange carriers may not refuse to deal with any local exchange carrier. Unless the Commission unequivocally establishes that principle, end

users may be left without service, competitive carriers may be forced into negotiating access rates with every interexchange carrier, and competition would be severely restricted.

It is therefore imperative that the Commission, in the strongest language possible instruct the interexchange carriers that the remedy established in the Telecommunications Act under Section 208 is the only remedy that it has if it believes that any carrier's access rates are too high.

III. THE *CALLS ORDER* DOES NOT PROVIDE ANY GUIDANCE FOR CLEC INTERSTATE ACCESS CHARGES

A. CALLS Rates and Rule Changes are Unlawful

In the *Public Notice*, the Commission seeks information on how CLEC access rates compare to those of incumbent local exchange carriers, especially after changes to ILEC rates negotiated by some ILECs and some interexchange carriers and established by the Commission in the *CALLS Order*.[15] This apparently reflects an assumption on the part of the Commission that price cap ILEC rates established in the *CALLS Order* are lawful. In fact, for the reasons presented in the petitions for reconsideration filed by ALTS, Focal and others those rates are unlawful.[16] More particularly, the rate adjustments and rule changes adopted in the *CALLS Order* are unlawful because, among other reasons, they are inherently arbitrary, such as the use of the X-Factor for non-productivity purposes; because the Commission's essential justification that the rate adjustments and rule changes adopted in the *CALLS Order* reflect an industry consensus was erroneous in that most price cap ILECs, most IXCs, and CLECs were excluded from formulation of the "consensus" proposal; because the Commission did not establish any procedures for

[15] *Access Charge Reform*, CC Docket Nos. 96-262, 94-1, 99-249, and 96-45, Sixth Report and Order in CC Docket Nos. 96-262 and 94-1, Report and Order in CC Docket No. 99-249, Eleventh Report and Order in CC Docket No. 96-45, FCC 00-193 (May 31, 2000)("*CALLS Order*").

[16] CC Docket Nos. 96-262 and 94-1, Petition for Reconsideration of Focal Communications Corporation and The Association for Local Telecommunications Services (July 21, 2000).

adjusting price cap rates based on industry negotiations instead of price cap rules; and because the size of the new universal service fund is completely arbitrary. Accordingly, the Commission may not establish any benchmark governing CLEC interstate access charges founded on any rates or rule changes adopted in the *CALLS Order*.

At a minimum, the Commission should resolve petitions for reconsideration of the *CALLS Order* and permit any appeals to be resolved before basing any CLEC benchmark in any respect on CALLS ILEC rates. Requiring CLECs to conform to CALLS rates before the lawfulness of those rates have been established could unnecessarily do significant harm to CLECs and impose unnecessary regulatory burdens.

B. ILEC Rates Negotiated by ILECs Have No Application to CLECs

In the *CALLS Order*, the Commission adjusted capped rates of interstate access charges of price cap ILECs and amended its access charge and price cap rules based on negotiations between some ILECs and some IXCs. The Commission viewed the CALLS plan as representing a negotiated solution to contentious access charge issues and justified adoption of the CALLS plan on that basis even though the rate adjustments and rule changes it adopted were otherwise completely inconsistent with price cap rules. Similarly, the *CALLS Order* established a new universal service fund on the basis of CALLS member negotiations instead of any cost-based estimate of the amount of implicit universal support in interstate access charges.

The Commenters believe that Commission-sponsored negotiations might form a suitable approach to resolving regulatory issues concerning CLEC interstate access charges. In this regard, The CLEC Commenters support the ALTS GREAT proposal. However, rates that ILECs negotiated by ILECs for themselves may not be presumed applicable, or automatically

applied, to CLECs. In fact, ILEC access rates were already a poor point of comparison to CLEC access rates even before the *CALLS Order*. As CLECs noted in the initial round of comments on CLEC access charges:

> For purposes of simplicity most CLECs do not utilize the complex access charge rate structure to which price cap incumbent LECs must adhere. Specifically, many CLECs do not assess subscriber line charges ("SLCs"), primary interexchange carrier charges ("PICC"), and other flat non-traffic sensitive fees imposed by incumbent LECs. Thus, it is inappropriate for AT&T and other IXCs to compare the per minute access charges assessed by CLECs (which may comprise the entire access charge), solely against the per minute charges assessed by incumbent LECs, thereby excluding the non-usage sensitive charges imposed by incumbent LECs.[17]

The Commission asserts in its *Public Notice* that it eliminated several of the flat-rated charges that participating LECs charge to IXCs, and seems to imply that a more meaningful comparison between ILEC and CLEC access rates is now possible.[18] The *CALLS Proposal* did not as much eliminate charges as it attempted to simplify common line charges by "combining the SLC, PICC and CCL charges into a single end-user charge."[19] Thus, while eliminating some charges, such as the residential and single-line business PICCs, it increased the SLC.[20] The goal was primarily to have "price cap LECs recover a large share of their NTS common line costs from end users who cause them instead of carriers, and to recover the costs on a flat-rated, rather than usage-sensitive basis."[21] This reallocation of cost recovery will not affect the ILECs revenues as they will be able to recover the revenue lost from elimination of some of the charges through increases in the SLC and universal service fund direct subsidies. The Commission

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17 CC Docket Nos. 96-262, 94-1, 98-157, CCB/CPD File No. 98-63, Comments of Focal Communications Corporation and Hyperion Telecommunications, Inc. d/b/a Adelphia Business Solutions at p. 10 (October 29, 1999)("Focal/Adelphia Comments").

18 CC Docket No. 96-262, Public Notice at ¶ 8 (December 7, 2000)

19 *CALLS Order* at ¶ 70.

20 *Id.* at ¶ 76.

21 *Id.*

compared ILEC revenues over the five-year period under the CALLS Proposal with what their revenues would be under the status quo and determined that they are roughly the same.[22]

The CALLS access charge regime, however, does not facilitate a direct comparison between price cap ILEC access rates and CLEC access rates. There are three main reasons why the CALLS rates will not serve as proper source of comparison for CLEC access rates and why the CALLS rates would be a poor source of a benchmark for CLEC access rates. First, the CLEC access rates are cost and marketplace driven, while the CALLS rates are more the arbitrary products of negotiations between the large players in the telecommunications industry. Second, the CALLS proposal insulates ILEC revenues by enabling ILECs to recover any reduction in switched access charges from other sources. CLECs do not have this revenue-insulation capability. Third, CLECs rates are more traffic sensitive and thus more per-minute charge oriented, while the CALLS ILEC rates are more directed to lowering per minute charges and relying on flat-rated, non-traffic sensitive charges. CLECs are still primarily relying on per minute charges to recover costs of access service while ILECs still utilize flat-rated charges such as the SLC.

1. CALLS Rates Bear Little Relation to Cost/Productivity

Price cap regulation was designed as a transitional regulatory scheme until the advent of actual competition would render such regulation unnecessary.[23] The ultimate goal of the Commission is to deregulate ILEC access rates and let competition bring about cost-based rates.[24] In short, the goal is to reach the situation currently in place with CLEC access rates, *i.e.*, have the market and competitive forces determine the rates. Price cap regulation was designed to

22 *Id.* at ¶ 41.
23 *Id.* at ¶ 16.
24 *Id.* at ¶ 35.

be a proxy for competitive forces. Price cap regulation allows prices to increase by a measure of inflation, minus a productivity offset, or X-factor.[25] The X-factor represents the amount by which LECs can be expected to outperform economy-wide productivity gains. Thus, proper use of the X-factor would allow ILEC access rates to more mirror market forces, *i.e.*, non-dominant companies would normally pass through increases in productivity to their customers through reduced rates. The Commission had determined that use of an industry-wide average productivity factor is consistent with the goal of creating price regulation that replicates the incentives provided by competition.[26]

The CALLS proposal transforms the X-factor from a productivity factor into a target factor that is designed to reduce rates to a negotiated amount, and is not linked to productivity.[27] The reductions are targeted to the baskets comprising switched access services with the goal being attainment of a particular negotiated interstate average traffic sensitive rate. Rates in untargeted baskets would remain largely unchanged.[28]

The CALLS proposal, thus, totally disengages itself from market factors and instead arbitrarily picks a target switched access rate and defines an X-factor for switched access that does not define productivity for that basket.[29] The price cap rates now have no relation to LEC productivity.[30] Thus, ironically, while purporting to have ILEC access rates defined by market forces, the CALLS rates are totally disengaged from market forces and are instead arbitrarily defined. The *status quo* rate structure displaced by the CALLS Proposal did a better job of

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25 *Id.* at ¶ 135.

26 *Price Cap Performance Review for Local Exchange Carriers*, CC Docket No. 94-1, 10 FCC Rcd. 8961, 9027.

27 *Id.* at ¶ 140.

28 *Id.* at ¶ 141.

29 Focal/ALTS Petition at p. 4.

30 *Id.*

assuring that the rate structures for access charges are more in line with the way that costs are incurred.[31] Thus, not only are the CALLS rates unlawful for the reasons raised in the petitions for reconsideration, they are arbitrary and totally displaced from notions of actually costs and productivity. As an economist analyzing the CALLS proposal noted, "the CALLS proposal to target reductions in switched access usage rates is not based on quantitative economic evidence regarding improvements in economic efficiency, promoting competition, and encouraging innovation."[32] This economist cautioned that the CALLS rates could be predatory noting:

> Notwithstanding the difficulties in measuring and defining forward-looking incremental costs, as a practical matter, cost information is required for a determination of predatory prices. The CALLS Proposal does not contain the relevant cost information. It further precludes an economic evaluation of switched access usage rate floors, by proposing that incumbent local exchange carriers would no longer be required to file cost studies on February 8, 2001 (see section 3.2.8 of the Modified Universal Service and Access Reform Proposal). In order to foster competition, and advance innovation, the FCC has determined that prices for interstate access, on average, should decline by 6.5% after adjusting for inflation. Due to extraordinary and targeted price reductions for switched access usage rates, and the paucity of (reliable) cost information, the possibility of predatory prices should not be summarily discounted.[33]

Even if the prices are not predatory, the targeted price reductions generate insufficient revenues in relation to costs incurred.[34] And, the CALLS proposal allows ILECs to offset these revenue reductions in other ways, and does not result in an overall decrease of revenues for the price cap ILECs. This will not be the case for CLECs who will be hamstrung in their ability to recover these revenues if the CALLS rates are used as any type of benchmark. For these reasons, the CALLS rates would be a very poor source of comparison to the CLEC access rates

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31 *Id.* at p. 8.

32 *Access Charge Reform/Price Cap Performance Review for Local Exchange Carriers*, CC Docket Nos. 96-262, 04-1, Comments of Focal Communications Corporation, Statement of Jeffrey I. Bernstein Concerning Revised Plan of the Coalition for Affordable Local and Long Distance Service, at p. 2 (April 3, 2000)("Bernstein Statement").

33 Bernstein Statement at p. 2.

because CLEC rates are actually being defined by competitive forces and are designed to recover their actual costs of providing switched access service.

2. The CALLS Proposal Insulates ILEC Revenues

As the Commission noted, the CALLS Proposal will not lead to any revenue reduction for the price cap ILECs. To overcome revenue deficiency, the CALLS Proposal provides for i) reduction of price cap offset; ii) removal of revenues from price cap basket; iii) rebalancing of rates within price caps.[35] Under the CALLS approach, special access services are removed from the targeted baskets, and are given a lower X-factor for the first year.[36] As CLECs noted, this allows the price cap ILECs to target rate reductions to traffic-sensitive rates, which are subject to competition, while revenues in less competitive areas are maintained.[37] CLECs do not have this luxury as they must rely primarily on their switched access charges to recover their costs of providing access service, and they can ill afford to price these services at the below-cost CALLS rates for switched access.

Second, ILEC USF assessments are removed from the existing price cap regulatory scheme. Instead, interstate access support for price cap ILECs will be buttressed by a new $650 million universal service support.[38] CLECs noted how the size of this fund, which was arbitrarily set, serves to "insulate a substantial portion of ILEC revenues from competition."[39] Finally, price cap ILECs can also recover revenues through higher subscriber line charges.[40]

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34 *Id.*
35 *Id.*
36 *CALLS Order* at ¶ 149.
37 Focal/ALTS Petition at p. 11.
38 *Id.* at ¶ 206.
39 Focal/ALTS Petition at p. 10.
40 Bernstein Statement at p. 3.