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Before the
Federal Communications Commission
Washington, D.C. 20554

In the Matter of	)	
	)	
Access Charge Reform	)	CC Docket No. 96-262
	)	
Hyperion Telecommunications, Inc. and Time Warner Petitions for Forbearance, Complete Detariffing for Competitive Access Providers and Competitive Local Exchange Carriers	)	CC Docket No. 97-146

REPLY COMMENTS OF
Z-TEL COMMUNICATIONS, INC.

Claudia J. Earls
Z-Tel Communications, Inc.
601 S. Harbour Island Blvd., Suite 220
Tampa, FL 33602
(813) 233-4637

Dated: January 26, 2001

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REPLY COMMENTS OF
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Z-Tel Communications, Inc. ("Z-Tel"), by its counsel, hereby submits its Reply Comments in response to the Commission's Notice in the above-captioned proceedings.[1] As a provider of competitive local exchange service to residential customers in twelve states, Z-Tel has a direct and vital interest in the outcome of this proceeding. Indeed, the outcome of this proceeding will affect substantially both the sustainability and expansion of competition in local exchange markets.

In these Reply Comments, Z-Tel endorses the Guaranteed Reduced Exchange Access Tariffs ("GREAT") Proposal described in the comments submitted by the Association for Local Telecommunications Services ("ALTS"). Z-Tel urges the Commission to adopt the GREAT Proposal or something very similar to it.

[1] *Common Carrier Bureau Seeks Additional Comment on Issues Relating to CLEC Access Charge Reform*, DA 00-2751 (rel. Dec. 7, 2000).

I. INTRODUCTION AND SUMMARY

Z-Tel, in its initial comments, expressed its support for the establishment of a benchmark for CLEC access charges so that tariffed access rates at or below the benchmark would be presumed to be just and reasonable. The GREAT Proposal puts forward exactly such a system, including a gradual decline of CLEC access charges over time. The GREAT Proposal's CLEC access rate of $0.025 per minute a) adequately allows for differences between the scale economies of CLECs and ILECs; b) does not unreasonably interfere with the pricing decisions of market participants; and c) constrains any potential abuse by CLECs of the alleged peculiarities in the supply of terminating access. In addition, by establishing a national benchmark rate, the GREAT Proposal eliminates the need for the Commission to engage in a multitude of complex rate cases. Further, according to data submitted by AT&T, the proposed benchmark rate represents, on average, an immediate 42% reduction in CLEC access charges.[2]

The reasons for supporting a benchmark proposal, such as the one clearly set forth in the GREAT proposal, are numerous, but most obviously: 1) mandatory detariffing of access charges, regardless of their level, would place Z-Tel at a substantial competitive disadvantage as compared to incumbent local exchange carriers ("ILECs") and Interexchange Carriers (IXCs) that are now entering the local exchange market; and 2) because ILECs continue to have the ability to bind IXCs with tariffs, detariffing would raise a *barrier to entry* into the local exchange market because Z-Tel, and other similarly situated CLECs, would have to incur the costs of negotiation of access arrangements with hundreds of IXCs to provide those same services while the incumbent monopolist do not.[3] Clearly, raising entry barriers and facilitating the abuse of

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2 See AT&T Comments, Appendix A

3 The use of the term "barrier to entry" often is incorrectly used in regulatory proceedings. In this particular case, however, mandatory detariffing clearly satisfies the standard, textbook definition of "barrier to entry" proposed by Nobel Economist George Stigler:

market power against CLECs by large IXCs, who may be rivals in the local exchange market, is not a policy that would facilitate the increase of competition in the local marketplace.

II. THE QUESTION OF MARKET POWER

Both AT&T and Sprint conclude that "market failure" is endemic to terminating access. AT&T and Sprint's premise is that LECs (any LEC, not just CLECs) possess market power in the terminating access "market" because terminating access is paid by a third-party (rather than the LEC's end user). The interexchange carrier cannot choose the terminating carrier, nor can an end user choose its terminating access provider independent of its originating access provider. In effect, AT&T and Sprint's argument is that each local exchange customer is a market unto itself – a market best described as a monopoly.

AT&T and Sprint claim that the root of market power in (terminating) access is the direct or causal link of supply between terminating and originating access and the third-party payment of terminating access. If this is true, then AT&T's detariffing solution to the alleged market power problem is untenable. Tariffs, generally speaking, are a means by which regulators monitor and control the prices of firms that possess, or may possess, market power. Absent tariffs, firms with market power will exploit that power by raising rates. If CLECs possess market power as AT&T claims, it would not be rational for AT&T to seek to detariff the CLECs' access rates and leave the determination of rates to negotiation. Detariffing does nothing to reduce the alleged market power; it only allows the CLECs to exploit it without constraint. If AT&T and Sprint's allegations of market power are valid, then mandatory detariffing is the last

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"A barrier to entry may be defined as a cost of producing (at some or every rate of output) which must be borne by a firm which seeks to enter an industry but is not borne by firms already in the industry (George Stigler, *The Organization of Industry*, Homewood, IL: Richard D. Irwin, 1986, p. 67).

thing the Commission should do. The existence of market power would give rise to the need for the regulation of access charges.

AT&T and Sprint's assertion of market power in the access market appears particularly odd when considering the fact that AT&T refuses to pay anything to Z-Tel for terminating access, and has refused to negotiate a terminating access rate with the company. Z-Tel apparently possesses no market power in relation to AT&T. Similarly, Sprint decides what it wants to pay Z-Tel, and refuses to pay Z-Tel's tariffed access rates. Indeed, if there is market failure in access markets, it does not appear to be on the side of the market AT&T and Sprint attribute it to. Rather, it is AT&T and Sprint that possess market power in the access market, not CLECs. Z-Tel is forced, by its own will to survive, to terminate AT&T traffic at a price of zero and Sprint's traffic at whatever rate Sprint decides to pay. Even if Z-Tel could block traffic from particular carriers, which it cannot, the company could not, as a practical business matter, block AT&T or Sprint traffic. No CLEC, including Z-Tel, could acquire residential customers with a product offering that excludes the ability to receive calls from well over half of all of households.[4] Through the power of network effects, AT&T and Sprint can decide unilaterally what a CLEC's terminating access rate will be.[5] Negotiation is not the alternative to tariffs; rather, the alternative is AT&T and Sprint deciding what access rates will be.

Evidence provided by AT&T and Sprint regarding market power in access markets is unconvincing. For example, Sprint asserts "[t]he only reason – the only reason – CLECs can

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4 At the end of 1996, AT&T controlled 63% and Sprint 7% of presubscribed access lines for a combined total of 70% of all presubscribed lines (Trends in Telephone Service, Table, July 1998, p. 41 and Table 10.1). The Commission's Industry Analysis Division no longer reports statistics on presubscription. Under the assumption that AT&T's share of presubscribed lines fell proportionately with its share of direct-dial minutes from 1996 through 1999, AT&T's share of presubscribed lines alone would be 54% at the end of 1999 (Trends in Telephone Service, December 2000, Table 10.10).

even contemplate charging rates for access that exceed those of the ILEC whose territory they serve is that, with respect to IXCs, CLECs have market power (p. 2, emphasis in original)." Under Sprint's evidentiary requirements for proof of market power, Sprint likewise must possess substantial market power in the domestic long distance industry. Sprint's Anytime rate of $0.10 per minute ($4.95 flat fee per month) is 30% greater than AT&T's One Rate of $0.07 per minute (with the same $4.95 flat fee per month).[6] Sprint's contention that price differences in the same market is indicative of market power speaks poorly of the competitiveness of the interexchange business. Of course, it is not Z-Tel's position that any interexchange carrier possesses market power in the interexchange market. Z-Tel provides interexchange service and is well aware of the intense rivalry present in that market. The point is that Sprint's assertion of market power, based simply on price differences, is unfounded. As Z-Tel made clear in its initial filing, price differences among competing firms may exist for a variety of reasons, including the influence of regulation.

III. COMPARING ACCESS RATES

Both AT&T and Sprint provide quantitative comparisons of CLEC and ILEC access rates. As discussed in Z-Tel's initial filing in this proceeding, exactly what these comparisons mean is difficult to ascertain. At least one insight, however, can be extracted from the data provided by Sprint.

Consider the access rates presented in Sprint's Appendix 3. For convenience, a summary of the table is provided below. As illustrated by the table, there is variation in access rates by ILEC. For example, the rate difference between Bell Atlantic South and Bell Atlantic North is

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5 AT&T could, without much doubt, get away with paying CLECs nothing for terminating access absent tariffs (much like it does today).

6 The prices were found at www.att.com and www.sprint.com.

47%. Pacific Telephone and SNET have rate differences of about 72%. Larger differences are observed between the rates of GTE and Sprint and those of the larger ILECs. Sprint's rate, for example, exceeds the SWBT rate by about 110%. Why do such large differences exist across markets? Do regulators allow Sprint to exercise market power more fully than they do the larger ILECs?

Table 1. Summary of Sprint's Access Calculations

ILEC	Rate	ILEC	Rate
Ameritech	0.00679	SNET	0.00717
Bell Atlantic South	0.00641	SWBT	0.00552
BellSouth	0.00768	USWEST	0.00675
Bell Atllantic North	0.00940	GTE	0.01335
Pacific Telephone	0.00418	Sprint LTD	0.01163

Source: Sprint Comments, Appendix 3, p. 2

The answer, of course, is that Sprint has higher costs than do the larger ILECs and regulators allow such costs to be reflected in access rates. It is surprising that Sprint, a company that benefits from cost-adjusted access rates, seeks so intently to prohibit costs from entering the calculation of CLEC rates. Sprint, and AT&T for that matter, cannot argue that the appropriate rate comparison between ILEC and CLEC is rates 'in the same market,' since they preclude the possibility that two firms can supply the same market. In the AT&T and Sprint view, each CLEC "has a monopoly over termination to its own customers (Sprint, p. 3)."[7]

[7] Similarly, Sprint's assertion that Commission precedent holds that "in a multi-carrier market, no single carrier is entitled to cover its costs (Sprint, p. 2)" is irrelevant. According to Sprint's theory of the terminating access monopoly, there can be no "multi-carrier market."

The reasonableness of adjusting LEC access rates for relative scale economies is set forth clearly in the Commission's recent CALLS Order. The omission makes very clear that scale economies is a legitimate factor in determining the reasonableness of access rates:

> We find that the lower target rate of 0.55 cents is reasonable for the larger BOC LECs and GTE due to their economies of scale and broad subscriber bases. We find that a slightly higher target rate of 0.65 cents is reasonable for other LECs that by definition do not have the subscriber bases and resources of the larger BOCs. In addition, we find that a target rate of 0.95 cents for very low-density price cap LECs is reasonable. Due to the nature of their service areas, very low-density price cap LECs experience costs that are significantly higher than other price cap LECs of their size, and are unable to spread those costs over a large subscriber base. Therefore, we agree that the higher level is appropriate for very low-density price cap LECs (CALLS Order, ¶177; emphasis added).

This statement clearly shows that the Commission allows an incumbent monopoly LEC, including Sprint, to establish its access rate according to its ability "to spread those costs over a large subscriber base." It is not unreasonable for a CLEC to request that the same standard apply to its rates.

IV. THE COMMISSION SHOULD CONSOLIDATE INTO THIS PROCEEDING THE PETITIONS FOR DECLARATORY RULING FILED BY AT&T AND SPRINT

On January 19, 2001 AT&T and Sprint each field a Petition for Declaratory Ruling asking the Commission to address two questions: (1) whether any statutory or regulatory constraints prevent an IXC from terminating or declining services ordered or constructively ordered, and if not, (2) what steps IXCs must take in order to avoid ordering or to cancel service after it has been ordered or constructively ordered.[8] Due to the fact that the issues on which

[8] *See* Order, *Advamtel, LLC v. AT&T Corp.*, Civil Action 00-643-A (Jan. 5, 2001); Order, *Advamtel, LLC v. Sprint Communications Co. L.P.*, Civil Action 00-1074-A (Jan. 5, 2001).

AT&T and Sprint are seeking Commission ruling are the exact questions already being addressed in this docket, the Commission should consolidate consideration of AT&T and Sprint's Petitions into this proceeding. Indeed, in its *Further Notice of Proposed Rulemaking* the Commission sought comment on unresolved issues arising out of the case of *MGC Communications v. AT&T Corp.*,[9] including (1) whether any statutory or regulatory constraints prevent an IXC from declining a CLEC's access service; (2) if there are circumstances in which an IXC may decline to purchase a CLEC's access service, what are the ramifications for the customer of the CLEC; and (3) whether such a regime is consistent with the goals of section 254 of the Act.[10]

Because the issues raised in the January 19, 2001 Petitions mirror those being addressed in this proceeding, the Commission's resources would be more efficiently expended by considering issues raised in the Petitions in the instant docket. Doing so would afford the Commission the ability to build on the already extensive record in this proceeding as it revisits issues that have been under consideration by the Commission and the industry for almost two and one half years.

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9 See *MGC Communications, Inc. v. AT&T Corp.*, 14 FCC Rcd. 11647 (Comm. Car. Bur. rel. July 16, 1999)

10 *See In the Matter of Access Charge Reform et al.*, CC Docket Nos. 96-262, 94-1, CCB/CPD File No. 98-63, 98-157, *Further Notice of Proposed Rulemaking*, FCC 99-206, ¶ 242 (rel. Aug. 27, 1999).

V. CONCLUSION

There can be little question that the terminating access "market" has its peculiarities, though it is not altogether clear that market power is one of them. What is clear is that the impact of multifirm supply, the rich mix of regulation and competition, and the familiar problems of network effects, make it difficult at this time to fully comprehend how market forces will influence rates. In this setting, a regulatory "soft touch," in the form of a benchmark rate, is appropriate. A benchmark rate, as proposed in the GREAT Proposal, is not highly intrusive and offers some protection for consumers during the transition to (what is hoped to be) a more competitive market.

The benchmark rate of the GREAT Proposal represents a sizeable decline in average CLEC access rates but does discriminate against CLECs by ignoring economies of scale. Further, the benchmark rate protects against the flow through of gross inefficiency, or even market power, to access rates and, consequently, consumers.

For the reasons presented herein, the Commission should adopt the GREAT Proposal, establishing a "benchmark rate" standard for CLEC access rates and confirming that IXCs may not utilize self-help measures against CLECs as a means of challenging access rates. Also, the Petitions for Declaratory Ruling filed by Sprint and AT&T should be consolidated and the issues raised therein addressed by the Commission in this proceeding.

Respectfully submitted,

Claudia J. Earls

Claudia J. Earls
Z-Tel Communications, Inc.
601 S. Harbour Island Blvd., Suite 220
Tampa, FL 33602
(813) 233-4637

Dated: January 26, 2001

CERTIFICATE OF SERVICE

I, Charles M. Hines III, hereby certify that a true and correct copy of the foregoing **"Reply Comments of Z-Tel Communications, Inc.; CC Docket Nos. 96-262 & 97-146"** was delivered by courier service this 26th day of January, 2001 to the individuals on the following list:

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

Wanda Harris
CCB Competitive Pricing Division
Federal Communications Commission
445 12th Street, S.W.
Washington, D.C. 20554

Thomas Power
Legal Advisor
Office of Chairman Kennard
Federal Communications Commission
445 12th Street
Washington, D.C. 20554

Linda Kinney
Legal Advisor
Office of Commissioner Ness
Federal Communications Commission
445 12th Street
Washington, D.C. 20554

Sarah Whitesell
Legal Advisor
Office of Commissioner Tristani
Federal Communications Commission
445 12th Street
Washington, D.C. 20554

Kyle Dixon
Legal Advisor
Office of Commissioner Powell
Federal Communications Commission
445 12th Street
Washington, D.C. 20554

Kevin Martin
Legal Advisor
Office of Commissioner Furchtgott-Roth
Federal Communications Commission
445 12th Street
Washington, D.C. 20554

Lawrence Strickling
Chief – Common Carrier Bureau
Federal Communications Commission
445 12th Street
Washington, D.C. 20554

Carol Mattey
Chief – CCB Policy Division
Federal Communications Commission
445 12th Street
Washington, D.C. 20554

Jane Jackson
Chief – CCB Competitive Pricing Division
Federal Communications Commission
445 12th Street
Washington, D.C. 20554

Jake Jennings
Common Carrier Bureau
Federal Communications Commission
445 12th Street, S.W.
Washington, D.C. 20554

Jordan Goldstein
Common Carrier Bureau
Federal Communications Commission
445 12th Street, S.W.
Washington, D.C. 20554

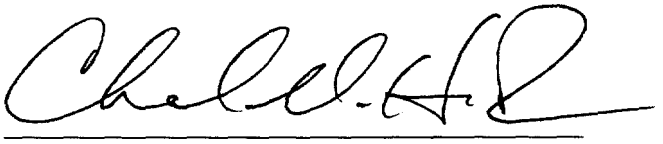
Janice Myles
Common Carrier Bureau
Federal Communications Commission
445 12th Street, S.W.
Washington, D.C. 20554

Claudia Fox
Common Carrier Bureau
Federal Communications Commission
445 12th Street, S.W.
Washington, D.C. 20554

Christopher Libertelli
Common Carrier Bureau
Federal Communications Commission
445 12th Street, S.W.
Washington, D.C. 20554

Michael Pryor
Common Carrier Bureau
Federal Communications Commission
445 12th Street, S.W.
Washington, D.C. 20554

ITS
1231 20th Street, N.W.
Washington, D.C. 20036



Charles M. Hines III