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

In the Matter of	)	
	)	
Policy and Rules Concerning the Interstate, Interexchange Marketplace	)	CC Docket No. 96-61
	)	
Implementation of Section 254(g) of the Communications Act of 1934, as amended	)	CC Docket No. 98-183
	)	
1998 Biennial Regulatory Review -- Review of Customer Premises Equipment And Enhanced Services Unbundling Rules In the Interexchange, Exchange Access And Local Exchange Markets	)	

REPORT AND ORDER

Adopted: March 22, 2001 **Released:** March 30, 2001

By the Commission:

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I. INTRODUCTION

1. In this proceeding, we eliminate the bundling restriction, adopted in the Commission's *Computer II* proceeding,[1] that limits the ability of common carriers to offer consumers bundled packages of telecommunications services and customer premises equipment (CPE) at a discounted price. We also clarify that under our rules, all facilities-based carriers may offer bundled packages of enhanced services and basic telecommunications at a single price, subject to existing safeguards. Our decision furthers the three goals that we identified in the Further Notice of Proposed Rulemaking in this docket:[2] it will benefit consumers by enabling them to take advantage of innovative and attractive packages of services and equipment; foster increased competition in the markets for CPE, enhanced, and telecommunications services; and allow us to repeal regulatory requirements that no longer make sense in light of current technological, market, and legal conditions. Moreover, the actions we take in this order further Congress' directive in the Telecommunications Act of 1996 Act (1996 Act) that we repeal or modify any regulation we determine to be no longer in the public interest.[3]

II. BACKGROUND

2. In 1980, the Commission released its *Computer II Order* in which it addressed regulatory issues associated with the convergence of telecommunications and "computer and data processing."[4] The cornerstone of the decision is that it distinguished between the

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[1] *Amendment of Section 64.702 of the Commission's Rules and Regulations*, CC Docket No. 20828, Final Decision, 77 FCC 2d 384 (1980) (*Computer II Order*), *recon.* 84 FCC 2d 50 (1980) (*Computer II Reconsideration Order*), *further recon.*, 88 FCC 2d 512 (1981), *aff'd sub nom., Computer and Communications Indus. Ass'n v FCC*, 693 F.2d 198 (D.C. Cir. 1982), *cert. denied*, 461 U.S. 938 (1983).

[2] *Policy and Rules Concerning the Interstate, Interexchange Marketplace; Implementation of Section 254(g) of the Communications Act of 1934, as amended; 1998 Biennial Review – Review of Customer Premises Equipment and Enhanced Services, Unbundling Rules in the Interexchange, Exchange Access and Local Exchange Markets*, CC Docket Nos. 96-61, 98-183, Further Notice of Proposed Rulemaking, 13 FCC Rcd 21531, 21534, para. 5 (1998) (*Further Notice*). A list of the parties commenting on the *Further Notice* is attached to this Report and Order.

[3] 47 U.S.C. § 161(a)(2).

[4] *Computer II Order*, 77 FCC 2d at 386, para. 2. The Commission stated that it must promulgate rules addressing this convergence "in the context of rapid technological and market developments affecting

common carrier offering of basic transmission service, which provides a communications path for the movement of information, and the offering of enhanced services, which then consisted primarily of data processing services.[5] Enhanced services are now referred to as "information services" in the 1996 Act and comprise services such as voice mail, e-mail and other Internet services, interactive voice response, audiotext information services, and protocol processing, among others.[6]

3. In the *Computer II Order*, the Commission determined that it would not serve the public interest to subject enhanced service providers to traditional common carriage regulation under Title II because, among other things, the enhanced services market was "truly competitive."[7] The Commission was concerned, however, that carriers providing both basic telecommunications services and enhanced services could discriminate against competitive enhanced service providers that sought to purchase underlying transmission capacity from the carrier.[8] It stated that enhanced services are dependent upon the common carrier offering of basic services and that a basic service is the "building block" upon which enhanced services are offered.[9] The Commission said an essential thrust of *Computer II* was to provide a mechanism whereby non-discriminatory access can be had to basic transmission services by all enhanced service providers.[10]

4. The Commission implemented enhanced services unbundling requirements to ensure such nondiscriminatory access to basic services. For the Bell Operating Companies,

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communications and data processing services, the ever-increasing reliance upon common carrier transmission facilities in the movement of all kinds of information, and the need to tailor communications-related services to individual user requirements." *Id.* at para. 84.

[5] *Computer II Order*, 77 FCC 2d at 418-28, paras. 92-113. The Commission stated that enhanced service "combines basic service with computer processing applications that act on the format, content, code, protocol or similar aspects of the subscriber's transmitted information or provide the subscriber additional, different, or restructured information, or involve subscriber interaction with stored information." *Id.* at para. 5. *See also* 47 C.F.R. § 64.702(a).

[6] *Implementation of the Non-Accounting Safeguards of Section 271 and 272 of the Communications Act of 1934, as amended*, CC Docket No. 96-149, First Report and Order and Further Notice of Proposed Rulemaking, 11 FCC Rcd 21905, 21955-56, para. 102 (1996) (*Non-Accounting Safeguards Order*). To avoid confusion, and to be consistent with the terminology in the *Further Notice*, we will continue to use the term "enhanced services" to refer to the restrictions adopted in *Computer II*. *Further Notice*, 13 FCC Rcd at 21549, para. 32. The Commission has concluded that Congress sought to maintain the basic/enhanced distinction in its definition of "telecommunications services" and "information services," and that "enhanced services" and "information services" should be interpreted to extend to the same functions. *See Federal-State Joint Board on Universal Service*, CC Docket No. 96-45, Report to Congress, 13 FCC Rcd 11501, 11516-17, 11520, 11524, paras. 33, 39, 45-46 (1998).

[7] *Computer II Order*, 77 FCC 2d at 430-33, paras. 119, 124, 128.

[8] Basic communications services are regulated under Title II of the Communications Act. Basic services, such as "plain old telephone services (POTS)," provide pure transmission capability over a communications path that is virtually transparent in terms of its interaction with customer-supplied information. *Id.* at 420.

[9] *Id.* at 474-75, para. 231.

[10] *Id.*

which the Commission found to have sufficient market power on a national scale to engage in anticompetitive activity, it required that they establish a separate subsidiary to provide enhanced services. It also required the subsidiary to acquire its transmission capacity from the parent company pursuant to tariff.[11] The Commission explained that this meant that the same transmission facilities or capacity provided the subsidiary by the parent must be made available to all enhanced service providers under the same terms and conditions.[12] For other facilities-based carriers that lacked market power and therefore were not subject to the separate subsidiary requirement, the Commission required them to "acquire transmission capacity pursuant to the same prices, terms, and conditions reflected in their tariffs when their own facilities are utilized."[13] The Commission has interpreted this requirement to mean that "carriers that own common carrier transmission facilities and provide enhanced services must unbundle basic from enhanced services and offer transmission capacity to other enhanced service providers under the same tariffed terms and conditions under which they provide such services to their own enhanced service operations."[14] The Commission has not changed this requirement for these carriers. The Commission did replace the separate subsidiary requirements for the BOCs with nonstructural safeguards established in the *Computer III* proceeding because it found that they would perform as well as structural safeguards in combating discrimination by the BOCs and be less costly.[15] In doing so, it

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[11] *Id.* at 466-74, paras. 215-230.

[12] *Id.* at 474, para. 229.

[13] *Id.* at 474-75, para. 231. The Commission reemphasized this requirement in the *Computer II Reconsideration Order*. *Computer II Reconsideration Order*, 84 FCC 2d at 75 n.19 ("Those carriers not subject to the separate subsidiary requirement, when employing their own common carrier transmission facilities in the provision of enhanced services, must obtain transmission capacity pursuant to the terms and conditions embodied in their tariff.").

[14] *Independent Data Communications Manufacturers Association, Inc. Petition for Declaratory Ruling and American Telephone and Telegraph Company Petition for Declaratory Ruling*, Memorandum Opinion and Order, 10 FCC Rcd 13717, 13719 (1995) (*Frame Relay Order*); *Competition in the Interstate Interexchange Marketplace*, CC Docket No. 90-132, Memorandum Opinion and Order on Reconsideration, 10 FCC Rcd 4562, 4580 (1995).

[15] *Amendment of Section 64.702 of the Commission's Rules and Regulations (Computer III)*, Report and Order, CC Docket No. 85-229, Phase I, 104 FCC 2d 958 (1986) (*Phase I Order*), *recon.*, 2 FCC Rcd 3035 (1987) (*Phase I Recon. Order*), *further recon.*, 3 FCC Rcd 1136 (1988) (*Phase I Further Recon. Order*); *second further recon.*, 4 FCC Rcd 5927 (1989) (*Phase I Second Further Recon.*), *Phase I Order and Phase I Recon. Orders, vacated, California v. FCC*, 905 F.2d 1217 (9th Cir. 1990) (*California I*); Phase II, 2 FCC Rcd 3072 (1987) (*Phase II Order*), *recon.*, 3 FCC Rcd 1150 (1988) (*Phase II Recon. Order*), *further recon.*, 4 FCC Rcd 5927 (1989) (*Phase II Further Recon. Order*), *Phase II Order vacated, California I*, 905 F.2d 1217 (9th Cir. 1990); *Computer III Remand Proceedings*, 5 FCC Rcd 7719 (1990) (*ONA Remand Order*), *recon.*, 7 FCC Rcd 909 (1992), *pets. for review denied, California v. FCC*, 4 F.3d 1505 (9th Cir. 1993) (*California II*); *Computer III Remand Proceedings; Bell Operating Company Safeguards and Tier I Local Exchange Company Safeguards*, 6 FCC Rcd 7571 (1991) (*BOC Safeguards Order*), *recon. dismissed in part*, Order, CC Docket Nos. 90-623 and 92-256, 11 FCC Rcd 12513 (1996); *BOC Safeguards Order vacated in part and remanded, California v. FCC*, 39 F.3d 919 (9th Cir. 1994) (*California III*), *cert. denied*, 115 S.Ct. 1427 (1995); *Computer III Further Remand Proceedings: Bell Operating Company Provision of Enhanced Services; 1998 Biennial Review – Review of Computer III and ONA Safeguards and Requirements*, CC Docket Nos. 95-20; 98-10; Further Notice of Proposed Rulemaking, 13 FCC Rcd 6040 (1998) (*Computer III 1998 FNPRM*); Report and Order, 14 FCC Rcd 4289 (1999) (*Computer III March 1999 Order*)(addressing part of *Computer III 1998 Further Notice*), *recon.*, 14 FCC Rcd 21628 (1999) (referred to collectively as the *Computer III* proceeding).

affirmed and strengthened the requirement that the BOCs acquire transmission capacity for their own enhanced services operations under the same tariffed terms and conditions as competitive enhanced service providers.[16]

5. The Commission also deregulated CPE in the *Computer II Order*. It determined that the CPE market was becoming increasingly competitive and that in order to increase further the options that consumers had in obtaining equipment, it would require common carriers to separate the provision of CPE from the provision of telecommunications services. It found that the continued bundling of telecommunications services with CPE could force customers to purchase unwanted CPE in order to obtain necessary transmission services, thus restricting customer choice and retarding the development of a competitive CPE market.[17] The Commission determined that by separating the provision of CPE from a carrier's provision of monopoly telecommunications services, consumers would benefit not only through competitive sources of supply for CPE, but also through the option of leasing or owning equipment, competitive pricing and payment options, and improved maintenance.[18] It codified this "no bundling" requirement in rule section 64.702(e), which requires all common carriers to sell or lease CPE separate and apart from such carriers' regulated communications services, and to offer CPE solely on a deregulated nontariffed basis.[19] As the Commission pointed out in the *Further Notice*, this rule does not prohibit carriers from offering "one-stop shopping for CPE and telecommunications services, but requires only that the goods or services be priced separately.[20]

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[16] Computer *III Phase I Order*, 104 FCC 2d at 1011-13. *Computer III* established Comparably Efficient Interconnection (CEI) and Open Network Architecture (ONA) requirements. CEI is a nonstructural safeguard that requires that if a BOC offers enhanced service, it must offer network interconnection opportunities to competitive enhanced service providers that are comparably efficient to the interconnection that its own enhanced service operation enjoys. *See Computer III Phase I Order*, 104 FCC 2d at 1019, para. 112. Both the BOCs and AT&T were initially subject to CEI requirements. *Id.* at 1026-27, paras. 129-31. In subsequent orders, the Commission first modified, and then relieved, AT&T of the CEI requirements. *See Computer III March 1999 Order*, 14 FCC Rcd at 4294-95, n.17-18 (and cases cited therein). The Commission has never imposed CEI requirements on GTE or any other independent LEC. ONA is the overall design of a carrier's basic network services to permit all users of the basic network, including the enhanced service operations of the carrier and its competitors, to interconnect to specific basic network functions and interfaces on an unbundled and equal access basis. The Commission initially applied the ONA requirements to both AT&T and the BOCs, but later relieved AT&T of most of the requirements. *Computer III Phase I Order*, 104 FCC 2d at 1026-27, paras. 127-31. AT&T remains subject, however, to a modified ONA plan that the Commission approved in 1988, and must submit an annual affidavit that affirms that it has not discriminated in the quality of network services provided to competing enhanced service providers. *See Filing and Review of Open Network Architecture Plan*, CC Docket No. 88-2, Memorandum Opinion and Order, 4 FCC Rcd 2449 (1988). In 1994, the Commission extended ONA requirements to GTE. *Application of ONA and Nondiscrimination Safeguards to GTE Corporation*, CC Docket No. 92-256, 9 FCC Rcd 4922 (1994). The Commission has not applied ONA requirements to any other local exchange carriers.

[17] *Computer II Order*, 77 FCC 2d at 442-43, para 149.

[18] *Id.* at 439, para 141 (citing *Carterfone*, 13 FCC 2d 420 (1968)).

[19] 47 C.F.R. § 64.702(e).

[20] *Further Notice*, 13 FCC Rcd at 21533, n.5.

6. Although it imposed bundling restrictions in *Computer II*, the Commission recognized that bundling can benefit consumers if the markets for the components of the bundle are "workably competitive."[21] For example, bundling may reduce the "transaction costs" of assembling a desired package of goods and services. When the markets for both bundled and unbundled commodities are sufficiently competitive, consumers can decide whether the benefits of a package exceed the potential benefits of buying the components of the bundle individually.[22] The Commission reaffirmed these benefits when it allowed cellular CPE and cellular service to be offered on a bundled basis. It found, in particular, that the price of cellular CPE represented the greatest barrier to inducing subscription to cellular service and that bundling could be used as an "efficient distribution mechanism" and an "efficient promotional device" that allows consumers to obtain service and equipment "more economically than if it were prohibited."[23]

7. In light of the increasing competitiveness of the CPE and enhanced services markets, the Commission, on several occasions, has sought to reexamine the need for the bundling restrictions. It first sought comment in 1996 in the *Interexchange Notice* on its tentative conclusion to revise the CPE restriction by allowing nondominant interexchange carriers to bundle CPE with interstate, domestic, interexchange telecommunications services.[24] In response to the *Interexchange Notice*, AT&T suggested that the Commission also allow nondominant interexchange carriers to bundle enhanced services with interexchange services, while SBC asserted that the Commission should eliminate the CPE bundling restriction for all carriers, including incumbent local exchange carriers (LECs).[25] The bundling restrictions were among many issues raised in the *Interexchange Notice*, and although AT&T, SBC and other commenters addressed bundling, most focused their comments on other issues. In the *Interexchange Second Report and Order*, the Commission therefore deferred action on its tentative decision to modify the CPE bundling restriction, stating that it would issue a *Further Notice* addressing the continued application of both the CPE and enhanced services bundling restrictions.[26]

8. On October 9, 1998, the Commission released a *Further Notice* seeking comment on the economic, competitive, and regulatory implications of eliminating our CPE and

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[21] *Computer II Order*, 77 FCC 2d at 443, n.52.

[22] *Id.*

[23] *Bundling of Cellular Customer Premises Equipment and Cellular Service*, CC Docket No. 91-34, Report and Order, 7 FCC Rcd 4028, 4030-31, para. 19 (1992) (*Cellular Bundling Order*).

[24] *Policy and Rules Concerning the Interstate, Interexchange Marketplace, Implementation of Section 254(g) of the Communications Act of 1934, as amended*, CC Docket No. 96-61, Notice of Proposed Rulemaking, 11 FCC Rcd 7141, 7184-87, paras. 84-91 (1996) (*Interexchange Notice*).

[25] *Further Notice*, 13 FCC Rcd at 21535-36, paras. 7, 9.

[26] *Policy and Rules Concerning the Interstate, Interexchange Marketplace, Implementation of Section 254(g) of the Communications Act of 1934, as amended*, CC Docket No. 96-61, Second Report and Order, 11 FCC Rcd 20730, 20732, 20790-93, paras. 113-18 (1996) (*Interexchange Second Report and Order*), recon., 12 FCC Rcd 15014 (1997).

enhanced services bundling rules for nondominant interexchange carriers, and nondominant and incumbent local exchange carriers seeking to offer packages of transmission services, CPE, and enhanced services.[27] The Commission also explained in the *Further Notice* that in accordance with the requirement in section 161 of the 1996 Act, it had begun a comprehensive biennial review of telecommunications and other regulations to promote "meaningful deregulation and streamlining where competition or other considerations warrant such action," and therefore sought comment on the extent to which the continued application of both the CPE and enhanced services bundling restrictions are "no longer necessary in the public interest" pursuant to section 161(a)(2).[28]

III. DISCUSSION

9. In light of the record developed in response to the *Further Notice*, we now conclude that it is appropriate to eliminate the CPE bundling restriction in its entirety and clarify, but not eliminate, the enhanced services requirement so that all carriers may offer consumers packages of equipment, enhanced services, and telecommunications services at a single price. We find that consumers can benefit significantly by relying on the competitive markets that exist for the components contained in a bundle, and that as a result of this competition, and existing safeguards that are applicable in certain instances, we no longer need to rely on the CPE bundling regulation to ensure that carriers do not restrict consumers from taking advantage of competitive suppliers of CPE. We also clarify that under our existing rules, carriers may offer consumers bundles of enhanced and basic telecommunications services, subject to existing safeguards, thereby encouraging further options for consumers.

10. We discuss initially the public interest benefits of bundling, and find, in particular, that offering consumers the choice of purchasing packages of products and services at a single low-rate will encourage them to subscribe to new, advanced, or specialized services by reducing the costs that they have to pay up-front to purchase equipment, or by giving them a choice of relying on one provider instead of having to assemble the desired combinations on their own. Price bundling also eliminates the transaction costs that carriers have to absorb in order to comply with the bundling rules, thereby enabling them to offer better prices whenever possible. Indeed, facilitating consumer choice is what compels us to take action in this proceeding. The state of competition in the CPE and enhanced services markets and in the telecommunications markets is drastically different from the state of competition in these markets in 1980. Unlike in 1980, we now have no doubt that consumers who choose to purchase CPE or enhanced services on a stand-alone basis may do so from a myriad of suppliers. Coupled with this wide choice of CPE and enhanced services suppliers is now a wide choice of interexchange telecommunications carriers and a growing choice of local exchange carriers. Eliminating and clarifying our bundling restrictions will allow the suppliers of each of these components to compete more

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[27] *Further* Notice, 13 FCC Rcd at 21537, 21553, paras. 11-42.

[28] *Id.* at 21535, para. 8 (citing 47 U.S.C. § 161(a)(2); *1998 Biennial Review of FCC Regulations Begun Early*, FCC News Release (rel. Nov. 18, 1997); *FCC Staff Proposes 31 Proceedings as Part of 1998 Biennial Regulatory Review*, FCC News Release, Report No. GN 98-1 (rel. Feb. 5, 1998).

freely, making consumers the beneficiaries of deregulation, as we believe Congress intended when it passed the 1996 Act.

11. It is also compelling to us that all carriers, both incumbent and nondominant carriers, in all markets, demonstrate a desire to compete for customers through bundled service offerings. We find that it is appropriate to grant bundling relief to all of them, and address the ability of these carriers to provide specific service combinations. We find first that nondominant carriers should be able to offer packages of service that include CPE, enhanced services, and interstate, domestic, interexchange services at one price. Because these markets are competitive, the risk of anticompetitive conduct that the Commission cited originally in enacting the bundling restrictions has been virtually eliminated. We also find that it is in the public interest to allow nondominant carriers to bundle CPE and enhanced services with local exchange service. Although the local exchange market is not substantially competitive, the 1996 Act eliminated barriers for carriers seeking to enter this market. Competitive carriers have made steady progress in doing so, increasing their market size by 53 percent during the first half of 2000. Because these carriers have no market power in the local exchange market, it is undisputed in the record that they cannot engage in anticompetitive conduct if we grant them the flexibility to respond to consumer demand for packages that contain local exchange service.

12. We further find that incumbent local exchange carriers should be able to offer packages of service that include CPE, enhanced services, and local exchange service at one price. We acknowledge that because the local exchange market is not substantially competitive and because incumbent LECs have market power, we must balance the risk that the incumbents can act anticompetitively with the public interest benefits associated with bundling. After undertaking this analysis, we conclude that the risk of anticompetitive behavior by the incumbent LECs is low, not only because of the economic difficulty that even dominant carriers face in attempting to link forcibly the purchase of one component to another, but also because of the safeguards that currently exist to protect against this behavior. In particular, incumbent LECs will, under state law, offer local exchange service separately on an unbundled tariffed basis if they bundle such service with CPE. We also require them to offer exchange access service and any other service for which the Commission considers them to be dominant separately on nondiscriminatory terms if they bundle such service with CPE. We go on to conclude that the risk is also outweighed by the consumer benefits of allowing bundling. In the case of enhanced services, we emphasize that we are not eliminating at this time the fundamental provisions contained in our *Computer II* and *Computer III* proceedings that facilities-based carriers continue to offer the underlying transmission service on nondiscriminatory terms, and that competitive enhanced services providers should therefore continue to have access to this critical input.

13. Finally, we address the impact of bundling on our universal service requirements, and we suggest methods that carriers may use to determine their universal service obligations. We also find that permitting carriers to bundle will not impact our Part 68 requirements that attached CPE not cause harm to the public switched network, and that our network disclosure rules in Part 51 will ensure that competitive CPE suppliers continue to obtain access to network information they require from the incumbent carriers.

A. Overall Benefits of Bundling CPE and Enhanced Services With Telecommunications Services

14. We conclude that allowing all carriers to bundle products and services is generally procompetitive and beneficial to consumers. Bundling encourages competition by giving carriers flexibility both to differentiate themselves from their competitors and to target segments of the consumer market with product offerings designed to meet the needs of individual customers.

15. We view bundling as the offering of two or more products or services at a single price, typically less than the sum of the separate prices.[29] This is different from "one-stop" shopping arrangements in which consumers may purchase the components of a bundle, priced separately, from a single supplier.[30] While "one-stop" shopping is convenient for consumers, we conclude that they can benefit even more from bundled packages offered at a price discount. We agree, in particular, with the commenters who point out that consumers benefit from bundling because it eliminates the need for carriers to separately provision, market, and bill services, and therefore reduces the transaction costs that carriers pass on to consumers.[31] Indeed, we have recognized that bundling provides benefits that packages of separately priced services do not, finding in the case of two merged companies that by offering products "as a package at a price below that of the individual prices of the package's components when sold separately, the merged firm would both lower costs and pass at least some of those cost savings on to consumers."[32] Bundling can further reduce costs for consumers by eliminating the time and effort needed to find products and services in the market, negotiate appropriate purchase terms, and assemble the desired combinations. This

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[29] *See* Letter from Charles E. Griffin, Government Affairs Director, AT&T, to Magalie Roman Salas, Secretary, FCC, CC Docket Nos. 96-61 and 98-183 (filed June 21, 2000), Attachment, *Ex Parte* Declaration of Janusz A. Ordover and Robert D. Willig on Behalf of AT&T Corp. (*AT&T Ordover/Willig Decl.*) at 6.

[30] The Commission explained in the *Further Notice* that the *Computer II* CPE bundling restriction does not prohibit carriers from offering "one-stop" shopping for CPE and telecommunications services; the rule requires only that the goods and services be priced separately. For example, some carriers jointly market CPE, such as a modem, and a telecommunications service. Because of the CPE bundling restriction, however, these carriers are required to price separately each item in the package and often have to either offer the tariffed telecommunications service at a discounted promotional rate, or offer a discounted price or rebate on the CPE, in order to sell the total package at an attractive price. *Further Notice*, 13 FCC Rcd at 21533, para. 5.

[31] Network Plus Comments at 21; KMC Comments at 3. *See also* Letter from Charles E. Griffin, Government Affairs Director, AT&T, to Magalie Roman Salas, Secretary, FCC (filed Dec. 17, 1999), Attachment at 5 (bundling allows carriers to streamline operations and reduce advertising, marketing, and billing costs). *See also* GTE Comments at 4-6 and Attachment 1 (Aff. of Gregory M. Duncan) (*GTE Duncan Aff.*) at 5-8 (bundling allows service providers to mitigate risks associated with introducing new services and products, promotes innovation and spurs consumer interest in new goods and services that can allow the carrier to spread the fixed cost of providing service over a larger population of users).

[32] *Applications for Consent to the Transfer of Control of Licenses and Section 214 Authorizations from Tele-Communications, Inc., Transferor, to AT&T Corp., Transferee*, CC Docket No. 99-178, Memorandum Opinion and Order, 14 FCC Rcd 3160, 3219, para. 125 (1999).

is particularly important for enhanced services and CPE, package components that many consumers may perceive to be complex.[33]

16. We also agree with the commenters who assert that allowing carriers to bundle transmission services with CPE and enhanced services will enable them to offer innovative packages of goods and services that will provide customers with efficiencies and pricing that they demand,[34] and find that the Commission's rules should not unnecessarily restrict consumer choice in this area. As far back as 1980, the Commission recognized that "trends in technology enable CPE to function as an enhancement to basic common carrier services and many enhanced service applications involve interaction with sophisticated terminal equipment."[35] Today, we believe that eliminating and clarifying our bundling restrictions will encourage the competitive deployment of telecommunications services, enhanced services, and CPE. The record shows that consumers want the option to purchase bundled packages of products and services, and that carriers facing competition in various service markets seek the ability to respond to this demand.[36]

17. In particular, commenting carriers want the ability to bundle Digital Subscriber Line (DSL) service with CPE and enhanced Internet services for residential customers and provide other sophisticated service bundles to business customers that offer voice, frame relay services, enhanced Internet-protocol (IP) services, and other types of basic and enhanced services.[37] MCI WorldCom explains that there is a growing number of customers that are seeking service packages at a single per minute rate in order to achieve the lowest per-unit cost of service available, as well as the ability to rely on a single provider to implement and maintain advanced telecommunications networks.[38] Other commenters assert that they can reduce start-up costs for consumers by bundling specialized CPE and internet access with advanced services, thereby stimulating consumer demand for these services.[39] As we found in the *Cellular Bundling Order*, the influx of new subscribers due to the bundling of advanced telecommunications services with enhanced services and CPE may cause the fixed costs of providing service to be spread over a larger population of users, achieving economies of scale and lowering the cost of providing service to each subscriber.[40]

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[33] *AT&T Ordover/Willig Decl.* at 11-12.

[34] *See, e.g.*, Ohio PUC at 2-3; AT&T Comments at 4-5, Bell Atlantic Comments at 12-13.

[35] *Computer II Order,* 77 FCC 2d at 447, para. 160.

[36] *See GTE Duncan Aff.* at para. 13 (stating that one of the most important ways in which carriers seek to compete is by differentiating their product offerings through bundling.).

[37] *See, e.g.*, API Comments at 4-6; Bell Atlantic Comments at 15-16.

[38] Letter from Karen T. Reidy, Attorney, Federal Law and Public Policy, MCI Worldcom, CC Docket Nos. 96-61 and 98-183, Attachment at 1-2 (filed Apr. 10, 2000).

[39] *See, e.g.*, Ameritech Comments at 2; Bell Atlantic Comments at 16; Next Level Comments at 3-5.

[40] *See Cellular Bundling Order*, 7 FCC Rcd at 4031, para. 20.

18. We emphasize that the benefits associated with allowing carriers to bundle products and services at one price do not exist where the provider maintains sufficient market power to require that a customer purchase multiple goods or services in order to obtain one of the components in the package.[41] Antitrust laws particularly prohibit unlawful tying arrangements in which the seller has enough market power to force a customer to purchase a component of the package that he or she would not otherwise purchase in a competitive market.[42] Indeed, one of the primary reasons the Commission adopted the *Computer II* CPE bundling restrictions was to prevent carriers from forcing consumers to buy unwanted carrier-supplied CPE in order to obtain transmission service.[43] On the other hand, allowing carriers to market products and services together at a single price, but requiring them to offer the components of the bundle to consumers separately, ensures that carriers cannot restrain competition or impede consumer choice.[44] As we explain below, the separate availability of the components of a package on nondiscriminatory terms, whether through the functioning of a competitive market for each component or through existing regulatory requirements, is essential to prevent the improper extension of market power.

B. CPE Bundling

1. CPE Bundling with Interstate, Domestic, Interexchange Service

19. We adopt our tentative conclusion to eliminate the bundling restriction codified in section 64.702(e) of our rules in order to allow nondominant interexchange carriers to bundle CPE with their interstate, domestic, interexchange services. We conclude that both the CPE market and the interstate, domestic, interexchange market are sufficiently competitive such that it is extremely unlikely that interexchange carriers could engage in anticompetitive behavior if we permit them to provide packages of services and CPE bundled at a single price. Competition has therefore supplanted the need for the bundling restriction, and we accordingly repeal it, as Congress intended.[45] We find that doing so will promptly allow consumers to pick and choose among service and equipment providers that offer packages best suited to their needs.

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[41] *See Further Notice*, 13 FCC Rcd at 21538-39, para. 13, n.37 (citing *Jefferson Parish Hospital District No. 2 v. Hyde*, 466 U.S. 2, 12-14, 16-18 (1984) (*Jefferson Parish Hospital*); *Digidyne Corp. v. Data General Corp.*, 734 F.2d 1336, 1341 (9th Cir. 1984), *cert. denied*, 473 U.S. 908 (1985)).

[42] Section 3 of the Clayton Act, 15 U.S.C. § 14. *See also Further Notice*, 13 FCC Rcd at 21538-39, n.37; *Interexchange Notice*, 11 FCC Rcd at 7186, para. 87 (*citing Jefferson Parish Hospital*, 466 U.S. at 12; Michael D. Whinston, *Tying, Foreclosure, and Exclusion*, 80 Am. Econ. Rev. 837, 837 (1990)).

[43] *Computer II Order*, 77 FCC 2d at 442-43, paras. 149-50.

[44] *See GTE Duncan Aff.* at para. 8 ("Mixed bundling allows the consumer to select either the bundle or individual components . . . Further, it is intuitively obvious that mixed bundling is the superior option from a customer's perspective. A mixed bundling strategy enhances welfare by allowing both high and low-demand users to satisfy their preferences by joining the appropriate consumption groups. Mixed bundling provides consumers with a choice, which is something that consumers both want and need.").

[45] 47 U.S.C. § 161(a)(2).

a. Competitiveness of the CPE Market

20. The Commission explained in the *Further Notice* that the basis for its tentative conclusion in the *Interexchange Notice* to allow nondominant interexchange carriers to bundle CPE with interstate, domestic, interexchange services is that both the CPE and interstate, domestic, interexchange markets are substantially competitive and that nondominant interexchange carriers do not possess market power in the interstate, interexchange market. Thus, the Commission tentatively concluded in the *Interexchange Notice* that allowing such carriers to bundle CPE with interstate, domestic, interexchange services is unlikely to lead to the anticompetitive conduct that led the Commission to prohibit the bundling of CPE with telecommunications services. The Commission stated in the *Further Notice* that it would continue to apply this analysis when determining whether or not to eliminate the CPE bundling restriction.[46]

21. It is undisputed in the record that the CPE market is highly competitive.[47] The bundling restrictions were adopted, in part, in recognition that competition was only beginning to emerge in the CPE market. In the *Computer II Order*, the Commission found that the CPE market faced "an increasing amount of competition as new and innovative types of CPE are constantly introduced into the marketplace."[48] The Commission observed subsequently in the *Interexchange Notice* that the CPE market is widely recognized to be competitive, [49] and we agree with the commenters who point out that this competition has intensified.[50] Indeed, the Commission's goal in *Computer II* to increase consumer choice for innovative CPE and open equipment markets to full and fair competition[51] has been achieved. CPE is so widely available that it has been described as a "commodity industry" in that CPE is available from a diversity of vendors and prices have been declining steadily for many types of CPE.[52] AOL asserts that there has been a proliferation of CPE available to residential and business consumers that offer them increased control and functionality, and that the broad availability of CPE has been an important factor in allowing information service providers (ISPs) to deliver increasingly sophisticated multimedia content to their

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[46] *Further Notice*, 13 FCC Rcd at 21546, para. 28.

[47] *See, e.g.*, AOL Comments at 4; API Comments at 7; AT&T Comments at 6-7; CompTel Comments at 5; SBC Comments at 5; Sprint Comments at 2.

[48] *Computer II Order*, 77 FCC 2d at 439, para. 141.

[49] *Interexchange Notice*, 11 FCC Rcd at 7185, para. 86 (citing *Price Cap Performance Review for Local Exchange Carriers*, CC Docket No. 94-1, First Report and Order, 10 FCC Rcd 8961, 9122 (1995); *Procedures for Implementing the Detariffing of Customer Premises Equipment and Enhanced Services (Second Computer Inquiry)*, CC Docket No. 81-893, Memorandum Opinion and Order, 8 FCC Rcd 3891, 3891 (1993)).

[50] *See, e.g.*, AT&T *Ordover/Willig Decl.* at 24-25; Bell Atlantic Comments at 7-10, CompTel Comments at 3; SBC Comments at 5.

[51] *See Computer II Order*, 77 FCC 2d at 453, para. 180.

[52] Bell Atlantic Comments at 8 (citing Multimedia Telecommunications Association and Telecommunications Industry Association, 1998 Multimedia Telecommunications Market Review and Forecast at 113).

customers.[53] The CPE industry also reported that it expected record sales growth in 2000, especially in the area of computer modems used to access the Internet.[54] Indeed, CEMA summarizes that the bundling restrictions have been highly successful in contributing to the development of a fully competitive CPE market.[55]

b. Competitiveness of the Interstate, Domestic, Interexchange Market

22. It is also undisputed that the interstate, domestic, interexchange market is competitive. In 1995, the Commission reclassified AT&T as a nondominant interexchange carrier based on its finding that AT&T lacked unilateral market power in the long distance market, which it stated was subject to "substantial competition."[56] It concluded that competitors in the long distance market had enough readily available excess capacity to constrain other competitors' pricing behavior, and that both residential and business customers were highly price sensitive and would switch among competitors to obtain price reductions and desired features.[57] When the Commission approved the merger of MCI and WorldCom in 1998, it found that these competitive market trends continued, and that since AT&T had been reclassified as nondominant, AT&T's market share had continued to decline as the number of carriers offering long distance services had risen.[58] These trends have continued and, indeed, accelerated since that time. The Commission has also authorized Bell Atlantic to provide in-region long distance service in New York and authorized SBC to provide the same service in Texas, Kansas, and Oklahoma.[59] Finally, in light of the overall

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[53] AOL Comments at 4.

[54] Consumer Electronics Association, 2000 Growth Projection at 1 (rel. Jan. 6, 2000) at http://www.ce.org (stating that in addition to computer modems, it expects to sell 80 million corded and cordless telephones at total dollar sales of $2.4 billion).

[55] CEMA Comments at 5-6.

[56] *Motion of AT&T Corp. to be Reclassified as a NonDominant* Carrier, 11 FCC Rcd 3271, 3288, para. 26 (1995) (*AT&T Nondominance Order*).

[57] *Id.* at 3305-06 (citing *Competition in the Interstate Interexchange Marketplace*, Report and Order, 6 FCC Rcd 5880, 5887 (1991)).

[58] *Application of WorldCom, Inc. and MCI Communications Corporation for Transfer of Control of MCI Communications Corporation to WorldCom, Inc.*, CC Docket No. 97-211, Memorandum Opinion and Order, 13 FCC Rcd 18025, 18050-51 (1998). *See also Trends in Telephone Service*, Industry Analysis Division, Common Carrier Bureau, FCC, issued Mar. 2000, at 11-10, Table 11.5; *Long Distance Market Shares*, Industry Analysis Division, Common Carrier Bureau, FCC, issued Mar. 31, 1999, at 16, Table 3.2.

[59] *Bell Atlantic-New York Authorization Under Section 271 of the Communications Act to Provide In-Region InterLATA Service in the State of New York,* 15 FCC Rcd 3953 (1999); *Application by SBC Communications Inc., Southwestern Bell Telephone Company, and Southwestern Bell Communications Services, Inc. d/b/a Southwestern Bell Long Distance, Pursuant to Section 271 of the Telecommunications Act of 1996, to Provide In-Region, InterLATA Services in Texas*, CC Docket No. 00-65, Memorandum Opinion and Order, 15 FCC Rcd 18354 (2000); *Joint Application by SBC Communications Inc., Southwestern Bell Telephone Company, and Southwestern Bell Communications Services, Inc. d/b/a Southwestern Bell Long Distance for Provision of In-Region, InterLATA Services in Kansas and Oklahoma*, CC Docket No. 00-217, Memorandum Opinion and Order, FCC 01-29 (rel. Jan. 22, 2001).

competitiveness of the market, the Commission has ordered the complete detariffing of interstate, domestic, interexchange service by nondominant carriers in order to avoid hindering them from responding competitively to the needs of customers.[60] In sum, we have previously found the interstate, domestic, interexchange market to be highly competitive and continue to do so.

c. Likelihood of Anticompetitive Conduct

23. In light of our findings that both the CPE and interstate, domestic, interexchange markets are competitive, we conclude that section 64.702(e) of our rules is no longer "necessary in the public interest" under section 11 of the Communications Act[61] to the extent that it prohibits nondominant interexchange carriers from bundling CPE and interstate, domestic, interexchange service. The competition in both the CPE and interstate, interexchange service markets makes it extremely unlikely that nondominant interexchange carriers could restrict consumer choice for components of a bundle, as the Commission feared when it adopted the CPE restriction in 1980. To be sure, the Commission was concerned that a carrier could refuse to sell one product that a customer desired unless the customer also agreed to purchase a second product from the carrier.[62] It is a well established economic principle, however, that in order for a buyer to be harmed by such an arrangement, the seller must have market power over the desired product such that the buyer has no choice but to purchase it from the seller.[63] Nondominant interexchange carriers have no market power in either the CPE or interstate, domestic, interexchange markets, making it virtually impossible for them to require consumers to purchase one bundled product in order to obtain the other.[64]

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[60] *Policy and Rules Concerning the Interstate, Interexchange Marketplace*, Second Report and Order, 11 FCC Rcd 20730 (1996) (*Detariffing Order*), *aff'd*, *MCI WorldCom, Inc. v. Competitive Telecommunications Association, et al.*, No. 96-1459 (Apr. 28, 2000). Interexchange carriers have until July 31, 2001 to complete the process of detariffing mass market consumer services. They were required to complete the process of detariffing domestic contract-type services by January 31, 2001. *Common Carrier Bureau Extends Transition Period for Detariffing Consumer Domestic Long Distance Services*, Public Notice, CC Docket No. 96-61, DA 01-282 (rel. Feb. 5, 2001).

[61] 47 U.S.C. § 160(a)(2).

[62] *See Computer II Order*, 77 F.C.C.2d at 443, n.52.

[63] Phillip E. Areeda, *Antitrust Law*, Vol. IX, para. 1700(d)(3) (1991) (*Areeda Vol. IX*).

[64] *AT&T Ordover/Willig Decl.* at 25-26; MCI Comments at 6-7; Sprint Comments at 4. *See also Areeda Vol. IX* at para. 1702 (stating that two of the conditions that define an illegal tying arrangement are that "the customer takes the second ('tied') product not because he prefers it on its own merits but only because he must take it in order to obtain a desired ('tying') product, either at all or on favorable terms" and "the supplier possesses substantial economic power over the tying product."). IDCMA's reference to *Eastman Kodak Company v. Image Technical Services, Inc.* to argue that firms without market power in one market can force customers to buy products in another market is misplaced. *Further Notice*, 13 FCC Rcd at 21538-39, para. 13 (citing IDCMA Comments at 33-36 and *Eastman Kodak Company v. Image Technical Services, Inc.*, 504 U.S. 451 (1992) (*Eastman Kodak*)). The Supreme Court in *Kodak* found that although Kodak may not have had market power in the photocopier market, it did have market power for replacement parts for photocopiers, and on that basis it refused to grant Kodak summary judgment on the claim that it had abused that market power by tying replacement parts and repair service. *Eastman Kodak*, 504 U.S. at 462. Eastman *Kodak* is consistent with

24. We disagree with the few commenters who argue that bundling would allow carriers to offer packages that combine telecommunications service with "free" CPE in a manner that would injure competition in the CPE market.[65] Nondominant interexchange carriers are unable to harm competition by offering products below cost. For instance, if a carrier lacks market power, it cannot raise the rates of its transmission service in order to support below-cost pricing of CPE.[66] We agree, in particular, with the commenters who argue that whatever pricing advantage an interexchange carrier could offer by selling service and CPE at a bundled discounted price would have to be cost-based or the carrier could not offer profitably such a bundled discount in the long run.[67] This inability to engage in anticompetitive pricing is also inconsistent with the arguments of the few commenters that claim that a nondominant interexchange carrier would discriminate unreasonably against customers who agreed to use carrier-provided CPE by offering them transmission service at a lower price than that offered to non-CPE customers.[68] To the contrary, eliminating the bundling restriction should allow these carriers to compete vigorously and fairly in the CPE and interexchange markets by offering bundles of service and equipment that meet demonstrated customer demand.

25. We do not agree with CEMA that eliminating the bundling restrictions for nondominant interexchange carriers is somehow inconsistent with the procompetitive intent of Congress, as demonstrated by section 629 of the Communications Act, which relates to the creation of a competitive retail market for multichannel video programming distribution system "navigation devices."[69] The purpose of section 629 is to expand opportunities for consumers to purchase programming equipment from sources other than the service provider.[70] As the Commission stated when it promulgated the rules implementing section

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the Supreme Court's holding in *Jefferson Parish Hospital* that the essential characteristics of an invalid tying arrangement lie in the seller's exploitation of its control, or market power, over the tying product to force the buyer into the purchase of a tied product that the buyer either did not want at all, or might have preferred to purchase elsewhere on different terms. *Jefferson Parish Hospital*, 466 U.S. at 12-14, 16-18. *See also* AT&T Comments at 10-11; MCI WorldCom Comments at 8. Nondominant interexchange carriers, by definition, lack market power in the interexchange market, which would be the tying market under IDCMA's argument, and therefore cannot force customers to purchase service and CPE through an anticompetitive arrangement.

[65] *See, e.g.*, Letter from Jerome R. Karl, President, Jencom, Inc., to Chairman Reed Hundt, FCC, CC Docket No. 96-61 (filed Oct. 6, 1996); Letter from Mel Sarowitz, President, Datatran Network Systems, Inc., to Chairman Reed Hundt, FCC, CC Docket No. 96-98 (filed Oct. 17, 1996); Mitel Comments at 1.

[66] *Cf. Policy and Rules Concerning Rates for Competitive Common Carrier Services and Facilities Authorizations Therefor*, CC Docket No. 79-252, First Report and Order, 85 FCC 2d 1 (1980) (distinguishing between dominant and nondominant interexchange carriers and determining that nondominant carriers could not charge rates that contravene the Communications Act of 1934). *See also* Sprint Comments at 5.

[67] MCI WorldCom Comments at 7.

[68] *See Further Notice*, 13 FCC Rcd at 21540, para. 16.

[69] *See id.* at 21539-40, para. 15 (citing 47 U.S.C. § 629); CEMA Comments 3-4.

[70] *Implementation of Section 304 of the Telecommunications Act of 1996, Commercial Availability of Navigation Devices*, CS Docket No. 97-80, 13 FCC Rcd 14775, 14775, para. 1 (1998) (*Navigation Devices Order*).

629, competition in the market for navigation devices is "in the early stage of development and the enormous technological change resulting from the movement from analog to digital communications is underway."[71] The Commission's rules were designed to facilitate the emergence of a competitive marketplace for navigation devices. The statute specifically provides, moreover, that regulations adopted under section 629 will cease to apply when, *inter alia*, the Commission determines that the market for multichannel video programming distributors and the market for navigation devices are fully competitive.[72] We also note that a cable operator will not be subject to the related restrictions on cable equipment pricing contained in section 623 of the Act and section 76.923(b) of the Commission's rules, where the Commission finds that the cable operator is subject to effective competition.[73] The CPE market is already fully competitive, in large part as a result of the Commission's bundling policies, and it is therefore unnecessary to retain the bundling restriction for nondominant interexchange carriers.[74]

26. We decline to adopt an "unbundled option" requirement that interexchange carriers offer interstate, domestic, interexchange services separately on an unbundled basis if they offer packages of CPE and interexchange service.[75] In a competitive market, carriers have an incentive to offer bundles or stand-alone offerings that a customer needs or the customer will switch to another carrier.[76] The extensive choice of stand-alone CPE provided by competitive suppliers and the availability of interexchange service from many competitive carriers makes it highly unlikely that consumers would be forced to purchase high-cost interexchange service just because they declined to use carrier-supplied CPE.[77] Requiring

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[71] *Id.* at 14775, para. 3.

[72] 47 U.S.C. § 549(e)(1), (2); 47 C.F.R. § 79.923(b).

[73] 47 U.S.C. § 543(a)(2); 47 C.F.R. § 76.923(b).

[74] Allowing nondominant interexchange carriers to bundle interstate, domestic, interexchange service with CPE, without having to offer the transmission component of the bundle separately, is consistent with the U.S. Government's obligations concerning the interconnection of terminal equipment with the public transport network under the General Agreement on Trade in Services (GATS) and North American Free Trade Agreement (NAFTA). GATS requires the U.S. to allow suppliers from other countries to "purchase or lease and attach terminal or other equipment which interfaces with the [public telecommunications transport] network and which is necessary to supply [their] services." *Further Notice*, 13 FCC Rcd at 21543, para. 22 (citing GATS Annex of Telecommunications, at para. 5(b). The GATS is Annex 1B of the Marrakesh Agreement Establishing the World Trade Organization, 33 I.L.M. 1167 (1994)). NAFTA contains a similar requirement. *Further Notice*, 13 FCC Rcd at 21543, para. 22 (citing NAFTA, Dec. 17, 1992, U.S.-Ca.-Mex., Art. 1302(2), H.R. Treaty Doc. 159, 103d Cong., 1st Sess. (1993)). To the extent that these agreements encompass CPE provided by competitive foreign suppliers, and for the reasons explained above, we agree with AT&T that allowing nondominant interexchange carriers to offer bundled products in no way restricts the interconnection of such equipment with the carriers' networks. AT&T Comments at 12.

[75] *See Further Notice*, 13 FCC Rcd at 21542-42, para. 21.

[76] *See AT&T Ordover/Willig Decl.* at 7 ("If consumers do not value bundles, market participants [in competitive markets] will have every incentive to offer unbundled components on a stand-alone basis."); ENTUA Comments at 2.

[77] *See* MCI WorldCom Comments at 9-10.

nondominant interexchange carriers to offer interstate, domestic, interexchange service on an unbundled basis is therefore unnecessary and would be contrary to the goal of section 11 of the Act to eliminate regulations that are no longer "necessary in the public interest" as a result of meaningful competition.[78] It would also be inconsistent with the Commission's *Detariffing Order* in which it found that market forces, as opposed to a tariffing regime, will ensure that carriers offer services at the prices and on the terms and conditions that consumers demand.[79]

27. Contrary to IDCMA's concern,[80] allowing nondominant interexchange carriers to bundle CPE with interstate, domestic, interexchange services will not require the Commission to "re-regulate" CPE by ensuring that bundles of CPE and transmission service comply with the tariff and pricing requirements under Title II of the Act. In the *Computer II Order*, the Commission found that CPE was not a common carrier activity and that charges for CPE provided by carriers no longer needed to be regulated because of competition in the CPE market.[81] Nothing in this Order changes the non common carrier nature of CPE. Rather, as argued by U S West, the Commission is not extending the reach of its common carrier regulation to CPE by allowing bundling because, in effect, the CPE that a carrier offers would continue to be priced separately from the basic transmission service, but a package discount is applied when customers purchase both products.[82] More significantly, the Commission has found that it should forbear from the requirement that nondominant interexchange carriers file tariffs pursuant to section 203 of the Act for interstate, domestic, interexchange service, and in fact will not permit nondominant interexchange carriers to file interstate tariffs for this service.[83] Accordingly, interexchange carriers will be unable to tariff such services whether or not it is bundled with CPE.

28. We adopt our tentative conclusion that to the extent the BOCs' section 272 affiliates, as well as independent incumbent LECs' affiliates, are classified as nondominant in the provision of interstate, domestic, interexchange services, these carriers may bundle CPE with such services to the same extent as other nondominant carriers.[84] As we explained in the *Further Notice*, the Commission has concluded that the requirements established by, and the

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[78] 47 U.S.C. § 161(a)(2).

[79] *Detariffing Order*, 11 FCC Rcd at 20742-43, para. 21

[80] *See Further Notice*, 13 FCC Rcd at 21540, para. 17 (citing IDCMA Comments at 22-24).

[81] *See Computer II Order*, 77 FCC 2d at 446-47, paras. 159-60.

[82] U S West Comments at 7.

[83] *Detariffing Order*, 11 FCC Rcd at 20732, para. 3.

[84] *Further Notice*, 13 FCC Rcd at 21544, para. 24 (citing 47 U.S.C. §§ 271, 272 that permit BOCs to provide in-region, interLATA service once the requirements of those sections are met). BOCs are classified as nondominant carriers for their provision on both out-of-region and in-region interexchange service. They have to comply with the safeguards contained in section 272 for in-region long distance service. Independent LECs are required to provide in-region interexchange service through separate affiliates that satisfy the requirements in the *Competitive Carrier Fifth Report and Order*. *Id.* at 21545, n. 69 (citing *Competitive Carrier Fifth Report and Order*, CC Docket No. 79-252, 98 FCC 2d 1191 (1984)).

rules implemented pursuant to, sections 271 and 272 of the Act, together with other Commission rules, limit sufficiently the ability of a BOC's section 272 affiliate to use the BOC's market power in the local exchange or exchange access market to raise and sustain prices of interstate, interLATA services above competitive levels.[85] It has therefore determined that a BOC entering the in-region interLATA market through a section 272 affiliate will be regulated as a nondominant interexchange carrier. BOCs providing out-of-region interstate, domestic, interexchange service are also nondominant. We agree with BellSouth that these findings demonstrate that, once a BOC that has satisfied the requirements of sections 271 and 272 of the Act, its long distance affiliate has the same market characteristics as any other nondominant interexchange carrier and that there is no basis for denying them the same bundling relief that we grant to those other carriers.[86] AT&T is the only commenter that argued that we should exclude BOC section 272 affiliates from bundling relief, stating that we need not decide this issue until BOCs obtain approval to provide in-region interLATA service pursuant to section 271 of the Act.[87] We have now, of course, approved section 271 applications for several states,[88] making AT&T's argument moot.

29. Similarly, the Commission has also classified independent incumbent LECs' affiliates as nondominant in the provision of in-region, interstate, interexchange services, and has required independent incumbent LECs that provide this service solely on a resale basis to do so through a separate corporate division as opposed to a separate legal entity.[89] The Commission found that independent LECs that provide in-region long distance services solely on a resale basis are less likely to engage in anticompetitive activity than facilities-based independent providers, thus eliminating the need for a separate affiliate that is a separate legal entity.[90] Facilities-based independent LECs that provide in-region long distance services must do so through separate affiliates that satisfy the requirements established in the *Competitive Carrier Fifth Report and Order*.[91] We conclude that our nondominant classification of independent LECs that provide in-region, interstate,

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[85] *Further Notice*, 13 FCC 21544-45, para. 24 (citing *Regulatory Treatment of LEC Provision of Interexchange Services Originating in the LEC's Local Exchange Area and Policy and Rules Concerning the Interstate, Interexchange Marketplace*, CC Docket Nos. 96-149, 96-61, Second Report and Order in CC Docket No. 96-149 and Third Report and Order in CC Docket No. 96-61, 12 FCC Rcd 15756, 15802 (1996) (*BOC 272 Affiliate Classification Order*), Order on Reconsideration, 12 FCC Rcd 8730 (1997)).

[86] BellSouth Reply Comments at 4.

[87] AT&T Comments at 15.

[88] *See supra* note 59.

[89] *Regulatory Treatment of LEC Provision of Interexchange Services Originating in the LEC's Local Exchange Area and Policy and Rules Concerning the Interstate, Interexchange Marketplace*, CC Docket Nos. 96-149, 96-61, Second Order on Reconsideration and Memorandum Opinion and Order, 14 FCC Rcd 10771 (1999) (*LEC Classification Second Reconsideration Order*).

[90] *Id.* at 10787-10793, paras. 22-28.

[91] *Further Notice*, 13 FCC Rcd at 21544-45, para. 24 (citing *Competitive Carrier Fifth Report and Order*, 98 FCC 2d 1191). *See also* 47 C.F.R. § 64.1903.

interexchange service and the separate entity and affiliate requirements ensure that these incumbent LECs have the same market characteristics as other nondominant interexchange carriers, and that allowing them to bundle interstate, domestic, interexchange service with CPE is in the public interest.[92]

2. CPE Bundling with Local Exchange Service

30. We further conclude that it is in the public interest to remove the bundling restriction to allow all nondominant LECs, or competitive LECs, and incumbent LECs to bundle CPE and local exchange service.[93] We recognize that the competitiveness of the local market has increased only a limited amount during the time since the Commission imposed the CPE bundling restriction in the *Computer II Order* and that incumbent LECs have market power in the provision of local exchange services. We find, however, that the consumer benefits of bundling outweigh the risk that incumbent LECs can use this power to harm competition. Our risk-benefit analysis is informed by other factors, such as the removal of barriers to entry in the local market contained in the 1996 Act and the subsequent increase in local competition, as well as the Commission's decision to lift similar bundling restrictions in the cellular markets, that tip the balance in favor of lifting the bundling restriction on the incumbent LECs' provision of local exchange service and CPE.

a. Competitiveness of Local Exchange Market

31. We recognize that the local exchange market is not substantially competitive and that incumbent LECs remain the dominant providers in this market. Yet, competitive carriers have made steady progress in entering the local exchange market since we issued the *Further Notice* in 1998. The Commission's December 2000 report on local competition shows that competitive LECs provided 6.7 percent of the total nationwide end user telephone lines as of June 30, 2000. This represents a 53 percent growth in market size during the first

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[92] We do not address the issue contained in the *Further Notice* of whether there are anticompetitive effects of allowing nondominant interexchange carriers to bundle CPE with interstate, domestic, interexchange service, when such services, in turn, are packaged with international services. *Further Notice*, 13 FCC Rcd at 21543-44, para. 23. The Commission received virtually no comments on this issue, and there is therefore no information in the record regarding the extent to which bundling international services with CPE would be in the public interest. We have just found that the statutory requirement that nondominant common carriers file tariffs for their international interexchange service is no longer necessary for the majority of international services as a result of competition in the market for international interexchange services, and we ordered the complete detariffing of these services subject to a transition period. *2000 Biennial Review: Policy and Rules Concerning the International Interexchange Marketplace*, IB Docket No. 00-202, Report and Order, FCC 01-93, para. 7 (rel. Mar. 20, 2001). We will develop a more complete record on international bundling and address this issue in the future .

[93] The *Further Notice* sought comment on the effects of allowing carriers to "offer local exchange and exchange access services in conjunction with the bundled offering of CPE and interstate, domestic, interexchange service." *Further Notice*, 13 FCC Rcd at 21546, para. 27. Carriers have not sought the ability to bundle exchange access service, by itself, with interexchange service, and therefore, for purposes of this order, we will consider local exchange service and exchange access service to be a single component of a package of service, and will refer to them as local exchange service.

six months of this year.[94] The Commission's data also indicate that the rate at which competitive LECs are providing service using unbundled network elements from the incumbent LECs is increasing. The number of lines that incumbent LECs provided as unbundled network elements doubled in the first half of 2000 from about 1.5 million to 3 million lines.[95] The Commission has also approved the entry of Bell Atlantic and SBC into the in-region long distance markets in New York, Texas, Kansas, and Oklahoma, marking the first time that the Commission has found that the local markets in those states are open to competition as required by section 271 of the 1996 Act.[96] Overall, the local exchange market is clearly more competitive than the cellular market was at the time that the Commission allowed carriers to bundle CPE with cellular service. At that time, the Commission's rules allowed no more than two facilities-based cellular carriers in each market, and the Commission had determined that resellers did not compete effectively with these carriers.[97]

b. Likelihood of Anticompetitive Conduct

(i) Nondominant LECs

32. For most of the same reasons discussed in connection with nondominant interexchange carriers, we conclude that it is extremely unlikely that any nondominant LEC would be able to restrict competition if it were permitted to bundle CPE with local exchange service.[98] By definition, nondominant carriers do not have market power. Customers will switch carriers if nondominant LECs attempt to make them purchase bundles that contain undesirable CPE product offerings.[99] At the same time, bundling offers consumers the benefits that we have identified, and may encourage them to seek competitive alternatives for local exchange service if competitors can offer this service as part of a package. No commenter seriously challenges this conclusion. Accordingly, we find it in the public interest and consistent with the purposes of section 11 of the Act to eliminate our restriction on the bundling of CPE with local exchange service by nondominant LECs.

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[94] *Local Telephone Competition Status as of June 30, 2000*, December 2000, Industry Analysis Division, Common Carrier Bureau, FCC, at 1 (*December 2000 Local Competition Report*).

[95] *Id.* at 2.

[96] *See supra* note 59.

[97] *Cellular Bundling Order*, 7 FCC Rcd at 4029, para. 11.

[98] We note that we have jurisdiction to allow carriers to bundle CPE with local exchange service. *See* 47 U.S.C. §§ 152(a), 153(52); *Computer and Communications Industry Association*, 693 F.2d at 214-18 (affirming the Commission's authority to deregulate CPE in accordance with the *Computer II Order* and citing *North Carolina Utilities Comm'n. v. FCC*, 552 F.2d 1036 (4th Cir. 1977)).

[99] Section 251(b)(2) of the Act places a duty on all LECs to provide number portability so that customers may switch local service providers without changing their existing telephone number, a requirement that Congress determined will lower barriers to entry and promote competition in the local exchange market. *See* 47 U.S.C. § 251(b)(2); *Telephone Number Portability*, CC Docket No. 95-116, First Report and Order and Further Notice of Proposed Rulemaking, 11 FCC Rcd 8352, 8352, para. 2 (1996).

(ii) Incumbent LECs

33. We also conclude that incumbent LECs may bundle CPE with local exchange service. Compared to our prior determinations, an evaluation of whether to eliminate the restriction on bundling CPE with local exchange service by incumbent LECs requires a more difficult analysis, and ultimately, a balancing of interests. Despite the inroads made by competitors into the local exchange market that we described above, incumbent LECs retain market power in the provision of local service within their respective territories. Thus, unlike our previous analysis of the interexchange market or nondominant LECs, incumbent LECs possess one of the essential characteristics for engaging in anticompetitive behavior – market power with respect to one of the components in the bundle. Nonetheless, we conclude, in light of the existing circumstances in these markets, that the risk of anticompetitive behavior by the incumbent LECs in bundling CPE and local exchange service is low and is outweighed by the consumer benefits of allowing such bundling.[100] We view the risk as low not only because of the economic difficulty that even dominant carriers face in attempting to link forcibly the purchase of one component to another, but also because of the safeguards that currently exist to protect against this behavior.

34. We look first at the particular benefits associated with allowing carriers to bundle CPE with local exchange service. Although we believe that these benefits accrue equally to consumers regardless of whether a nondominant LEC or incumbent LEC provides service, we highlight them here as part of our incumbent LEC analysis. In particular, incumbent LECs have asserted that the high price of CPE is one of the greatest barriers to inducing customers to subscribe to a new service.[101] Bundling can reduce this barrier by allowing carriers to offer new customers CPE and local exchange service more economically than if it were prohibited. We are particularly persuaded that bundling can promote the deployment of advanced telecommunications services. For example, as several commenters explain, many advanced telecommunications services require specialized CPE that customers would otherwise need to buy separately because they represent new technologies that traditional CPE does not support.[102] By providing the necessary equipment as part of a discounted package, possibly including leasing or amortizing the purchase of the equipment, a carrier can eliminate some of the up-front investment cost that inhibits customers from subscribing to the service.[103]

35. Indeed, the Commission has recognized that giving consumers the option of avoiding high up-front expenditures by bundling service and equipment was one of the

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[100] *Cellular Bundling Order*, 7 FCC Rcd at 4030-31, paras. 19-21.

[101] *See, e.g.*, Bell Atlantic Comments at 2, 12-16; BellSouth Comments at 11; BellSouth Reply Comments at 7; Next Level Comments at 5.

[102] Bell Atlantic Comments at 15-16, GTE Reply Comments at 6-7. *See also* SBC Comments at 9 (stating that bundling allows carriers to address technical issues associated with CPE that new customers may have by, for example, allowing it to offer preprogrammed CPE that allows customers to more easily use different services).

[103] Bell Atlantic Comments at 15. *See also* Next Level Comments at 4; GTE Reply Comments at 6-8.

factors that contributed to the significant growth in the cellular market.[104] Deregulation in the wireline CPE market can offer the same potential to encourage customers to purchase new services. An increase in demand for transmission service has the secondary benefit of expanding the market for related CPE. For example, the Commission concluded in the *Cellular Bundling Order* that bundling would assist the conversion from analog to digital cellular service. It stated that because digital handsets, at the time, would be larger, heavier, and more expensive than analog models, allowing carriers to market attractively priced packages of new service and equipment would speed the deployment of digital cellular service and equipment.[105] Similarly, equipment that customers need to purchase today to access certain advanced services may be costly, appear technically complicated, and be subject to frequent design changes or upgrades. We believe that bundling can encourage demand for these CPE products and the services they support. In particular, bundling can reduce the initial costs of new technology until sufficient demand for it develops, thereby driving down prices for equipment and services to competitive levels.

36. In conjunction with these benefits, we recognize risks associated with incumbent LEC bundling of CPE with local exchange service. As we stated in the *Computer II Order*, there is the risk that an incumbent LEC with market power in the local exchange market could force a customer to purchase CPE in order to obtain local exchange service.[106] We must now take into account, however, that the 1996 Act changed dramatically the telecommunications landscape by, among other things, removing entry barriers in the local market. For instance, section 251 imposes a duty on LECs possessing market power in the local exchange market to negotiate in good faith and provide interconnection to competitive carriers, and provides a list of minimum standards that the incumbent LEC must offer, including unbundled access to its network and interconnection that is at least equal in type, quality, and price that the incumbent LEC provides to itself or any other party.[107] Incumbent LECs must also offer for resale at wholesale rates any retail telecommunications service.[108] Section 253 of the Act also mandates that states may not enact any requirement that prohibits or has the effect of prohibiting any entity from providing interstate or intrastate telecommunications service, and requires states and localities to manage rights-of-way to which competitors need access in a competitively-neutral and non-discriminatory manner.[109] As a result, local competition has begun to grow as we indicated above. As this competition increases, we believe that incumbent LECs will either offer bundled or unbundled packages as consumers demand or risk losing ground to more responsive competitors. In addition, we note that since the Commission lifted restrictions on bundling cellular service and cellular

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[104] See Navigation *Devices Order*, 13 FCC Rcd at 14810-11, 14813, paras. 87, 94 (citing *Cellular Bundling Order*, 2 FCC Rcd at 4028).

[105] *Cellular Bundling Order*, 7 FCC Rcd at 4031, para. 20.

[106] *Computer II Order*, 77 FCC 2d at 442-43, paras. 149-50.

[107] 47 U.S.C. § 251; Joint Statement of Managers, S. Conf. Rep. No. 104-230, 104th Cong., 2d Sess., at 117-18 (1996).

[108] 47 U.S.C. § 251(c)(4).

[109] 47 U.S.C. § 253.

equipment, sales of cellular telephones and overall subscribership to cellular service have increased dramatically.[110] While we recognize that this growth is due to many factors, we view bundling, as we stated above, as one of the positive factors that encouraged it. We find all of these changed circumstances to be persuasive in our decision to allow incumbent LECs to bundle CPE with local exchange service.

37. There are also other factors that we take into account in evaluating the ability of incumbent LECs to act anticompetitively. In order to harm the vitality of competition in the CPE market by forcing consumers to purchase a package of CPE and local exchange service, the incumbent LEC must preempt so many consumers from purchasing competitively-supplied CPE that not enough remain to support a competitive number of CPE suppliers.[111] For example, there is a risk that incumbent LECs could harm CPE competition by requiring customers that purchase local exchange service from them to also purchase CPE. Yet, as Professor Areeda explains, a seller only has an incentive to act in such an anticompetitive manner if by bundling the product (in this case, CPE) it can reduce costs or otherwise gain by pricing the product above competitive levels. If a seller can not do either because the product is subject to highly competitive prices, then there is little reason to worry about impairing competition for that product.[112] Overall, we believe that incumbent LECs do not have the ability to engage in sustained anticompetitive practices with regard to CPE because even if an incumbent were to attempt to corner the local retail CPE market and began charging high CPE prices, other CPE providers could supply retailers with affordable CPE. Customers would then be able to purchase the lower-priced CPE and obtain local exchange service at the same rates as if the customer had bought the CPE from the carrier because local exchange service will remain available on an unbundled, non-discriminatory basis.[113] To ensure such availability, incumbent LECs assert that they are required by state law to offer local exchange service separately on an unbundled tariffed basis if they bundle such service with CPE.[114] We also require incumbent LECs to offer exchange access service and any other service for which the Commission considers them to be dominant separately on

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[110] *See Trends in Telephone Service*, FCC Common Carrier Bureau Industry Analysis Division, December 2000, at 12-1, 12-4 (stating that wireless telephone subscribers increased from approximately 8.8 million in June 1992 to over 97 million in June 2000). Consumer Electronics Association, "2000 Will Ring in Record Growth in Consumer Electronics Sales – Digital Technologies and Workstyle Products Continue to Drive Sales," at 1 (rel. Jan. 6, 2000); Bell Atlantic Comments at 7 (stating that the number of wireless CPE manufacturers increased from 17-25 in 1992 to more than 100 in 1998 and that wireless handsets are redesigned and updated frequently);

[111] *Areeda Vol. IX* at para. 1704(a).

[112] *Id.* at para. 1704(b). We also note that the BOCs are unlikely to have lower costs than competing suppliers because they are prohibited from manufacturing CPE except as permitted under section 273 of the 1996 Act. Section 273 allows the BOCs to do so if the Commission authorizes them to provide interLATA services pursuant to section 271(d). Upon gaining manufacturing relief, a BOC will enter a highly competitive market with zero percent market share, making it difficult to leverage a bundled offering in an anticompetitive manner. *See* BellSouth Comments at 5, n.5.

[113] *See Cellular Bundling Order*, 7 FCC Rcd at 4030, para. 13.

[114] *See* Ameritech Comments at 6; Bell Atlantic Reply Comments at 4; BellSouth Reply Comments at 11-13; GTE Comments at 13.

nondiscriminatory terms if they bundle such service with CPE. As competition increases, customers will also have the ability to switch local providers if the incumbent LEC offers unattractive bundled offerings.

38. An incumbent LEC that seeks to bundle CPE with any regulated transmission service could potentially offer low-priced CPE by recovering the cost of the CPE through its regulated rates. Again, several factors help balance this risk. Importantly, as we stated above, where local competition exists, incumbent LECs have a strong incentive to keep local rates low, not to increase them to support sales of other products or services.[115] There are also several existing regulatory safeguards that are in place to address this concern. The Commission's Part 64 cost allocation rules require large incumbent LECs to separate their regulated costs from nonregulated costs and contain multiple provisions, including mandatory audits, that require them to demonstrate how they are allocating costs between regulated and unregulated activities.[116] Consistent with our findings in the *Cellular Bundling Order*, incumbent LECs that are subject to price cap regulation in both the state and federal jurisdictions do not have an incentive to shift unregulated CPE costs because absent a guaranteed rate-of-return on their local exchange investment, these carriers cannot expect to recover CPE discounts by including them in their regulated rate base.[117] There is an increased risk of cross-subsidization by incumbent LECs still subject to rate-of-return regulation, but the requirement that incumbent LECs file tariffs and cost support at the state level restricts their ability to lower prices uneconomically.[118] As local exchange service becomes more competitive, we also expect the risk associated with cross-subsidization to decrease. Overall, we find that the potential anticompetitive impact of allowing incumbent LECs to bundle local exchange service with CPE is outweighed by the public interest benefits associated with bundling.

C. Enhanced Services Bundling

39. In this section, we clarify that there is currently no prohibition on the bundling of basic telecommunications service and enhanced service at a single, discounted price for any carrier. This clarification will allow carriers to offer innovative packages of enhanced services bundled with basic telecommunications service and CPE. In order to ensure that competitive enhanced service providers continue to have non-discriminatory access to the underlying transmission capacity, we do not eliminate the existing requirement that facilities-

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[115] The *December 2000 Local Competition Report* states that as of June 30, 2000, at least one competitive LEC was serving customers in 54 percent of the nation's zip codes. In California, New York, and Texas, more than one-fifth of zip codes have seven or more competitive LECs that reported service in response to the Commission's reporting requirements. *December 2000 Local Competition Report* at 3.

[116] 47 C.F.R. §§ 64.901-904.

[117] *See* Ameritech Comments at 12-13; GTE Reply Comments at 13-14. We do not find that price cap regulation eliminates all possible incentive to shift costs. Rather, the incentives under price caps are much less significant than under rate-of-return regulation because the carriers are no longer entitled to increase rates to recoup cost increases. *See BOC Safeguards Order*, 6 FCC Rcd at 7571, 7596-97, n.95.

[118] *See GTE Duncan Aff.* at 13.

based carriers offer such capacity to these providers on the same terms and conditions under which they provide such service to their own enhanced service operations.

1. Existing Requirements for Nondominant Carriers

40. We clarify that the requirement in *Computer II*, that carriers not subject to the separate subsidiary requirement acquire transmission capacity pursuant to the same prices, terms, and conditions reflected in their tariffs when their own facilities are used, does not prohibit them from offering packages of telecommunications service, including interstate, domestic, interexchange service or local exchange service, and enhanced services at a single price.[119] As long as they comply with the requirement to make their underlying transmission capacity for the enhanced service available on nondiscriminatory terms, it is consistent with the Commission's reasoning in *Computer II* to clarify that these carriers may offer bundled packages. In particular, the Commission found in *Computer II* that carriers that had no control over local bottleneck facilities, and therefore no market power, would not be in a position to act anticompetitively if they had integrated basic and enhanced services operations.[120] It pointed out specifically that any advantages from anticompetitive conduct "would be short-lived, as customers could readily avail themselves of alternative suppliers."[121] The Commission also found that the potential for these carriers to offer innovative services to a broader range of customers would increase if they were not subject to the structural separation requirements.[122] We conclude that a natural outcome of allowing these carriers to operate on an integrated basis is that they would be able to offer packages of telecommunications and enhanced services at a single price, and indeed, there is no restriction against such packaging for these carriers in *Computer II*, provided that they comply with the safeguard to make available the underlying transmission capacity for the enhanced service.[123]

41. We also clarify the scope of the bundling that carriers may undertake. While nearly all commenters agree that nondominant carriers should be permitted to bundle enhanced services with telecommunications services,[124] there is some confusion in the record regarding the extent to which carriers already bundle these services. In particular, MCI WorldCom states that in the *Non-Accounting Safeguards Order*, the Commission explained

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[119] Dominant facilities-based carriers must also acquire the underlying transmission capacity for an enhanced service in the same manner as other competitive enhanced services providers. This requirement stems primarily from having to provide enhanced services through a fully separate subsidiary under *Computer II*. *Computer II Order*, 77 FCC 2d at 474, para. 229; para. 42 *infra*.

[120] *See id.* at 466-69, paras. 215-222.

[121] *See id.* at 468-69, para. 221.

[122] *See id.* at 469, para. 222.

[123] *See Frame Relay Order*, 10 FCC Rcd at 13723, para. 46 (finding that AT&T was free to continue its practice of packaging CPE and enhanced protocol processing services with basic frame relay service, so long as the underlying basic service is separately offered under tariff.).

[124] *See, e.g.*, API Comments at 9; AT&T Comments at 5-8; CompTel Comments at 5-7; Sprint Comments at 2-3.

that interLATA information service already includes a bundled interLATA telecommunications element because information service, itself, is a bundling of telecommunications service and the computer processing that is necessary to offer the information-based portion of the service. In that sense, it points out, all enhanced services are "bundled" services.[125] It suggests that carriers should be permitted a greater degree of enhanced service bundling than simply the bundling that is inherent in the provision of any interLATA enhanced service.[126] For example, it states that nondominant interexchange carriers should be able to bundle enhanced services, such as voice mail, with other separate interexchange services.[127] We agree. The benefits of bundling come from allowing consumers to purchase an all-inclusive bundle at a single price that consists of interstate, domestic, interexchange transmission services combined with their choice of enhanced service and CPE.

2. Existing Requirements for Dominant Carriers

42. Unlike nondominant carriers, dominant carriers are restricted under *Computer II* from offering enhanced services and basic telecommunications services at a single price. This is because dominant carriers that choose to operate pursuant to *Computer II*, as opposed to *Computer III*, are required to maintain a fully separate subsidiary for the provision of enhanced services with the separate subsidiary having its own operating, marketing, installation, and maintenance personnel for the services it offers.[128] The Commission stated that because of the difficulties that it believed existed in allocating joint and common costs between such regulated an unregulated entities, it eliminated the allocations by prohibiting any joint activities in the areas of provisioning or marketing.[129] The carrier is then also required to offer its underlying transmission facilities to all competitive enhanced service providers, including its own subsidiary, on an equal basis.[130] Under such a regime, the dominant carrier could not bundle an enhanced service and a basic telecommunications service at a single price.

43. In *Computer III*, the Commission replaced the structural safeguards established in *Computer II* with nonstructural safeguards, which it found would perform as well in combating discrimination by the BOCs and be less costly. In doing so, it allowed BOCs to integrate their enhanced and basic service operations, but affirmed the requirement that they acquire transmission capacity under the same tariffed terms and conditions as competitive

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[125] MCI WorldCom Comments at 33-34 (citing *Non-Accounting Safeguards Order*, 11 FCC Rcd at 21971-72, para. 136). *See also* BellSouth Comments at 13 (stating that there is a presumptive "resale" model for the carrier provision of enhanced services under which a carrier offers an enhanced service that incorporates an underlying transmission service to the customer as a single "bundled" offering).

[126] MCI WorldCom Comments at 33-34.

[127] *Id.* at 34.

[128] *Computer II Order*, 77 FCC 2d at 477, para. 239.

[129] *Id.* at 477, para. 238.

[130] *Id.* at 474, para. 229. *See also Frame Relay Order*, 10 FCC Rcd at 13725, para. 59.

enhanced service providers.[131] This unbundling is accomplished primarily through CEI and ONA requirements. The Commission recognized specifically that this integration would permit the BOCs to "engage in joint marketing of enhanced and basic services."[132] It is clear, however, that although BOCs are permitted to market telecommunications services jointly with enhanced services, they remain obligated to offer the telecommunications service component separately. We therefore agree with U S West that BOCs can already jointly market basic and enhanced services under our existing requirements, but must continue to offer the basic service separately pursuant to tariff.[133] Indeed, the BOCs do not advocate that the Commission eliminate this requirement, but argue instead that we make it clear that they already may bundle enhanced services with local exchange service at one price in the same manner that CPE can be bundled. As we stated above, we agree with this interpretation of *Computer III*.[134]

44. There are other existing safeguards that are applicable to incumbent LECs that seek to bundle. There is no dispute in the record that the BOCs and all incumbent LECs are required to offer basic local exchange service on an unbundled, tariffed, nondiscriminatory basis. Indeed, there is no evidence in the record that these carriers are relieved of this obligation in any state in which they provide local exchange service. Customers would therefore be able to purchase enhanced services from competitive providers and still obtain local service from the incumbent pursuant to the tariff. This prevents the incumbent carriers from discriminating against customers who purchase enhanced service from competitive suppliers. As the Commission found in the *Cellular Bundling Order*, the separate availability of the transmission service is fundamental to ensuring that dominant carriers cannot discriminate against customers who do not purchase all the components of a bundle from the carriers, themselves.[135] Incumbent LECs are also subject to specific safeguards in sections 260, 274 and 275 of the Act for the provision of telemessaging, electronic publishing and alarm monitoring services.[136]

45. In addition, our cost-accounting rules reduce significantly the BOCs' incentive and ability to misallocate costs between their regulated and unregulated service operations. We reject the unsubstantiated arguments of the commenters who contend that our cost

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[131] *Computer III Phase I Order*, 104 FCC 2d at 1011-13.

[132] *Id.* at 1012, para. 99.

[133] U S West Comments at 7-9. *See also* BellSouth Comments at 13-14; Letter from Linda L. Kent, Associate General Counsel, USTA, to Magalie Roman Salas, Secretary, FCC, CC Docket No. 98-183, at 2 (filed Feb. 15, 2001). We note that in the *Computer III 1998 FNPRM*, the Commission, in response to a petition, raised the issue of whether BOCs should be prohibited from using the same personnel and facilities to jointly market basic services and information services even though they are allowed to provide such services on an integrated basis under the *Computer III* requirements. *Computer III 1998 FNPRM*, 13 FCC Rcd at 6114, para. 129. Should the Commission's requirements change to an extent that it would impact our bundling decision, we will address the issue at that time.

[134] *See* Ameritech Comments at 18-19; BellSouth Comments at 13-14; U S West Comments at 7-9.

[135] *Cellular Bundling Order*, 7 FCC Rcd at 4028, 4030-31, paras. 1, 13, 23.

[136] 47 U.S.C. §§ 260, 274, 275.

allocation rules will not prevent cross-subsidization.[137] These rules consist of detailed cost allocation requirements and related cost accounting safeguards that separate nonregulated enhanced service costs from regulated service costs, cost accounting mechanisms to enforce the joint cost rules (including the filing and approval of cost allocation manuals), and the requirement that carriers submit to independent audits.[138] The Commission has also found that these cost allocation safeguards provide sufficient information for the states to protect against cross-subsidies at the intrastate level.[139] It explained that the operation of the joint cost and jurisdictional separations rules result in a BOC intrastate assignment of basic service costs. To protect against cross-subsidy of enhanced services by intrastate ratepayers, which is an important issue if BOCs can bundle interstate enhanced services with local exchange service, a state need only use its normal regulatory mechanisms to ensure that intrastate rates are not too high in light of that assignment.[140]

46. We also emphasize that section 202 applies equally to all carriers, both dominant and nondominant, that provide transmission service to competitive enhanced service providers. In particular, Internet Service Providers have raised issues regarding their ability to obtain DSL service on nondiscriminatory terms.[141] The internet service providers require DSL service to offer competitive internet access service. We take this issue seriously, and note that all carriers have a firm obligation under section 202 of the Act to not discriminate in their provision of transmission service to competitive internet or other enhanced service providers. Indeed, the Commission has already found that where there is an incentive for a carrier to discriminate unreasonably in its provision of basic transmission services used by competitors to provide enhanced services, section 202 acts as a bar to such discrimination.[142] In addition, we would view any such discrimination in pricing, terms, or conditions that favor one competitive enhanced service provider over another or the carrier, itself, to be an

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[137] *See, e.g.*, Letter from Charles E. Griffin, AT&T, to Magalie Roman Salas, Secretary, FCC, CC Docket Nos. 96-61 and 98-183 (filed Sept. 18, 2000) at 2.

[138] *BOC Safeguards Order*, 6 FCC Rcd at 7576-77, para. 11 (citing 47 C.F.R. Parts 31, 43, 67 and 69). In its review of the *Computer III* proceeding, the U.S. Court of Appeals for the Ninth Circuit found that the Commission's cost allocation rules would reduce significantly the BOCs' ability to misallocate costs between enhanced and basic services. *California v. FCC*, 39 F.3d at 926. It also found that mandatory price cap regulation for the BOCs decreases their incentive to shift costs from nonregulated activities to regulated ones because they are not able to increase regulated rates to recapture the costs associated with enhanced services. *Id.*

[139] *BOC Safeguards Order*, 6 FCC Rcd at 7592-93, n.86.

[140] *Id.* at 7592-93, n.86.

[141] *See* Letter from Mark J. O'Connor, Donna N. Lampert Associates, P.C., on behalf of EarthLink, to Magalie Roman Salas, Secretary, FCC, CC Docket No. 98-183 (filed Dec. 22, 2000); Letter from Donna N. Lampert and Mark J. O'Connor, Lampert & O'Connor, P.C., on behalf of EarthLink, Inc., to Dorothy Attwood, Chief, Common Carrier Bureau, FCC, CC Docket No. 98-183 (filed Jan. 3, 2001).

[142] *Frame Relay Order*, 10 FCC Rcd at 13719, para. 13. *See also Deployment of Wireline Service Offering Advanced Telecommunications Capability*, CC Docket No. 98-147, Second Report and Order, FCC 99-330, para. 21 (rel. Nov. 9, 1999) (stating that bulk DSL services sold to internet service providers as an input component to the internet service provider's high-speed Internet service offering, which is an information service, must be provided by incumbent LECs on just, reasonable, and nondiscriminatory terms.).

unreasonable practice under section 201(b) of the Act. We also note that the Commission's Title II resale requirements mandate that wireline common carriers provide telecommunication services to competitors.[143]

D. Universal Service Allocation

47. Section 254 of the Act requires every telecommunications carrier that provides interstate telecommunications service to "contribute, on an equitable and non-discriminatory basis, to the specific, predictable, and sufficient mechanisms established by the Commission to preserve and advance universal service."[144] The Commission's rules require entities with interstate end-user revenues to contribute to the universal service fund.[145] Further, contributions are based solely on end-user telecommunications revenue, and thus exclude enhanced services and CPE.[146]

48. When carriers generate revenues from stand-alone service or product offerings, the calculation of their universal service contributions is relatively straightforward. Carriers report revenues from telecommunications services and revenues from non-telecommunications offerings (including CPE and enhanced services revenues) in separate sections of the Commission's revenue worksheet, which is submitted semi-annually.[147] Carriers are assessed universal service contributions only on their revenues from telecommunications services. If carriers generate revenues from bundled packages of telecommunications services and CPE/enhanced services, however, the calculation of their universal service contributions becomes more complicated. Thus, we sought comment in the *Further Notice* on how to allocate revenue when telecommunication services and CPE/enhanced services are offered as a bundled package, for purposes of calculating a carrier's universal service contribution.[148] Only two carriers commented on this issue. MCI

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[143] *See Resale and Shared Use*, 60 FCC 2d 261(1976), *aff'd sub nom. AT&T v. FCC*, 572 F.2d 17 (2d Cir.), *cert. denied.*, 439 U.S. 895 (1978); *Resale and Shared Use of Domestic Public Switched Network Services*, 83 FCC 2d 167 (1980) *recon. denied*, 86 FCC 2d 820 (1981).

[144] 47 U.S.C. § 254(d).

[145] 47 C.F.R. § 54.706.

[146] 47 C.F.R. § 54.709. The Commission has stated that merely combining telecommunications service with an enhanced service does not automatically deem the combined service enhanced. Rather, "the issue is whether, functionally, the consumer is receiving two separate and distinct services." *Federal-State Joint Board on Universal Service*, Fourth Order on Reconsideration, CC Docket No. 96-45, *Access Charge Reform, Price Cap Performance Review for Local Exchange Carriers, Transport Rate Structure and Pricing, End User Common Line Charge*, Report and Order, CC Docket Nos. 96-262, 94-1, 91-213, 95-72, 13 FCC Rcd 5318, 5474-75, para. 282 (1997) (*Fourth Order on Reconsideration*).

[147] *See* Form 499, available at <http://www.fcc.gov/formpage.html>. Form 499 sets forth the information that contributors must submit so that the administrator of the universal service mechanism may calculate and assess contributions.

[148] *Further Notice*, 13 FCC Rcd. at 21541, para. 18.

Worldcom asked the Commission to defer a decision on this matter to another proceeding,[149] while GTE did not address the funding issues raised by bundling.[150]

49. In this Order, we suggest two methods that contributors may use to allocate revenue when telecommunication services and CPE/enhanced services are offered as a bundled package. Our primary goal is to have a framework that deters carrier gaming while being competitively neutral, easy to administer, and simple to understand. Our existing rule requires carriers to contribute to the universal service support mechanism based on interstate end-user telecommunications revenue.[151] We recognize that carriers may bundle goods and services in a multitude of ways that cannot be anticipated, and thus we afford carriers the needed flexibility to determine the appropriate allocation of revenues for universal service support purposes. In reporting revenues, carriers should remain mindful of their contribution obligation under our current rule and are expected to exercise good faith in reporting revenues. Detailed below are two ways carriers could report revenues that would afford them "safe harbor" protection under the rule. The overriding intent is to maintain stability and predictability in funding the universal service support mechanisms.

50. First, contributors may elect to report revenues from bundled telecommunications and CPE/enhanced service offerings based on the unbundled service offering prices,[152] with no discount from the bundled offering being allocated to telecommunications services. For example, assume that a carrier offers voice-mail service, an enhanced service, as a stand-alone offering for $6.00, and also offers basic phone service, a telecommunications service, for $20.00. The carrier offers the two services for the bundled price of $22.00, resulting in a discount of $4.00. Under this approach, the carrier would report telecommunications service revenue of $20.00 per month (the stand-alone price for the phone service) and non-telecommunications revenue of $2.00 per month (the stand-alone price for voice-mail minus the discount from the bundled offering). As we note in this Order, carriers will likely continue to offer both bundled and unbundled telecommunications service offerings.[153] Because incumbent local exchange carriers will continue to tariff services separately and nondominant carriers will likely continue to offer unbundled pricing to meet the needs of consumers, this method provides carriers with an easily ascertainable method of allocating revenues for purposes of calculating universal service contributions.

51. Alternatively, contributors may elect to treat all bundled revenues as telecommunications service revenue for purposes of determining their universal service obligations. For example, assume that a carrier offers a bundled package of voice-mail and basic phone service to end-users at $25.00 per month. The carrier decides that it cannot distinguish revenue for the basic service (the telecommunications service) from voice-mail

[149] MCI Worldcom Comments at 10.

[150] GTE Comments at 18-20 (GTE's comments focused on issues pertaining to provision of universal service support).

[151] 47 C.F.R. §§ 54.706, 54.709.

[152] For interexchange carriers, this rate would be determined by their standard business offerings, whereas for local exchange carriers, it would be determined based on their tariffed rates.

[153] *See supra* para. 26.

(the non-telecommunications service). This carrier would report telecommunications revenue of $25.00 per month. This option would permit those contributors that are unable or unwilling to separate end-user telecommunications revenues from non-telecommunications revenue to comply with their universal service obligations when they generate revenues from bundled telecommunications services and CPE/enhanced service offerings.

52. These allocation methods are "safe harbors" and will be afforded a presumption of reasonableness in an audit or enforcement context.[154] Both of the above-described methods enable carriers to allocate revenues for purposes of universal service contributions in an easily ascertainable and reasonable manner. These methods also decrease the investigative burden in an audit or other enforcement proceeding because the necessary information is easily obtained and verified. Thus, these allocation methods provide certainty to both carriers and the Commission, and we encourage their use.

53. Carriers may choose to use allocation methods other than the two described above. Carriers should realize, however, that any other allocation methods may not be considered reasonable, and will be evaluated on a case-by-case basis in an audit or enforcement context. In evaluating the reasonableness of any alternative methods, we will apply the standards underlying the safe harbors described above. For example, carriers should not apply discounts to telecommunications services in a manner that attempts to circumvent a carrier's obligation to contribute to the universal service support mechanisms. Should an audit or enforcement proceeding be initiated, carriers will need to provide evidence that the amount of reported telecommunication revenues that they report reflects compliance with the carrier's obligation to contribute to the universal service support mechanism based on interstate end-user telecommunications revenue. [155]

54. As explained above, the methods outlined in this Order are examples of how carriers may report revenues for universal service purposes, and carriers may choose to use a different method altogether. We adopt this approach in recognition of the fact that, at this time, we cannot anticipate the various ways in which carriers may choose to bundle their goods and services. We conclude that this flexible, simple, and easily administered approach will continue to maintain stability and predictability in the universal service fund, while granting carriers considerable freedom in deciding how to bundle their offerings. Finally, we note that as we gain experience with carrier practices,[156] we may in the future seek comment on whether we need to adopt additional rules.

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[154] Carriers will be asked to check a box on Form 499 that indicates whether they have reported revenues based on one of the safe harbor approaches. The Certification Statement in Form 499 will apply to this information.

[155] 47 C.F.R. §§ 54.706, 54.709.

[156] We remind filers that USAC monitors carrier filings for compliance with the reporting requirements and advises the Commission on any enforcement issues that arise. *See* 47 C.F.R. § 54.711 (a).

E. Impact of Bundling on Network Disclosure and Part 68 Requirements

1. CPE Bundling

55. We conclude that our existing network disclosure policy and rules ensure that carriers that bundle CPE and transmission services will continue to provide CPE suppliers with access to information about the carriers' networks that the suppliers require to offer competitive products. The Commission sought comment in the *Further Notice* on whether the network disclosure requirement promulgated in *Computer II* that was referred to as the "all-carrier" rule would provide competitive CPE suppliers with adequate disclosure of a carrier's network interfaces.[157] In 1999, the Commission eliminated the "all carrier" rule in a separate proceeding.[158] It found that interexchange carriers are not likely to gain the individual market power that would allow them profitably to withhold information about their network interfaces that competitive CPE suppliers require, and that the rule, as it applied to interexchange carriers, was therefore no longer necessary.[159] We also emphasized that sections 201 and 202 of the Communications Act impose nondiscrimination requirements that prohibit carriers that manufacture CPE from favoring their own CPE over that of competitive suppliers.[160] We continue to believe that normal market forces pressure interexchange carriers to provide CPE suppliers with necessary network information, and that sections 201 and 202 of the Act safeguard against anticompetitive conduct in this area. We therefore do not find that any additional public disclosure requirements are necessary for interexchange carriers that bundle CPE with interstate, domestic, interexchange services.

56. Our rules require incumbent LECs to disclose network changes that could affect the manner in which CPE is attached to their networks.[161] When the Commission eliminated the *Computer II* "all-carrier" rule, it extended the disclosure requirements in section 51.325(a) of our rules to require incumbent LECs to provide public notice of any network changes that will affect CPE manufacturers.[162] This rule applies to all interconnected CPE whether or not the incumbent LEC provides the CPE as part of a bundled offering. It is necessary because failure to disclose network changes that affect CPE could give incumbent LECs a significant head start in providing fully compatible equipment and could thereby adversely affect competition in the CPE market.[163] While we believe that incumbent LECs,

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[157] *Further Notice*, 13 FCC Rcd at 21542, para. 20. The "all-carrier" rule required that all carriers owning basic transmission facilities disclose to the public all information relating to network design "insofar as such information affects either intercarrier interconnection or the manner in which interconnected CPE operates."

[158] *Computer III March 1999 Order*, 14 FCC Rcd at 4320-23, paras. 48-53.

[159] *Id.* at 4320-22, paras. 48-50. The Commission retained requirements for incumbent LECs to disclose network information to CPE suppliers that are codified at 47 C.F.R. § 51.325(a). *Id.* at 4322-23, paras. 52-53.

[160] *Id.* at 4322-23, paras. 51-52.

[161] 47 C.F.R. § 51.325(a)(3). *See also Computer III March 1999 Order,* 14 FCC Rcd at 4322-23, paras. 52-53. BOCs that manufacture equipment are also subject to the CPE safeguards contained in 47 U.S.C. § 273.

[162] *Computer III March 1999 Order*, 14 FCC Rcd at 4323, para. 53 (citing 47 C.F.R. § 51.325(a)).

[163] *Id.* at 4322-23, para. 52.

like other carriers, should have a business incentive to make interconnection to their networks available to all customers regardless of the type of CPE they use, this rule requires incumbent LECs to provide the specifications that competitive CPE suppliers need to provide compatible equipment.

57. We also conclude that allowing carriers to bundle CPE with transmission services will not affect the Commission's requirement that CPE not cause harm to the network. We sought comment in the *Further Notice* on whether the "demarcation point" between telephone company communications facilities and terminal equipment, as defined in section 68.3 of the Commission's rules,[164] would change if CPE and interexchange carriers' network offerings were bundled and what effect, if any, this would have on the Commission's Part 68 program.[165] In November 2000, the Commission adopted an Order eliminating certain portions of the Part 68 regulations governing the development of technical criteria and registration procedures for CPE.[166] It found that the highly competitive nature of the CPE market makes it no longer necessary for the Commission to establish technical criteria for CPE or approve the use of new CPE.[167] The Commission stated that eliminating these regulations should bring innovative equipment to the marketplace faster, thereby increasing choices available to consumers.[168] Accordingly, our action with regard to Part 68 should enhance further the ability of consumers to secure new and innovative CPE separately or as part of a bundled offering. Allowing carriers to bundle CPE with transmission service does not affect the technical criteria that the telecommunications industry will now establish on its own to ensure that CPE does not cause harm to the network, and we agree, in particular, with KMC that the *Further Notice* did not contemplate allowing carriers to technically bundle CPE and telecommunications service in such a way as to contravene the requirement that CPE not cause harm to the network.[169] Moreover, as the Commission noted in the *Part 68 Streamlining Order*, providers of telecommunications have an inherent interest in preventing harm to the public switched network,[170] and therefore also have an incentive to ensure that bundled CPE does not cause such harm.

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[164] 47 C.F.R. § 68.3.

[165] *Further Notice*, 13 FCC Rcd at 21541-42, para. 19.

[166] *See 2000 Biennial Review of Part 68 of the Commission's Rules and Regulations*, CC Docket No. 99-216, Report and Order, FCC 00-00-400, para. 2 (rel. Dec. 21, 2000) (*Part 68 Streamlining Order*). In this Order, we retain our rules prohibiting harms to the public switched telephone network. *Id.* at paras. 15, 69. In addition, we retain in our rules the technical criteria relating to inside wiring, hearing aid compatibility and volume control, and consumer protection provisions. We also maintain enforcement procedures for terminal equipment. *Id.* at paras. 4, 68-70, 115-26.

[167] *See id.* at paras. 11, 20-23.

[168] *See id.* at para. 21.

[169] KMC Comments at 7.

[170] *Part 68 Streamlining Order* at para. 119. We continue to permit providers to discontinue temporarily service to subscribers that connect harmful equipment. *See* 47 C.F.R. § 68.108.

2. Enhanced Services Bundling

58. We find that the Commission's network disclosure rules will also act as an important safeguard to prevent incumbent LECs that bundle enhanced services with local exchange service from acting in an anticompetitive manner. The Commission found, as several commenters assert in this proceeding,[171] that enhanced service providers remain dependent on incumbent LECs for local access to their customers, and that we must ensure that these carriers do not withhold network information that enhanced service providers need to interconnect with the incumbent LECs' networks.[172] We recognize that incumbent LECs may be able to leverage control over their local exchange facilities into market power over new or existing services if they are allowed to modify network interfaces without disclosing the changes to competitors. Our network disclosure rules therefore require all incumbent LECs to disclose publicly, at a minimum, "complete information about network design, technical standards and planned changes to the network."[173] These rules will continue to apply to incumbent LECs that bundle enhanced services with local exchange service.

IV. FINAL REGULATORY FLEXIBILITY ACT ANALYSIS

59. The Regulatory Flexibility Act (RFA)[174] requires that regulatory flexibility analyses be prepared for notice and comment rulemaking proceedings, unless the agency certifies that "the rule will not, if promulgated, have a significant economic impact on a substantial number of small entities."[175] The RFA generally defines the term "small entity" as having the same meaning as the terms "small business," "small organization," and "small governmental jurisdiction."[176] The RFA defines a "small business" to be the same as a "small business concern" under the Small Business Act.[177] Under the Small Business Act, a "small business concern" is one that: (1) is independently owned and operated; (2) is not dominant in its field of operation; and (3) meets any additional criteria established by the Small Business Administration (SBA).[178]

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[171] *See, e.g.*, CIX Comments at 2-3; ISPC Comments at 5-7.

[172] *Computer III March 1999 Order*, 14 FCC Rcd at 4321, para. 49.

[173] *See id.* at 4317-18, para. 43 (citing *Implementation of the Local Competition Provisions of the Telecommunications Act of* 1996, CC Docket No. 96-98, Second Report and Order and Memorandum Opinion and Order, 11 FCC Rcd 19392 (1996)); 47 C.F.R. § 51.327.

[174] The RFA, *see* 5 U.S.C. § 601 *et. seq.*, has been amended by the Contract With America Advancement Act of 1996, Pub. L. No. 104-121, 110 Stat. 847 (1996) (CWAAA). Title II of the CWAAA is the Small Business Regulatory Fairness Act of 1996 (SBREFA).

[175] 5 U.S.C. § 605(b).

[176] 5 U.S.C. § 601(6).

[177] 5 U.S.C. § 601(3) (incorporating by reference the definition of "small business concern" in 5 U.S.C. § 632).

[178] 15 U.S.C. § 632.

60. Consistent with the effort to reduce regulation wherever conditions warrant,[179] this Report and Order reviews the state of competition in the CPE and enhanced services market to determine if such competition warrants amending the bundling restrictions adopted in the *Computer II Order*. It also reviews the state of competition in the interstate, domestic interexchange, and local exchange markets to determine the likelihood that nondominant and incumbent carriers in these markets could engage in anticompetitive behavior if they are permitted to bundle such telecommunications services with CPE or enhanced services. In undertaking this analysis, the Report and Order acknowledges that because the local exchange market is not fully competitive and because incumbent LECs have market power, the Commission must balance the risk that incumbents can act anticompetitively with the public interest benefits of bundling. In light of the significant benefits of bundling outlined in the record developed in response to the *Further Notice* and the state of competition in the various component markets, the Report and Order finds that it is appropriate to eliminate the CPE bundling restriction for all carriers. In the case of enhanced services, it retains the requirement that facilities-based carriers continue to offer the underlying transmission service component of an enhanced service on nondiscriminatory terms, and clarifies that as long as the carriers meet this requirement, they may bundle enhanced services with telecommunications services at a single price.

61. We considered the potential impact of the Report and Order on three categories of entities: "small interexchange carriers;" "small incumbent LECs;" and "small non-incumbent LECs." The Report and Order will not have a significant economic impact on a substantial number of these entities because it relieves them of regulations that have prohibited them from offering consumers packages of telecommunications services and CPE at a single price. Removal of these rules will provide small entities the necessary flexibility to market services and CPE in a less restricted manner. In addition, these small entities will not have to incur certain transactional costs associated with separately offering and billing consumers for the components of a service package. In fact, it is expected that any economic impact will be a positive one. The Report and Order clarifies that small interexchange carriers, small incumbent LECs and small non-incumbent LECs may offer packages of enhanced services and telecommunications services at a single price, provided that they continue to comply with the existing requirements to offer competitive enhanced service providers access to the underlying transmission service component of an enhanced service on non-discriminatory terms. By clarifying this requirement, the Report and Order provides regulatory certainty. Therefore, there is no significant economic impact on such entities.

62. In addition, we considered the impact of the proposed rule revisions on information service providers (ISPs) and other competitive enhanced service providers. ISPs that described themselves as small businesses indicated in the record that they could suffer an economic impact from the rules proposed in the *Further Notice* if the Commission did not maintain the requirement that they be able to acquire underlying transmission capacity to provide enhanced services from the incumbent LECs on nondiscriminatory terms.[180] We have maintained this requirement for all incumbent LECs. ISPs also indicated that they

[179] *See* 47 U.S.C. § 161.

[180] *See* ISP/C Comments at 5-7.

could not acquire the transmission service on nondiscriminatory terms if incumbent LECs were permitted to bundle CPE with telecommunications services.[181] The Report and Order confirms that the transmission service component of CPE bundles will be separately available from the incumbent LECs on a non-discriminatory basis. Therefore, there is no significant economic impact on small ISPs and small competitive enhanced service providers.

63. Accordingly, we certify that the Report and Order will not have a significant economic impact on a substantial number of small entities.

64. The Commission will send a copy of this Report and Order, including a copy of this final certification, in a report to Congress pursuant to the Small Business Regulatory Enforcement Fairness Act of 1996.[182] In addition, the Report and Order and this final certification will be sent to the Chief Counsel for Advocacy of the Small Business Administration, and will be published in the Federal Register.[183]

V. ORDERING CLAUSES

65. Accordingly, IT IS ORDERED that pursuant to sections 1, 2, 4, 10, 11, 201-205, 215, 218, 220, and 303(r) of the Communications Act of 1934, as amended, 47 U.S.C. §§ 151, 152, 154, 160, 161, 201-205, 215, 218, 220, and 303(r), this REPORT AND ORDER IS ADOPTED.

66. IT IS FURTHER ORDERED that section 64.702(e) of the Commission's Rules, 47 C.F.R. § 64.702(e), as set forth in Appendix B hereto, is effective 30 days after publication in the Federal Register.

67. IT IS FURTHER ORDERED that the Commission's Consumer Information

[181] *See* CIX Comments at 7-8.

[182] 5 U.S.C. § 801(a)(1)(A).

[183] 5 U.S.C. § 605.

Bureau, Reference Information Center, SHALL SEND a copy of this REPORT AND ORDER, including the Final Regulatory Flexibility Certification, to the Chief Counsel for Advocacy of the Small Business Administration.

FEDERAL COMMUNICATIONS COMMISSION

Magalie Roman Salas

Magalie Roman Salas
Secretary

APPENDIX A-LIST OF PARTIES
(CC Docket Nos. 96-61; 98-183)

Parties are listed and referred to by the name under which they submitted their comments:

AT&T Corp. (AT&T)
American Petroleum Institute (API)
America Online, Inc. (AOL)
Ameritech
Bell Atlantic
BellSouth
Cincinnati Bell Telephone Company (CBT)
Commercial Internet eXchange Association (CIX)
Competitive Telecommunications Association (CompTel)
Consumer Electronics Manufacturers Association (CEMA)
Enterprise Networking Technologies Users Association (ENTUA)
GTE Service Corporation (GTE)
Information Technology Association of America (ITAA)
Internet Service Providers' Consortium (ISP/C)
KMC Telecom, Inc. (KMC)
MCI WorldCom, Inc. (MCI WorldCom)
Mitel, Inc. (Mitel)
Network Plus, Inc. (Network Plus)
Next Level Communications (Next Level)
Public Utilities Commission of Ohio (Ohio PUC)
Nationwide Business Telephone Systems, L.L.C. d/b/a Team Centrex (Team Centrex)
Telecommunications Resellers Association (TRA)
U S West Communications, Inc. (U S West)
SBC Communications Inc. (SBC)
Saco River Telegraph and Telephone Company (Saco River)
Sprint Corporation (Sprint)
Tandy Corporation (Tandy)
United States Telephone Association (USTA)

APPENDIX B-FINAL RULES

For the reasons discussed in the preamble, 47 CFR Part 64 is amended as follows:

PART 64 – MISCELLANEOUS RULES RELATING COMMON CARRIERS

1. The authority citation for Part 64 continues to read as follows: 47 U.S.C. 154, 47 U.S.C. 225, 47 U.S.C. 251(e)(1).151, 154, 201, 202, 205, 218-220, 254, 302, 303, and 337 unless otherwise noted. Interpret or apply sections 201, 218, 225, 226, 227, 229, 332, 48 Stat. 1070, as amended. 47U.S.C. 201-204, 208, 225, 226, 227, 229, 332, 501 and 503 unless otherwise noted.

2. Section 64.702 by revising paragraph (e) is amended to read as follows:

* * * * *

(e) Except as otherwise ordered by the Commission, the carrier provision of customer premises equipment used in conjunction with the interstate telecommunications network may be offered in combination with the provision of common carrier communications services, except that the customer premises equipment shall not be offered on a tariffed basis.