Before the
FEDERAL COMMUNICATIONS COMMISSION
Washington, DC 20554

In the Matter of	)	
	)	
AT&T Corp.	)	
	)	RM No. 10593
Petition for Rulemaking to Reform	)	
Regulation of Incumbent Local Exchange	)	
Carrier Rates for Interstate Special	)	
Access Services	)	

OPPOSITION OF QWEST COMMUNICATIONS INTERNATIONAL INC.

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EXECUTIVE SUMMARY

In the *Pricing Flexibility Order*, the Commission established a framework to provide price cap LECs with pricing flexibility for their special access services in areas where competitive triggers have been met. The Commission recognized that such relief would provide significant benefits to special access customers, by allowing price cap LECs to provide offerings tailored to their customers' individual needs.

Now, only two years after the *Pricing Flexibility Order* was unanimously upheld by the Court of Appeals, and after only eight months of experience operating under that *Order* in the Qwest region, AT&T seeks to have that *Order* repealed. In so doing, AT&T aims to prevent Qwest and other price cap LECs from competing with the customer-specific offerings of many competitive LECs, and to restore the same burdensome, regulatory asymmetry against which it fought in the long distance market, notwithstanding a market share of up to 80% or more. AT&T does not stop there, however. It also urges the Commission to roll back the last twelve years of price cap regulation, and once again regulate the price cap LECs' special access services based on their rate of return.

Despite these extraordinary requests, AT&T's petition offers nothing that should make the Commission question the soundness of its decisions in the *Pricing Flexibility Order*. The weakness of AT&T's petition is demonstrated by its substantial reliance on the price cap LECs' regulated rate of return for special access services, in an attempt to demonstrate that the price cap LECs' special access rates are "excessive" and "exorbitant." The rate-of-return computations generated by the federal cost allocation system in Parts 32, 64, 36, and 69 bear no relationship to economic profit, and, as the Commission has recognized, those rules have failed to evolve despite fundamental changes in network technology and service offerings.

In fact, the BOCs' average revenue per line between 1996 and 2001 decreased by more than one percent per year in nominal terms and by more than three percent per year in constant dollars. This is not surprising given the existence of substantial competition in special access markets, both in terms of self-provisioning and competitive supply by third parties. Several independent estimates put the current competitive LEC share of special access revenues -- not including the large extent to which carriers such as AT&T and WorldCom supply their own needs -- at approximately 30 percent.

In short, there is no basis for the Commission to reverse its longstanding approach of relying on market forces to discipline incumbents' pricing, if competitive conditions warrant, as they do in special access markets, particularly where the pricing flexibility triggers have been met. As a result, the Commission must deny AT&T's petition.

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Qwest Communications International Inc. ("Qwest") respectfully submits its Opposition to the petition for rulemaking ("petition") filed by AT&T Corp. ("AT&T"), which seeks repeal of the *Pricing Flexibility Order* and re-regulation of the interstate special access services provided by the price cap local exchange carriers ("LECs" also referred to as "incumbents") on the basis of their regulated rate of return for those services. In short, AT&T fails to justify its request that the Federal Communications Commission ("Commission") discontinue its "market-based approach" to the regulation of access services, and its petition lacks any *new* evidence in this regard that would warrant the initiation of a rulemaking. Consequently, the Commission must deny AT&T's petition.

I. INTRODUCTION

The Commission has long recognized that rate-of-return regulation can produce uneconomic signals to regulated carriers and result in waste and inefficiency. In 1990, the Commission launched a program of price cap regulation that began to separate large incumbent LECs' prices from their regulated costs. The price cap rules were intended to provide a more efficient type of price regulation for services that were not subject to sufficient competition to be deregulated. However, especially following the Telecommunications Act of 1996 (or "1996

Act"), competition in the special access market flourished in many areas. Consequently, the Commission began to consider regulatory alternatives that would rely on competition, rather than prescriptive regulation, to discipline special access pricing.

In 1999, building on this "market-based approach" to access regulation, the Commission adopted the *Pricing Flexibility Order*,[1] which provided price cap LECs an opportunity for increased flexibility in their pricing of special access services, thus allowing them to compete on more equal terms with their competitors. Once competitive triggers are met in a metropolitan statistical area ("MSA"), the price cap LEC serving that MSA is permitted to respond to the demands of special access customers for volume and term discounts and contract offerings.[2] The Commission found that such offerings would benefit special access customers because they "enable incumbent LECs to tailor their services to their customers' individual needs."[3] The Commission also concluded that continuing to prohibit price cap LECs from making such offerings could "reduce the efficiency of the market for access services by reducing the incumbent LECs' ability to meet customers' needs,"[4] and that "existing rules clearly limit[ed] price cap LECs' ability to respond to competition."[5]

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[1] *In the Matter of Access Charge Reform; Price Cap Performance Review for Local Exchange Carriers; Interexchange Carrier Purchases of Switched Access Services Offered by Competitive Local Exchange Carriers; Petition of U S West Communications, Inc. for Forbearance from Regulation as a Dominant Carrier in the Phoenix, Arizona MSA*, *Fifth Report and Order and Further Notice of Proposed Rulemaking*, 14 FCC Rcd. 14221 (1999) ("*Pricing Flexibility Order*" or "*Order*"), *aff'd, WorldCom v. FCC*, 238 F.3d 449 (D.C. Cir. 2001).

[2] Even with pricing flexibility, however, price cap LECs are subject to much more regulation than their special access competitors. For example, in areas subject to Phase I pricing flexibility, the price cap LECs' special access services are still subject to price cap regulation, and, in all areas, the price cap LECs must tariff their special access services.

[3] *Pricing Flexibility Order*, 14 FCC Rcd. at 14291 ¶ 128.

[4] *Id.*

[5] *Id.* at 14273 ¶ 92.

AT&T firmly opposed the adoption of the *Pricing Flexibility Order*. Now, only two years after that *Order* was unanimously upheld by the Court of Appeals, and after only eight months of experience operating under the *Order* in the Qwest region, AT&T seeks to have that *Order* repealed. In so doing, AT&T seeks to prevent the price cap LECs from competing with the customer-specific offerings of many competitive LECs, and to restore the very same burdensome, regulatory asymmetry against which it fought in the long distance market, notwithstanding a market share of up to 80% or more. AT&T does not stop there however. It also urges the Commission to roll back the last twelve years of price cap regulation, and once again regulate the price cap LECs' special access services based on their rate of return.

AT&T's extraordinary request is supported with evidence that is flimsy at best. AT&T asserts that the pricing flexibility regime has been a failure, as demonstrated by what AT&T calls the price cap LECs' "excessive" and "exorbitant" special access rates. AT&T's "analysis" of the special access rates relies almost exclusively on its computation of the price cap LECs' regulated rate of return for special access services, which, for Qwest, AT&T claims is 46 percent. This analysis is fatally flawed for several reasons.

<u>First</u>, the federal cost allocation process specified in Parts 32, 64, 36, and 69 is not capable of generating a meaningful estimation of a price cap LEC's rate of return for special access services.[6] Given the inherent averaging and allocation of common costs among categories of facilities and services in that process, it is highly questionable whether the federal cost allocation process ever provided an accurate estimate of the economic rate of return earned in providing a particular service. In any case, whatever precision once resided in this allocation process has dramatically eroded since the Commission reduced, and then severed, the link

between the price cap LECs' reported costs by access elements and interstate rates. Such disuse and decreasing importance caused the Commission last year to "freeze" many of the factors and relationships at the heart of jurisdictional separations. In doing so, the Commission referred to the separations rules as "outdated regulatory mechanisms that are out of step with today's rapidly-evolving telecommunications marketplace."[7] Over the years, the separations regime has been "largely unmodified,"[8] despite the rise of packet switching, Internet traffic, and many new services that call into question some of the fundamental assumptions in the federal cost allocation system. Since Part 69 directly feeds from the results of Part 36, if Part 36 is outdated, the same is true of Part 69. As a result, the underlying assumptions in Parts 36 and 69 that drive the allocation of costs among services do not reflect the realities of the networks that price cap LECs use today to provide special access and other services, and therefore cannot be used to compute a meaningful total interstate rate of return, let alone a rate of return for special access services.

Second, there are a number of factors in the Commission's rules that lead to an understatement of costs assigned to special access services and thereby an overstatement of special access rates of return. Most notably, the rules assign revenues associated with Digital Subscriber Line ("DSL") services and interstate packet switching services to the special access element, but assign a significant portion of the associated interstate costs to other elements. Taken together, these issues significantly inflate the rate-of-return numbers upon which AT&T places so much reliance.

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6 For simplicity, Qwest refers to the costing rules in Parts 32, 64, 36, and 69 as the "federal cost allocation process."

7 *In the Matter of Jurisdictional Separations and Referral to the Federal-State Joint Board*, *Report and Order*, 16 FCC Rcd. 11382, 11383 ¶ 1 (2001) ("*Separations Freeze Order*").

8 *Id.*

Third, as explained by Drs. Alfred E. Kahn and William E. Taylor ("Kahn and Taylor"),[9] regulatory profits do not measure economic profits and serve no useful purpose in determining whether the allowance of pricing flexibility for special access services has achieved the Commission's objectives outlined in the *Pricing Flexibility Order*. In fact, as anticipated by the Commission, pricing flexibility has led to a more efficient market for these services, as price cap LECs have been able to customize their special access offerings to their customers' individual needs.

Fourth, AT&T has a major timing problem. Even if the rate-of-return data relied on by AT&T were meaningful, which they are not, they would say nothing about the impact of pricing flexibility. In particular, Qwest did not have pricing flexibility during any of the period covered by AT&T's data.[10]

The other evidence relied on by AT&T for revocation of pricing flexibility is equally flawed. As an initial matter, AT&T's arguments are remarkably similar to the points it made before the Commission and the Court of Appeals for the D.C. Circuit challenging the adoption and application of the *Pricing Flexibility Order*. For example, AT&T continues to claim that the collocation triggers adopted by the Commission are "inherently flawed," and that contract tariffs give the price cap LECs the ability to "target" their alleged market power. Needless to say, both the Commission and the D.C. Circuit have already rejected AT&T's arguments. In fact, the

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9 Declaration of Alfred E. Kahn and William E. Taylor On Behalf of BellSouth Corporation, Qwest Corporation, SBC Communications, Inc., and Verizon ("Kahn and Taylor Declaration") at 7. The declaration of Drs. Kahn and Taylor is appended as Attachment A.

10 *Id.* at 4-5. Qwest was granted pricing flexibility on April 24, 2002. *In the Matter of Qwest Petition for Pricing Flexibility for Special Access and Dedicated Transport Services*, *Memorandum Opinion and Order*, 17 FCC Rcd. 7363 (Comm. Carr. Bur. 2002). AT&T provides data on returns and revenues for 1996-2001. Petition at 9.

Commission previously rejected such arguments about the horrors of pricing flexibility in granting AT&T streamlined regulatory treatment for its long distance services in the 1980s.

AT&T's allegations about the absence of price reductions for special access is equally baseless, inconsistent with other allegations, and contradicts its advocacy for deregulation of the long distance market. Specifically, this allegation ignores the reductions implemented by price cap LECs in special access rates via volume and term discounts and contract tariffs. Indeed, elsewhere in its petition, AT&T actually attacks these price reductions. This is exactly the scenario contemplated in the *Pricing Flexibility Order*. The Commission noted that price increases for some customers were a likely outcome of a shift toward market-based regulation of special access services, but that such impacts would be outweighed by the positive benefits that would arise from greater pricing flexibility. Indeed, AT&T's advocacy here is deeply ironic. As a "dominant" interexchange carrier ("IXC"), AT&T fought for and received the flexibility to offer volume and term discounts, "single-customer" offerings and "contract" tariffs, correctly dismissing the arguments of competitors and others -- virtually identical to those now asserted by AT&T here -- alleging the absence of other price reductions, anticompetitive intent or effects, and similar arguments.

AT&T's assertion that it lacks competitive alternatives to the incumbents' special access services is also completely without merit. In those areas where Qwest has received pricing flexibility, AT&T generally has numerous competitive alternatives to Qwest's special access services, most notably its own burgeoning high capacity plant. As pointed out by Drs. Kahn and Taylor, AT&T's analysis ignores its ability to self-provision special services, particularly through its affiliate TCG, one of the largest competitive access providers ("CAP").[11] In addition,

[11] Kahn and Taylor Declaration at 24.

given the point-to-point nature of special access services, a ubiquitous network is not necessary to succeed as a supplier of dedicated circuits. In all events, even if the Commission were to conclude that the price cap LECs retain market power over special access services, this would not undermine the *Pricing Flexibility Order*. The Commission made clear -- both in the *Pricing Flexibility Order* and before the D.C. Circuit -- that, unlike a finding of nondominance, its grant of pricing flexibility did not depend on a conclusion that the price cap LECs lacked market power over special access services. Rather, the Commission found that its findings of irreversible competitive entry were sufficient to justify the more limited relief granted in the *Pricing Flexibility Order*, as compared to a declaration of nondominance.

Finally, there is no basis for AT&T's argument that pricing flexibility somehow allows the incumbent LECs to impede competition in long distance markets, by raising rivals' costs or engaging in a price squeeze. The Commission has repeatedly dismissed the likelihood of such conduct, both in light of regulatory requirements and standard economic theory. There is no justification to depart from those sound holdings in this proceeding.

II. AT&T'S UNQUALIFIED RELIANCE ON ARMIS-GENERATED RATE-OF-RETURN ESTIMATES AS A MEASUREMENT OF THE REASONABLENESS OF SPECIAL ACCESS RATES IS ENTIRELY MISPLACED

Throughout its petition, AT&T claims that Qwest's special access rates are "exorbitant" and "grossly excessive," based solely on the allegation that its reported rates of return for special access services, as computed via the federal cost allocation process, is approximately 46 percent. While such an argument might have some simplistic and superficial appeal, it falls apart when subjected to even the mildest scrutiny. Moreover, as explained in Section III, AT&T's analysis is fundamentally inconsistent with the Commission's approach to regulation of access services over the past 12 years.

A. It Is Not Possible To Compute A Meaningful Rate Of Return For Special Access Services Using Data Generated By The Federal Cost Allocation Process

Given its inherent averaging and allocations of common costs, it is questionable whether the federal cost allocation process was ever capable of providing a reliable estimate of the actual rate of return achieved for a particular interstate service. The adoption of price cap regulation of interstate access services, which does not depend on incumbent LECs' ARMIS cost information, has further undermined the usefulness of Part 69 data for computing rates of return for special access services. Thus, the regulatory rates of return relied on by AT&T bear no relationship to economic profits.[12]

1. The Inherent Averaging and Numerous Allocations in the Federal Cost Allocation Process Preclude Accurate Rate of Return Computations for Individual Services

The Commission's separations and Part 69 processes rely extensively on averaging.[13] For example, instead of separately tracking investment costs associated with copper and fiber cable and wire facilities, the separations process simply adds those costs together and then spreads them equally across all facilities.[14] In reality, the costs of particular types of facilities often vary significantly. The separations rules also include a number of allocation factors for apportioning costs that are not associated with a particular service. As one authority has stated with regard to common costs, "[a]bsent causation data that is usually unavailable, there is no 'correct'

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12 Kahn and Taylor Declaration at 7.

13 *See, e.g.,* 47 C.F.R. § 36.1(d) ("In assigning book costs to categories, the costs used for certain plant classes are average unit costs which equate to all book costs of a particular account or subaccount[.]").

14 *See* 47 C.F.R. § 36.154(a) ("The first step in apportioning the cost of exchange line cable and wire facilities among the operations is the determination of an average cost per working loop. This average cost per working loop is determined by dividing the total cost of exchange line cable and wire Category 1 in the study area by the sum of the working loops[.]").

allocation here -- every allocation is arbitrary to some degree."[15] While the 75/25 subscriber plant factor ("SPF") used to allocate non-traffic sensitive subscriber plant costs between the federal and state jurisdictions is the most familiar, there are many other allocations of common costs that can have a significant impact on the total cost allocated to a particular category of services.[16] In particular, the Commission's rules assign both secondary expenses and investments, such as maintenance costs, and tertiary expenses, such as general support facilities, on the basis of the primary investment assigned to a category. Thus, any inaccuracy in the allocation of primary investment costs, such as described above with regard to cable and wire investment, will be significantly amplified because that allocation also determines the assignment of other investment and expenses. In other words, if too little cable and wire investment expense is assigned to private line, other costs allocated on the basis of this investment, such as maintenance, depreciation, general support facilities, and corporate operations expenses, will also be understated. Since Part 69 utilizes the results of Part 36, any understatement in separations results will likely be reflected in Part 69 as it allocates costs to interstate access elements.

The imprecision of the federal cost allocation process is also illustrated in its use of residuals, whereby the remaining unassigned costs for a particular type of plant, such as cable and wire, are assigned to a particular category.[17] While the use of residual assignment may be

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15 Huber, Kellogg, Thorne, FEDERAL TELECOMMUNICATIONS LAW, 2d Ed., § 2.2.2.5 (1999).

16 *See* Kahn and Taylor Declaration at 8-9 (allocation of costs to special access generally is not based on causation).

17 *See, e.g.,* 36 C.F.R. § 153(b) ("The cost of the remaining wire accounted for as toll is assigned to the appropriate Interexchange Cable & Wire Facilities categories.").

appropriate for regulatory costing rules to make sure that all costs are assigned to one category or another, it would never be used for determining the actual economic cost of a product.

2. Over Time, the Commission's Separations Costing Methodology has Become Much Less Reflective of Reality

Since 1990, the Commission's separations costing process has not been used directly to set interstate rates for price cap LECs. As a result, the separations rules have received much less attention from the Commission and the Joint Board than in the past, with few changes made in the past several years despite dramatic changes in technology (*e.g.*, increased fiber in the network, SONET, new switching technologies) and the rise of the Internet, broadband, and wireless services. As the Commission has noted,

> [t]he current Part 36 separations regime, which has been largely unmodified for the past several decades, was developed when local telephone service was provided largely through circuit-switched networks operated by companies with monopoly power in the local market, with clear delineation between interstate and intrastate services. Since the enactment of the Telecommunications Act of 1996, however, and the growing presence of new, high-bandwidth technologies and services in the local market, including the Internet, the telecommunications landscape has changed significantly, and lines between interstate and intrastate services are increasingly blurred.[18]

Consequently, many of the key assumptions underlying the separations rules often do not reflect the realities of today's networks, so that the costs assigned to a particular category of services similarly do not reflect the costs that are actually incurred in providing those services, which in turn artificially influences the reported special access rates of return relied on by AT&T. In particular, the Commission has found that such changes as the growth of Internet usage and packet switching could cause cost shifts in separations results "because these and other new

[18] *Separations Freeze Order*, 16 FCC Rcd. at 11383 ¶ 1.

technologies, such as digital subscriber line (DSL) services, as well as a competitive local exchange marketplace are not sufficiently contemplated by the Part 36 rules."[19]

Such concerns led the Commission to freeze the factors and relationships used in separations, beginning on July 1, 2001.[20] Thus, with each passing day, the ARMIS data on which AT&T relies becomes less reliable. The Commission adopted the freeze in part as a step toward simplifying the Part 36 separations process, recognizing that applicable law is satisfied as long as the separations process provides a "reasonable allocation" between jurisdictions.[21] As with the Commission's decision in 1982 to freeze the SPF, the Commission has placed a priority on reducing sudden cost shifts from changes in usage of the telephone network, rather than ensuring precision in cost allocations.[22]

B. In Many Respects, The ARMIS Data Tend To Understate Special Access Costs, Thereby Overstating Regulatory Rates Of Return For Special Access Services

Besides the general imprecision of the separations process, the computation of a regulated rate of return for a particular service category can be skewed due to the way in which: (1) costs and revenues are assigned among categories of services; (2) costs and revenues are split between the interstate and state jurisdictions; and (3) costs and revenues are "matched" with respect to categories of services and jurisdictions. As noted, even a relatively small inaccuracy in the assignment of "primary investment" costs, such as cable and wire, among service

[19] *Id.* at 11389-90 ¶ 12.

[20] In doing so, the Commission followed the recommendation of the Joint Board that the Commission institute a five-year freeze of all Part 36 category relationships and allocation factors for price cap carriers, and a freeze of the allocation factors for rate-of-return carriers. *In the Matter of Jurisdictional Separations Reform and Referral to the Federal-State Joint Board, Recommended Decision*, 15 FCC Rcd. 13160, 13161-62 ¶ 2 (2000).

[21] *Separations Freeze Order*, 16 FCC Rcd. at 11393 ¶ 17 (citing *Smith v. Illinois Bell Tel. Co.*, 282 U.S. 133 (1930)).

[22] *Id.* at 11391 ¶ 15.

categories can have a dramatic impact on the total costs assigned to a service category, because other investment and expense costs are assigned on the basis of the investment allocations.

Given the complexity of the separations process, there are many different factors that could cause the rate-of-return estimates relied on by AT&T to be overstated. Among others, the treatment of DSL and other packet-based services, and packet switching itself, could significantly and artificially inflate the regulated rate of return for special access services.

DSL. The Commission's current rules assign DSL revenues to the interstate special access basket, while much of the cost of providing DSL services are assigned to the common line basket,[23] resulting in a revenue-cost mismatch that is a significant component of the rates of return computed by AT&T.

Packet Switching. The Commission's rules include the costs of packet switching in the general switching category, none of which is assigned to special access services,[24] despite the fact that packet switching is used to provide frame relay, ATM and other services. This is yet another example of the way in which the rate-of-return computations relied on so heavily by AT&T fail to comport with reality.

When combined, the underassignment of just these types of costs to special access services has a substantial impact on the computation of the regulated rate of return for special access services, and by themselves render the numbers relied on by AT&T virtually meaningless.

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23 *See In the Matter of GTE Telephone Operating Cos., GTOC Tariff No. 1, GTOC Transmittal No. 1148*, *Memorandum Opinion and Order*, 13 FCC Rcd. 22466 (1998).

24 Since packet switching costs are included in the Account 2210 Central Office Switching Investment, Part 36 only allows those costs to be categorized between Tandem Switching (Category 2) and Local Switching (Category 3). There is no means in the rules to assign this investment to any other category. As a result, Part 69 allocates the interstate amount of Tandem Switching (Category 2) to the transport element and Local Switching (Category 3) to the local switching element.

For all these reasons, the Commission should give no weight to the regulated rate-of-return computations presented by AT&T.

III. RELYING ON ARGUMENTS THAT HAVE ALREADY BEEN REJECTED BY THE COMMISSION, AT&T PROPOSES TO ROLL BACK REGULATION A DOZEN YEARS FOR ONE OF THE MOST COMPETITIVE TELECOMMUNICATIONS MARKETS

In the *Pricing Flexibility Order*, the Commission adopted a framework for pricing flexibility for special access services provided by price cap LECs, based on a set of easily-verifiable triggers. Such pricing flexibility gives price cap LECs the opportunity to provide some of the same types of service offerings as their competitors, such as volume and price discounts and contract tariff offerings specifically-tailored to their customers' needs.

In allowing for pricing flexibility, the Commission recognized that, in areas where the Phase I collocation triggers are met, competitors "have made irreversible investments in the facilities needed to provide the services at issue, thus discouraging incumbent LECs from successfully pursuing exclusionary strategies."[25] While Phase I relief permits LECs to offer contract tariffs and volume and term discounts, it requires them "to maintain their generally available price cap-constrained tariffed rates, thus protecting those customers that lack competitive alternatives."[26] Before obtaining Phase II pricing flexibility, the incumbent "must demonstrate [via the Phase II triggers] that competitors have established a significant market presence in the provision of the services at issue."[27] The Commission found that, "[u]nder those

25 *Pricing Flexibility Order*, 14 FCC Rcd. at 14258 ¶ 69.

26 *Id.*

27 *Id.*

market conditions, the availability of alternative providers will ensure that rates are just and reasonable."[28]

The grant of pricing flexibility for special access services was just one step in the Commission's move from rate-of-return to incentive-based regulation. "Beginning in 1990, the FCC has taken several steps to encourage innovation, cost-reduction, and greater efficiency by reducing regulatory strictures in favor of market discipline."[29] Thus, before the D.C. Circuit, the Commission contended that the *Pricing Flexibility Order* "should not be viewed in isolation, but rather as an additional step along the road of greater deregulation and pricing flexibility in the interstate access market."[30] In fact, the Commission's adoption of pricing flexibility for special access services also mirrored its regulation of AT&T's interexchange services as the long distance market became increasingly competitive, but before AT&T was declared nondominant.[31] Despite these trends, AT&T urges the Commission not only to repeal the *Pricing Flexibility Order*, but also to roll back price regulation to the 1980s, when prices were set according to rate of return.[32] Thus, AT&T simply ignores the tremendous growth in competition in the intervening years, particularly following the passage of the

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[28] *Id.* In fact, these triggers underestimate the amount of sunk competitive investment in each wire center because they focus on collocation and ignore investment and competition that makes no use of the BOCs' facilities. Kahn and Taylor Declaration at 5.

[29] *WorldCom v. FCC*, 238 F.3d at 460.

[30] *Id.*

[31] *See In the Matter of Motion of AT&T Corp. to be Reclassified as a Non-Dominant Carrier*, *Order*, 11 FCC Rcd. 3271, 3278-79 ¶ 9 (1995) ("*AT&T Reclassification Order*").

[32] Petition at 39. Oddly, AT&T proposes that the Commission reduce special access rates *in Phase II pricing flexibility areas* to rates that would produce an 11.25% rate of return. Thus, AT&T would have the Commission impose the most onerous price regulation in those areas that are most competitive, according to the tests the Commission adopted in the *Pricing Flexibility Order*.

Telecommunications Act of 1996, as well as the Commission's steady move away from regulating access prices by traditional rate of return.

Given the radical nature of AT&T's request, one would expect AT&T to provide a bevy of compelling evidence to justify its requested relief. To the contrary, however, AT&T provides nothing new in this regard. In addition to the fatally-flawed rate-of-return data discussed above, AT&T merely repeats a series of unsound and irrelevant arguments that, for the most part, have already been rejected by the Commission and the D.C. Circuit.[33]

A. Since 1990, The Commission Has Moved Away From The Type Of Rate Regulation Sought By AT&T, Particularly For Services Such As Special Access That Are Subject To Significant Competition

In its petition, AT&T argues that the Commission should reduce special access rates in Phase II areas to a level that would produce an 11.25% rate of return, as measured under existing separations and cost allocation rules.[34] Such a regulatory result would be remarkably similar to the price regulation that existed prior to the Commission's introduction of price cap regulation in 1990. Prior to that time, prices for special access and other interstate services generally were set

33 AT&T's petition also appears to be inconsistent with the CALLS agreement to which it was a party. Although AT&T contends that the CALLS agreement does not bar the requested relief, because section 4.2 of the agreement purportedly applies only to switched access rates, it ignores sections 3.2.7 and 3.2.8. *See* Letter from John T. Nakahata, Counsel for CALLS, to Magalie Roman Salas, FCC, CC Docket Nos. 94-1, 96-45, 99-249, 96-262 (Mar. 8, 2000) (attaching Modified Universal Service and Access Reform Proposal). Section 3.2.7 states that the X-factor applied to special access services will be 6.5% in 2002 and 2003, and zero thereafter. Despite this agreement, AT&T now requests that the Commission "reinitialize" price caps. The petition also appears contrary to section 3.2.8 of the modified agreement, which states that incumbent LECs would no longer be required to file cost studies for special access services, which would have otherwise been required by the *Access Reform First Report and Order*. Although AT&T does not formally demand that the price cap LECs file cost studies, the proposal to "reinitialize" price caps for special access services would basically lead to that result.

34 Petition at 39. AT&T also requests the Commission to override any contractual obligations that would prevent AT&T and other special access customers from taking advantage of this regulatory windfall. *Id.* at 40.

through a "cost-plus" system of regulation, by which the rates incumbents could charge for services were based on costs plus a return on invested capital.[35]

In the *LEC Price Cap Order*, the Commission replaced cost-plus regulation with an incentive-based system of regulation similar to that used to regulate AT&T at the time.[36] The goal of the price cap system was "to harness the profit-making incentives common to all businesses to produce a set of outcomes that advance the public interest goals of just, reasonable, and nondiscriminatory rates, as well as a communications system that offers innovative, high quality services."[37] LECs that could outperform the productivity factor embedded in the price cap mechanism would be rewarded with the ability to retain higher earnings than would be available under rate-of-return regulation.[38] Initially, the Commission limited the overall interstate return that an incumbent could earn under the price cap system, by returning to subscribers earnings over a certain threshold, in order to provide for the possibility that the initial price cap productivity factor had not been set correctly.[39] In 1995, however, the Commission took actions to eliminate sharing obligations, finding that "sharing severely blunts the efficiency incentives of price cap regulation by reducing the rewards of LEC efforts and decisions."[40] Such

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35 *In the Matter of Policy and Rules Concerning Rates for Dominant Carriers*, *Second Report and Order*, 5 FCC Rcd. 6786, 6787 ¶ 1 (1990) ("*LEC Price Cap Order*"). However, even before that time, LECs were granted limited pricing flexibility in the form of optional volume discounts for private line and special access services. *See* Kahn and Taylor Declaration at 4.

36 *LEC Price Cap Order*, 5 FCC Rcd. at 6787 ¶ 1.

37 *Id.* at 6787 ¶ 2. It was also anticipated that adoption of the price cap system would give incumbents "the incentive to provide more services, to the benefit of ratepayers." *Id.* at 6791 ¶ 35.

38 *Id.* at 6787 ¶ 2.

39 *Id.* at 6787 ¶ 3.

40 *See In the Matter of Price Cap Performance Review for Local Exchange Carriers; Access Charge Reform*, *Fourth Report and Order in CC Docket No. 94-1 and Second Report and*

reduced incentives could be expected "to generate lower LEC efficiency, which in turn would reduce the benefits of price caps to consumer[s]."[41]

As competition continued to develop, the *Pricing Flexibility Order* established a framework for granting price cap LECs further pricing flexibility for special access services. The Commission concluded that although the price cap regime gave LECs some pricing flexibility and incentives to operate efficiently, significant regulatory constraints remained, and that "[a]s the market becomes more competitive, such constraints become counter-productive."[42]

AT&T's petition fundamentally conflicts with the Commission's policymaking in this area since 1990. Adopting AT&T's proposal to "re-initialize" price caps, which is simply a euphemism for return to rate-of-return regulation, would nullify more than a decade of the Commission's efforts to reform regulation of interstate telecommunications. It would also distinctly contradict the purpose of this reform, because it would severely reduce the incentive for a price cap LEC to innovate and become more efficient. Given the current competitive state of the market, such action cannot be justified in the absence of an overwhelming record. To the contrary, as shown in the next section, the competitive marketplace envisioned by the Commission has continued to grow and flourish.

Order in CC Docket No. 96-262, 12 FCC Rcd. 16642, 16700 ¶ 148 (1997), referring to the Commission's *LEC Price Cap Performance Review*, 10 FCC Rcd. 8961, 9045 ¶ 187 (1995).

[41] *Id.* Initially, the LEC price cap system also included a low-end adjustment mechanism, which permitted LECs earning rates of return less than 10.25 percent in a given year to increase their price cap indices to a level that would enable them to earn 10.25 percent. However, in the *Pricing Flexibility Order*, the Commission eliminated the low-end adjustment mechanism for price cap LECs that qualify for and elect to exercise either Phase I or Phase II pricing flexibility. *Pricing Flexibility Order*, 14 FCC Rcd. at 14304 ¶ 162. The Commission noted that the low-end adjustment mechanism guaranteed only a 10.25 percent rate of return, and "*price cap LECs should be able to achieve much greater profits by trying to increase their productivity growth.*" *Id.* at 14304-05 ¶ 163 n.409 (emphasis supplied).

[42] *Id.* at 14233 ¶ 19.

B. As The Commission Has Found, The Special Access Market Is Subject To Significant Competition In Areas Meeting The Pricing Flexibility Triggers, And Pricing Flexibility Relief Is Pro-Competitive

In the *Pricing Flexibility Order*, the Commission concluded that, where the Phase I or II triggers have been satisfied, there are viable competitive alternatives to the incumbents' special access services, given the sunk investment made by competitors in those areas.[43] As a result, the Commission found that additional pricing flexibility for those services was warranted. Thus, the Commission has already considered and rejected AT&T's claim that there are no competitive alternatives to the incumbents' special access services, as well as AT&T's concerns that pricing flexibility should be withheld because it would allow incumbents to engage in exclusionary pricing behavior and undermine competition in long distance markets. Other than its dubious rate-of-return claims, AT&T has presented no evidence that should cause the Commission to reconsider its decisions in the *Pricing Flexibility Order*.

1. Contrary to AT&T's Suggestions, There Are Substantial Alternatives to the Incumbents' Special Access Services

AT&T makes the counterintuitive argument that the incumbents' "excessive" and "exorbitant" special access rates, rather than incenting competitive entry, somehow impede the ability of competitive LECs to self-deploy alternative transmission facilities. Similarly, AT&T claims that IXCs and competitive LECs have no choice but to purchase special access from the incumbents. These arguments are baseless.

As an initial matter, AT&T's arguments in this regard suffer from the same nexus problem that plagues its rate-of-return data. AT&T fails to explain how its ability to obtain alternatives to the incumbents' special access services has been adversely affected by the grant of pricing flexibility. Instead, AT&T simply reiterates the same qualitative arguments about the difficulties of purchasing and supplying alternative dedicated transmission and channel termination services that it has thoroughly discussed in other proceedings.[44] This fact alone should cause the Commission to reject these arguments as a basis to initiate a rulemaking to consider repealing the *Pricing Flexibility Order*.

It should also be noted that AT&T's petition relies to a large extent on its comments and affidavits submitted in the *Triennial Review*, even though that proceeding is focused on unbundled network elements, rather than special access. AT&T's advocacy in both dockets suggests that it is seeking to avoid responsibility for building its own facilities, and would prefer to rely on the incumbents' networks.[45] AT&T's arguments about the availability of enhanced extended links ("EELs") are irrelevant to the question of whether pricing flexibility should be retained for special access services. In any case, as both the Commission and the D.C. Circuit have suggested, EELs are not intended for carriers solely providing interexchange services.[46]

With regard to self-provisioning, AT&T claims that it would be uneconomic for AT&T to self-supply special access facilities. As discussed by Drs. Kahn and Taylor, however, there is a long history of deployment of competitive special access facilities that pre-dates the 1996 Act. In fact, the business plans of CAPs were premised on their ability to provide alternative

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[43] *Id.* at 14263 ¶ 79.

[44] Kahn and Taylor Declaration at 27-28.

[45] *See id.* at 24 (explaining that the result of requests "might well be more entry, but it would surely be *less* facilities-based and more based on use of RBOC circuits and services.").

[46] *In the Matter of Implementation of the Local Competition Provisions of the Telecommunications Act of 1996*, *Supplemental Order Clarification*, 15 FCC Rcd. 9587, 9594-95 ¶ 14 (2000), *aff'd*, *Competitive Telecoms. Ass'n v. FCC*, 309 F.3d 8 (2002) ("*CompTel*"); *CompTel*, 309 F.3d at 13-14. Qwest has proposed alternatives to the current use and commingling restrictions to ensure that they are available to carriers wishing to use EELs to provide local services. *See* Letter from Cronan O'Connell, Qwest, to Marlene H. Dortch, FCC, CC Docket Nos. 01-338, 96-98, 98-147 (Nov. 14, 2002).

transmission facilities to IXCs and large corporate customers.[47] As the Commission has found, particularly where the pricing flexibility triggers have been met, there are significant competitive alternatives to the incumbents' special access services. Moreover, the three largest IXCs still dominate the market for large business customers, which is the most significant retail market that uses special access as an input. As noted by Drs. Kahn and Taylor, "[that] fact demonstrates that IXCs can successfully compete in one of the most competitive retail markets relying on some combination of their own special access facilities and those of the other competitive suppliers and the RBOCs."[48]

The growth of competitive special access is not surprising given that such buildout can be incremental as the carrier acquires wholesale or retail customers. "[S]pecial access dedicated transport and channel terminations are point-to-point, not switched services, and a ubiquitous network is not necessary to participate successfully as a competitive supplier."[49] Moreover scale economies are less important for special access than local exchange services, because special access services do not use switches and individual customer locations provide a high volume of usage. Finally, AT&T's claim that marketing expense is greater for new entrants misses the point, because special access services are largely sold to IXCs, not to retail end users, and in any case, AT&T and WorldCom have long established brands and name recognition, particularly in the market segments for which special access is purchased.[50]

47 Kahn and Taylor Declaration at 21-22.

48 *Id.* at 4.

49 *Id.* at 25.

50 *See id.* at 26.

2. Pricing Flexibility Relief Is Pro-Competitive and Beneficial to Special Access Customers

Ignoring the Commission's specific findings in the *Pricing Flexibility Order*, AT&T asserts that the relief granted in that *Order* is anticompetitive. In the *Pricing Flexibility Order*, the Commission found that allowing price cap LECs to provide volume and term discounts and contract tariffs, where the collocation triggers have been satisfied, would "enable incumbent LECs to tailor services to their customers' individual needs."[51] The Commission acknowledged the theoretical possibility that pricing flexibility could be used for exclusionary pricing, but found that the risk of such behavior was outweighed by the benefits of pricing flexibility in those areas where competitors had made irreversible investments in facilities.[52]

As a major customer of special access services, AT&T presumably benefits from such flexibility.[53] Through volume and term discounts and contract tariffs, AT&T and other large customers are able to obtain advantageous service offerings that the price cap LEC could not offer prior to obtaining pricing flexibility.[54] Nevertheless, and contrary to its complaints about the incumbents' special access services being priced *too high*, AT&T asserts that giving incumbents the ability to cut prices to their largest customers is not in the public interest. In taking this position, AT&T seems to be arguing as a competitor of Qwest's special access services, not, as in most of its petition, an involuntary user of Qwest's services.

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[51] *Pricing Flexibility Order*, 14 FCC Rcd. at 14291 ¶ 128.

[52] *Id.* at 14263-64 ¶¶ 79-80. As noted in Section III.C *infra*, the Commission, as well as the D.C. Circuit, has already considered and rejected AT&T's argument that the collocation triggers adopted by the Commission fail to measure the extent to which competitors have made sunk investment in facilities used to compete with the incumbent.

[53] In fact, AT&T's ostensible efforts to have this Commission increase the very special access rates it proclaims are excessive casts serious doubt on the *bona fides* of its petition.

[54] Qwest has received a large amount of interest in such arrangements from its largest special access customers.

As explained by Drs. Kahn and Taylor, however, "regulators should always look upon proposals to restrict price reductions with a jaundiced eye[, because] they are the essence of the competitive process."[55] While there is no question that it would be easier for individual competitors to succeed in the market if incumbents were hobbled in their ability to offer volume and term discounts and other tailored service offerings demanded by large customers, such handicapping would fail to promote meaningful competition in any market. "[O]ne of the most fundamental distinctions in economics generally, and antitrust law specifically, is between the inflicting of harm on competitors, with a resulting net increase in consumer welfare, from weakening or impairment of the competitive process, resulting in an ultimate or net decrease in consumer welfare."[56] Applying that standard here, it is clear that restricting the incumbents' ability to offer optional discount plans would harm consumers by reducing the vigor of the special access market.[57]

AT&T's confusion on this point is particularly evident, as it claims that "the existing pricing flexibility rules permit the Bells to price discriminate in order to prevent entry or drive competitors out of the market and to use long term contracts to deny competitors access to the traffic necessary to justify facilities deployment."[58] AT&T ignores the fact that such price differentiation and long-term commitments are standard practice in the telecommunications

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[55] Kahn and Taylor Declaration at 29.

[56] *Id.* at 30.

[57] *See Pricing Flexibility Order*, 14 FCC Rcd. at 14291 ¶ 128 (continuing to prohibit such behavior could "reduce the efficiency of the market for access services by reducing the incumbent LECs' ability to meet customers' needs.").

[58] Petition at 18.

industry, and widely used by AT&T itself.[59] In fact, even when AT&T was still regulated as a dominant IXC, it received the authority to use the same types of offerings to obtain and maintain customers.[60] As a result, and consistent with the Commission's reasoning in the *Pricing Flexibility Order*, [61] precluding the incumbents from offering such pricing plans would place them at a significant competitive disadvantage in the special access market.[62]

Furthermore, AT&T's complaints about the incumbents' discount plans overlook the fact that these plans are optional. Qwest offers month-to-month and term plans for all of its special access services. With term plans, special access customers can receive rate reductions of up to 30 percent. In exchange, Qwest requires guarantees that the services will remain in place for a period of time, as is standard in the industry. Qwest also offers a Regional Commitment Plan, which is very popular with IXCs, whereby special access customers can buy DS1 and DS3 services on a month-to-month basis, at a 20 percent discount, as long as they maintain an overall volume of circuits across Qwest's region. Thus, there is no penalty for termination of an individual special access circuit, as long as the customer maintains the overall commitment.[63]

AT&T's assertion that it has no bargaining power relative to the incumbents regarding the terms of such plans conflicts with the Commission's findings in the *Pricing Flexibility*

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[59] Kahn and Taylor Declaration at 30 (penalties in long-term contracts are "an inherent part of the bargain" and "without such penalties, the plans could not be offered and the increase in consumer welfare, both direct and indirect, would be lost.").

[60] *In the Matter of Competition in the Interstate Interexchange Marketplace*, *Report and Order*, 6 FCC Rcd. 5880, 5897 ¶ 91 (1991).

[61] *See Pricing Flexibility Order*, 14 FCC Rcd. at 14291 ¶ 128.

[62] Kahn and Taylor Declaration at 32 ("Long-term contracts are used to minimize risk exposure and stabilize production requirements and costs over time.").

[63] Qwest has no knowledge of the basis for AT&T's allegation that "Qwest's plans require AT&T to pay 125% of the remaining value of the [optional pricing plan] OPP for circuits that are converted to UNEs." Petition at 22 n.36.

Order: "[T]he customers for the[se] services . . . are IXCs and large businesses, not residential or small business end users. These large and sophisticated customers generate significant revenues for the incumbent and are not without bargaining power with respect to the incumbent."[64] In Qwest's experience, the largest IXCs often use the threat of self-provisioning to obtain more favorable terms from Qwest. In any case, AT&T admits that such plans provide it more savings than would otherwise be available, so that the availability of the discount plans clearly makes AT&T better off, regardless of whether it chooses to take advantage of those plans.[65]

Finally, AT&T's suggestion that long term contracts allow the incumbents to "lock up" the largest special access customers has no relevance to the appropriateness of pricing flexibility. By definition, long-term contracts require a term commitment by both parties, and non-incumbents are just as capable of maintaining their customers in this way as are incumbents. This is especially the case in the special access market, where the largest customers are the largest IXCs and competitive LECs, namely AT&T and WorldCom, which possess extensive special access networks of their own.[66]

Of course, the Commission was aware of these considerations when it allowed price cap LECs to obtain increased flexibility in their pricing of special access services, subject of course to general nondiscrimination requirements.[67] Once again, AT&T fails to present anything new in this regard, and does not even allege that the price cap LECs have actually used their pricing flexibility to gain an anticompetitive advantage.

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64 *Pricing Flexibility Order*, 14 FCC Rcd. at 14297 ¶ 142.

65 Petition at 22.

66 Kahn and Taylor Declaration at 33.

67 *See Pricing Flexibility Order*, 14 FCC Rcd. at 14291 ¶ 128.

3. Pricing Flexibility Does Not Have an Anticompetitive Impact on the Long Distance Market

As it has many times in the past, AT&T asserts that setting access charges above incremental cost has anticompetitive effects in the long distance market, by enabling incumbents to raise their rivals' costs and engage in a price squeeze. However, the Commission has previously recognized the flaws in AT&T's theoretical reasoning. The pricing of special access services above incremental costs is not anticompetitive because the BOC long distance affiliates buy special access out of the same tariffs as AT&T, as provided by Section 272(e)(3) of the Act. Section 272(e)(3) also requires BOCs to impute those access charges into their long distance prices, so that all long distance competitors effectively pay the same price for the same access services.[68] So an increase in access prices cannot create a differential advantage for a BOC's long distance service, or impose an anticompetitive price squeeze on an unaffiliated IXC.[69] Given opportunity costs, such is the case even if the cost the BOC incurs to provide access to itself is less than the cost its rivals incur when they buy access services from the BOC.[70]

AT&T also once again fails to tie the potential harms it alleges to the Commission's grant of pricing flexibility. In fact, the Commission adopted certain safeguards to prevent an incumbent from using pricing flexibility to discriminate in favor of its long distance affiliate. In particular, the Commission prohibited price cap LECs from entering into contract tariffs with an

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68 47 U.S.C. § 272(e)(3). *See In the Matter of Accounting Safeguards Under the Telecommunications Act of 1996*, *Report and Order*, 11 FCC Rcd. 17539, 17577 ¶ 87 (1996); *In the Matter of Implementation of the Non-Accounting Safeguards of Sections 271 and 272 of the Communications Act of 1934, as amended*, *First Report and Order and Further Notice of Proposed Rulemaking*, 11 FCC Rcd. 21905, 22028-30 ¶¶ 256-58 (1996) (implementing section 272(e)(3)); Kahn and Taylor Declaration at 34, n.44.

69 Kahn and Taylor Declaration at 34.

70 *Id.*

affiliate unless and until an unaffiliated customer first purchases service pursuant to that contract.[71]

4. The Incumbents' Pricing of Month-to-Month Special Access Services Does Not Represent an Exercise of Market Power

The fact that price cap carriers have maintained or, in some cases, increased prices for certain special access services offered on a month-to-month basis in Phase II pricing flexibility areas does not represent the exercise of market power, as AT&T suggests. In the *Pricing Flexibility Order*, the Commission acknowledged that the removal of price caps "may enable incumbent LECs to increase access rates for some customers."[72] In a competitive market, it is rare that all customers pay the same price for goods and services. Nevertheless, the Commission concluded that such pricing flexibility was appropriate because some access rate increases may be warranted, and that, in those areas satisfying the Phase II triggers, "the public interest is better served by permitting market forces to govern the rates for the access services at this point."[73] In addition, the Commission noted that these services are generally purchased by IXCs, not individual end users. "IXCs are sophisticated purchasers of telecommunications services, fully capable of finding competitive alternatives where they exist and determining which competitor can best meet their needs."[74] Any increases in special access prices are also consistent with general trends in the telecommunications industry, particularly in more competitive markets. During the boom in telecommunications, oversupply led carriers to cut prices below sustainable

71 *Pricing Flexibility Order*, 14 FCC Rcd. at 14292 ¶ 129.

72 *Id.* at 14301 ¶ 155.

73 *Id.*

74 *Id.*

levels; the telecom shakeout has now enabled carriers to restore prices to realistic market levels.[75] As if to document this point, WorldCom just announced that it is significantly increasing its retail rates for some long distance customers.[76]

The fact that demand for special access services has grown, despite the general lack of price decreases on special access services purchased on a monthly basis, also is not an indication of market power. As an initial matter, many special access customers choose to purchase special access services through a term contract, so that their purchase rate would not be affected by an increase in the month-to-month rate. In addition, as pointed out by Drs. Kahn and Taylor, the ARMIS data on which AT&T relies shows a rapid and accelerating growth of BOC special access lines, which is consistent with the conventional wisdom that demand for data services recently has been growing at a much faster rate than for wireline voice services. In fact, the BOCs' average revenue per line between 1996 and 2001 decreased by more than one percent per year in nominal terms and by more than three percent per year in constant dollars.[77] AT&T also ignores the significant growth in demand for DSL service, which has also contributed to increases in special access revenues. Thus, the growth in special access revenues cited by AT&T is largely, if not completely, attributable to an increase in special access lines and does not constitute an exercise of market power.[78]

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75 Communications Daily (Oct. 22, 2002) (quoting Sprint CEO William Esrey as not surprised with some increases in telecommunications rates because prices had fallen to the point where they were "destructive to the industry").

76 WorldCom's MCI Raises Prices to Counter Revenue Drop, WSJ Says, Bloomberg News (Nov. 22, 2002) (reporting increase in some prices of 80 percent). *See also* AT&T's Cable Rates Rising 7.8% on Average; Comcast Merger Not a Factor Company Says (Nov. 23, 2002).

77 Kahn and Taylor Declaration at 12-15.

78 *Id.* at 14-15.

5. Pricing Flexibility Has Not Caused a Degradation in the Service Quality of the Incumbents' Special Access Services

AT&T also mistakenly asserts that the BOCs' performance in provisioning special access services confirms the BOCs' continuing market power. AT&T does not even attempt to explain how this issue relates to the Commission's grant of pricing flexibility. In any case, the ARMIS data, measured per access line or per provisioning order, tells a very different story. On average, trouble reports per access line have fallen throughout the 1996-2001 period, and the percentage of installation order commitments met has been high and increasing throughout the period.[79]

Thus, the facts show that there are substantial competitive alternatives to the incumbents' special access services, and that the Commission's actions in the *Pricing Flexibility Order* have actually improved the operation of the special access market, by allowing price cap LECs to offer special access services tailored to their customers' individual needs. AT&T has also failed to provide any new evidence or arguments suggesting that pricing flexibility has had a negative impact on the long distance market or service quality in the special access market.

C. The Commission Has Already Considered, And Rejected, The Arguments Raised By AT&T

As discussed in detail above, AT&T's petition must be denied because its arguments lack merit. The Commission should also dismiss AT&T's petition because it clearly is an attempt to relitigate issues resolved in the *Pricing Flexibility Order* and upheld by the D.C. Circuit. In this regard, AT&T's petition is at best a distraction from the Commission's legitimate priorities. While AT&T attempts to dress-up its petition with references to the incumbents' "excessive" and "exorbitant" rates of return, as explained above, such arguments have no foundation, and, because of a timing mismatch, say nothing about the impact of pricing flexibility.

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[79] *Id.* at 16-17.

At bottom, AT&T still dislikes the Commission's decision in the *Pricing Flexibility Order*, notwithstanding its unsuccessful court challenge to that *Order*. It continues to assert that the pricing flexibility triggers adopted by the Commission are erroneous,[80] even though both the Commission and the court considered AT&T's arguments and soundly rejected them. The Commission concluded that proposals to require a full-blown market-power analysis before granting pricing flexibility were unworkable,[81] as well as unnecessary given that the *Pricing Flexibility Order* provided the price cap LECs with significantly less relief than would a finding of nondominance. The Commission concluded that "a collocation-based trigger provides an administratively simple and readily verifiable mechanism for determining whether competitive conditions warrant the grant of pricing flexibility."[82] AT&T also dislikes price cap regulation, despite the fact that price caps have been in place for more than a decade. AT&T's petition offers no basis for the Commission to question the correctness of these actions.

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80 Petition at 20.

81 *Pricing Flexibility Order*, 14 FCC Rcd. at 14271-72 ¶ 90. *See also WorldCom v. FCC*, 238 F.3d at 459 ("Petitioners, for their part, offer no alternative save a painstaking analysis of market conditions such as that which is required when an LEC seeks classification as a non-dominant carrier or the forbearance of dominant carrier regulation under Section 10 of the Communications Act.").

82 *Pricing Flexibility Order*, 14 FCC Rcd. at 14267 ¶ 84.

IV. CONCLUSION

For the reasons discussed above, the Commission should reject AT&T's petition for rulemaking. There is no merit to AT&T's attacks on the *Pricing Flexibility Order*, and the rate-of-return-based regulation sought by AT&T would effectively reverse the Commission's move toward incentive-based regulation of special access services over the past dozen years.

Respectfully submitted,

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