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Before the
FEDERAL COMMUNICATIONS COMMISSION
Washington, DC 20554

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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	)	

COMMENTS OF LDMI TELECOMMUNICATIONS, INC.

LDMI TELECOMMUNICATIONS, INC.

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SUMMARY

LDMI is an Integrated Communications Provider, *i.e.*, it offers consumers solutions to all of their voice and data telecommunications needs without regard to historic regulatory-created labels. It supports AT&T's petition and urges the Commission to initiate a rulemaking proceeding for the purpose of establishing appropriate rules to ensure that incumbent local exchange carrier special access rates are just and reasonable and are not unreasonably discriminatory. The unintended consequences of the Commission's 1999 deregulation of ILEC special access rates combined with Commission rules which make loop/transport combinations (commonly known as Enhanced Extended Loops or EELs) as unbundled network elements priced at TELRIC rates unavailable to many competing providers have enabled the ILECs to create a price squeeze. This price squeeze is caused by the interplay of 1) favorable pricing of loop/transport to preferred customers; 2) limitations on EELs which render them unavailable to many ICPs; and 3) unregulated special access pricing which yields "creamy returns" sometimes in excess of fifty percent to ILECs.

The predictions which underlied the Commission's 1999 decision to deregulate special access pricing have not been borne out. The Commission has an obligation to revisit that decision in light of current circumstances and to adjust its rules for regulation of ILEC special access as needed to ensure lawful rates. Pending completion of the rulemaking process, LDMI urges the Commission to take interim action to stop the rapid and uncontrolled escalation of ILEC special access prices. While there may be other interim steps which could be taken, LDMI agrees that an interim prescription based on an 11.25 percent rate of return has merit and should be considered for adoption.

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COMMENTS OF LDMI TELECOMMUNICATIONS. INC.

LDMI Telecommunications, Inc. ("LDMI"), by its attorneys, hereby submits its comments in support of the above-captioned petition filed October 15, 2002 by AT&T Corp. ("AT&T),[1] and states as follows:

INTRODUCTION

LDMI is a competitive provider of telecommunications services headquartered at Hamtramck, Michigan. Although established initially in the early 1990s as a provider of interexchange services, LDMI has evolved into a full service telecommunications provider offering customers competitive local exchange voice and data services as well as long distance services. Indeed, LDMI is an Integrated Communications Provider (ICP). That is. it offers to consumers of all sizes – business and residential – solutions to their

[1] By Public Notice issued October 29, 2002, the Commission invited comments on AT&T's petition. See Public Notice – Wireline Competition Bureau Seeks Comment on AT&T's Petition for Rulemaking to Reform Regulation of Incumbent Local Exchange Carrier Rates for Interstate Special Access Services, DA 02-2913.

telecommunications requirements without regard to the market segmentation definitions such as local exchange, intraLATA, interLATA, exchange access, voice, data, intrastate and interstate -- which have their genesis in an earlier era and which are based on regulator-created scrvicc boundaries which the 1996 Telecommunications Act was enacted to eliminate.

Like virtually all ICPs, including those still branded with the labels "CLECs" or "IXCs", LDMT is dependent on access to essential facilities and services provided by incumbent local cschange carriers (ILECs), including the largest of the ILECs -- the Bell Operating Companies (BOCs). With the largest portion of its customer base located in Michigan, its headquarters state, LDMI is especially dependent on SBC Corporation's Ameritech Michigan affiliate for such services and facilities.

LDMI and other competitive ICPs do not enjoy the benefit of owning ubiquitous networks extending to each customer's premises built over many decades with monopoly ratepayer-funded dollars. For that reason, LDMI, like other competitive providers, must utilize such connections of tlie incumbent companies. Under the current regulatory environment established by the Commission, when those connections and transport facilities are used to provide what are perceived to be "local" service, they are called Enhanced Extended Links, are provided as Unbundled Network Elements subject to Section 251(c)(3) of the Communications Act of 1934, as amended,' and are priced based on the Total Element Long Run Incremental Cost (TELRIC) methodology promulgated by the Commission arid implemented by tlie state commissions (including the Michigan Public Service Commission). When those same facilities are used for the origination or

[2] 47 U.S.C. § 251(c) (3)

termination of services labclcd as long distance service, they are called "Special Access" and are priced in accordance with rules and policies established by the Commission for acccss scrvices

Notwithstanding the facts that the facilities are physically and operationally Identical and that the historic distinction between "local" and "long distance" telecommunications is rapidly eroding, the regulatory construct currently applicable to thesc facilities causes dramatic price differences depending on whether they are provided as Unbundled Network Elements or as Spccial Access. As a provider of competitive local cxchanyc and interexchange services, LDMI is disappointed that the Commission has chosen to restrict the availability of EELs at TELRIC-based prices and urges the Conimission to revisit that issue at the earliest opportunity. These comments, however, are directed at the specific special access pricing issues raised in AT&T's petition for rulemaking – a petition which LDMI enthusiastically supports.

I. The Unintended Consequences of Deregulated Special Access Rates Combined With Limitations on the Availability of Loop and Transport Combinations at TELRIC Prices Has Created a Price Squeeze Which Has Undermined Development of Competing Networks

Underlying AT&T's petition for rulemaking is one simple premise based upon irrefutable factual evidence: the Commission's 1999 decision to "deregulate" incumbent local exchange carrier spccial access services based upon anticipated competition in the provision of those services has not produced the anticipated results. In its Pricing Flexibility Order,[3] the Commission granted the wish of the major ILECs, including the Bell Operating Companics in general and Ameritech in particular, to be relieved of price

[3] Access Charge Reform. *et al*, 14 FCC Rcd 14,421 (1999), *aff'd sub nom.* WorldCom, Inc. *et al* v. FCC, 238 F. 3d 449 (D.C. Cir. 2001).

cap regulation of their special access rates based not upon any demonstration that they were subject to actual competition and no longer possessed market power in those services, but rather based on a "proxy" for erosion of inarket power, *i.e.*, that other providers had collocated in those companies' central offices anywhere within a Metropolitan Statistical Area (MSA). In the Pricing Flexibility Order, the Commission made the predictive judgment that such collocation would act to restrain the prices for special access services and that market forces would be sufficient to protect consumers and ensure rates that are just and reasonable.

Unforlunatcly, as AT&T's petition and supporting documentation demonstrates and as LDMI has learned all too well, however reasonable the Commission's predictive judgment may have been in 1999, those predictions have not been borne out by actual experience in the marketplace. What has occurred since 1999 with respect to special access pricing is well-documented and uncontradicted. Special access rates haw spiraled upward to exorbitant levels.

As noted by AT&T, the Bell Operating Companies' rates of return on special access services, based on ARMIS data on file with the Commission, are outrageous. None are more outrageous than the return levels of SBC Corporation – parent of Ameritech Michigan, which is LDMI's primary vendor of special access scrvices. According lo that data, in 2001, SBC earned a return on special access of nearly fifty-five percent![4] Such outlandish returns are understandable when one considers the rates which are charged by Ameritech Michigan for special access. In November 2001, LDMI's Senior Director of Regulatory Affairs, Jerry W. Finefrock, submitted testimony on behalf

[4] AT&T Petition at 8

of the Competitive Local Exchange Carriers Association of Michigan and several of its member companies in a formal complaint proceeding before the Michigan Public Service Commission.[5] In his testimony, Mr. Finefrock described Ameritech Michigan's pricing behavior and provided graphic and compelling examples of how excessive are those rates. For example, Mr. Finefrock indicated that Ameritech Michigan's standard rate for an eighteen mile DS-I facility provided pursuant to its special access tariff on file with the Commission is $1,129.16 per month, with an installation charge of $1,493. If a customer elects to obtain that facility subject to a five year service commitment (thereby foregoing any opportunity either to construct its own facilities or to consider other suppliers for a five year period without incurring burdensome termination charges), the monthly charge would be $502.80 with an installation charge of $50.00. Incredibly, the identical facility is made available to certain end users and Internet Service Providers in Michigan at a rate of $195 per month with no installation charge. Other examples of excessive ILEC special access prices both within and outside Michigan abound.

When a company which enjoys a *de facto* monopoly in the provision of an essential service is permitted by a Commission regulatory policy based upon predictive judgments and proxies for actual competition to charge potential competitors and captive customers nearly six times what it charges selected customers (not considered to be CLECs or IXCs) for the identical facility or service, albeit it with a different name, and those customers have no alternative source for obtaining such facilities or services, it is

[5] Case No. U-13193 In the matter of the complaint of the Competitive Local Exchange Carriers Association of Michigan. CMC Telecom, Inc., Long Distance of Michigan, Inc., McLeod USA Telecommunications, Inc., MichTel, Inc.. and the Association of Communications Enterprises against Ameritech Michigan for anticompetitive acts and acts violating the Michigan Telecommunications Act.

no wonder that tlie company is able to enjoy a rate of return in excess of fifty percent. As AT&T's petition notes, ILEC special access pricing under the Commission's Pricing Flexibility Order epitomizes the very sorts of "creamy returns" which the U.S. Court of Appeals for the District of Columbia Circuit has found so inappropriate.[4]

The fact that the market forces anticipated by tlie Commission in 1999 to somehow discipline special access pricing have not had that effect is well-documented and is beyond serious question. However, the importance of revisiting the need to appropriately regulate special pricing and to impose a regulatory regime which will ensure rates which arc just and reasonable and which are not unreasonably discriminatory is about far more than just preventing monopolists' ability to enjoy "creamy returns." It is also about promoting competition and achieving the public interest objectives underlying the Telecommunications Act of 1996 as well as the Commission's own often-stated goals.

As noted above and as has been explained by AT&T, special access services are physically and operationally identical to EELs with the difference being EELs are, pursuant to Commission rule, to be used for "local" competition, whereas special access is to be used for origination and termination of "interexchange" traffic. There no longer is such a "bright line" between local and interexchange markets – except perhaps in Conimission regulatory requirements. In the real world, customers demand solutions to all of their telecommunications needs, and carriers seek to fulfill those needs. These customer demands and expectations have led to the emergence of the ICP concept of service provider. When LDMI wishes to acquire "last mile" facilities from Ameritech

[4] Fanners Union Credit Exchange, Inc. v. FERC, 734 F.2d 1486, 1502-1503 (D.C. Cir. 1984).

Michigan so that it can scrvc a customer beginning at the customer's premises, it does not do so for the specific purpose of being the customer's long distance carrier or thc customer's local exchange service provider. It does so for the purpose of' being the customer's scrvicc provider, without rcgard to distance.

Without its own connections to each and every customer premises, LDMI. like all other non-ILEC telecommunications scrvicc providers, is necessarily reliant on access to thc ILEC's connection to that customer in order to serve tlie customer. Notwitlistanding any predictions, speculations, or expectations that the Commission might have harbored in 1999, the simple and undeniable fact is that now and for the foreseeable future, LDMl and similarly-situated ICPs have no other source for those "last mile" connections to their customers. That is true irrespective of whcthcr thc cuslomer will use LDMI's service for long distance calling, for local cxchange calling, for voice or for data, or, as is the situation for many of its customers, for all of its telecommunications needs without regard lo scrvicc labels. Nothing in the 1996 Act or its legislative history indicates that Congress' intent in requiring thc ILECs to open their networks and to allow competitors to use those networks on an unbundled element basis to compete with those companies was to be limited to services that the Commission considers to fall on the "local" side of tlie local/long distance "bright line" – a line which no longer exists in the real world.

The distortion of the 1996 Act described in the preceding paragraph is amplified by thc fact that the special access rates which LDMl and other ICPs are required to pay for thosc "last mile" connections are essentially deregulated, unrestrained by market forces, and arc yielding returns of more than fifty percent in some cases for those companies who are allowed to charge those prices, In the nearly seven years since enactment of the 1996 Act, much has been written and said about the importance of facilities-based competition. LDMI concurs that in the lony run, competition to serve customers over alternative networks will produce the important public interest benefits of lower prices, increased choice and improved service quality. However, in determining when unbundled network elements should be available from ILECs and how special access should be priced, the Commission should realize that Facilities-based competition does not occur simply by passing legislation and announcements that government regulators favor it. It takes time and capital to construct competiny networks. Investors need incentives to commit the resources to build those networks. As noted in AT&T's petition as well as in Mr. Finefrock's November 2001 testimony in the Michigan PSC proceeding, today those incentives do not exist. To the contrary, the current "price squeeze" sanctioned by the Commission has created enormous disincentives to invest in competing networks.

Under the current regulatory environment, the BOCs, including, for example, Ameritech Michigan, and other ILECs, have the ability to demand unregulated high rates Tor those "last mile" special access facilities while, at the same time, offering physically and operationally identical services and facilities to "ordinary" customers (*i.e.*, anyone other than a customer deemed to be an "IXC" purchasing the service for long distance access) at far more favorable prices. Ameritech Michigan and others have exploited this opportunity by offering favorable pricing to those "ordinary" customers willing to commit to long-term agreements. Once a customer is effectively "locked in" to the incumbent's "last mile" facility for live years or more, there is no opportunity for other vendors to compete for those customers' business. With the customers effectively precluded from moving their traffic, there is no economic justification for other vendors, including ICPs, to invest in constructing competing networks. The inevitable consequence of this price squeeze created by the interplay of 1) favorable pricing for prefcrrcd customers, 2) limitations on EELs which render them unavailable for niost ICPs, and 3) unregulated special access rates yielding "creamy returns," has impeded the development of the facilities-based telecommunications service compctition (without rcgard to scrvicc category or distance) which the 1996 Act was intended to foster

Ideally, all threc factors enumerated above which have created the price squeeze and discouraged investment in alternative networks would be addressed in a simultaneous nianner. LDMI recognizes that such simultaneous treatment of multiple facets of the same problem may not be feasible. Accordingly, LDMI respectfully urges the Commission to at least start the process by addressing one of those facets: the cxccssively high special rates being charged by Anieritech Michigan and other ILECs in the wake of the Commission's <u>Pricing Flexibility Order</u>, and the unintended consequences of that order,

II. The Commission Has the Authority and the Statutory Responsibility to Revisit the Appropriate Regulation of Special Access Rates Based on Current Circumstances and To Establish Interim Rates Pending Completion of that <u>Review</u>

AT&T's petition requests that the Commission commence a rulemaking proceeding for the purpose of reforming and tightening the regulation of price cap ILECs' special access services. As described above, the current system of allowing pricing flexibility bascd on proxies for competition which have proven unreliable has led to rapidly escalating prices for what remain monopoly services, and have had the perverse effect of actually impeding development of facilities-based competition. There is a demonstrable need to revisit the Pricing Flexibility Order and the rules promulgated therein regarding special access pricing.

Those entities who most benefit from those rules, *i.e.*, the price cap ILECs, can be expected to oppose AT&T's petition by characterizing it as an untimely petition for reconsideration of the Pricing Flexibility Order. It is nothing of the sort Rather, the Commission is being asked to determine what is the most appropriate means for regulating special access pricing to ensure lawful rates based on current circumstances – not based on circumstances that the Commission in 1999 thought might occur in the future. Adjusting rules and policies based on current conditions is neither improper nor unusual and is indeed a essential aspect of the administrative process. As Judge Harold Leventhal of the U.S. Court of Appeals for the District of Columbia Circuit stated long ago in a different, but analogous, context, "a month of experience will be worth a year of hearings."[7]

Significantly, the rules adopted in the Pricing Flexibility Order were adopted without the benefit of any hearings. More importantly, the telecommunications industry and the Commission have had many months of experience (more than three years' worth of experience) since those rules were promulgated in 1999. Moreover, the American Airlines court expressly recognized that regulatory agencies have an obligation to make re-examinations and adjustments to their rules and policies in the light of experience.[8] The experience gained in the area of special access since 1999 includes substantial rate increases, poor service, "creamy returns" as high as fifty percent or greater, and captive

[7] American Airlines. Inc. v. CAB, 359 F.2d 624 at 633 (D.C. Cir. 1966).
[8] *Id., citing to* National Broadcasting Co. v. U.S. 319 U.S. 190 (1943) and United States v. Storer Broadcasting Co., 351 U.S. 192 (1956).

customers who have no competitive alternatives to those services. Consideration of rules and policies that are appropriate for special access pricing based on that experience is long overdue. LDMI concurs with AT&T that a rulemaking proceeding looking toward the establishment of pricing rules for special access which will ensure lawful rates should be undertaken iminediately.

Although LDMI urges the Commission to begin the rulemaking process forthwith, it recognizes that the rulemaking process takes time. A notice of proposed rulemaking must be issued, comments and reply comments tiled, and the Commission staff must review and analyze the extensive record likely to be compiled in that proceeding, rules must be crafted, and a report and order written to be considered by the Coniniission. It is unlikely that this process could be completed in less than a year – perhaps longer. For that reason, LDMI shares AT&T's concerii that <u>immediate</u> interim action *to* stop the rapid escalation of special access prices must also be taken. While there may be other possible interim solutions, an interim prescription based on an 11.25 percent rate of return has inerit and should be considered to adoption.[9]

[9] The Commission's authority to mandate interim rate level ceilings has been long acknowledged and well-documented. <u>See</u>, *e.g.*, <u>Lincoln Tel & Tel. Co. v. FCC</u>, 659 F.2d 1092 (D.C.Cir. 1981).

CONCLUSION

For the reasons stated in these comments, LDMT supports AT&T's petition for rulemaking and respectfully asks that the Commission commence a rulemaking proceeding to re-examine the appropriate means *for* ensuring just and reasonable special access rates, and that it implement an interim prescription based on a 11.25% rate of return for special access.

Respectfully submitted,

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