Before the

Federal Communications Commission

Washington, D.C. 20554

In the Matter of	)	
	)	
Section 272(f)(1) Sunset of the BOC Separate Affiliate and Related Requirements	))	WC Docket No. 02-112
	)	
2000 Biennial Regulatory Review Separate Affiliate Requirements of Section 64.1903 of the Commission's Rules	)))	CC Docket No. 00-175

REPLY COMMENTS OF AMERICATEL CORPORATION

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Americatel Corporation ("Americatel"),[1] through counsel, respectfully submits its reply comments in the above-captioned proceeding.[2]

I. <u>Summary and Introduction</u>

Americatel believes that, in order to prevent re-monopolization of the long distance market by the Bell Operating Companies ("BOCs"), the Federal Communications Commission ("FCC" or "Commission") must compel the BOCs to continue to provide long distance services only through separate subsidiaries and impose additional regulations, as

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[1] Americatel, a Delaware corporation that is a subsidiary of ENTEL Chile, is a common carrier providing domestic and international telecommunications services. ENTEL Chile is the largest provider of long distance services in Chile. Americatel also operates as an Internet Service Provider ("ISP"). Americatel specializes in serving Hispanic communities throughout the United States, offering presubscribed (1+), dial-around, and prepaid long distance services, as well as private line and other high-speed services to its business customers. The majority of traffic carried by Americatel is dial-around in nature.

[2] *Section 272(f)(1) Sunset of the BOC Separate Affiliate and Related Requirements* and *2000 Biennial Regulatory Review Separate Affiliate Requirements of Section 64.1903 of the Commission's Rules,* Further Notice of Proposed Rulemaking, WC Docket No. 02-112 and CC Docket No. 00-175, FCC 03-111 (rel. May 19, 2003) ("*Further Notice*").

discussed herein. Americatel also believes that the BOCs' economic analysis is flawed and misleading. In their economic analysis, the BOCs have used an incorrect definition of the product market that ignores the changes brought about by the bundling of local and long distance services together for a single price. Americatel maintains that the BOCs must be compelled to continue to provide long distance services only through separate subsidiaries because history demonstrates that regulatory penalties do not deter their anti-competitive conduct. Similarly, the claims of the BOCs with respect to predatory pricing do not withstand scrutiny. Also, despite their claims to the contrary, the BOCs' ability to engage in anti-competitive pricing to control the market is not hindered by price cap regulation. In fact, price cap regulation has the same effect on the market as would the unlawful and unfair allocation of costs by the BOCs for competitive services to regulated services.

AT&T's economic analysis more correctly describes market and regulatory reality than the analysis submitted by the BOCs. AT&T has correctly demonstrated that independent long distance carriers cannot compete with the BOCs' service bundles. Moreover, AT&T and MCI make a compelling case for re-regulation of the BOCs' provision of billing and collection services. The record before the FCC demonstrates a strong need for the Commission and/or state public utility commissions ("PUCs") to investigate the bundling of services by the BOCs, especially to prevent the cross-subsidization of competitive long distance services. Ultimately, the Commission must decide whether it desires a long distance market with the BOCs having market shares of 50-60% within their local exchanges or whether the FCC prefers a competitive long distance market similar to that which exists in Chile, a situation with which Americatel is very familiar as a result of its status as a subsidiary of the company (ENTEL Chile) that was formerly the monopoly provider of long distance services in Chile before that company was successfully transitioned to competition.

If competition is to survive, much less flourish, the Commission must impose more, and not less, regulation on the BOCs. Americatel makes the following specific recommendations:

- The BOCs should not be permitted to offer interstate and international, interexchange services on an integrated basis.

- In view of the numerous concerns about the joint anti-competitive collaboration between the BOCs and their long distance affiliates, those affiliates, like the BOC local service provider, should be classified as "Dominant Carriers" for the provision of in-region long distance services.

- The Commission should prohibit any cross-subsidies between bundled services and either regulate the bundling of services by the BOCs in a manner similar to the regulation of bundling in Australia or permit the PUCs to do so, in order to prevent any cross-subsidies of competitive services.

- The Commission should consider imposing further restrictions on the BOCs as has occurred in Chile with considerable success in increasing competition, including:

    - the mandatory provision of billing and collection services to all carriers on the same terms and conditions that the BOCs provide those services to their affiliates, including the requirements to bill long distance competitors' charges on the same invoice as the BOC's own charges and to disconnect all services for non-payment of long distance charges;

    - the re-targeting of BOC price cap indices and access charges to the authorized rate of return and the imposition of a requirement that access charges be based on the BOCs' incremental costs to provide network connections;

    - the institution of streamlined procedures within the Enforcement Bureau's Investigations and Hearings Division to investigate and prosecute, when appropriate, any problems related to the interconnection of competitors to a BOC's network, as well as other aspects of long distance competition;

    - additional Commission oversight of the BOC's compliance with the Commission's rules for sharing Customer Proprietary Network Information ("CPNI") with their long distance affiliates; and

- the mandatory disclosure by the BOCs to competing carriers of all customer information in their possession that would not be inconsistent with the CPNI rules so that all long distance carriers can compete on a level playing field.

- In addition to previously listed requirements for the BOCs and in light of the BOCs' ongoing record of anti-competitive conduct, the Commission could also consider whether the BOC's affiliate should also be required to have an appropriate level of independent ownership as previously recommended by Americatel.

II. The BOCs' Economic Analysis is Flawed and Misleading; Therefore, the Commission Must Continue to Require the BOCs to Provide Long Distance Services Only Through Separate Affiliates

Three of the four remaining BOCs, SBC Communications ("SBC"), Verizon Communications ("Verizon") and Qwest Communications International ("Qwest"), proffered the joint declaration of three principals of Lexecon, Inc., a well-respected economic consulting firm, in support of their comments in the captioned proceeding.[3] Economists Dennis Carlton, Hal Sider and Allan Shampine (collectively the "BOC Consultants") are experienced advisors to, and expert witnesses for, the BOCs. They have worked on a variety of FCC and state public utility commission ("PUC") proceedings and court cases.

The BOC Consultants draw several economic conclusions about the BOCs' provision of interstate, interexchange services and international, interexchange services and its impact on competition. They conclude, for example, that "permitting the BOCs … to integrate their long-distance and local exchange operations will not adversely affect competition."[4] The BOC Consultants also conclude that "there is no economic basis for imposing dominant carrier

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[3] Declaration of Dennis W. Carlton, Hal Sider and Allan Shampine, attached to Comments of SBC,, Comments of Qwest, , and Comments of Verizon. For ease of understanding, this declaration will be referred herein as the "*BOC Declaration.*"

[4] *BOC Declaration*, at 4 (footnote omitted).

regulation on the BOCs' in-region long distance service based on the sunset of Section 272 structural separation requirements."[5]

As demonstrated below, the assumptions underpinning these conclusions are questionable. Therefore, Americatel submits that the BOC Consultants' conclusions that are based on flawed economic assumptions cannot stand. Rather, sound economic analysis leads to the conclusion that the Commission should actually impose additional restrictions on the BOCs in order to preserve competitive markets.

A. The BOC Consultants Have Used an Incorrect Definition of the Product Market and have Not Defined the Relevant Geographic Market

The BOC Consultants attempt to dodge the Commission's question of definition of the product market. They note that rapid changes in the telecommunications industry "have blurred traditional distinctions between wireline and wireless services and between local and long distance services," and state that such changes have also "complicate[d] the delineation of a precise market definition."[6] However, rather than offer a new potential definition of the relevant product market, the BOC Consultants argue that it is not necessary for the Commission to define the product market because, in their view, whatever the new market is defined as, it is essentially more competitive than the long distance market was when the FCC concluded in 1995 that AT&T was no longer that market's dominant carrier.[7]

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5 *Id.*

6 *Id.*, at 9.

7 *Id.*

This reasoning is simply wrong. AT&T and the BOCs are not comparable. When the FCC concluded in 1995 that AT&T was no longer a dominant long distance carrier,[8] AT&T was not also in the local exchange service market and, therefore, obviously, did not possess market power in the local market or have access to huge revenue streams producing large gross margins from an enormous local service base, as do the BOCs today. Likewise, in 1995, AT&T was not bundling local and long distance services at prices that did not reflect cost, as are the BOCs.

In contrast, the BOCs today are in the local exchange business as incumbent carriers, continue to dominate that market, earn significant financial margins as a result of price cap regulation, and are bundling service packages at prices that do not reflect the package components' actual costs. There simply is no fair comparison between the AT&T of 1995 and the BOCs of 2003. Therefore, the BOC Consultants' conclusions drawn from such a comparison are invalid.

First, it is clear that, for an ever-growing portion of the population, the current product market definition as interstate, interexchange service is no longer material. There may well be emerging a whole new sub-market for bundled local and long distance services. The BOCs have been marketing packages of bundled local and long distance services aggressively to their local service customers,[9] while deliberately avoiding competing for interexchange business

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[8] *Motion of AT&T Corp. to be Reclassified as a Non-Dominant Carrier*, Order, 11 FCC Rcd 3271 (1995) ("*AT&T Reclassification Order*").

[9] *See, e.g.,* SBC, Form 10-Q, filed with the United States Securities and Exchange Commission ("SEC"), on May 9, 2003. This document is available online at http://www.sec.gov/Archives/edgar/data/732717/000073271703000415/q103_10q.htm (visited July 11, 2003). "Additionally, in April 2003, we launched our new 'All Distance' bundle in certain states, which includes unlimited domestic long-distance voice and local calls for a fixed

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in other regions.[10] With more and more customers purchasing packages of unlimited domestic calling from the BOCs at flat rates, the FCC needs to develop an accurate definition of the product market, including any relevant sub-markets. The FCC should conduct further economic studies that would assist the Commission in developing an accurate definition before it would even consider granting the BOCs any regulatory relief.

Moreover, every definition of a relevant market has both a product and a geographic market component. The BOCs are relatively silent on the facts that would define a geographic market in which the existence of competition should be measured, preferring to measure competition on a national basis if possible. It seems clear that, given the BOCs' general reluctance or refusal to compete in each other's local exchanges and the bundling of local and long distance calls, the geographic market is likely a BOC's local calling area—at least for packages of bundled services.[11] As AT&T correctly noted, the BOCs have, at least tacitly, agreed not to enter each other's local service markets.[12] Indeed, AT&T quoted Qwest Chairman (and former Ameritech Chairman) Richard Notebaert as saying that Qwest's entry into Ameritech's (a/k/a SBC) local service markets, "might be a good way [for Qwest] to turn a quick

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monthly fee. During the remainder of 2003, we plan to continue our focus on bundling strategies."

10 *See* n.13, *infra* and accompanying text.

11 *See also,* Declaration of Lee L. Selwyn on Behalf of AT&T Corp., at 4, 37-41 ("*Selwyn Declaration*") filed in this proceeding as a part of AT&T's Comments. Similarly, Dr. Selwyn argues that, because of the bundling of local and long distance services for BOC customers, the relevant geographic market is also becoming the BOC's local service market area. *Id.*, at 36. Americatel concurs with Dr. Selwyn's conclusion.

12 Comments of AT&T, at 16, n.36 and accompanying text.

dollar" but "that doesn't make it right."[13] The BOCs seemingly are willing to compete only on their home turf where they have the advantages of incumbency. The general failure of the BOCs to compete as CLECs against other BOCs also constitutes strong evidence that the proper geographic market for evaluating the BOCs' economic power is their local exchange market, as suggested by Dr. Selwyn.

Americatel submits that there simply is an insufficient record for the FCC to define the appropriate markets for analysis of the BOCs' market power. This entire area needs more economic analysis before the FCC could rationally consider any BOC request for relaxation of regulation.

In the event that the Commission were to examine the BOCs' market power on a local exchange basis, the argument that the BOCs have no power in the market would fall apart rapidly. The BOCs still control the local service market throughout their territory. If this were not true, BellSouth would have not been able to have told its investors and the SEC that local competition has not yet had any significant negative impact on BellSouth's ability to maintain its monopoly pricing policies. "Increasing competition could cause us to reduce our prices, restructure bundled service packages to provide more services without increasing prices, and increase our advertising and promotional spending."[14]

The BOC Consultants' analysis is premised on an assumption that the product market does not include local service. For example, they calculate an approximate HHI (Herfindahl-Hirschman Index) for the national presubscribed long distance market in 2005

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[13] *Id.*, *quoting* "Ameritech Customers Off-Limits: Notebaert," CHICAGO TRIBUNE, Oct. 31, 2002.

[14] *See* http://www.sec.gov/Archives/edgar/data/732713/000104746903007358/a2104641z10-k.htm (visited June 24, 2003).

versus the HHI for that same market in 1995.[15] They calculate the 1995 HHI as 4,708 and project the 2005 HHI to be 1,060, which, *ceteris peribus*, would lead one to conclude that the interstate, interexchange market, with the BOCs' presence therein, would be very competitive.

Given the facts, however, it would likely be reversible error for the Commission to hold all other factors constant in this instance. To the extent that competition continues to move the market to unlimited packages of domestic calling for a single price, any reasonable estimation of an HHI for the combined local and long distance service product market (or sub-market) at the local exchange level could well show that such market (or sub-market) would be highly concentrated and dominated by the BOCs. If market trends continue, many carriers that today compete only for segments of this unified product market would be forced either to enter the local services and, probably, the wireless markets, or to leave the telecommunications business altogether. Moreover, were UNE Switching to be eliminated as means for CLECs to compete, as the BOCs so fervently crave, there would likely be no meaningful competition—save wireless—for any segment of the market.

The demise of *a la carte* competition could have a detrimental impact on consumers even when they prefer to purchase packaged services because *a la carte* competition can serve as a check on prices for bundled services. So long as consumers have the option of creating their own service packages from several suppliers, large carriers will be forced to hold prices for their bundled packages in check. Similarly, while packaged services can provide consumers with added convenience and savings, not every consumer would benefit from the purchase of bundled services. "[F]ully bundled plans aren't for everybody. Many Americans—

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[15] *BOC Declaration*, at 15, Table 1.

perhaps even a majority—might not spend enough time on the phone to justify their cost. And consumers can often find greater savings by buying *a la carte*."[16]

One of the key issues in this proceeding is: Whether there will be any independent carriers left to provide *a la carte* competition? Americatel submits that, in the event that the BOCs are able to gain control of their local exchange markets through the bundling of services and their facilities-based competitors fall by the wayside or are acquired by the BOCs, the barriers to entry into the long distance business are very likely to increase substantially.

Since the Commission opened long distance services to competition in the late 1970s and early 1980s, the barriers to market entry have not generally been excessive. A putative long distance carrier can enter the market on a resale basis without a significant capital investment, but only because other facilities-based carriers (such as AT&T, MCI and Sprint) have already heavily invested in switching and transport facilities, which can be readily resold by new entrants.

In the event that the BOCs were, however, able to drive those large facilities-based carriers out of the market through acquisition or otherwise, such that interexchange switching and transport capacities were no longer readily available for resale at low prices, the entry barriers for the long distance market would likely become much more formidable. An aspiring carrier would likely be required to make higher levels of investment in its own network plant and/or pay much higher wholesale prices to the BOCs for interexchange switching and transport. Moreover, in light of the vast sums lost by investors in CLECs and the investment community's resulting strong reluctance to risk capital on telecom upstarts, the market demise of

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16 Jeffrey Bartash, "A 'Bundle' of Money: Consolidated Telecom Services Can Cost More," CBS
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AT&T, MCI and Sprint, for example, would likely make it virtually impossible for a new entrant to obtain the financing necessary to compete against the BOCs.

The FCC must first redefine the product market before it decides to weaken any regulations controlling the BOCs' provision of interstate and international, interexchange services. Moreover, as Americatel proposed in its initial comments, the FCC should undertake or authorize detailed studies of the telecommunications market and not simply rely on the record developed so far in this proceeding.[17]

B. History Demonstrates that Regulatory Penalties do not Deter the BOCs

The BOC Consultants argue that the elimination of the FCC's structural separation rules for the BOCs' provision of in-region long distance services would not result in any increased incentive for the BOCs to engage in non-price discrimination because the elimination of the structural separation rules would not reduce the applicable penalties for discriminatory conduct on the part of the BOCs.[18] The BOC Consultants note that such conduct could be punishable by "fines, the potential loss of the authority to provide long distance services, and exposure to antitrust penalties."[19]

That conclusion is contradicted by the facts. FCC fines, at least at current levels, do not deter the BOCs from anti-competitive conduct. As Americatel noted in its comments filed in this proceeding, the FCC has imposed civil forfeitures amounting to millions of dollars

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MarketWatch.com, July 14, 2003.

[17] Americatel's Corrected Comments, at 5.

[18] *BOC Declaration*, at 15.

[19] *Id.*

against the BOCs for their violations of Commission rules and applicable statutes.[20] However, given the vast resources and revenues of the BOCs, FCC fines are essentially "parking tickets" to the BOCs and certainly do not deter their anti-competitive conduct.[21]

Similarly, the imposition of anti-trust penalties does not seem to deter the BOCs. By way of example, Qwest's predecessor, US West, Inc. ("USW"), was the subject of two enforcement actions that went before Judge Greene under the Modification of Final Judgment ("MFJ").[22] In the first enforcement case, USW was accused by one of its competitors of providing an unlawful information service in violation of Section 11(D) of the MFJ. A consent decree, a Civil Enforcement Consent Order ("CECO"), imposing new sanctions on USW was accepted by the court.[23]

This serious run-in with Judge Greene and the imposition of further anti-trust sanctions did not deter USW from similar unlawful conduct. Just a short time later, USW found itself in a second MFJ enforcement action.[24] In that case, USW, as punishment for engaging in several violations of the MFJ, was ordered to pay a civil penalty of $10 million and institute even more severe internal review processes.

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[20] Americatel's Corrected Comments, at 28.

[21] The latest BOC fine imposed for anti-competitive behavior was levied by the FCC on July 17, 2003, when BellSouth agreed to pay $1.4 million for acts related to its provision of interLATA services before it obtained FCC authority to do so and for improperly rejecting requests to provide interLATA services to customers of CLECs. *BellSouth Corp.*, Order, File Nos. EB-02-IH-0683 and EB-02-IH-0805 (rel. July 17, 2003).

[22] *United States v. American Tel. & Tel. Co.*, 552 F. Supp. 131 (D.D.C. 1982), *aff'd sub nom., Maryland v. United States*, 460 U.S. 1001 (1983).

[23] *United States v. Western Electric Co., Inc.*, 1989-1 Trade Cases 68,421 (D.D.C. 1989).

[24] *United States v. Western Electric Co., Inc.,* 1991-1 Trade Cases 69,329 (D.D.C. 1991).

Even then, USW-Qwest was not chastened by this fine such that it limited it operations to lawful activities and conduct. Instead, it has continued to push, indeed, tear the envelope in the area of operating within legal and regulatory limits. Before its merger with Qwest, USW was found by the FCC to have agreed to sell Qwest's interLATA services in an unlawful manner.[25] Also, as previously noted by Americatel, Qwest was just recently fined $6.5 million by the FCC for improperly offering interLATA services without first obtaining FCC permission.[26] The BOCs simply do not fear the imposition of civil fines either by the courts or the FCC. The unvarnished fact is: the BOCs do whatever they want to do, whenever they want to do it, regardless of regulatory requirements.

Therefore, from the BOC Consultants' list of deterrents, this leaves only the threat of a potential loss of the BOCs' authority to provide interLATA services as a real deterrent for anti-competitive behavior. In theory, with the market moving toward unlimited calling for a fixed fee, a BOC's top management would seemingly be deterred from permitting its corporation from engaging in any conduct that could jeopardize its ability to meet the market demands for end-to-end service. However, as a practical matter, those who operate deep within a BOC's inner sanctum probably discount the Commission's will to terminate the BOC's interLATA authority and will likely continue to do so unless and until the FCC were actually to release an order that revoked a BOC's interLATA authority.

Moreover, even if the FCC were to release such an order terminating a BOC's interLATA authority, it is likely that the affected BOC could use the administrative and judicial

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25 *AT&T Corporation v. Ameritech Corporation*, 13 FCC Rcd 21438 (1998), *aff'd sub nom., US West Communications, Inc. v. FCC*, 177 F3d 1057 (D.C. Cir. 1999).

26 Americatel's Corrected Comments, at 28.

processes to prevent the order from taking effect for years to come. Meanwhile, all of the BOCs would likely band together in an attempt to seek federal legislation that would undo the FCC's de-certification.[27] The plain truth is that the BOCs are simply too big and too powerful to be deterred from anti-competitive conduct by threats of government punishment. Only by imposing and enforcing strong regulatory safeguards can the FCC even hope to control the telecommunications behemoths and to ensure that competition in all telecom markets develops and flourishes.

C. *The BOCs do not Need to Drive their Rivals from the Market to Control the Market*

Additionally, the BOC Consultants argue that the BOCs would have no economic incentive to engage in predation to drive their rivals from the market because "it is widely recognized that predation is rarely a profitable strategy. In pursuing this strategy the ILEC sacrifices revenue with the goal of driving its rivals from the market and later recouping its investment in the form of higher prices."[28] The BOC Consultants then argue why such strategy would not be actively pursued by the BOCs. A predation strategy is rarely profitable, according to the *BOC Declaration*. "[F]irms that engage in predation incur some short-run losses in order to obtain longer-term gains."[29] Long-terms gains would be possible only if there were barriers to entry that would protect the successful predator from future competition. Because of the

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27 The BOCs regularly attempt to reverse PUC or judicial setbacks in the states by seeking and often obtaining the passage of remedial legislation. For example, BellSouth was price regulated in South Carolina under a plan approved by the South Carolina Public Service Commission. According to BellSouth, that plan was rejected by the South Carolina Supreme Court in 1999, and later that same year, BellSouth was able to select a new price regulation plan under a brand new statute that BellSouth presumably shepherded through the legislature. BellSouth, 2002 Form 10-K, at 77-8.

28 *BOC Declaration*, at 29.

presence of large and robust competitors (*i.e.,* AT&T, MCI, and Sprint) in the market and the ability of others to purchase assets of defunct carriers, the BOC consultants argue that there are no barriers to long distance market entry.[30] Finally, they argue that the BOCs would not be successful at recovering future excess profits even if the BOCs could drive out their rivals because the government would simply re-regulate the BOCs' services.[31]

The BOCs' arguments are flawed for several reasons. One, as discussed in greater detail below, price cap regulation of the BOCs permits them to obtain high gross margins from their monopoly-like services, which, in turn, permits them to offer competitive services at or below cost. In other words, price cap regulation permits the BOCs to undercut their competitors without the need to incur short-term losses.

The existence of mature price cap regulation plans and the lack of effective competition in the local market have enabled the BOCs to earn profit levels in excess of their capital costs, which, in turn, permits them to price competitive services at very low prices without the necessity of incurring foregone profits in the sense contemplated by the courts. In one of the leading cases rejecting a claim of predatory pricing, *Matsushita Elec. Industrial Co., Ltd. v. Zenith Radio Corp.*, the Court noted that inherent in a claim of predatory pricing is the notion that the alleged predator must be willing to "forego profits that free competition would offer [it]."[32] Competitors that do not have the benefit of the BOCs' local market power and deep

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29 *Id.*

30 *Id.,* at 29-30.

31 *Id.,* at 30.

32 *Matsushita Elec. Industrial Co., Ltd. v. Zenith Radio Corp.*, 475 U.S. 574, 588 (1985).

pockets cannot afford to offer competitive services at prices that do not permit them to recover their direct costs, overhead costs and a fair profit level. In other words, the predator must be willing to give up profit levels that meet its cost of capital. The Court concluded that such conduct would not make economic sense. However, if the predator were a regulated company subject to rules that permitted it to earn profits in excess of its cost of capital, the predator could afford to lower its prices to injure competition without also lowering its profits to a level below its cost of capital. Under those circumstances, predatory pricing would make economic sense even where the predator had no reasonable hope of recouping all of its profits foregone through low-ball pricing.

Two, the BOCs do not need to eliminate their rivals from the telecom market, but only to retain the BOCs' control of that market. The BOCs can successfully control a market that still contains weak competitors.

A classic case of predation would be a small geographic market served by three dry cleaners, all of which compete for customers based on both price and quality of service. At some point, a new dry cleaner with deep financial pockets opens a competing store, offering prices at or below its marginal costs. The existing dry cleaners, without deep pockets, cannot afford to compete at these low-ball prices and eventually close shop. At that point, the deep-pocket dry cleaner (now a monopolist) raises cleaning prices and recoups its earlier losses until challenged by new competitors.

Given the nature of the dry cleaning market, with fairly low barriers to entry, it is quite likely that the "deep-pocket" dry cleaner that tried to gouge it monopoly customers would soon likely see other cleaners enter the market to challenge the high prices of the "deep pockets" cleaner. However, as discussed in greater detail above at section II.B. herein, the elimination of large facilities-based carriers, such as AT&T, MCI and Sprint, from the market, when coupled with the huge capital losses incurred by investors in CLECs, would likely result in a shortage of capital to fund new long distance market competitors, thus, creating much higher barriers to entry. Those higher barriers to entry would make it more likely that the BOCs could sustain high prices after they had successfully committed predation in the marketplace.

Moreover, as noted above, BellSouth's latest SEC Form 10-K annual report boasts that local service competition has not yet forced BellSouth to "reduce [its] prices, restructure bundled service packages to provide more services without increasing prices, and increase [its] advertising and promotional spending."[33] Yet, according to the FCC's most recent report on local competition, CLECs are serving 13% and 15% of the access lines in Florida and Georgia respectively, BellSouth's largest markets.[34]

When it can "lose" almost 15% of its access lines to competitors in its largest markets while still retaining its monopoly-era prices for local services, why would BellSouth need to drive out its local service competitors? The plain simple truth is that BellSouth (and its sister BOCs, for that matter) need not drive out their competitors to meet their financial goals. They can tolerate the relatively ineffective competitors they have faced so far in the local services market and still reap profits that greatly exceed what rate-of-return regulated carriers, such as rural telephone companies, are permitted to earn.

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[33] *See* n.11, *supra.*

[34] FCC, "Local Telephone Competition: Status as of December 31, 2002." (rel. June 2003).

D. The BOC Declaration's Implication that the BOCs Would be Forced to Accept Very Low Profits Were They to Engage in Predation is Incorrect Because of Price Cap Regulation

The BOC Consultants offer a misleading implication when they argue that "predation requires a firm to sacrifice profits (relative to the level that would otherwise prevail) during the period in which its rivals are driven from the market."[35] While one might argue that, in a theoretical world, this statement would always be true, the statement implies that the predator would be forced to earn at below-market rates during the period of time in which it was attempting to drive out all competition.

That implication simply is not true in the case of the BOCs because of the existence of price cap regulation. For example, BellSouth's interstate access charges are subject to the FCC's price cap regulations and all of its intrastate rates are also price regulated.[36] Data from the FCC's ARMIS (Automated Reporting Management Information System) database shows that BellSouth's interstate operations earned 21.37% for Florida (SBFL) and 14.17% for Georgia (SBGA) during 2002.[37] As the FCC is well aware, the current prescribed rate-of-return for non-price cap ILECs is 11.25%.[38]

Similarly, most states imposing some type of price cap regulation on the BOCs' intrastate services do not also regulate profit levels. Indeed, the BOCs generally are not even

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[35] *BOC Declaration*, at 31-2.

[36] BellSouth, 2002 Form 10-K, at 8.

[37] http://svartifoss2.fcc.gov/eafs/MainMenu.cfm (visited July 14, 2003).

[38] See generally, *Multi-Association Group (MAG) Plan for Regulation of Interstate Services of Non-Price Cap Incumbent Local Exchange Carriers and Interexchange Carriers; Federal-State Joint Board on Universal Service; Access Charge Reform for Incumbent Local Exchange Carriers Subject to Rate-of-Return Regulation;* and *Prescribing the Authorized Rate of Return for Interstate Services of Local Exchange Carriers*, Notice of Proposed Rulemaking, 66 Fed. Reg. 7725 (2001).

required to report their intrastate earnings in many of those states. It is very likely that state price regulation also enables the BOCs to earn much higher earnings than if they were still regulated under rate-of-return principles as a condition of being permitted to bundle interstate services with local ones.

A small rural telephone company that is regulated by the FCC and a PUC on a rate-of-return basis would not be permitted to retain such excessive profits, which could be used to subsidize its entry into competitive markets. Such a carrier would be required to reduce its rates for regulated services and likely refund its excess earnings. The BOCs, on the other hand, have free reign to use those huge gross margins generated by price cap regulation to subsidize their entry into competitive services. Therefore, at a bare minimum, the FCC should retarget the BOCs' access charges to the authorized rate-of-return before they would be permitted to offer long distance services on an integrated basis. Similarly, to prevent the BOCs' competitive services from being unfairly subsidized by excessive intrastate earnings, the FCC should also urge the states to do likewise for their price cap plans for the BOCs.

Dr. Selwyn's economic analysis also points out the many anti-competitive flaws in price cap regulation as it actually operates. He discusses, for example, an audit report by the California Public Utilities Commission identifying improper cross-subsidies flowing from SBC's regulated operations to its unregulated affiliates, all which occurred since SBC's local rates were subject to price regulation in California.[39] Also, Dr. Selwyn identifies the amounts available for

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[39] *Selwyn Declaration*, at 93-8.

subsidizing long distance rates that are available from the BOCs' bundles of local services, the purchase of which are generally tied to the BOCs' low-ball long distance rates.[40]

E. The BOC Consultants' Example of the CPE Market is not Persuasive Because There has been no Large-Scale Bundling of CPE and Wireline Services

The "economic legerdemain" proffered by the BOC Consultants continues as they argue that, since the BOCs have provided Customer Premises Equipment ("CPE") on an integrated basis for some time without engaging in anti-competitive conduct, there is no reason to expect that a similar offering of long distance services by the BOCs on an integrated basis would produce anti-competitive conduct by the BOCs.[41] This argument fails, however, because, unlike in the wireless market, there simply has been little bundling of CPE with wireline services since the time at which the FCC permitted the BOCs to offer CPE on an integrated basis.[42] For example, Verizon offers its Washington, D.C. residential customers a variety of calling packages (Big Deal, Call Manager, Verizon Freedom[sm], Local Package Plus, Local Package Basic, Local

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[40] *Id.*, at 96-7. The BOCs' mark-ups on the vertical features that are included in the service bundles are enormous. For example, the Florida Public Service Commission found that, in 1999, BellSouth charged residential customers $4.00 per month for Call Waiting service, while its monthly cost was $0.0082, for a gross profit margin of $3.99 per month (48,680%). *Report of the Florida Public Service Commission on the Relationships Among the Costs and Charges Associated with Providing Basic Local Service, Intrastate Access, and Other Services Provided by Local Exchange Companies, in Compliance With Chapter 98-277, Section 2(1), Laws of Florida* and *The Conclusions of the Florida Public Service Commission as to the Fair and Reasonable Florida Residential Basic Local Telecommunications Service Rate, in Compliance with Chapter 98-277, Section 2(2)(A), Laws Of Florida*, (Fla. P.S.C. 15, 1999) ("*Florida Cost Report*"), available online at http://www.psc.state.fl.us/pai/trilogy/intercon/frrrprt.pdf (visited July 14, 2003).

[41] *BOC Declaration*, at 34.

[42] *Amendment of Section 64.702 of the Commission's Rules and Regulations (Third Computer Inquiry); Policy and Rules Concerning Rates for Competitive Common Carrier Services and Facilities Authorizations Thereof;* and *Communications Protocols under Section 64.702 of the Commission's Rules and Regulations*, Report & Order, 104 FCC 2d 958 (1986) (subsequent history omitted).

Package, and Local Package Standard service bundles), but none of them include CPE as a part of the bundled package of services.[43]

The BOCs' claim for innocence in this area is, therefore, similar to that of the non-Bridge-playing person who seeks to reassure the local Poker club of his honesty by informing them that he has never cheated at Bridge. The reassurance has little value to anyone who knows the facts. Similarly, if the BOCs do not cross-subsidize service bundles that contain CPE, it is only because their service bundles do not include CPE.

F. Price Cap Regulation has the Same Effect on the Market as Would the Unlawful and Unfair Allocation BOCs of Costs for Competitive Services to Regulated Services

The BOC Consultants argue that price cap regulation prevents a BOC from shifting costs from its integrated long distance operations to its local telephone operations.[44] They continue to reason that, since rates for regulated services are set without regard to costs under price cap regulation,[45] shifting costs from long distance services to local services provides no financial benefit to the BOCs and, therefore, is not likely to occur.[46]

What the BOC Consultants' argument misses is the fact that the high margins earned by the BOCs under price cap regulation (because it divorces a regulated service's price from its costs, which have been slashed repeatedly by the BOCs' management teams) has the

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43 http://www22.verizon.com/foryourhome/sas/res_cat_VZPackages.asp (visited July 14, 2003).

44 *BOC Declaration*, at 32.

45 Under price cap regulation, a carrier's rates are set based on their relationship to price indices, which, in turn, are adjusted periodically to reflect the impact of inflation and productivity gains, rather than strictly based on the carrier's actual costs for providing service. *See, e.g.,* 47 C.F.R. §§61.41 through 61.49;. OHIO ADMIN. CODE §§4901:1-4-01 *et seq.* (Freezing SBC's basic local rates indefinitely, but permitting rate increases for certain vertical services and specialty business services after 2004 and for all other services immediately.)

very same effect as if the BOC were able to over-allocate its costs to regulated services. An example would be appropriate. As discussed above, the Florida Commission determined in 1999 that BellSouth incurred less than one cent of real costs per month to provide Call Waiting service. Yet in 1999, BellSouth charged its customers $4.00 per month for the service, producing a gross margin of $3.99. Given the technology involved, it is likely fair to assume that BellSouth's monthly costs for Call Waiting service have probably stayed constant (if not gone down) through 2003; however, BellSouth's Call Waiting monthly rate for its Florida customers has jumped to $5.50.[47] Under this assumption, BellSouth's monthly gross margin for Call Waiting service approximates $5.49.

A gross margin of $5.49 equates to $0.0432 per minute of interstate and international calling (hereinafter "interstate") per access line, per month, in Florida based on calling patterns in Florida.[48] This gross margin becomes a potential source of economic subsidy for competitive services. As more fully explained in Americatel's comments,[49] BellSouth and its long distance affiliate, BellSouth Long Distance Services ("BSLD"), working together as they do pursuant to FCC rules, could afford to charge their Florida customers who also subscribe to

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46 *Id,* at 32-3.

47 BellSouth General Subscriber Service Tariff (Fla. P.S.C.) §A13.9.3(A)(1)(c) (effective June 28, 2002).

48 According to ARMIS data, BellSouth's Florida customers made and received 18,131,560,000 minutes of interLATA toll calls in 2002 over their 5,953,460 switched access lines. For purposes of illustration, if one were to assume that these interLATA toll calls represented interstate and international toll calls and that BellSouth's interLATA toll call origination/termination ratio was one-to-one, approximately 127 minutes of interstate and international toll calls were made over each BellSouth switched access line in 2002. If one were to divide BellSouth's $5.49 monthly gross margin for Call Waiting by 127 interstate (and international) minutes of use per month, one would obtain a potential "contribution level" of $0.0432 per interstate minute of use per month, per access line.

Call Waiting approximately $0.04 cents per minute less for each interstate call made than they might charge another customer who does not also purchase Call Waiting, while remaining whole financially. BellSouth and BSLD could, if they so desired, price their services in this manner, while still complying with all applicable cost allocation rules. Cost allocation rules have much less impact when services are regulated based on a price cap plan, rather than on the carrier's actual costs incurred in providing those services.

Should a BellSouth residential customer also purchase Caller ID, , BellSouth and BSLD would have even more money to use for toll subsidies. In 1999, the Florida Commission determined that BellSouth's monthly cost to provide Caller ID service (including the Caller Name feature) was $0.2230.[50] BellSouth's monthly rate for this service was $7.50 in 1999, which produce a gross margin of $7.28 per month (3263%).[51] At the present time, BellSouth has raised its monthly rate for this Caller ID service to $7.95.[52]

The ability to engage in non-cost-based pricing for Caller ID service offers BellSouth and BSLD even more funds for subsidizing long distance rates without having to adjust a single cost allocation factor. The 1999 gross margin for Caller ID service equates to $0.0573 for each minute of interstate calling for the average Florida access line. This means that Florida's largest carrier and its long distance affiliate could afford to reduce long distance rates by more than five cents per minute for every customer willing to purchase Caller ID Deluxe

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49 Americatel's Corrected Comments, at 14-8.

50 *Florida Cost Report*, at 38.

51 *Id.*

52 BellSouth General Subscriber Service Tariff (Fla. P.S.C.) §A13.9.4(A)(8) (effective July 21, 2001).

service. When one applies this analysis to those BellSouth customers who purchase large bundles of local services, it is only a matter of time before BellSouth and BSLD will control almost all of the local and long distance markets that they elect to serve.

It is also clear that, if BellSouth's Florida rates were subject to rate-of-return regulation that also included a requirement that rates for individual services be based on or closely related to their actual costs, BellSouth would not be able to charge its Florida customers $5.50 per month for Call Waiting service or $7.95 per month for Caller ID service. If BellSouth were required to offer cost-based or cost-related rates for Call Waiting and Caller ID service, each of those prices would likely be well below $1.00 per month. Needless to say, in such a regulatory environment, BellSouth would not be making huge gross margins that could be used to assist BSLD offer low-ball long distance rates. Similarly, BellSouth would not be able to charge its customers high-margin prices for local service features if it truly faced strong competition similar to that which exists in the Florida wireless market where carriers regularly include both Call Waiting and Caller ID service in their most basic calling plans at no additional charge.

Since, under price cap regulation, the BOCs are able to charge prices that produce huge margins for many of their services, there is no need for them to attempt to move costs from unregulated to regulated services. Price cap regulation has permitted the BOCs to price most services without any regard to their underlying costs and to use the huge gross margins from those services to offer low-ball prices for competitive services.

III. Americatel's Previous Recommendations that the BOCs Must Not be Permitted to Offer Long Distance Services on an Integrated Basis and that More Regulations Should be Imposed on the BOCs Are Supported by AT&T's Economic Analysis

AT&T also proffered the declaration of a highly experienced and respected economist, Dr. Lee Selwyn. Americatel has reviewed Dr. Selwyn's declaration and generally endorses it as containing a more accurate description than the *BOC Declaration* of both the telecommunications market and state and federal regulation of that market. Dr. Selwyn's analysis speaks for itself and, as such, Americatel will not address most of the points made in the *Selwyn Declaration*. Rather, Americatel will comment on only a few of the conclusions made therein.

A. Independent Long Distance Carriers Cannot Compete with the BOCs' Service Bundles

Dr. Selwyn discusses the fact that the bundling of local and long distance services by the BOCs and other large ILECs has a created a situation where only those long distance carriers willing to become CLECs can compete with the BOCs.[53] Included in his analysis is the following statement: "By Verizon's own admission, only IXCs that bundle local and long distance services into the same service package can compete with its 'free' long distance calling plans."[54]

Standing alone, one might conclude that, if consumers truly want bundled services, only those carriers that become full-service providers should survive. However, that conclusion would ignore the still huge barriers to entry facing any carrier that desires to enter the local market.

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[53] *Selwyn Declaration*, at 46-7.

The BOCs' rhetoric on local competition is adorned with head counts of CLECs and other generally misleading statistics. From this, they argue that there are no true barriers for a long distance carrier to become a CLEC as well. However, this rhetoric is contradicted by the BOCs' own conduct in entering or, more accurately, in not entering other local exchange markets. The BOCs have simply not devoted any significant resources to competing with each other or any other ILEC for that matter, most likely because the BOCs can well-appreciate the barriers to entry posed by other ILECs or have even agreed tacitly to allocate markets, which would probably constitute a direct violation of the antitrust laws.[55]

For some BOCs, such as Qwest, their refusal to become a CLEC is overt. For others, such as SBC, their actions are more oblique. For example, as part of the Public Utilities Commission of Ohio's ("PUCO") approval of the SBC-Ameritech merger, SBC was ordered to compete with other Ohio ILECs as a CLEC in selected exchanges.[56] An SBC affiliate, SBC Telecom, Inc. ("SBCT"), has undertaken this task. However, SBC's most recent report to the PUCO clearly demonstrates SBCT's foot dragging in this effort to compete with other ILECs.

> Expansion into New Markets – SBC Telecom (SBCT), a separate affiliate of SBC/Ameritech, has worked diligently to meet the SBC/Ameritech merger commitment to offer local exchange service in four designated Ohio markets. Most significantly, SBCT has obtained tariff approval, obtained interconnection agreements with four ILECs in the state, has gained certification to operate as a CLEC in Ohio, and began offering service in the Delaware market on January 27, 2002, and in the Lebanon/Mason

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54 *Id.*, at 47.

55 *See* n.13, *infra.*

56 *In re Joint Application of SBC Communications, Inc., SBC Delaware, Inc., and Ameritech Ohio for Consent and Approval of a Change of Control*, Opinion & Order, Case No. 98-1082-TP-AMT (Ohio P.U.C. April 8, 1999) ("*SBC Ohio Order*").

> market on May 18, 2002. As required, the initial resale service offering includes resale of a basic POTS access line for residence and business customers. Entry into the two remaining markets, Cincinnati and Hudson/Twinsburg, is pending FCC approval of a request for a LATA waiver permitting the SBCT local calling areas in these markets to mirror that of the incumbent LEC.[57]

It is crystal clear that SBC is only slowly going through the motions of competing as an Ohio CLEC simply to satisfy the requirements of the PUCO. More significant is the fact that SBCT had not yet even entered the largest PUCO-required market for entry as a CLEC—Cincinnati. Given SBC's position as a world-class LEC that knows the local exchange business forward and backward, Cincinnati is a large market that should be attractive to SBCT if SBC truly viewed CLEC market entry as a reasonably workable strategy.

The plain and simple facts behind SBC's foot dragging in Ohio and Qwest Chairman Notebaert's "moral reluctance" to enter even the huge Chicago market are that the BOCs know the full extent of the actual barriers to successful local market entry and they are not willing to commit the resources necessary to assault those barriers successfully even though the BOCs are experts in the market. Interestingly, these are the very same BOCs that, earlier in the 1990s, spent hundreds of millions of dollars trying to enter the video programming markets—markets about which they knew virtually nothing. Yet today, the remaining BOCs, despite knowing the local exchange business forward and backward, have spent next to nothing to enter the local exchange business as CLECs.

Under these facts, it is unconscionable for the BOCs to suggest that any long distance carrier wishing to compete with the BOCs' bundled service offerings only needs to

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[57] Ameritech Ohio Third Annual Compliance Report Pursuant to Stipulation and Recommendation–Case No. 98-1082-TP-AMT , at 3 (filed November 15, 2002).

become a CLEC. The real question is: Will the FCC countenance that unconscionable behavior by loosening the already weak restrictions on the BOCs' provision of long distance services?

B. *There is a Compelling Case for the Re-Regulation of the BOCs' Provision of Billing and Collection Services*

Dr. Selwyn points out how the BOCs are unfairly providing low-ball billing and collection services to their long distance affiliates through volume discounts that are designed to favor those affiliates.[58] The BOCs offer this deregulated service to long distance carriers at market prices, which are, according to Dr. Selwyn, priced at an average of $1.00 per bill. Yet, the BOCs offer special volume discounts that do not seem cost-based to their affiliates that reduce the effective charge per bill to the BOCs' own affiliates well below what unaffiliated long distance carriers must pay.

Similarly, MCI documents the real lack of competition in the billing and collection market and the practice of the BOCs where they refuse to permit their competitors to include in their bills any statements not approved by the BOC.[59] This policy is used prevent other carriers from promoting their services to customers of theirs who are billed by the BOCs. Americatel made these same points, especially as they apply to dial-around carriers, in its initial filing.

Americatel submits that it is now time for the FCC to revisit it earlier decision to deregulate billing and collection services because of the BOCs' entry into the interLATA market. The market context for billing and collection services has changed radically since the FCC first

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58 *Selwyn Declaration*, at 65-7.

59 Comments of MCI, at 23-5.

proposed to detariff billing and collection services in 1985.[60] In 1985, the BOCs were not permitted to offer interLATA services. Therefore, the BOCs could not offer interLATA billing and collection services to themselves or to a corporate affiliate when the FCC decided to deregulate. In its *B&C Notice*, the Commission discussed the fact that it had earlier imposed a rate-of-return ceiling on billing and collection services because of its fear that the Bell System might seek to impose excessive costs on other service providers.[61] The FCC originally decided to regulate billing and collection services in order to prevent the BOCs and other ILECs from discriminating against some long distance carriers.[62] Since the BOCs were not in the interLATA business, there could be little potential for discrimination through unfair self-dealing by the BOCs. Therefore, the FCC decided to detariff billing and collection services, concluding that, under the operative facts at that time, billing and collection services were not common carrier services. However, it is unlikely that the FCC would have made the same decision if the BOCs or their affiliates had been permitted to provide interLATA services.

Now that the BOCs are "back in the interLATA business," it would seem appropriate for the FCC to reexamine whether billing and collection services should again be treated as a common carrier service.[63] Alternatively, the Commission should prohibit a BOC

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60 *Detariffing of Billing and Collection Services*, Notice of Proposed Rulemaking, 100 FCC 2d 607 (1985) ("*B&C Notice*").

61 *Id.*, at ¶2.

62 *Detariffing of Billing and Collection Services*, Report & Order, 102 FCC 2d 1150, at ¶5 (1986) ("*B&C Report*").

63 Also, the FCC should require all carriers, including the BOCs, to exchange customer billing information under specific parameters developed by the industry through the Ordering and Billing Forum ("OBF"), as previously requested by Americatel. Americatel's Petition for Declaratory Ruling (CG Docket No. 02-386) (filed September 5, 2002).

from providing billing and collection services for its own interLATA services or those provided by its affiliate.

C. *A Strong Need Exists for the Commission and/or PUCs to Investigate the Bundling of Services by the BOCs*

In its comments, Americatel discussed how the Australian Competition and Consumer Commission ("ACCC") has adopted rules that require incumbent carriers to provide documentation concerning their offering of service bundles and to provide that information to the ACCC for potential further action.[64] Americatel urged the FCC to adopt similar rules for the BOCs and either to regulate service bundles offered by the BOCs or to permit the PUCs to do so.[65] This additional regulation is necessary to prevent unfair cross-subsidization of competitive long distance services by the BOCs as discussed by Dr. Selwyn.

Through the *Selwyn Declaration*, AT&T has provided strong evidence supporting adoption of Americatel's recommendation on bundling. Dr. Selwyn identifies a bundling problem created by Verizon in Virginia. He presented information about two of Verizon's bundles of services: 1) the Local Package Plus (a package of local services) and Voice Mail Service, which together are priced at $39.45 per month; and 2) Veriations Freedom^sm Local Package Plus (the same package of services as the Local Package Plus, with Voice Mail service, and unlimited intraLATA toll service), which is priced at $39.95 per month.[66] Therefore, the effective price for unlimited intraLATA toll in the Veriations Freedom^sm package is fifty cents per month. What is more, Dr. Selwyn demonstrates, using Verizon's own data and

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64 Corrected Comments of Americatel, at 31-2.

65 *Id*., at 32-3.

66 *Selwyn Declaration*, at 82.

representations, that the imputed access charge cost for those intraLATA toll calls approximates $22.50 per month.[67] Verizon need not part with any cash, it merely needs to impute the price of the access charges to its long distance affiliate's rates.

Of course, Verizon's competitors, including Americatel and AT&T, would be required to pay Verizon real cash were they to offer a competing plan. This bundling constitutes bald discriminatory conduct on the part of Verizon, which would clearly seem to violate the requirements of Section 272(e)(3) of the Communications Act of 1934, as amended ("Act").[68] That section requires that a BOC must charge its affiliate or "impute to itself, an amount for access to its telephone exchange service and exchange access that is no less than the amount charged to any unaffiliated interexchange carriers for such service." This situation requires an immediate investigation.

D. The Commission Must Decide Whether it Desires a Long Distance Market with the BOCs Having Market Shares of 50-60% or Whether it Desires a Competitive Long Distance Market Similar to that in Chile, the HomeBase of Americatel's Parent

AT&T documented the success of the BOCs to grow long distance market share at unprecedented rates once they became able to market local and long distance services jointly. In contrast to the post-Divestiture market, where it took all non-AT&T long distance carriers five years after the implementation of equal access by the LECs to reach 22.92% of all presubscribed lines, Verizon was able to capture 34.2% of the interLATA service market in New York within two years of receiving Section 271 authority.[69] SBC predicts that, based on its experience in

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67 *Id.*, at 83-4.

68 47 U.S.C. §272(e)(3).

69 *Selwyn Declaration*, at 52 (internal citations omitted).

Connecticut, where it operates the state's largest LEC, it will ultimately have a long distance market share of 60% in all of its states.[70]

In contrast, Chile, home to Americatel's parent corporation, ENTEL Chile, has a much more robust long distance market in both the national and international segments. The following data calculated by ENTEL Chile in January 2003 shows market shares of the largest long distance carriers based on minutes of traffic. What is even more significant is the fact that long distance competition in Chile did not truly begin until 1994, when Chile's regulatory agency, Subtel (Subsecretaría de Telecommunicaciones de Chile), issued eleven new long distance carrier licenses to compete in what had been ENTEL's monopoly market.

[70] *Id.*, at 6. This too demonstrates the importance of a carefully delineated geographic market in which to measure the existence of competition.

Table 1

Shares of the National Long Distance Market in Chile							
Year	**Entel**	**CTC Mundo**	**Chilesat**	**BellSouth**	**CNT**	**VTR**	**Others**
1997	39.5%	33.8%	15.5%	1.2%	3.4%	3.1%	3.5%
1998	40.5%	33.9%	13.8%	1.0%	3.8%	2.5%	4.5%
1999	38.0%	31.8%	18.9%	1.6%	3.6%	2.8%	3.3%
2000	40.0%	33.0%	15.0%	1.8%	4.1%	2.6%	3.5%
2001	37.6%	35.3%	14.3%	1.6%	4.8%	2.8%	3.6%
2002	37.2%	37.5%	13.2%	1.7%	4.4%	2.9%	3.1%

Table 2

Shares of the International Long Distance Market in Chile							
Year	**Entel**	**CTC Mundo**	**Chilesat**	**BellSouth**	**CNT**	**VTR**	**Others**
1997	30.9%	22.3%	18.1%	11.1%	1.3%	9.3%	7.0%
1998	34.9%	23.3%	16.5%	9.6%	1.6%	7.1%	7.0%
1999	35.5%	22.8%	19.5%	9.4%	1.6%	6.0%	5.2%
2000	37.1%	22.7%	16.4%	8.0%	2.6%	6.2%	7.0%
2001	37.6%	23.1%	17.5%	6.5%	2.4%	5.1%	7.8%
2002	38.9%	27.1%	12.5%	6.1%	2.3%	5.2%	7.9%

The Chilean long distance market, in both its domestic and international segments, is clearly more competitive than the long distance market in Connecticut, for example.[71] CTC Mundo, which is an affiliate of Chile's dominant local exchange carrier, Telefónica CTC Chile, has proven to be a strong competitor in the long distance market. However, in large part because of the sturdy, pro-competitive rules imposed and enforced by Subtel, Chile's telecommunications regulatory agency, CTC Mundo has not been able to

[71] Given SBC's market share in Connecticut and Texas (21% within nine months of the date it received Section 271 authority to provide interLATA services) and Verizon's 34.4% share of the New York interLATA market two years after entry, Americatel simply does not understand BellSouth's remarks that the interLATA market shares "held by the BOCs, collectively and individually, is modest. Comments of BellSouth, at 7. To the extent that SBC's predictions of a 50-60% market share in its states are applicable to the other BOCs, such shares could fairly be considered as "modest" only by BOC standards. In order to prevent such a result, which, in turn, would likely result in higher prices for consumers, the Commission must take action now to restrain the anti-competitive intentions of the BOCs.

dominate Chile's long distance market. Similarly, ENTEL Chile, the former monopoly long distance carrier, remains a formidable toll service provider, but must compete vigorously every day on price and service in order to maintain itself as an important carrier in the marketplace.

The Chilean National Congress has enacted strong regulatory requirements to protect and stimulate long distance competition, and requirements are vigorously enforced by Subtel. These strict requirements include: 1) fixing exchange access charges at the LEC's incremental costs; 2) regulatory agency enforcement of short time limits for a LEC to interconnect with and provide access services to long distance carriers; 3) the mandatory provision of Billing and Collection services by a LEC to long distance carriers, together with the inclusion of long distance charges for all carriers on the LEC's billing invoice; 4) the obligatory disconnection of all services when long distance charges are not paid in full;[72] 5) the mandatory provision of all relevant information by the LEC about individual customers' network usage to competing carriers;[73] 6) on-going monitoring by Subtel of long distance competition; and 7) aggressive prohibition against the dominant LEC's provision of long distance services on an integrated basis.

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[72] ENTEL has found that the serving LEC's ability and responsibility to disconnect local service for the non-payment of toll charges is critical to the maintenance of a fully competitive long distance market and, ultimately, the lowest possible prices for all consumers. Accordingly, both the FCC disconnection policy in an effort to provide maximum consumer benefits from long distance competition.

[73] Americatel realizes, of course, the information with respect to an individual customer's network usage would constitute CPNI that cannot be released to other carriers without the affected customer's approval. At the same time, it would be quite simple for that type of information to be shared by the BOC with its affiliate, such that the Commission should step up its audits of BOC compliance with the CPNI rules. However, the FCC should still adopt a rule that would require the BOCs to provide competing carriers with all customer information that would not violate applicable CPNI rules in order to promote long distance competition.

Which marketplace—one like Connecticut or one like Chile—would best serve the American public? Americatel submits that the answer is clearly "Chile."

IV. Even the Largest Customers Are Mortally Fearful of the BOCs' Market Power

As evidenced by the comments of the Ad Hoc Telecommunications Users Group ("Ad Hoc"), even the largest private sector consumers of telecommunications services are mortally fearful of the BOCs' market power. Ad Hoc notes that its membership would be the first beneficiaries of deregulation of the BOCs' interLATA services market if that market were truly competitive. Ad Hoc's members, as heavy consumers of telecommunications services, are in the best position to negotiate the most favorable prices for the BOCs' services in a competitive market.[74] These very large consumers do not, however, see the market as sufficiently competitive to trust market forces to prevent the BOCs from price gouging. Ad Hoc states as follows: "[L]ocal markets are not yet sufficiently competitive for market forces to discipline prices and stimulate demand-responsive service innovation. As a result, ILECs have the ability to leverage their market power in the local exchange and exchange access markets in order to obtain anti-competitive advantages in long distance markets."[75]

Even more compelling is the reason why the large end user customers are afraid of the BOCs' behavior and market power. Ad Hoc notes that, upon receiving FCC permission to price Special Access services on a flexible basis, the BOCs immediately raised the rates for these services.[76] One would think that, if the local exchange and exchange access market were truly

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[74] Comments of Ad Hoc, at 2-3.

[75] *Id*., at 3.

[76] *Id*., at 4-5.

competitive, the BOCs would have lowered their prices for Special Access services. The plain truth is that the BOCs simply do not face adequate competition in any market, with adequate competition being defined as a level of competition that is sufficient to force down their prices for service in a manner that is similar to what has regularly occurred in the wireless service market. Unless the FCC maintains a requirement for the BOCs to provide long distance services only through a separate affiliate; imposes new rules on the BOCs and their affiliates, as recommended by Americatel; and vigorously enforces those regulations, the BOCs will soon re-monopolize the entire long distance market.

V. <u>If Competition is to Survive, Much Less Flourish, the Commission Must Impose More, and not Less, Regulation on the BOCs</u>

From the perspective of the BOCs' competitors, their customers, and even state officials,[77] the FCC's relaxation of any existing regulations on the BOCs' provision of long distance services would be similar to the California Board of Prison Terms voting to grant a parole to Charles Manson, convicted killer of actress Sharon Tate and six other people. The California Board has repeatedly denied Mr. Manson's many parole requests because the Board simply does not believe that the public would be safe with Charles Manson on the streets of California, based in part, on his post-conviction conduct. After the Board denied Manson's tenth request in April 2002, Los Angeles Assistant District Attorney Stephen Kay stated that: He's [Manson] really not much different than he was in 1969 or 1970."[78]

Given the reasoned opposition from every party except the BOCs and the United States Telecom Association ("USTA") and the BOCs' long history of anti-competitive conduct,

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[77] *See generally,* Comments of the New Jersey Ratepayer Advocate; Comments of the Texas Attorney General; Comments of the Texas PUC.

both post-1984 Divestiture and post-1996 Telecommunications Act,[79] there simply are no reasons why the FCC should trust the BOCs to behave in a –pro-competitive manner. A truly competitive long distance market that is more like Chile than Connecticut is not safe without continued strong regulation of the BOCs. The public interest would strongly be harmed were the Commission to relax any existing regulations on the BOCs' provision of long distance services.

VI. Conclusion

The BOCs should not be permitted under any circumstances to offer interstate and international, interexchange services on an integrated basis. Moreover, in light of the BOCs' continuing record of anti-competitive conduct and evidence submitted to the Commission in this proceeding, the FCC should promptly adopt and release a second further notice of proposed rulemaking to consider the imposition of additional regulations on the BOCs in order to prevent their re-monopolization of all wireline services within their local exchanges. Americatel submits that the following items should be included in such second further notice:

- The BOCs should not be permitted to offer interstate and international, interexchange services on an integrated basis.
- In view of the numerous concerns about the joint anti-competitive collaboration between the BOCs and their long distance affiliates, those affiliates, like the BOC local service provider, should be classified as "Dominant Carriers" for the provision of in-region long distance services.
- The Commission should prohibit any cross-subsidies between bundled services and either regulate the bundling of services by the BOCs in a manner similar to the regulation of bundling in Australia or permit the PUCs to do so, in order to prevent any cross-subsidies of competitive services.

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78 http://www.cbsnews.com/stories/2002/04/25/national/main507237.shtml (visited July 17, 2003).

79 *See* Corrected Comments of Americatel, at 23-9.

- The Commission should consider imposing further restrictions on the BOCs as has occurred in Chile with considerable success in increasing competition, including:
  - the mandatory provision of billing and collection services to all carriers on the same terms and conditions that the BOCs provide those services to their affiliates, including the requirements to bill long distance competitors' charges on the same invoice as the BOC's own charges and to disconnect all services for non-payment of long distance charges;
  - the re-targeting of BOC price cap indices and access charges to the authorized rate of return and the imposition of a requirement that access charges be based on the BOCs' incremental costs to provide network connections;
  - the institution of streamlined procedures within the Enforcement Bureau's Investigations and Hearings Division to investigate and prosecute, when appropriate, any problems related to the interconnection of competitors to a BOC's network, as well as other aspects of long distance competition;
  - additional Commission oversight of the BOC's compliance with the Commission's rules for sharing CPNI with their long distance affiliates; and
  - the mandatory disclosure by the BOCs to competing carriers of all customer information in their possession that would not be inconsistent with the CPNI rules so that all long distance carriers can compete on a level playing field.

- In addition to previously listed requirements for the BOCs and in light of the BOCs' ongoing record of anti-competitive conduct, the Commission could also consider whether the BOC's affiliate should also be required to have an appropriate level of independent ownership as previously recommended by Americatel.

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Dated: July 28, 2003

CERTIFICATE OF SERVICE

I, Lila A. Myers, do hereby certify that the foregoing **REPLY COMMENTS OF AMERICATEL CORPORATION** was served on this 28th day of July, 2003 upon the following in the fashion indicated:

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