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

In the Matter of	)	
	)	
Special Access Rates for Price Cap Local Exchange Carriers	)	WC Docket No. 05-25
	)	
AT&T Corp. Petition for Rulemaking to Reform Regulation of Incumbent Local Exchange Carrier Rates for Interstate Special Access Services	)	RM-10593
	)	

Comments of CompTel/ALTS, Global Crossing North America, Inc., and NuVox Communications.

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SUMMARY

Over the past few years, the Bells have had great success in eliminating access to their networks with the mantra "old wires, old rules." Interestingly enough (though hardly surprising), the Bells have consistently and scrupulously avoided this argument with respect to the oldest wires of all – the pre-Telecom Act special access regime. Instead, for these oldest-of-old wires, the Bells have, for all practical purposes, argued for "old wires, no rules." However, even the Bells' opportunistic policy advocacy through sloganeering must be held to some standards of consistency for the Commission's previous policy determinations to maintain a level of integrity. Thus, it is time for the Commission to give the Bells what they have been asking for and to "level the competitive playing field" – by substantially overhauling the BOCs' special access regime.

Special access services are a critical input for virtually every telecommunications or information service in the country. CompTel/ALTS members are major purchasers of BOC special access, which they use to provide downstream services, increasingly in direct competition with the BOC or BOC affiliate. CompTel/ALTS members also seek to provide wholesale competitive alternatives to BOC special access services. In either case, BOC abuses of the Commission's special access pricing make it increasingly difficult to compete with the BOC in wholesale and retail markets. The Commission must address these abuses quickly and comprehensively.

The case for a comprehensive revision of the special access pricing regime is compelling and undeniable. The evidence previously submitted in this and related proceedings, and as supplemented by these comments, overwhelmingly demonstrates that

the Commission's experiment with special access deregulation has been a dismal failure resulting in dramatic price increases and a substantial loss of consumer benefit. BOC special access rates are excessive, resulting in rates of return that vastly exceed any reasonable level. BOCs have used their Phase II pricing flexibility not to lower rates to meet competition, but to sustain rates well in excess of price cap levels. Whereas the rest of the industry largely has moved to distance insensitive pricing, the BOCs continue to impose high mileage charges that unreasonably increase the costs of lengthy transport facilities.

BOCs continue to have market power in special access services, requiring robust regulation over pricing and terms and conditions.[1/] This market power is derived from the undeniable fact that they are the only carrier that can provide access in many cases, and the only carrier that can provide ubiquitous access in all cases. BOCs are using their market power to impose exclusionary terms and conditions in their special access discount plans that lock up demand and undermine the very competition the Commission ostensibly seeks to foster. The BOCs confront carriers with the Hobson's choice of sky-high monthly rates or substantial discounts in exchange for promises to keep all or virtually all of their demand throughout the BOC region on the BOC networks for long periods of time. Once in such plans, termination and shortfall penalties make it virtually impossible to shift demand to competitive carriers. Through these types of pricing plans,

[1/] The Bell companies clearly recognize the need for regulation where there is market power. In the intercarrier compensation proceeding, for example, the Intercarrier Compensation Forum (ICF), which includes SBC, calls for continued prescription of termination rates. *Developing a Unified Intercarrier Compensation Regime*, CC Docket No. 01-92, Comments of the Intercarrier Compensation Forum (filed May 23, 2005).

the BOCs leverage their ubiquity in urban, suburban, and rural areas to preclude or minimize the ability of customers to utilize competitive supply where it is available.

These well-documented abuses require a substantial and broad re-assessment of the special access regime. CompTel/ALTS, Global Crossing, and NuVox (collectively referred to herein as "CompTel/ALTS") propose a series of interdependent reforms designed to support competition in the broad array of services that rely on special access and in the wholesale market for special access. First, the Commission must re-initialize price caps at reduced levels that will foster competition in downstream markets. CompTel/ALTS respectfully urges the Commission to explore the use of competitors' prices as a benchmark for new price cap special access rates. Use of competitors' prices has significant advantages over traditional ratemaking approaches. Traditional ratemaking, including price caps, attempts to mimic rates and rates of return that could be charged in a competitive market, but are not intended to actually foster the competition that could ultimately eliminate the need for prescriptive rate regulation. With the substitution of special access for unbundled network elements as the input for competing in virtually all downstream markets, the Commission must ensure that special access rates foster such competition.

Re-initializing rates is not sufficient if BOCs escape regulation in an increasing number of Phase II pricing flexibility areas, despite their continuing market power. Phase II pricing flexibility must be eliminated and the newly initialized price caps must be extended to all services now deregulated under Phase II. There is no reasonable pricing flexibility "fix" in terms of adjusting the geographic market or proxy triggers that effectively can cabin BOC market power. Pricing flexibility instead should be limited to the ability to actually lower prices where necessary to meet competition and then only so long as the BOC makes such lower prices reasonably available to similarly situated customers.

Equally important is the elimination of exclusionary discount pricing plans that lock up demand for special access services. The Commission should declare those practices unlawful so as to unlock demand and thus foster competitive entry. Carriers must be permitted to opt out of such plans under reasonable terms and conditions.

Finally, the Commission immediately should adopt interim relief to curb the most excessive abuses. This includes placing a moratorium on new Phase II pricing flexibility, imposing price caps in current Phase II areas, and adjusting those price caps by, at a minimum, restoring the last judicially approved productivity factor.

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CompTel/ALTS, Global Crossing North American, Inc., on behalf of its U.S. operating subsidiaries ("Global Crossing"), and NuVox Communications ("NuVox"), submit their initial comments in the above-captioned proceedings. CompTel/ALTS was formed in March 2005 by the merger of CompTel/ASCENT and the Association for Local Telecommunications Services ("ALTS"). With more than 300 members, CompTel/ALTS is the leading industry association representing competitive, facilities-based telecommunications service providers, emerging VoIP providers, integrated communications companies, and their supplier partners. CompTel/ALTS members both purchase Bell Operating Company ("BOC") special access services as a critical input to their own service offerings and seek to provide competitive wholesale alternatives to BOC special access service. Global Crossing and NuVox are CompTel/ALTS members that rely on special access services.

Global Crossing provides telecommunications solutions over the world's first integrated global Internet Protocol-based network to business customers. Its core network connects more than 300 cities in 30 countries worldwide, and delivers services to more than 500 major cities, 50 countries, and 6 continents around the globe. Global Crossing offers a full range of managed data and voice products to enterprise customers, governments, system integrators, carriers, and ISPs. Global Crossing relies heavily on BOC special access "last mile" services to reach its domestic end users. The company, for example, purchases over $100 million of special access services annually from SBC alone. Moreover, given the services that it provides, unbundled network elements (UNEs) are not viable alternatives to special access services for Global Crossing.

Unlike Global Crossing, NuVox provides local exchange service, relying predominantly on UNEs to access its small to medium sized business customers. Notwithstanding its reliance on UNEs, NuVox historically has purchased special access services to reach its customers under some circumstances. Moreover, with the recently adopted restrictions on high capacity UNE transport and loop availability, NuVox anticipates its reliance on special access services to increase substantially. In order to remain competitive in the local exchange market, NuVox must have access to BOC special access services at reasonable rates and pursuant to reasonable terms and conditions.

I. The BOC Special Access Regulatory Regime Must Be Substantially Revised

The current regulatory regime governing BOC special access services has resulted in grossly excessive rates, premature deregulation, and the development of exclusionary pricing plans that undermine facilities-based competition and harms business end users of all sizes.[2/] At bottom these problems are all a reflection of the BOCs' continuing market

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[2/] *See, e.g., SBC Communications, Inc. and AT&T Corp. Applications for Approval of Transfer of Control*, WC Docket No. 05-65, Reply Declaration of Susan M. Gately on Behalf of Ad Hoc Telecommunications Users Committee at 4-5, ¶ 6 (filed May 10, 2005) ("*Gately Reply Declaration*") (reporting that business and government customers are power over special access services. The evidence substantiating the existence of these problems is set forth in this section and proposed remedies follow in section II.

A. Special Access Rate Elements

Before reviewing the evidence that the current special access pricing regime is broken, we address a recurring question posed by the Commission because of its central importance. Throughout the *Special Access NPRM*, the Commission seeks comment on whether it should distinguish among (1) special access channel terminations used between the BOC wire center and the customer premises, (2) special access channel terminations between an IXC POP and the BOC serving wire center (*i.e,* an entrance facility), (3) or any other special access "product market" (*e.g.,* interoffice mileage).[3/] These distinctions may well serve useful purposes in term of developing rules to guard against BOC abuses. For example if the Commission determines to maintain some type of Phase II pricing flexibility, which CompTel/ATLS opposes, the Commission should at a minimum require evidence of competition for each of these three product subcategories prior to any regulatory relief. Evidence of competition for entrance facilities, for example, cannot justify relief for special access channel terminations between the BOC wire center and the customer premises.

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being overcharged $17.5 million per day because of excessive special access rates of return).

3/ *See, e.g., Special Access Rates for Price Cap Local Exchange Carriers*, WC Docket No. 05-25, Order and Notice of Proposed Rulemaking, 20 FCC Rcd. 1994, 2013-14, ¶ 51 (2005) ("*Special Access NPRM*") (seeking comment on whether to establish separate special access pricing basket categories predicated on those distinctions); *Id*. at 2022-23, ¶¶ 81-82 (seeking comment on whether channel terminations to the customer, channel terminations to the POP or other special access facilities (interoffice transport) constitute separate product markets).

Moreover, current pricing structures enable BOCs to impose grossly excessive mileage charges for the interoffice rate element. BOC special access rate structures must be brought into line with industry pricing that is becoming increasingly distance insensitive. BOC special access services remain one of the last bastions of distance sensitive pricing and mileage charges are often the primary reason why special access rates vastly exceed forward looking costs or competitors' pricing. The ability of BOCs to extract grossly excessive mileage fees is a direct reflection of continuing BOC dominance over last-mile access services.

B. BOC Special Access Rates Are Excessive

There is no question that current BOC special access rates are grossly excessive. As stated in the *Notice*, "the BOCs have earned special access accounting rates of return substantially in excess of the prescribed 11.25 rate of return that applies to rate of return LECs."[4/] BOC rates of return have increased year after year,[5/] and the trend of ever increasing returns continued in 2004. As noted in a recent filing by the Ad Hoc Telecommunications Users Committee, BOC rates of return for 2004 reached all time highs.[6/] Rates of return for RBOCs in 2004 were as follows: Verizon 31.5%, SBC 76.2%, Qwest 76.8%, and BellSouth 81.9%.[7/] The average for the four BOCs was 53.7%.[8/] The result of these excessive rates of return has been a substantial transfer of

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4/ *Special Access NPRM* at 2009, ¶ 35.

5/ *Id*. at 2009, ¶ 35 (identifying accounting rates of return for the years 1998 to 2003 of 18, 23, 28, 38, 40, 44 percent, respectively).

6/ *Gately Reply Declaration* at 5-9 (filed May 10, 2005).

7/ *Id*. at 8.

8/ *Id*.

wealth from special access customers to the BOCs and a concomitant loss of consumer benefit.[9/]

The BOCs have argued that accounting rates of return are not a reasonable measure of their economic returns because of cost allocation issues.[10/] Anticipating such arguments, the *Gately Reply Declaration* demonstrates that costs actually have been over-allocated to special access services, indicating that accounting rates of return may in fact *understate* BOC returns.[11/] Moreover, in other contexts, the BOCs have embraced these numbers.[12/]

Regardless of cost allocation questions – and the Commission has invited the BOCs to re-run the numbers after removing any expenses and investments they believe are not directly assignable,[13/] – the Commission correctly points out that the year over year numbers demonstrate a relationship between demand growth and growth in expenses and investment that "suggest [] that the BOCs realized scale economies."[14/] In other words, the BOCs can meet ever-increasing demand for their special access services on an

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9/ *See, e.g., Id*. at 4-5, ¶ 6 (reporting that excessive BOC returns result in business and government customers being overcharged $6.4 billion, or $17.5 million per day).

10/ *Special Access NPRM* at 2007, ¶ 29.

11/ *Gately Reply Declaration* at 9-10 (pointing out that almost one-third of total interstate investment is found in the special access category, even though special access lines only accounted for 2.5% of total RBOC access lines). *See also AT&T Petition for Rulemaking to Reform Regulation for Incumbent Local Exchange Carrier Rates for Interstate Special Access Services*, RM 10593, Reply Comments of AT&T Corp. at 38 (filed Jan. 23, 2003) ("*AT&T Reply Comments*") ("[I]t appears that the Bells' [sic] are over-allocating costs to the special access accounts.").

12/ *See AT&T Reply Comments* at 36 ("[T]he Bells' [sic] consistently champion the use of the ARMIS data as an accurate measure of returns when such use in to their advantage.").

13/ *Special Access NPRM* at 2007, ¶ 29.

14/ *Id*. at 2006-07, ¶¶ 27, 29.

incremental cost basis, and the failure of the BOCs to flow through its economies of scale to the consumer and carrier market has led to excessive rates of return. In a competitive market, or even under the Commission's previous price cap rules, such efficiency gains would be passed along to the consumer in the form of lower prices.[15]

The BOCs' excessive rates of return for special access services are indicative of two particularly problematic aspects of the current regime – premature deregulation that has resulted in sustained price increases for services subject to Phase II pricing flexibility, and supra-competitive rates for mileage. These issues are discussed below.

C. The Evidence Shows that BOCs Have Imposed and Sustained Higher Rates Where They Have Received Pricing Flexibility

The Commission seeks comment on whether there have been substantial and sustained price increases for BOC special access services in defined markets. The evidence already submitted in the record demonstrates that BOC special access rates in price flexibility MSAs have exceeded price caps on a sustained basis. Further evidence is provided herein by Global Crossing.

Given its reliance on BOC special access services,[16/] Global Crossing closely tracks BOC special access pricing and has done so for years. Based on its review, BOC special access prices in price flex MSAs consistently exceed price cap rates for the same services. Table 1, of the attached declaration of Janet S. Fischer[17/] provides a snapshot

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15/ *AT&T Reply Comments* at 29 ("[I]n competitive markets, a decline in costs should lead to *lower* prices." (emphasis in original)).

16/ Global Crossing spends more than $100 million per year just for SBC's special access services. *SBC Communications Inc. and AT&T Corp. Applications for Transfer of Control*, WC Docket 05-65, Comments of Global Crossing North America, Inc., at 2 (filed April 25, 2005).

17/ *Special Access Rates for Price Cap Local Exchange Carriers*, WC Docket No. 05-25, Declaration of Janet S. Fisher on Behalf of Global Crossing North America, Inc., comparison of BOC special access pricing for DS1 and DS3 channel terminations and mileage under price caps and pricing flexibility. The table shows the range of pricing disparity between price cap and pricing flexibility rates expressed in percentage terms. Thus, for example, DS1 channel terminations are 22% to 47% higher in Qwest price flex MSAs than under Qwest's price caps, and DS1 mileage rates are 13% to 71% higher in BellSouth price flex MSAs than under BellSouth's price caps.

Tables 2 and 3 of the *Fisher Declaration* also compare price cap and price flex rates at a point in time and similarly show, in bar graph form, that rates in areas where the BOCs have received pricing flexibility are either the same, or, much more often, higher, than the rates for comparable services under BOC price caps. For example, DS1 channel termination monthly rates are $112.30 under Qwest's price caps and $165.00 in price flex MSAs. Similarly, Verizon's price cap monthly rate for a DS1 channel termination is $197.00, but $225.63 under pricing flexibility. The same pattern holds true for the mileage component of special access rates. SBC/PacBell's monthly price cap rate for DS1 mileage, computed on a per DS0 circuit mile equivalence, is $0.58, but $0.79 under price flexibility. Verizon's monthly price cap for the same service is $0.99 under price caps, but $1.37 in areas under pricing flexibility. Similar disparities exist for DS3 circuits.[18/]

Tables 4 through 7 track special access price capped and pricing flexibility rates over time. These charts demonstrate that rates in price flex areas have persistently exceeded price capped rates for the same services, whether compared on a monthly basis

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at Table 1 (filed June 13, 2005, as an attachment to these comments) ("*Fischer Declaration*").

[18/] *Id*. at Table 2, Table 3.

or under term plans. Table 4, for example, tracks BellSouth special access rates from July 1997 to June 2005.[19/] The graphs show that price capped rates were trending down throughout the period for DS1 and DS3 rate elements, both channel terminations and mileage. (The sole exception is the price cap rates for BellSouth DS1 channel terminations, which remained flat until July 2001, then began to decline while price flex rates increased). Once pricing flexibility was granted, the downward trend stopped for deregulated rates. While price capped rates continued to decline, deregulated rates either remained flat (leading to an increasing disparity), or increased. Similar trends appear for each of the RBOCs.[20/] This data is significant, as it shows that prices for services subject to Phase II pricing flexibility exceed, an a sustained basis, rates for the same services under price cap regulation.

The Global Crossing data are fully consistent with evidence previously submitted in response to AT&T's petition and in other proceedings. AT&T, for example, submitted an extensive analysis of price cap versus price flexibility rates in the Triennial Review Remand proceeding.[21/] The *Stith Reply Declaration* compares special access monthly and term plan rates by state for identical DS1 and DS3 circuits both before and after price flexibility. Dr Stith's analysis, comparing rates from May 1, 2001 to August 31, 2004, found that pricing flexibility rates have seen few decreases, and those were nowhere near

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19/ Id. at Table 4.

20/ *See Id*. at Tables 4 through 7.

21/ *See Unbundled Access to Network Elements*, WC Docket No. 04-313, Reply Comments of AT&T Corp., Declaration of M. Joseph Stith (filed Oct. 19, 2004) ("*Stith Reply Declaration*"). *See also AT&T Petition for Rulemaking to Reform Regulation for Incumbent Local Exchange Carrier Rates for Interstate Special Access Services*, RM 10593, Ex Parte Submission by AT&T Corp., Declaration of M. Joseph Stith (filed Dec. 7, 2004) (submitting this declaration in this proceeding).

the decreases under price caps.[22/] Dr. Stith also found that the decreases that occurred under price caps are attributed largely, if not wholly, to the effects of regulation. *Id.*

Similarly, the Ad User Telecommunications Users Committee recently compared monthly rates for a ten-mile DS1 circuit offered by SBC under price caps and in pricing flexibility areas from 2001 through 2004.[23/] That analysis showed that SBC charged customers in price flex areas prices that were more than 25% higher than the prices subject to price cap regulation.[24/]

D. BOC Supra-Competitive Profits Are Greatest In the Mileage Component of Special Access

CompTel/ALTS has already pointed out in this proceeding that one aspect of the BOCs' anticompetitive strategic pricing behavior involves extracting the bulk of their supra-competitive profits from the distance sensitive component of their special access pricing.[25/] Similarly WorldCom has noted that, "[u]nder price cap regulation, the BOCs have chosen to pursue a pricing strategy in which their customers pay outrageously high per-mile rates for transport, despite the fact that the rest of the telecommunications industry has long recognized that, once a network is built, transport costs are largely

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22/ *Stith Reply Declaration* at 2, ¶ 5.

23/ *Gately Reply Declaration* at 13, Fig. 3.5.

24/ *Id*. at 13-14, ¶ 17. *See also AT&T Petition for Rulemaking to Reform Regulation for Incumbent Local Exchange Carrier Rates for Interstate Special Access Services*, RM 10593, Reply Comments of AT&T Corp., at 20-27 (filed Jan. 23, 2003) (discussing BOC failure to reduce special access prices in price flex areas).

25/ *AT&T Petition for Rulemaking to Reform Regulation for Incumbent Local Exchange Carrier Rates for Interstate Special Access Services*, RM 10593, Comments of the Competitive Telecommunications Association, at 5 (filed Dec. 2, 2002).

distance-insensitive."[26/] BOCs have been able to impose supracompetitive mileage rates because they face little, if any, competition on longer routes.

In its analysis, WorldCom compared UNE prices to special access prices disaggregated by loops/channel terminations, fixed transport charges, and per mile transport charges for DS1 and DS3 circuits of varying length. The analysis found relatively smaller variances between UNE and special access loop/channel termination and fixed transport charges.[27/] The major variance occurred with respect to interoffice mileage. For example, the average DS1 UNE per mile charge was $1.52 versus $13.72 for special access, for DS3s, UNE mileage was $23.35 versus $57.84 for special access DS3 mileage.[28/]

NuVox pointed out similar disparities in its comments in the Triennial Review Remand proceeding. There it noted that, in Atlanta, the mileage component of a 10-mile (UNE) EEL was $1.80 whereas BellSouth charged $180.00 in mileage under month-to-month special access prices or $80.00 under BellSouth's special access discount plan for the same 10-mile facility. Similar disparities existed in Southwestern Bell and Ameritech

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[26/] *Review of the Section 251 Unbundling Obligations of Incumbent Local Exchange Carriers*, CC Docket No. 01-338, Ex Parte Submission of WorldCom, Inc., at 7 (filed Oct. 29, 2002) ("*WorldCom Ex Parte*").

[27/] The analysis found that DS1 UNE loops were about 18% less than comparable special access prices and DS3 UNE loops 28% less. The fixed portion of transport under UNEs was about 10% less for DS1s and the fixed DS3 transport UNE prices were actually higher than special access. *Id*.

[28/] *Id*.

states.[29/] Additionally, NuVox found that BellSouth's mileage costs were twice as high in price flex MSAs ($8.00 per mile) than under price caps ($3.90 per mile).[30/]

The Global Crossing data discussed above makes the same point. Table 8 of the *Fisher Declaration*, for example compares DS1 charges for 10-mile and 30-mile circuits. Whereas the competitors' charges increase somewhat between the 10-mile and the 30-mile circuit, BOC charges substantially increase between the two, and in each the charge is higher still for pricing flexibility rates than under price cap rates.[31/]

E. BOC Market Dominance Enables the Imposition of Exclusionary Terms and Conditions in Tariffs and Pricing Flexibility Contracts

BOCs have been able to entrench their market power by adopting pricing plans in their tariffs and pricing flexibility contracts that effectively lock up demand and undermine the ability of carriers to reach sufficient scale to become effective competitors either by deploying their own facilities (for self-supply or to wholesale) or by migrating to alternative networks. If the Commission permits the BOCs to continue the practices discussed below, then eventually all competitors will simply be forced to resell the BOCs' network.

There is already substantial evidence in the record of the exclusionary nature of certain BOC discount plans. For example, the Declaration of Michael D. Pelcovitz, filed with WorldCom's Reply Comments in this proceeding,[32/] explained the exclusionary

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29/ *Unbundled Access to Network Elements*, WC Docket No. 04-313, Initial Comments of NuVox, Inc., at 21-22, 33-34 (filed Oct. 4, 2004).

30/ *Id.* at 22.

31/ *Fisher Declaration* at Table 8.

32/ *AT&T Petition for Rulemaking to Reform Regulation for Incumbent Local Exchange Carrier Rates for Interstate Special Access Services*, RM 10593, Reply effect of BOC commitment plans. As explained by Dr. Pelcovitz, the key to exclusionary pricing under these plans is the ability to "condition the pricing on the monopoly portion of the customer's demand on the choices the customer makes for the competitively sensitive portion of demand," so that the customer pays a higher price on the monopoly demand if it deals with a competitor on the portion of demand that could be met by the competitor.[33/]

The *Notice* refers to this conditioning of monopoly demand on competitive demand as the bundling or aggregating of services and/or geographic regions, practices that are a key aspect of many BOC discount plans, as demonstrated below.[34/] Plans that bundle services and/or areas and then impose substantial penalties for failing to meet revenue commitments have profoundly anticompetitive effects. CLECs cannot compete for any portion of the customer's demand committed to the BOC because the CLEC would have to provide an enormous discount to offset the higher costs incurred by the customer by shifting some of the committed business to the CLEC.[35/]

The BOCs' pricing structure effectively forces customers into these discount programs because they are the only way customers can avoid the BOCs' exorbitant monthly rates.[36] Thus, a critical component of addressing the anti-competitive effects of

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Comments of WorldCom, Inc., Declaration of Michael D. Pelcovitz on Behalf of WorldCom, Inc. (filed Jan. 23, 2003) ("*Pelcovitz Declaration*").

33/ *Id*. at 7.

34/ *Special Access NPRM* at 2034-35, ¶¶ 119-25.

35/ *AT&T Petition for Rulemaking to Reform Regulation for Incumbent Local Exchange Carrier Rates for Interstate Special Access Services*, RM 10593, Ex Parte Submission of MCI, Inc. (filed June 30, 2004).

36 *See AT&T Petition for Rulemaking to Reform Regulation for Incumbent Local Exchange Carrier Rates for Interstate Special Access Services*, RM 10593, Reply Declaration of Professors Janusz A. Ordover and Robert D. Willig at 5, ¶ 9 (filed Jan. 23,

lock up discount plans is to set the BOCs' monthly rates at reasonable prices to begin with, for example, by pegging special access rates to competitive prices as advocated above.[37/]

Many BOC discount plans, however, are not predicated on volume but simply require maintaining and/or increasing use of BOC special access services. These plans exhibit the key characteristics of exclusionary tariffs and contracts in that they: (1) require that the customer commit all or substantially all of its demand to the BOC; (2) impose substantial liquidated damages for failing to meet the commitment; and (3) bundle noncompetitive routes and/or services with competitive routes and/or services.[38/]

2003 as Exhibit 3 of the *AT&T Reply Comments*) ("*Ordover/Willig Reply Declaration*") ("[T]he Bells present carriers with only two choices: excessively priced month-to-month rates or long term [optional pricing plans] with discounts off the month-to-month rate."). *See also* T. RANDOLPH BEARD, GEORGE S. FORD, AND LAWRENCE J. SPIWAK, QUANTITY-DISCOUNT CONTRACTS AS A BARRIER TO ENTRY 7 (Phoenix Center Policy Paper Series No. 20, 2004), *available at* http://www.phoenix-center.org/ppapers.html ("[I]n order to get relief from paying the incumbent what otherwise would be the monopoly price for Special Access services, purchasers of Special Access service are typically required to accept significant long-term volume discount . . . contracts [that] usually contain onerous penalties for failing to meet the contract's volume and term commitments.").

[37/] *See* Beard, Ford, and Spiwak, *supra* note 36, at 4 ("[T]he entry-deterring efficacy of the [BOC's special access discount] contracts can be eliminated if high-capacity circuits are made available on a wholesale basis at cost-based prices (e.g., TELRIC) without use restrictions historically applied to such access."). To the extent that the BOC can justify discounts off of reasonably set monthly rates based on efficiency considerations, volume discounts may be permitted. *See AT&T Corp. v. BellSouth Telecommunications, Inc.*, File No. EB-04-MD-010, Memorandum Opinion and Order, 19 FCC Rcd. 23898, at 23906-07, ¶ 22 (2004) ("*BellSouth Enforcement Order*") (noting the Commission generally has looked favorably on proportional volume discounts for special services because volume and cost appear to have "a fairly direct, inverse relationship that reflects the economies and efficiencies gained as volume increases.") *See also, Ordover/Willig Reply Declaration* at5, ¶ 9 ("[I]f the month-to-month rate were established in an effectively competitive market, the general availability of a lower contractual rate, even one that required a sizable term and/or volume commitment, could not be considered harmful to competition.").

[38/] *See Pelcovitz Declaration* at 5.

Moreover, these exclusionary contracts do not require the BOC to forego current profits, as does the concept of predatory pricing. Exclusionary contracts are thus an ideal vehicle for dominant carriers too maintain their position in the market.

Examples of various BOC discount plans that exhibit exclusionary pricing follow. We emphasize that these are merely some examples of exclusionary tariff plans and not, by any means, intended to be an exhaustive list.

1. Examples of Exclusionary BOC Tariffs

a. SBC Plans

i. SBC's Managed Value Plan ("MVP") Tariff[39/]

SBC's MVP plan is typical of many of the BOC exclusionary contracts and has been discussed in previous filings.[40/] The MVP Plan is an overlay tariff, *i.e.,* it provides discounts on top of those available under SBC's base tariff discount plan. It provides the additional discounts in exchange for carrier commitments to maintain 100% of their historical spending levels for a bundle of services over a five-year period.[41/] The plan is

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39/ Each of the SBC regional companies has essentially identical MVP Tariff terms. *See, e.g.,* Southwestern Bell Telephone Company, Tariff FCC No. 73, § 38 at 3rd Revised Page 38-1 through Original Page 38-25 ("*SWBT MVP Tariff*"); Ameritech Operating Companies, Tariff FCC No. 2, § 19 at 7th Revised Page 659 through Original Page 679.8. We will cite solely to the *SWBT MVP Tariff*, but identical provisions are contained in each of the company's tariffs.

40/ *See, e.g., Pelcovitz Declaration* at 14-15; *Unbundled Access to Network Elements*, WC Docket No. 04-313, Ex Parte Submission of AT&T Corp., at 2-3 (filed Nov. 12, 2004) ("*AT&T Unbundled Access Ex Parte*").

41/ *SWBT MVP Tariff* § 38.1, at 5th Revised Page 38-2. The discounts increase each year, starting at 9% the first year, increasing to 14% the last year. *Id*. § 38.3(E)(3), at 3rd Revised Page 38-9. The MVP plan also waives nonrecurring installation charges on circuits ordered for at least three years or the MVP Plan terms are met. *Id*. § 38.3(E)(5), at 5th Revised Page 38-11 through 4th Revised Page 38-12.

only available for carriers that spend at least $10 million annually on SBC special access services.[42/]

MVP discounts are available regardless of volume – the same discount is available regardless of whether customer purchases $10 million or $100 million in SBC special access services.[43/] The sole requirements to obtain the discount are a commitment to continue using SBC special access and a promise not to use UNEs.

The MVP plan establishes a Minimum Annual Revenue Commitment (MARC) that consists of the carrier's total recurring billing for virtually any type of transport service offered by SBC.[44/] The carrier must maintain this level of spending with SBC for the five year term of the plan or face substantial penalties.[45/] The revenue commitment can be increased, but never decreased.[46/] The discount does not apply to services purchased in excess of the MARC unless the MARC is increased. There is thus an

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42/ *Id*. at 5th Revised Page 38-2, § 38.1.

43/ The MVP is not a simple volume discount. *See BellSouth Enforcement Order* at 23906-07, ¶ 22 (noting that typical volume discounts are linear, rising in close proportion to volume).

44/ The MARC is established by taking a carrier's previous three months billing for qualified services, which is defined as virtually all SBC transport services multiplied by four. *SWBT MVP Tariff* § 38.3(C)(1), at 3rd Revised Page 38-5. Qualified services include, inter alia, entrance facilities, high capacity services (DS1, DS3), SONET Ring services, OC 192 Sonet Ring Service and OCn point-to-point services. *Id*. § 38.2, at 5th Revised Page 38-2 through Original Page 38-2.1.

45/ *Id*. § 38.3(B)(1), (2), at 3rd Revised Page 38-3.

46/ *Id*. § 38.3(C)(2), at 3rd Revised Page 38-5. By not allowing for declining volumes, SBC adds insult to injury for those carriers that are refocusing or retrenching their business in order to meet the challenges posed by a distressed telecommunications industry. The failure of a carrier to meet its quota with SBC results in substantial penalties that simply exacerbate the difficult financial situation many competitive carriers face.

incentive to place additional services under the plan. Once increased, the new MARC governs for the remainder of the term.

In addition to maintaining recurring revenue, the MVP also requires carriers to purchase their facilities from special access tariffs rather than for using UNEs. The MVP Plan establishes an Access Service Ratio that requires carriers to purchase at least 95% of their SBC transport services from SBC's interstate tariff, effectively restricting the ability of MVP participants from utilizing SBC's UNEs.[47/]

Failure to meet the MARC or the 95% Access Service Ratio results in substantial penalties. Failure to meet the MARC requires the carrier to choose between paying the difference between its minimum annual commitment and the actual amount spent (becoming effectively a take-or-pay contract) or terminate the agreement and pay termination liabilities.[48/] The termination penalty requires repayment of all MVP discounts received in the six months preceding the termination date plus a specified percentage of the MARC for remainder of the term.[49/] For example if the carrier terminates during year 3 of the plan, it must pay 12.5% of the MARC for the remaining portion of the year 3 plus 12.5% of the MARCs for the remaining years of the agreement. The MVP tariff cites as an example a carrier that terminates 3.5 years into the agreement, that had a MARC of $10.6 million, and that had received MVP discounts in 4 of the 6

47/ *Id*. § 38.3(D), at 3rd Revised Page 38-6 through 3rd Revised Page 38-7. In some recent tariffs, BOCs have offered plans that require maintenance of an Access Service Ratio of 98%. *See, e.g.*, Southwestern Bell Telephone Company, FCC Tariff No. 73, § 41.31.2(D), at Original Page 41-231; Ameritech Operating Companies, FCC Tariff No. 2, § 22.43.2(D), at Original Page 22-327.

48/ *Id*. § 38.3(I), at 3rd Revised Page 38-19.

49/ *Id*. § 38.3(J), at 3rd Revised Page 38-20 through 2nd Revised Page 38-21.1.

months prior to termination. Total early termination penalties would be $3,771,833.33.[50/] All previously waived non-recurring charges must also be repaid.

As Dr. Pelcovitz noted, SBC's MVP tariff fits the pattern of an exclusionary contract.[51/] The discounts are tied to maintaining traffic on SBC's network and, through its penalty structure, the MVP plan creates virtually insurmountable barriers for competitors to overcome.[52/] Dr. Pelcovitz determined, for example, that a CLEC seeking to serve 20% of the demand of a customer under an MVP tariff would have to give a customer a 45% to 70% discount.[53/]

AT&T has similarly submitted evidence of the anticompetitive effect of SBC's MVP plan. Customers under SBC's MVP plan cannot rationally utilize competitive carriers', or self-supply, access services. AT&T posits an example of an MVP customer with a monthly commitment of $10 million comprised of 40,000 DS1 circuits each costing $250. Assume that a competitive carrier offers to provide 10% of this demand, or 4,000 circuits, at a price of $200. If the MVP customer took that offer, it would now only be buying $9 million (36,000 * 250) from SBC, creating a $1 million shortfall. Under the MVP, the shortfall penalty is the difference between the commitment and actual spend, or $1 million. Thus, the MVP customer would have to pay $1 million to SBC plus pay the new carrier $800,000 (4,000 circuits * $200 per circuit); for a total cost of $1.8 million. No rational carrier would put itself in that position.[54/]

50/ *Id*. § 38.3(J)(1), at 3rd Revised Page 38-21.

51/ *Pelcovitz Declaration* at 14.

52/ *Id*.

53/ *Id*. at 14-15.

54/ *AT&T Unbundled Access Ex Parte* at 2, n.6.

ii. SWBT Price Flexibility Tariff No. 15[55/]

Another SBC plan, a pricing flexibility contract that offers substantial discounts, includes a specific requirement that the customer move traffic from competitors onto SBC's network. It requires customers, to qualify for the steep discount offered by the plan, to not only commit to maintaining 100% of past revenue (as required by the company's MVP), but also requires that a "minimum of 4% of [the annual commitment] must come from services previously provided by a carrier other than Southwestern Bell Telephone Company and its affiliates."[56/] Failure to document this 4% minimum transfer of service will require customers to suffer the full termination penalty under the tariff – repayment of all discounts given plus 25% of committed revenue for each remaining year.[57/]

b. BellSouth

Each of the Bell companies has discount plans similar to SBC's MVP plan. BellSouth's Area Commitment Plan (ACP),[58/] for example, provides discounts in exchange for a commitment to purchase specified levels of special access rate elements throughout BellSouth's region for any period of time between 25 to 72 months. If the carrier falls below its commitment level, not only does the carrier lose the discount, but it

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55/ Southwestern Bell Telephone Company, Tariff FCC No. 73, § 41.15, at Original Page 41-88 through Original Page 41-97 ("*SWBT Price Flexibility Tariff*"). Other SBC Companies offered the same plan. *See, e.g.*, Ameritech Operating Companies, FCC Tariff No. 2, § 22.20.3(C), at Original Page 22-123; Southern New England Telephone, FCC Tariff No. 39, § 25.1.3(C), at Original Page 25-2.

56/ *SWBT Price Flexibility Tariff* § 41.15.3(C), at Original Page 41-89 through Original Page 41-90.

57/ *Id*.

58/ BellSouth Telecommunications Inc., FCC Tariff No. 1, § 2.4.8(B), at 10th Revised Page 2-49 through 5th Revised Page 2-49.0.2 ("*BellSouth ACP*").

is also subject to a shortfall penalty equal to the difference between the commitment level and the actual number of rate elements in service multiplied by 50% of the ACP.[59/] Dr. Pelcovitz also analyzed the effect of combining BellSouth's basic discount plans, such as the ACP with certain BellSouth pricing flexibility discounts that provide substantial additional discounts "on growth traffic."[60/] The effect is to preclude competitive inroads.[61/]

c. Verizon

To obtain the highest discounts under the Verizon Term Volume Plan (TVP) a customer must commit 90% of the DS1 lines it has under the tariff for a period of either eight or ten years.[62/] The Verizon TVP also includes a ratchet provision that automatically increases the required customer commitment. Under the Verizon TVP eight- and ten-year plans, for example, "[d]uring the annual review the commitment level will be reset to 90% of existing in-service [Special Access Lines]."[63/] Failure to meet the commitment level results in a shortfall charge equal to the average monthly recurring charge under the TVP plan multiplied by the shortfall multiplied by six. Thus, for

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59/ *Id*.

60/ *Pelcovitz Declaration* at 12-13 ("The most significant aspect of this tariff is that the discount is precisely targeted at the growth traffic of the customer.").

61/ *Id*. at 15 ("[I]f the ILECs are not constrained (from their exclusionary behavior], they will discourage competitors from making the investments necessary to challenge their market dominance."). *See also* Beard, Ford, and Spiwak, *supra* note 36, at 2-3 (BOCs "have successfully stymied competitive facilities-based entry into the Enterprise sector . . . through a form of exclusionary pricing structures incorporated into long-term contracts for high-capacity facilities . . . .").

62/ Verizon Telephone Companies, Tariff FCC No. 14, § 5.6.14(A) at 1st Revised Page 5-87.

63/ Verizon Telephone Companies, Tariff FCC No. 14, § 5.6.14(G) at 1st Revised Page 5-89.

example, if a customer committed to 9000 DS1 circuits at an average price of $123, but wanted to shift 300 DS1s to competitors, the customer would face a shortfall penalty of $221,400 ($123 x 300 x 6). To entice this customer away from Verizon, the competitor's price would have to be low enough to offset this penalty.

d. Qwest

Qwest's Regional DS1/DS3 Commitment Program (RCP) similarly requires a commitment of 90% of the customer's DS1 and DS3 lines.[64/] Qwest's RCP also includes an automatic ratcheting provision that requires that "[t]he actual quantity [of lines committed to the program] will be adjusted annually to reflect 90% of the current Company-provided in-service CTs."[65/] As with other BOC plans, failure to meet the commitment level results in a shortfall liability that effectively requires payment for the circuits not taken, converting the plan into a take or pay contract.[66/] The RCP imposes a termination liability of 50% "of RCPs established after Feb. 2, 2002," if a carrier decreases its commitment level prior to the end of the term.[67/]

II. Proposed Modifications To the BOC Special Access Regulatory Structure

The evidence recounted above overwhelmingly demonstrates the need for substantial revisions of the current BOC special access regulatory structure. CompTel/ALTS proposes a series of interdependent remedies designed to establish a

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64/ Qwest Corporation Tariff No. FCC No. 1, § 7.1.3.C.1, at 3rd Revised Page 7-115.1.

65/ Qwest Corporation Tariff No. FCC No. 1, § 7.1.3.C.3.a, at 1st Revised Page No. 7-115.5.

66/ Qwest Corporation Tariff No. FCC No. 1, § 7.1.3.C.3.c, at Original Page 7-115.6. ("[A] customer who commits to 350 DS1 Service CTs but only has 250 in-service, is charged for the total commitment level of 350.").

67/ Qwest Corporation Tariff No. FCC No. 1, § 7.1.3.C.5, at 2nd Revised Page 7-115.7.

special access regulatory structure that will promote and foster the competition needed to blunt the BOC's market power and prevent further leveraging of that power into downstream markets increasingly dominated by BOC affiliates. To successfully curb abusive BOC practices, each facet of the proposed revisions must be adopted.

First, the Commission must re-initialize price caps at rates that foster competition. CompTel/ALTS proposes that the Commission utilize the prices being charged by competitors in the market as an appropriate benchmark at which to re-set special access price caps. Second, these new price caps must be applied to all special access services, including those that have been deregulated under Phase II pricing flexibility, and that program must be terminated. Finally, the Commission must eliminate exclusionary BOC special access pricing plans that lock up demand in exchange for steep discounts.

A. BOC Special Access Rates Should Be Reinitialized At Levels that Foster Competition Utilizing Competitors' Prices as a Benchmark

The *Notice* identifies several alternative approaches to reinitializing the price cap rates. The Commission for example, seeks comment on whether to re-set price caps utilizing a rate of return benchmark, and if so, whether to undertake a detailed review of cost studies.[68/] The Commission recognizes, however, that there are a number of difficulties in utilizing a rate of return benchmark solely for special access services and seeks comment on other measures or indicators, in lieu of rate of return, to determine whether rates are just and reasonable.[69/] (As set forth herein, CompTel/ALTS suggests adopting competitors' pricing in lieu of a rate of return, as the benchmark for price caps). Alternatively, the Commission suggests the possibility of utilizing price cap rates for

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68/ *Special Access NPRM* at 2015-18, ¶¶ 60, 65.

69/ *Special Access NPRM* at 2015-17, ¶¶ 60-64.

"comparable" services, such as switched access service components, to establish "just and reasonable" rates.[70/] The Commission also seeks comment on whether a "significant factor" in setting new, lower price caps is the risk of reducing BOC incentives to operate at minimum cost and to innovate.[71/]

CompTel/ALTS urges the Commission to more fundamentally reassess the question of how to set just and reasonable price cap rates for special access services. Rate of return and cost of service-based approaches to setting price caps for special access services are no longer appropriate in a world in which those services are used to compete against the BOCs in all telecommunications markets. The current price cap regime, which the Commission appears inclined largely to perpetuate, is, like all rate-setting methodologies, predicated on the assumption of a continuing monopoly.[72/] That assumption is no longer valid. The 1996 Act calls for competition in all telecommunications markets and, increasingly, that competition is dependent on BOC special access services. Thus, the question of whether special access rates are just and

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70/ *Special Access NPRM* at 2018, ¶ 66.

71/ *Special Access NPRM* at 2018, ¶ 67. There is no basis to assume that lower rates will lead to less innovation. Moreover, high rates – such as those that are symptomatic of monopoly – are more consistent with output restriction rather than stimulation. The Supreme Court has observed, "Market power is the power 'to force a purchaser to do something that he would not do in a competitive market.' It has been defined as 'the ability of a single seller to raise price and restrict output.'" *Eastman Kodak Co. v. Image Tech. Servs.*, 504 U.S. 451, 464 (1992) (internal citations omitted). Current excessive rates clearly have not driven investment in special access services, as evidenced by the Commission's findings in the *Special Access NPRM*. *See Special Access NPRM* at 2006, ¶ 27 (noting BOC special access average investment decreased at a compounded annual rate of less than one percent from 2001 to 2003). Special access services appear to have become a cash cow for the BOCs, funding other investment and shareholder dividends, while BOCs disinvest in traditional special access facilities.

72/ Verizon Communications, Inc. v. FCC, 535 U.S. 467, 486-88 (2001).

reasonable must predominantly focus on the effect of those rates on competition and not, first and foremost, on whether they appropriately calibrate BOC investment incentives.

Prices caps were designed to emulate the rates and returns that a utility could charge in a competitive market.[73/] Although price caps were designed to mimic competitive markets, they were not designed to actually foster competition.[74/] As the Supreme Court noted in its review of rate making in *Verizon:*

> The enduring feature of ratesetting from *Symth v. Ames* to the institution of price caps was the idea that calculating a rate base and then allowing a fair rate of return on it was a sensible way to identify a range of rates that would be just and reasonable to investors and ratepayers. Equally enduring throughout the period was dissatisfaction with the successive rate-based variants. From the constancy of this dissatisfaction, one possible lesson was drawn by Congress in the 1996 Act, which was that regulation using the traditional rate-based methodologies gave monopolies too great an advantage and that the answer lay in moving away from the assumption common to *all* the rate-based methods, that the monopolistic structure within the discrete markets would endure.[75/]

Although the Supreme Court was addressing in particular the intent of Congress in requiring that rates for unbundled network elements be "based on the cost (determined without reference to a rate-of-return or other rate-based proceeding) of providing the . . .

73/ *See, e.g., Access Charge Reform*, CC Docket No. 96-262, Fifth Report and Order, 14 FCC Rcd. 14221, 14295, ¶ 138 (1999) ("[T]he Commission designed price cap regulation in part to replicate, to the extent possible, the results of a competitive market.") ("*Pricing Flexibility Order"*); *Special Access NPRM* at 2016, ¶ 61 ("The aim of price cap regulation is [to develop] rates that approximate those that a competitive firm would charge."); *Verizon Communications*, 535 U.S. at 486 (Rate regulation "was intended to give utilities an incentive to make smart investments deserving a 'fair' return, and thus to mimic natural incentives in competitive markets.").

74/ *Verizon Communications*, 535 U.S. at 486 (declaring rate regulation as designed to give investment incentive "without an eye to fostering the actual competition by which such markets are defined").

75/ *Verizon Communications*, 535 U.S. at 487-88 (emphasis added).

network element,"[76/] the conclusions expressed by the Court about the rate making processes should inform this Commission's re-assessment of special access rate-setting. The Commission has determined that carries must compete against BOCs or their affiliates in many downstream markets without having access to facilities priced at forward looking rates, *i.e.,* UNEs, that are designed to foster competition.[77/] Instead carriers must try to compete with the BOCs and their affiliates by utilizing BOC special access services whose regulated rates are designed principally to ensure a fair return to the BOC on the assumption that the BOC will be an enduring monopoly.[78/]

Verizon's critique of ratemaking, including price caps, as assuming continuing monopoly, coupled with the replacement of UNEs with special access as the inputs to compete in downstream markets, requires the Commission to reassess special access ratemaking. Special access rates must now be designed principally to foster competition, *not* simply to ensure a fair return on the continuing monopolists' (hopefully) prudent investment.[79/] Fostering competition thus cannot be achieved by tinkering with the price

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[76/] 47 U.S.C. § 252(d)(1)(A).

[77/] The Commission has ruled that UNEs are not available to provide CMRS or long distance services and has imposed ever-greater restrictions on the use of UNEs in the local market. *Unbundled Access to Network Elements*, WC Docket No. 04-313, Order on Remand, 20 FCC Rcd. 2533, 2552-53, ¶ 34 (2005). The Commission has eliminated UNE access in a number of BOC wire centers and bars use of UNEs to provide service above certain capacity levels. *Id*. at 2537-38, 2632, 2634, ¶¶ 5, 177, 181.

[78/] *Verizon Communications*, 535 U.S. at 486-88 (expressing that the assumption of all ratemaking is that a monopoly structure will endure).

[79/] One possible approach is to use comparable TELRIC rates for special access services. *See e.g., Review of the Commission's Rules Regarding the Pricing of Unbundled Network Elements and the Resale of Service by Incumbent Local Exchange* Carriers, CC Docket No. 03-173, Ex Parte Submission of Ad Hoc Telecommunications Users Committee at 7-8 (filed August 26, 2004) ("Competition in Access Markets: Reality or Illusion" prepared by Economics and Technology, Inc.). CompTel/ALTS would not oppose such an approach. CompTel/ATLS, however, urges the Commission cap regime's productivity factors or reestablishing rates at some regulatorily divined rate of return, which at bottom has the assumption of enduring monopolies.

Attempting to re-set price caps regulation through a rate of return, cost of service approach would also perpetuate another problem identified by *Verizon* with traditional ratemaking, which is that utilities, the BOCs here, have insurmountable advantages in terms of information.[80/] Although price caps can offset this advantage,[81/] there is still room for game-playing in setting productivity factors and exogenous costs and other adjustments that make up the Price Cap Index (PCI),[82/] and the BOCs' information advantage would be particularly acute if the FCC initiates a new cost proceeding to establish a new rate of return.[83/]

CompTel/ALTS thus respectfully suggests an alternative approach to setting special access rates -- benchmarking base (*i.e.,* monthly) BOC special access rates at the prices charged by competitors that have been able to enter the market and offer services

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to explore the use of actual competitors' prices as the benchmark for price capped rates, as explained herein.

80/ *Verizon Communications*, 535 U.S. at 486.

81/ *Verizon Communications*, 535 U.S. at 487 (describing "the price cap scheme" as "simply being a rate-based offset to the utilities' advantage of superior knowledge of the facts employed in cost-of-service ratemaking").

82/ *Verizon Communications*, 535 U.S. at 487.

83/ *Special Access NPRM* at 2017-18, ¶ 65. CompTel/ATLS recognizes that, in the short term, all the Commission may be able to accomplish is to reset special access rates at the last historically validated rate of return and productivity offset. *See, e.g., Special Access Rates for Price Cap Local Exchange Carriers*, WC Docket No. 05-25, Order, Ex Parte Submission of CompTel/ALTS (filed may 13, 2005) (supporting the eTUG/API proposal to set an interim 5.3% productivity factor). CompTel/ALTS strongly supports these adjustments on an interim basis pending the resolution of this proceeding, as discussed in Section III, below.

over their own facilities, *i.e.,* on-net services.[84/] Rather than undertake a cost of service, rate of return proceeding to approximate rates that a "competitive firm would charge,"[85/] the Commission should use actual rates charged by competing carriers.[86/]

By advocating the establishment of BOC special access rates with reference to prices charged by competing firms, CompTel/ALTS in no way means to suggest that the special access market is competitive. Although there are carriers that are able to offer special access services in competition with the BOC along discrete routes, the presence of these carriers has not induced the BOCs to lower their special access rates overall. Indeed, BOCs successfully are maintaining special access rates substantially higher than those charged by competing carriers, even on routes where competition exists, providing strong evidence of their continued market power and the need for continued price regulation.

Benchmarking rates at the on-net prices charged by firms entering the market will foster competition to a far greater extent than utilizing a rate setting procedure premised on continuing monopoly. For one, the prices charged by these competitive carriers much more closely approximate those that would be set in a functionally competitive market

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84/ It is important to use competitors' on-net rates, rather than prices based on resold BOC special access services, because the former provides a more accurate assessment of rates necessary to ensure a fair return on investment.

85/ *Special Access NPRM* at 2016, ¶ 61.

86/ The Commission need not set rates based on the costs of each individual industry participant. *Reform of Access Charges Imposed by Competitive Local Exchange Carriers*, Seventh Report and Order and Further Notice of Proposed Rulemaking, 16 FCC Rcd. 9923 ¶46 (2001). Indeed the Commission has assessed the reasonableness of rates by comparing the rates of other carriers, even in non-competitive markets. *See AT&T Corp. v. Business Telecom, Inc.* Memorandum Opinion and Order, 12 FCC Rcd. 12,312 ¶¶ 23-30 (2001).

because competitors' prices typically are based on forward looking costs.[87] Moreover, the prices set by competitors are free of any implicit subsidies, as should BOC special access rates.[88] Additionally, utilizing rates charged by competitors in the market mitigates the BOCs' natural informational advantage in cost setting proceedings. Rates based on competitor prices are readily discernable and avoid the need for a lengthy cost proceeding.

Benchmarking special access rates at competitors' prices will also reduce the BOCs' ability to load their special access prices with unreasonable mileage charges. As demonstrated above, the current price cap structure enables the BOCs to charge exorbitant rates for interoffice transport mileage, in contrast to pricing in the remainder of the telecommunications industry, which is largely distance-insensitive. Hence, one of the results of utilizing competitors' prices to benchmark BOC special access rates will be to introduce distance insensitivity into the BOC rate structure.

There may be a further reason to set BOC special access rates at the levels charged by competitors. Many of the competitive price points will be the wholesale rates charged by AT&T and MCI, the two most prominent special access competitors in the market. Should their respective mergers with SBC and Verizon be approved, AT&T and MCI will be wholly-owned BOC subsidiaries.[89] Upon culmination of the mergers, those

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87/ *Special Access NPRM* at 2017-18, ¶ 65 ("Embedded costs associated with past business decisions generally are irrelevant to a national profit-maximizing firm operating in a competitive market; only forward-looking costs matter to such a firm with regard to business decisions that it is required to make today.").

88/ *See Access Charge Reform*, CC Docket No. 96-262, First Report and Order, 12 FCC Rcd. 15982, 15986, ¶ 7 (1997).

89/ *See SBC Communications Inc. and AT&T Corp. Applications for Transfer of Control*, WC Docket 05-65, Description of the Transaction, Public Interest Showing, and Related Demonstrations, at 11 (filed Feb. 22, 2005) ("AT&T thus will become a wholly

AT&T and MCI "special access" price points will become BOC rates and, under section 202, SBC and Verizon must make those rates available to similarly situated carriers. Thus, in significant swaths of the country, competitive price points will, if the mergers are culminated, become BOC special access price points.[90/]

Finally, if a BOC believes that the rates set with reference to competitors' prices results in confiscatory rates, the BOC is free to request a waiver. The ability to request a waiver based on a concern that a prescribed rates is confiscatory was noted in the CALLS plan and should be carried forward.[91/]

1. Examples of Competitor Prices.

Market evidence shows that, where competitors can offer comparable services over their own facilities, called on-net services, competitors' prices typically are

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owned subsidiary of SBC."); *Verizon Communications Inc. and MCI, Inc. Applications for Approval of Transfer of Control*, WC Docket No. 05-75, Application for Transfer of Control, at i (filed March 11, 2005) ("Verizon and MCI have entered into an Agreement and Plan of Merger under which MCI will become a wholly-owned subsidiary of Verizon."). CompTel/ALTS strongly objects to these mergers and nothing herein should be taken as either supporting those acquisitions or indicating in any way that special access issues raised in those mergers should be set aside because of this proceeding.

[90/] SBC and Verizon should be required not only to file and make generally available their wholesale rates, but also the special access prices charged to their retail end users.

[91/] *Access Charge Reform*, CC Docket Nos. 96-262, 94-1, 99-249, 96-45, Sixth Report and Order in CC Docket Nos. 96-262 and 94-1, Report and Order in CC Docket No. 99-249, Eleventh Report and Order in CC Docket No. 96-45, 15 FCC Rcd. 12962, 12969, ¶17 (2000) (subsequent history omitted) ("*CALLS Order*") ("Moreover, a price cap LEC may petition the Commission to set its rates above the levels permitted by the price cap indices based on a showing that the authorized rate levels will produce earnings that are so low as to be confiscatory.") Alternatively, if the Commission hews closely to the existing price cap framework, CompTel/ALTS urges that, at a minimum, any price capped rate reflect forward looking costs, which, the Commission notes, "are generally viewed as more relevant to setting prices in a competitive market." *Special Access NPRM* at 2017-18, ¶ 65. Additionally, the price cap index (PCI) must include indexing tools to capture BOC productivity and/or average cost decreases attributable to demand growth. *See, e.g., Special Access NPRM* at 2010, ¶ 38.

substantially below BOC special access rates. Tables 8 through 10 of the *Fischer Declaration* compare BOC special access rates, both price capped rates and deregulated pricing flexibility rates, against prices charged by two competitive providers for: (1) DS1 point-to-point services (Table 8), (2) DS3 entrance facilities (Table 9); and (3) DS3 entrance facilities plus interoffice transport (Table 10) in various states. To make an apples-to-apples comparison, Global Crossing compared in each instance competitors' prices for a three-year term as actually made available to Global Crossing with BOC pricing for comparable facilities under a three-year BOC term plan.[92/] The tables show that competitors' rates are often one-half to one-third of the BOC special access rates. The tables also reinforce the point that BOC pricing flexibility rates are higher than price cap rates. Moreover, Table 8, which compares point-to-point rates for first ten-mile and then thirty-mile circuits, demonstrates particularly well that industry pricing is far less distance sensitive than BOC special access pricing. Table 8 shows that BOC special access prices increase substantially from a ten-mile to a thirty-mile circuit whereas the competitors' rates increase only slightly.[93/]

These examples illustrate the pricing power of the BOCs and provide the Commission with a sense of how wide the pricing gap is between BOC pricing and competitive pricing.

2. Rates Can be Adjusted Periodically

In addition to re-initializing price cap rates, the Commission also seeks comment on whether such rates should be adjusted on a periodic basis. Historically, price caps

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92/ *Fisher Declaration* at ¶ 9. The BOC tariff sections used for comparison purposes are identified on the tables.

93/ *Id*. at Table 8.

have been adjusted periodically by the Price Cap Index, which was based on a measure of inflation and exogenous costs, offset by a productivity factor or X-factor.[94/] The Commission seeks comment on whether, following any re-setting of rates, the Commission should review rates at fixed intervals to adjust the benchmark.

Periodic adjustments may be necessary if competitive prices deviate significantly from the initially established levels. Such adjustments could be based on a periodic review, for example every year, of competitors' prices to ensure that BOC price capped rates still reflect competitive prices. The rates could then be adjusted up or down as needed. Alternatively, once the price cap rates are appropriately re-set, the Commission could apply the CPI with an appropriate and rigorous productivity factor that ensures customers and the BOC reap the rewards of productivity gains, as would be the case in a functionally competitive market.

B. Phase II Pricing Flexibility Should be Repealed

Re-setting price caps at levels that promote competition is of little use if the BOCs can avoid price caps under the Commission's pricing flexibility regime, despite their continuing market power. The Commission hoped that the BOCs would utilize their regulatory freedom to reduce prices in response to competitive pressures.[95/] As demonstrated above, that clearly has not been the case. The Commission's predictive judgment that its collocation-based proxies could identify MSAs where sunk investment was sufficient to discipline BOC pricing behavior has proved unsound.

The limited competitive entry that has occurred in deregulated areas has been insufficient to moderate BOC prices as BOC rates continue to exceed not only price caps

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94/ *Special Access NPRM* at 1999-2000, ¶¶ 10-11.

95/ *Special Access NPRM* at 2019, ¶ 70.

but also to exceed substantially that of competitive carriers. The reason that BOCs can maintain these rates even in areas that are ostensibly competitive is that the BOCs are the only entities capable of providing service throughout the MSA. Competitors are able to offer alternatives, if at all, only on discrete routes within the MSA. Customers, whether end users or carriers, thus have no choice but to continue to purchase BOC special access services, even at prices far in excess of those offered by competitors.[96] In contrast to the Commission's hope that deregulation would enable BOCs to respond flexibly to market forces by reducing prices to meet competition,[97/] BOCs have responded to deregulation with persistently higher prices, as was demonstrated above.

There currently is no "fix" to the Commission's Phase II regime that would alleviate or cabin BOC market power, either in the form of revising the geographic market definition or the proxies. BOC special access rates must, therefore, be re-regulated in Phase II MSAs and be subject to the re-initialized price caps described above.

CompTel/ALTS does not, however, oppose downward pricing flexibility, that is, the ability of BOCs to actually lower rates to meet competition. Effectively, this could be accomplished by continuing Phase I pricing flexibility. Phase I pricing flexibility allows carriers to enter into individually negotiated contract tariffs and to offer volume and term discounts. The continuation of Phase I pricing flexibility must be conditioned, however, on the following: (1) customers have access to the reinitialized price cap rates as set forth

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96 *See, e.g., Gately Reply Declaration* at 14, ¶ 18 ("RBOCs remain the sole source of dedicated access connectivity at roughly 98% of all business premises nationwide, even for the largest corporate users."); *WorldCom Ex Parte* at 2 ("WorldCom, which operates one of the most extensive CLEC networks, provisions approximately 90% of its last-mile DS1s over ILEC special access facilities.").

97/ *Special Access NPRM* at 2019, ¶ 70.

herein; (2) volume and term contracts do not contain exclusionary terms and conditions; (3) the terms and conditions of individually negotiated contract tariffs are reasonably available to similarly situated customers.

C. Exclusionary Tariff and Contract Terms and Conditions Must Be Declared Unlawful

An integral aspect of any overhaul of BOC special access regulation must include the elimination of exclusionary BOC tariffs and contracts. The Commission must declare these provisions unlawful as they unreasonably impede competition and thereby unlock the demand currently frozen by these requirements contracts. This will allow carriers to compete on a level playing field with the BOC.

As the Commission recognized in the *Notice*, market power can be "exercised through exclusionary conduct . . . [that] may be evidenced from terms and conditions contained in a carrier's tariff offering."[98/] Such conduct has long been of concern to the Commission.[99/] As noted in AT&T's original petition, the Commission' *Pricing Flexibility Order* highlighted the potential that BOCs could foreclose competition by locking up customer demand.[100/] The *Notice* points out as well that the Commission has previously "found that some large discounts might be anticompetitive or raise questions

98/ *Special Access NPRM* at 2032, ¶ 114.

99/ *Id*. at 2032-33, ¶ 115.

100/ *AT&T Petition for Rulemaking to Reform Regulation for Incumbent Local Exchange Carrier Rates for Interstate Special Access Services*, RM 10593, Petition for Rulemaking, at 21 (filed Oct. 15, 2002) ("[A]n incumbent can forestall the entry of potential competitors by 'locking up' large customers . . . .") (quoting *Pricing Flexibility Order* at 14263-64, ¶ 79).

of discrimination,"[101/] and that it has barred carriers from offering growth discounts in their tariffs.[102/]

More recently, the Commission found that BellSouth's TSP discount plan violated Sections 272(c)(1) and 272(e)(3) because, by providing proportionately higher discounts to lower volume users, and by requiring carrier's to commit 90% of their spend with BellSouth, the TSP plan discriminated in favor of Bellsouth's long distance affiliate.[103/] The Commission found that the TSP's commitment requirement "resembles" a growth discount, which the Commission "has consistently rejected."[104/] The finding that such commitments operate like unlawful growth discounts is significant because a number of BOC tariffs and contracts contain similar commitments. Under the reasoning of the *BellSouth Enforcement Order*, all such commitments must be found unlawful.

Of particular concern are contracts that bundle various capacity levels, for example requiring the purchase of potentially competitive OC-level facilities along with less competitive DS1 or DS3 services. Such bundling occurs when BOC plans require a revenue commitment based on purchases of a broad range of services. Another concern are contracts that require region-wide commitments, which effectively require carriers to purchase BOC services along competitive routes as a condition of obtaining access to

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101/ *Special Access NPRM* at 2032-33, ¶ 115 (citing *Expanded Interconnection with Local Telephone Company Facilities*, CC Docket No. 91-141, Report and Order and Notice of Proposed Rulemaking, 7 FCC Rcd. 7369, 7447-70 (1992) ("*Expanded Interconnection Order*")).

102/ *Id*. (citing *Transport Rate Structure and Pricing,* CC Docket No. 91-213, Fourth Memorandum Opinion and Order on Reconsideration, 10 FCC Rcd. 12979, 12985, ¶ 17 (1995)).

103/ *AT&T Corp. v. BellSouth Telecommunications, Inc.*, File No. EB-04-MD-010, Memorandum Opinion and Order, 19 FCC Rcd. 23898, 23912-16, ¶¶ 34-42 (2004) ("*BellSouth Enforcement Order*").

104/ Id. at 23912-13, ¶ 37.

BOC services on uncompetitive routes. When such broad commitments are tied to liquidated damages far in excess of any reasonable cost-recovery justification, competition is substantially hindered.

As noted in the description of certain BOC special access discount plans above, the plans often provide discounts regardless of volume. The sole requirement is the promise to keep demand on the BOC network. They are thus far different from the linear, proportional discounts that the Commission has previously blessed. *See BellSouth Enforcement Order*, ¶ 22.

The Commission has authority to redress the anticompetitive effects of BOC tariffs in the context of a general rulemaking.[105/] (The Commission must also address in a separate context the market-altering acquisitions by SBC and Verizon of AT&T and MCI, respectively.) The Commission should use its authority to declare exclusionary tariffs and contracts unlawful. Carriers participating in such plans should be permitted to opt out of such plans without incurring unreasonable penalties and enter lawful discount plans, or to adopt month-to-month special access at the new rates set by the Commission as a result of this proceeding. There is clear precedent for such steps when tariff terms are found to impede competition.[106/]

III. The Commission Should Adopt Interim Relief

The *Notice* denies AT&T's request for interim relief pending the culmination of the rulemaking. AT&T proposed an immediate reduction of special access charges for services subject to Phase II pricing flexibility to the rate that would be produced with an

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105/ *See. e.g., Expanded Interconnection Order* at 7463-65, ¶ 201, n.468.

106/ *See Id*. at 7463-65, ¶¶ 201-02 (establishing a "fresh look" period during which carriers could be released from long-term access contracts, with penalties limited by FCC rule).

11.25% rate of return and a moratorium on further phase II designations.[107/] The Commission believed that these steps have not been justified base on the record developed to date. For example, at the time of AT&T's filing, only one year's worth of pricing flexibility price information was available.[108/]

The evidence gathered since AT&T's initial petition, much of which is recounted herein, demonstrates that pricing flexibility prices have continued to exceed price capped rates in each year since the inauguration of pricing flexibility, and that BOC rates of return for special access services exceed the 11.25% by increasingly larger amounts each year. This evidence is more than sufficient for the FCC to take immediate, interim action to reign in BOC special access rates.

At a minimum, the evidence of continued higher prices in Phase II pricing flexibility areas supports an immediate moratorium on any new Phase II pricing flexibility designations and the re-imposition of price cap regulation in existing Phase II pricing areas, if not at the levels that would reflect an 11.25% rate, then at least at current price cap levels. Moreover, there is ample justification to impose an immediate 5.3% productivity factor as suggested by the Commission,[109/] and supported by various parties, including CompTel/ALTS, in recent ex parte filings.[110/] As the Commission notes, there

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107/ *Special Access NPRM* at 2036, ¶ 128.

108/ *Id*. at 2036, ¶ 129.

109/ *Id*. at 2037, ¶ 131.

110/ *Special Access Rates for Price Cap Local Exchange Carriers*, WC Docket No. 05-25, Ex Parte Submission of CompTel/ALTS (filed May 13, 2005); *Special Access Rates for Price Cap Local Exchange Carriers*, WC Docket No. 05-25, Order Ex Parte Submission of eTUG and API (filed May 10, 2005); *Special Access Rates for Price Cap Local Exchange Carriers*, WC Docket No. 05-25, Order Ex Parte Submission of T-Mobile USA, Inc. (filed June 3, 2005).

is currently no productivity factor in place,[111/] yet the BOC companies have achieved enormous scale economies and the national productivity rate has been substantial (in relative terms) in recent years.[112/] These actions are sorely needed to restore some equilibrium in this market and reduce the enormous transfer of wealth occurring because of the BOC's supracompetitive profits.[113/]

111/ *Special Access NPRM* at 2037, ¶ 131.

112/ *Id*. at 2007, ¶ 29.

113/ *See, e.g., Gately Reply Declaration* at 4-5, ¶6 (noting BOC overcharges of $17.5 million per day).

CONCLUSION

For the reasons set forth herein, CompTel/ALTS urges the Commission to carefully review BOC special access rates, terms, and conditions and to undertake the recommended modifications so as to level the playing field for BOCs and their competitors.

/s/

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CERTIFICATE OF SERVICE

I, Ernest C. Cooper, hereby certify that on this 13th day of June 2005, the foregoing Comments of NuVox, Inc., were filed electronically through the FCC's Electronic Comments Filing System (ECFS) and copies were served on the following as indicated:

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