

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

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| In the Matter of |) | |
| |) | |
| Access Charge Reform |) | CC Docket No. 96-262 |
| |) | |
| Price Cap Performance Review for Local |) | CC Docket No. 94-1 |
| Exchange Carriers |) | |
| |) | |
| Interexchange Carrier Purchases of Switched |) | |
| Access Services Offered by Competitive Local |) | CCB/CPD File No. 98-63 |
| Exchange Carriers |) | |
| |) | |
| Petition of U S West Communications, Inc.) |) | |
| for Forbearance from Regulation as a Dominant |) | CC Docket No. 98-157 |
| Carrier in the Phoenix, Arizona MSA |) | |
| |) | |

**FIFTH REPORT AND ORDER AND FURTHER NOTICE OF PROPOSED
RULEMAKING**

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By the Commission: Commissioner Ness issuing a statement; Commissioner Furchtgott-Roth approving in part, concurring in part, dissenting in part, and issuing a statement.

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I. INTRODUCTION

1. In this Order, we revise the rules that govern the provision of interstate access services by those incumbent local exchange carriers (ILECs) subject to price cap regulation (collectively, "price cap LECs")¹ to advance the pro-competitive, de-regulatory national policies embodied in the Telecommunications Act of 1996 (1996 Act).² With these revisions, we continue the process the Commission began in 1997, with the *Access Reform First Report and Order*, to reform regulation of interstate access charges in order to accelerate the development of competition in all telecommunications markets and to ensure that our own regulations do not unduly interfere with the operation of these markets as competition develops.³

2. In the *Access Reform First Report and Order*, the Commission adopted a primarily market-based approach to drive interstate access charges toward the costs of providing these services.⁴ The Commission envisioned that this approach would enable it to give carriers progressively greater flexibility to set rates as competition develops, until competition gradually replaces regulation as the primary means of setting prices.⁵ In this Order, the Commission fulfills its commitment to provide detailed rules for implementing the market-based approach, pursuant

¹ The Commission instituted price cap regulation for the Regional Bell Operating Companies (BOCs) and GTE in 1991, and permitted other LECs to adopt price cap regulation voluntarily, subject to certain conditions. Policy and Rules Concerning Rates for Dominant Carriers, CC Docket No. 87-313, Second Report and Order, 5 FCC Rcd 6786, 6818-20 (*LEC Price Cap Order*). We emphasize that this Order applies only to price cap LECs. As stated in the *Access Reform First Report and Order*, the Commission intends to address interstate access charge reform for rate-of-return LECs in a separate proceeding. *Access Reform First Report and Order*, 12 FCC Rcd 16125-26. On June 4, 1998, the Commission released a Notice of Proposed Rulemaking initiating a comprehensive review of access charge reform for rate-of-return LECs. Access Charge Reform for Incumbent Local Exchange Carriers Subject to Rate-of-Return Regulation, CC Docket No. 98-77, Notice of Proposed Rulemaking, 13 FCC Rcd 14238 (1998) (*Rate of Return Access Reform NPRM*).

² Telecommunications Act of 1996, Pub. L. No. 104-104, 110 Stat. 56, *codified at* 47 U.S.C. § 151 *et seq.*

³ See *Access Reform First Report and Order*, 12 FCC Rcd at 15985, 16094. A list of parties submitting comments in response to various proceedings related to access reform is included at Appendix A. The list identifies the specific proceeding and how each commenter is identified in the text of this item. Unless otherwise noted, all cites to comments and replies refer to comments and replies submitted in response to Access Charge Reform, CC Docket No. 96-262, Notice of Proposed Rulemaking, 11 FCC Rcd 21354 (1996) (*Access Reform NPRM*).

⁴ *Access Reform First Report and Order*, 12 FCC Rcd at 16094. The Commission also adopted a "prescriptive backstop" to its market-driven approach: it required all price cap LECs to file cost studies no later than February 8, 2001, to demonstrate the forward-looking cost of providing those services that remain subject to price cap regulation. *Id.* at 16096-97.

⁵ *Id.* at 15989, 16094-95.

to which price cap LECs would receive pricing flexibility in the provision of interstate access services as competition for those services develops.⁶

3. The pricing flexibility framework we adopt in this Order is designed to grant greater flexibility to price cap LECs as competition develops, while ensuring that: (1) price cap LECs do not use pricing flexibility to deter efficient entry or engage in exclusionary pricing behavior; and (2) price cap LECs do not increase rates to unreasonable levels for customers that lack competitive alternatives. In addition, these reforms will facilitate the removal of services from price cap regulation as competition develops in the marketplace, without imposing undue administrative burdens on the Commission or the industry.

4. Specifically, this Order grants immediate pricing flexibility to price cap LECs in the form of streamlined introduction of new services, geographic deaveraging of rates for services in the trunking basket, and removal, upon implementation of toll dialing parity, of certain interstate interexchange services from price cap regulation. We also establish a framework for granting price cap LECs greater flexibility in the pricing of all interstate access services once they satisfy certain competitive criteria. In Phase I, we allow price cap LECs to offer contract tariffs and volume and term discounts for those services for which they make a specific competitive showing. In Phase II, we permit price cap LECs to offer dedicated transport and special access services free from our Part 69 rate structure and Part 61 price cap rules, provided that the LECs can demonstrate a significantly higher level of competition for those services.

5. We address additional pricing flexibility proposals in the Notice of Proposed Rulemaking (Notice) portion of this item. We seek comment on proposals for geographic deaveraging of the rates for services in the common line and traffic-sensitive baskets. We also invite comment on the appropriate triggers for granting Phase II relief for services in the common line and traffic-sensitive baskets, as well as for the traffic-sensitive parts of tandem-switched transport service.

6. In addition to adopting rules to implement the market-based approach to access reform, we take this opportunity to re-examine the rate structure for the local switching service category of the traffic-sensitive basket. Accordingly, in the Notice, we seek comment on a number of proposed changes to the rate structure so that it better replicates the operation of a competitive market. Generally, we invite parties to discuss proposed revisions to our rules that would require price cap LECs to develop capacity-based local switching charges rather than per-minute charges. We also solicit comment on whether the traffic-sensitive price cap index (PCI) formula should be modified. For the same reasons that we consider revising the local switching rate structure, we also seek comment on whether similarly to revise the rate structure for tandem-switched transport.

⁶ *Id.* at 15989, 16106.

7. Finally, we deny a petition for declaratory ruling filed by AT&T requesting that the Commission confirm that interexchange carriers (IXCs) may elect not to purchase switched access services offered under tariff by competitive local exchange carriers (CLECs).⁷ We decline to address AT&T's concerns in a declaratory ruling; however, we find that AT&T's petition and supporting comments suggest a need for the Commission to revisit the issue of CLEC access rates. Therefore, in the Notice, we initiate a rulemaking regarding the reasonableness of these charges and whether the Commission might adopt rules to address, by the least intrusive means, any failure of market forces to constrain CLEC access charges.

II. BACKGROUND AND SUMMARY

A. Price Cap Regime

1. Background

8. To recover the costs of providing interstate access services, incumbent LECs charge IXCs and end users for access services in accordance with our Part 69 access charge rules.⁸ Part 69 establishes two basic categories of access services: special access services and switched access services. Special access services do not use local switches; instead they employ dedicated facilities that run directly between the end user and the IXC's point of presence (POP).⁹ Switched access services, on the other hand, use local exchange switches to route originating and terminating interstate toll calls. The Commission has not prescribed specific rate elements in Part 69 for special access services.¹⁰ Part 69 does establish specific switched access elements and a mandatory switched access rate structure for each element.¹¹

9. Interoffice transmission services, known as transport services, carry interstate switched access traffic between an IXC's POP and the end office that serves the end user customer. Incumbent LEC transmission facilities that carry switched interstate traffic between an IXC's POP and the incumbent LEC end office serving the POP (this office is called the serving wire center, or

⁷ Petition for Declaratory Ruling filed by AT&T Regarding Interexchange Carrier Purchases of Switched Access Services Offered by Competitive Local Exchange Carriers (Oct. 23, 1998) (*AT&T Declaratory Ruling Petition*).

⁸ 47 C.F.R. Part 69.

⁹ A POP is the physical point where an IXC connects its network with the LEC network.

¹⁰ *Access Reform NPRM*, 11 FCC Rcd at 21367.

¹¹ *Id.* at 21367.

SWC), are known as entrance facilities.¹² Incumbent LECs currently offer two types of interstate switched transport service between a SWC and an end user's end office. Under the first service, direct-trunked transport, calls are transported between the SWC and the end office by means of a direct trunk, a dedicated facility, that does not pass through an intervening switch.¹³ The second service, tandem-switched transport, routes calls from the SWC to the end office through a tandem switch located between the SWC and the end office. Traffic travels over a dedicated circuit from the SWC to the tandem switch and then over a shared circuit, which carries the calls of many different IXCs, from the tandem switch to the incumbent LEC end office.¹⁴ Incumbent LEC tandem switches and end office switches switch interstate traffic between the transport trunks carrying traffic to and from the IXC POPs and the end users' local loops.

10. Charges for special access services generally are divided into channel termination charges and channel mileage charges. Channel termination charges recover the costs of facilities between the customer's premises and the LEC end office and the costs of facilities between the IXC POP and the serving wire center. Channel mileage charges recover the costs of facilities (also known as interoffice facilities) between the serving wire center and the LEC end office serving the end user.

2. Price Caps

11. In 1990, the Commission replaced rate-of-return regulation for the BOCs and GTE with an incentives-based system of regulation that encourages companies to: (1) improve their efficiency by developing profit-making incentives to reduce costs; (2) invest efficiently in new plant and facilities; and (3) develop and deploy innovative service offerings.¹⁵ The price cap plan is designed to replicate some of the efficiency incentives found in fully competitive markets and to act as a transitional regulatory scheme until actual competition makes price cap regulation unnecessary.¹⁶

¹² See 47 C.F.R. § 69.110 (requiring LECs to impose flat-rated charges on IXCs to recover the costs of entrance facilities).

¹³ See 47 C.F.R. § 69.112 (requiring LECs to impose a flat-rated charge on IXCs to recover the costs of direct-trunked transport).

¹⁴ See 47 C.F.R. § 69.111 (prescribing a three-part rate structure for LEC recovery from IXCs of tandem-switched transport costs: a flat-rated charge for the dedicated facility from the LEC serving wire center to the tandem switch, a per-minute tandem switching charge, and a per-minute charge for common transport from the tandem switch to the LEC end office).

¹⁵ Price Cap Performance Review for Local Exchange Carriers, CC Docket No. 94-1, Second Further Notice of Proposed Rulemaking, 11 FCC Rcd 858, 863 (1995) (*Price Cap Second FNPRM*). As noted *supra* at Section I, other local exchange carriers could opt into price cap regulation. *Id.*

¹⁶ Rules governing price cap LECs are set forth in Part 61 of our rules. 47 C.F.R. Part 61.

12. Under the original price cap plan, interstate access services were grouped into four different baskets: the common line, traffic-sensitive, special access, and interexchange baskets.¹⁷ In the *Second Transport Order*, the Commission combined transport and special access services into the newly created trunking basket.¹⁸ Each basket is subject to a price cap index (PCI), which caps the total charges a LEC may impose for interstate access services in that basket.¹⁹ The PCI is adjusted annually by a measure of inflation minus a "productivity factor," or "X-Factor."²⁰ A separate adjustment is made to the PCI for "exogenous" cost changes, which are changes outside the carrier's control and not otherwise reflected in the price cap formula.²¹

13. Within the traffic-sensitive and trunking baskets, services are grouped into service categories and subcategories. Rate revisions for these services are limited by upper and, in the original price cap plan, lower pricing bands established for that particular service.²² Originally, the pricing band limits for most of the service categories and subcategories were set at five percent above and below the Service Band Index (SBI).²³ In 1995, however, the Commission increased the lower pricing bands to ten percent for those service categories in the trunking and traffic-sensitive baskets and 15 percent for those services subject to density zone pricing.²⁴ These pricing

¹⁷ *LEC Price Cap Order*, 5 FCC Rcd at 6788. Originally, interexchange services were to be included in the basket containing special access offerings; however, the Commission concluded that combining these services into one basket "raised issues concerning the flow-through of exogenous costs that can be solved by separating the interexchange activity from interstate access." *Id.* Accordingly, the Commission created the interexchange basket for those LECs that offer interexchange services. *Id.*

¹⁸ Transport services originally were placed in the traffic-sensitive basket. *Transport Rate Structure and Pricing*, CC Docket No. 91-213, Second Report and Order, 9 FCC Rcd 615, 622 (1994) (*Second Transport Order*).

¹⁹ *Id.*

²⁰ *Price Cap Second FNPRM*, 11 FCC Rcd at 863. For a complete discussion of the "X-Factor," see *Price Cap Performance Review*, 10 FCC Rcd at 9005-6; see also *Price Cap Performance Review for Local Exchange Carriers*, CC Docket No. 96-262, Fourth Report and Order, 12 FCC Rcd 16642 (1997) (*Price Cap Fourth Report and Order*), *aff'd in part, rev'd in part*, U.S. Telephone Ass'n v. FCC, --- F.3d ----, 1999 WL 317035 (D.C.Cir. May 21, 1999) (NO. 97-1469).

²¹ *LEC Price Cap Order*, 5 FCC Rcd at 6792.

²² 1993 Annual Access Tariff Filings, CC Docket No. 93-193, Phase I, Part 2, Memorandum Opinion and Order, 12 FCC Rcd 6277, 6286 (1997); see also *Access Reform NPRM*, 11 FCC Rcd at 21372; *Price Cap Second FNPRM*, 11 FCC Rcd at 864. We note that there are no upper and lower banding requirements imposed on the common line basket and the interexchange baskets. *LEC Price Cap Order*, 5 FCC Rcd at 6811.

²³ 1993 Annual Access Tariff Filings, CC Docket No. 93-193, Phase I, Part 2, Memorandum Opinion and Order, 12 FCC Rcd 6277, 6286 (1997). The SBI is a subindex of the prices for each category or subcategory.

²⁴ *Price Cap Performance Review for Local Exchange Carriers*, CC Docket No. 94-1, First Report and Order, 10 FCC Rcd 8961, 9129-30, 9141 (1995) (*Price Cap Performance Review*). Density zone pricing is a system that permits LECs to reduce gradually rates in geographic areas that are less costly to serve, and to increase rates in

bands give price cap LECs the ability to raise and lower rates for elements or services as long as the actual price index (API)²⁵ for the relevant basket does not exceed the PCI for that basket, and the prices for each category of services within the basket are within the established pricing bands.²⁶ Together, the PCI and pricing bands restrict a price cap LEC's ability to offset price reductions for services that are subject to competition with price increases for services that are not subject to competition.²⁷

B. Pricing Flexibility

14. When it adopted the *LEC Price Cap Order* in 1990, the Commission required price cap LECs to offer all interstate special and switched access services at geographically averaged rates for each study area.²⁸ Since that time, the Commission has taken significant steps to increase the LECs' pricing flexibility and ability to respond to the advent of competition in the exchange access market. In the *Special Access* and *Switched Transport Expanded Interconnection Orders*, the Commission permitted LECs to introduce density zone pricing for high capacity special access and switched transport services in a study area, provided that they could demonstrate the presence of "operational" special access and switched transport expanded interconnection arrangements and at least one competitor in the study area.²⁹ The Commission also permitted price cap LECs to

areas that are more costly to serve. Transport Rate Structure and Pricing, CC Docket No. 91-213, Third Memorandum Opinion and Order on Reconsideration, 10 FCC Rcd 3030, 3042 (1994). As discussed in more detail below, the Commission subsequently eliminated the lower service band indices. See *infra* Section II.B.

²⁵ The "actual price index" is a weighted index of the rates that a price cap carrier is charging, or proposes to charge, for the services in a particular basket. See 47 C.F.R. §§ 61.3(b), 61.46.

²⁶ *Access Reform NPRM*, 11 FCC Rcd at 21372, 21485.

²⁷ The ability of a price cap LEC to raise rates for some services as a result of rate reductions for other services within the same basket or band is referred to as "headroom."

²⁸ *LEC Price Cap Order*, 5 FCC Rcd at 6788 (1990) (*LEC Price Cap Order*); see also *Price Cap Second FNPRM*, 11 FCC Rcd at 866.

²⁹ Expanded Interconnection with Local Telephone Company Facilities; Amendment of the Part 69 Allocation of General Support Facility Costs, CC Docket Nos. 91-141 and 92-333, Report and Order, 7 FCC Rcd 7369, 7454 n.411 (1992) (*Special Access Expanded Interconnection Order*), vacated in part and remanded, *Bell Atlantic Tel. Cos. v. FCC*, 24 F.3d 1441 (D.C. Cir. 1994); Expanded Interconnection with Local Telephone Company Facilities, 9 FCC Rcd 5154, 5196 (1994) (*Virtual Collocation Order*); Switched Transport Expanded Interconnection with Local Telephone Company Facilities, CC Docket No. 91-141, Second Report and Order and Third Notice of Proposed Rulemaking, 8 FCC Rcd 7374, 7425-32 (1993) (*Switched Transport Expanded Interconnection Order*), *aff'd*, *Virtual Collocation Order*, 9 FCC Rcd 5196; see also Section V, *infra*. "Expanded interconnection" refers to the interconnection of one carrier's circuits with those of a LEC at one of the LEC's wire centers so that the carrier can provide certain facilities-based access services. See *Virtual Collocation Order*, 9 FCC Rcd at 5158. An expanded interconnection offering is deemed "operational" when at least one interconnector has taken a switched cross-connect element. *Switched Transport Expanded Interconnection Order*, 8 FCC Rcd at 7426-27.

offer volume and term discounts for special access and switched transport services upon specific competitive showings.³⁰

15. Subsequently, the Commission eliminated the lower service band indices, concluding that this action would lead to lower prices and encourage LECs to charge rates that reflect the underlying costs of providing exchange access services.³¹ The Commission found that the PCI and upper pricing bands adequately control predatory pricing and that greater downward pricing flexibility would benefit consumers both directly through lower prices and indirectly by encouraging only efficient competitive entry.³²

16. In that same order, the Commission also relaxed the procedures for introducing new switched access services, in response to arguments that new services and technologies do not fit the Part 69 rate structure requirements.³³ The Commission prescribed the original rate structure for introducing new switched access services in 1983.³⁴ At that time, incumbent LECs were required to file a Part 69 waiver each time they wanted to introduce a new rate element for switched access service that did not conform to the prescribed switched access rate structure.³⁵ A Part 69 waiver required incumbent LECs to demonstrate that "special circumstances warrant deviation from the general rule and that such deviation will serve the public interest."³⁶ Incumbent

³⁰ *Special Access Expanded Interconnection Order*, 7 FCC Rcd at 7463; *Switched Transport Expanded Interconnection Order*, 8 FCC Rcd at 7435. The Commission allowed LECs to offer volume and term discounts for switched transport services in a study area upon demonstration of one of the following conditions: (1) 100 DS1-equivalent switched cross-connects (*i.e.*, the cabling inside the LEC central office that connects the LEC network to the collocated equipment dedicated to a competitive access provider using expanded interconnection) are operational in the Zone 1 offices in the study area; or (2) an average of 25 DS1-equivalent switched cross-connects per Zone 1 office are operational. In study areas with no Zone 1 offices, volume and term discounts may be implemented once five DS1-equivalent switched cross-connects are operational in the study area. *Switched Transport Expanded Interconnection Order*, 8 FCC Rcd at 7435.

³¹ *Access Reform NPRM*, 11 FCC Rcd at 21487.

³² *Id.*

³³ *Id.* at 21488.

³⁴ See 47 C.F.R. Part 69; see also MTS and WATS Market Structure, CC Docket No. 78-72, Phase I, Third Report and Order, 93 FCC 2d 241 (1983) (*Access Charge Order*). The Commission has not prescribed a special access rate structure. *Access Charge Order*, 93 FCC 2d at 314-15.

³⁵ Section 1.3 permits the Commission to grant waivers of any of its rules if "good cause therefor is shown." 47 C.F.R. § 1.3.

³⁶ See *Northeast Cellular Telephone Company v. FCC*, 897 F.2d 1164, 1166 (D.C. Cir. 1990) (*Northeast Cellular*); *WAIT Radio v. FCC (WAIT Radio)*, 418 F.2d 1153 (D.C. Cir. 1969) ("Good cause" is interpreted to require petitioners to show that "special circumstances warrant deviation from the general rule and such deviation will serve the public interest.")

LECs also had to comply with the "new services" test, which required an incumbent LEC to demonstrate that its tariffed rates for new services would recover no more than the carrier's direct costs of providing the service, plus a reasonable amount of overhead, and no less than the carrier's direct costs of providing the service.³⁷ Finally, incumbent LECs were directed to file their tariffs introducing a new service on at least fifteen days' notice and to incorporate the new service into the appropriate price cap basket and indices within six to eighteen months after the new service tariff became effective.³⁸

17. The Commission found that the Part 69 rate structure imposed a costly, time-consuming, and unnecessary burden on incumbent LECs and significantly impeded the introduction of new services.³⁹ Accordingly, the Commission modified the Part 69 rate structure rules to permit an incumbent LEC to introduce a new service by filing a petition based on a "public interest" standard that is easier to satisfy than the general standard applicable to waivers of the Commission's rules.⁴⁰ In addition, under the new rules, once an initial incumbent LEC has satisfied the public interest requirement for establishing new rate elements for a new switched access service, another incumbent LEC may file a petition seeking authority to introduce an identical new service, and its petition will be reviewed within ten days of the release of a Public Notice. The LEC may introduce the new rate element following the ten-day period, unless the Common Carrier Bureau (the Bureau) informs the LEC before that time that its new service does not qualify for "me too" treatment.⁴¹

18. The Commission also recognized that additional modifications to the Part 69 rate structure could increase consumer choice, streamline regulation, and increase consumer welfare

³⁷ A new service is one that expands the range of service options available to a customer. In the *LEC Price Cap Order*, the Commission concluded that it would not limit the definition of "new services" to services that employ a new technology or functional capability. *LEC Price Cap Order*, 5 FCC Rcd at 6824; see also 47 C.F.R. § 61.49(f)(2); Amendments of Part 69 of the Commission's Rules Relating to the Creation of Access Charge Subelements for Open Network Architecture, CC Docket Nos. 89-79 and 87-313, Report and Order and Order on Further Reconsideration and Supplemental Notice of Proposed Rulemaking, 6 FCC Rcd 4524, 4531 (1991) (adopting the direct cost test); Amendments of Part 69 of the Commission's Rules Relating to the Creation of Access Charge Subelements for Open Network Architecture, CC Docket Nos. 89-79 and 87-313, Memorandum Opinion and Order on Second Further Reconsideration, 7 FCC Rcd 5235, 5237 (1992) (eliminating the pre-existing net revenue test as superfluous).

³⁸ See Implementation of Section 402(b)(1)(A) of the Telecommunications Act of 1996, CC Docket No. 96-187, Report and Order, 12 FCC Rcd 2170, 2203 (1997) (*Tariff Streamlining Order*) (LECs must file their tariffs introducing a new service on at least fifteen days' notice.); 47 C.F.R. § 61.43 (Tariffs introducing a new service must be incorporated into the appropriate price cap basket and indices within six to eighteen months after the new service tariff takes effect.)

³⁹ *Access Reform NPRM*, 11 FCC Rcd at 21490.

⁴⁰ *Id.*; see also 47 C.F.R. § 69.4(g).

⁴¹ *Access Reform NPRM*, 11 FCC Rcd at 21490.

by increasing incentives for innovation.⁴² The Commission, therefore, sought comment on whether to permit price cap LECs to establish new switched access rate elements without prior approval.⁴³ The Commission also invited comment on whether to eliminate the new services test and permit LECs to offer new services free from price cap regulation.⁴⁴ In the *Access Reform First Report and Order*, the Commission deferred resolution of these issues, as well as other issues concerning the timing and degree of pricing flexibility, to a future report and order.⁴⁵

C. Summary

1. Pricing Flexibility

19. Since the release of the *Access Reform First Report and Order*, we have re-examined the record generated in response to the *Access Reform NPRM* and the *Price Cap Second FNPRM*; we have observed competition develop in the marketplace; and we have invited parties to update and refresh the record relating to access charge reform to reflect any changes that may have taken place since May 1997.⁴⁶ In addition, we have received and reviewed several petitions (and the associated records) from BOCs seeking pricing flexibility in the form of forbearance from dominant carrier regulation in the provision of certain special access and high capacity services.⁴⁷ Although our current price cap regime gives LECs some pricing flexibility and considerable incentives to operate efficiently, significant regulatory constraints remain. As the market becomes more competitive, such constraints become counter-productive. We recognize that the variety of access services available on a competitive basis has increased significantly since the adoption of our price cap rules. Therefore, in response to changing market conditions, we grant price cap LECs immediate flexibility to deaverage services in the trunking basket and to introduce new services on a streamlined basis. We also remove certain interstate interexchange services from price cap regulation upon implementation of intra- and interLATA toll dialing parity, and we establish a framework for granting price cap LECs further pricing flexibility upon satisfaction of

⁴² *Id.* at 21440-41.

⁴³ *Id.*

⁴⁴ *Id.*

⁴⁵ *Access Reform First Report and Order*, 12 FCC Rcd at 16094.

⁴⁶ Commission Asks Parties to Update and Refresh the Record for Access Charge Reform and Seeks Comment on Proposals for Access Charge Reform Pricing Flexibility, CC Docket No. 96-262, Public Notice, 13 FCC Rcd 21522 (1998) (*October 5 Public Notice*).

⁴⁷ In the order that they were filed, these forbearance petitions are: U S West Forbearance Petition (Phoenix), CC Docket No. 98-157 (filed Aug. 24, 1998); SBC Communications, Inc. Forbearance Petition, CC Docket No. 98-227 (filed Dec. 7, 1998); U S West Forbearance Petition (Seattle), CC Docket No. 99-1 (filed Dec. 30, 1998); Bell Atlantic Telephone Companies Forbearance Petition, CC Docket No. 99-24 (filed Jan. 20, 1999); and Ameritech Forbearance Petition, CC Docket No. 99-65 (filed Feb. 5, 1999).

certain competitive showings and seek comment on additional flexibility for certain switched access services.

a. Immediate Regulatory Relief

20. As discussed above, the original rate structure for interstate switched transport services required price cap LECs to charge averaged rates throughout a study area.⁴⁸ The Commission subsequently found that this requirement forced LECs to price above cost in the high-traffic, lower-cost areas where competition is more likely to develop.⁴⁹ In the *Switched Transport Expanded Interconnection Order*, therefore, the Commission created a density zone pricing plan that allows some degree of deaveraging of rates for switched transport services.⁵⁰ The Commission concluded that relaxing the pricing rules in this manner would enable price cap LECs to respond to increased competition in the interstate switched transport market.⁵¹

21. Although the density zone pricing plan afforded some pricing flexibility to price cap LECs, it contained several constraints, such as the increased scrutiny applicable to plans with more than three zones. We now conclude that market forces, as opposed to regulation, are more likely to compel LECs to establish efficient prices. Accordingly, for purposes of deaveraging rates for services in the trunking basket, we eliminate the limitations inherent in our current density zone pricing plan and allow price cap LECs to define the scope and number of zones within a study area, provided that each zone, except the highest-cost zone, accounts for at least 15 percent of the incumbent LEC's trunking basket revenues in the study area and that annual price increases within a zone do not exceed 15 percent. In addition, we eliminate the requirement that LECs file zone pricing plans prior to filing their tariffs.

22. We also permit price cap LECs to introduce new services on a streamlined basis, without prior approval. Generally, we modify the Commission's rules to eliminate the public interest showing required by Section 69.4(g) and to eliminate the new services test (except in the case of loop-based new services) required under Sections 61.49(f) and (g).⁵² These modifications will eliminate the delays that now exist for the introduction of new services as well as encourage efficient investment and innovation.

23. Certain interstate interexchange services provided by price cap LECs are found in the interexchange basket, including interstate intraLATA services and certain interstate interLATA

⁴⁸ *Switched Transport Expanded Interconnection Order*, 8 FCC Rcd at 7423-24.

⁴⁹ *Id.* at 7424.

⁵⁰ *Id.* at 7426.

⁵¹ *Id.*

⁵² *See* Section III, *infra*.

services called "corridor services." In this Order, we allow price cap LECs to remove from the interexchange basket, and, hence, price cap regulation, their interstate intraLATA toll services and corridor services, provided the price cap LEC has implemented intra- and interLATA toll dialing parity in all of the states in which it provides local exchange service. The presence of competitive alternatives for these services, coupled with implementation of dialing parity, should prevent price cap LECs from exploiting over a sustained period any market power may possess with respect to these services and thus warrants removal of these services from price cap regulation.

b. Relief that Requires a Competitive Showing

24. In addition, we adopt a framework for granting further regulatory relief upon satisfaction of certain competitive showings. Relief generally will be granted in two phases and on an MSA (Metropolitan Statistical Area) basis.⁵³ To obtain Phase I relief, price cap LECs must demonstrate that competitors have made irreversible, sunk investments in the facilities needed to provide the services at issue. For instance, for dedicated transport and special access services,⁵⁴ price cap LECs must demonstrate that unaffiliated competitors have collocated in at least 15 percent of the LEC's wire centers within an MSA or collocated in wire centers accounting for 30 percent of the LEC's revenues from these services within an MSA.⁵⁵ Higher thresholds apply, however, for channel terminations between a LEC end office and an end user customer. In that case, the LEC must demonstrate that unaffiliated competitors have collocated in 50 percent of the price cap LEC's wire centers within an MSA or collocated in wire centers accounting for 65 percent of the price cap LEC's revenues from this service within an MSA. For traffic-sensitive, common line, and the traffic-sensitive components of tandem-switched transport services, a LEC must show that competitors offer service over their own facilities to 15 percent of the price cap LEC's customer locations within an MSA. Phase I relief permits price cap LECs to offer, on one day's notice, volume and term discounts and contract tariffs for these services, so long as the services provided pursuant to contract are removed from price caps. To protect those customers that may lack competitive alternatives, however, LECs receiving Phase I flexibility must maintain their generally available, price cap constrained tariffed rates for these services.

25. To obtain Phase II relief, price cap LECs must demonstrate that competitors have established a significant market presence (*i.e.*, that competition for a particular service within the MSA is sufficient to preclude the incumbent from exploiting any individual market power over a sustained period) for provision of the services at issue. Phase II relief for dedicated transport and

⁵³ Pricing flexibility also is available for the non-MSA sections of a study area, provided the price cap LEC satisfies the triggers adopted herein for MSAs.

⁵⁴ For purposes of this Order, "dedicated transport services" refer to entrance facilities, direct-trunked transport, and the dedicated component of tandem-switched transport.

⁵⁵ To satisfy the collocation triggers we adopt herein, an incumbent LEC must demonstrate, with respect to each wire center with collocation, that at least one of the competitors therein uses transport services provided by a transport provider other than the incumbent LEC.

special access services is warranted when a price cap LEC demonstrates that unaffiliated competitors have collocated in at least 50 percent of the LEC's wire centers within an MSA or collocated in wire centers accounting for 65 percent of the LEC's revenues from these services within an MSA. Again, a higher threshold applies to channel terminations between a LEC end office and an end user customer. In that case, a price cap LEC must show that unaffiliated competitors have collocated in 65 percent of the LEC's wire centers within an MSA or collocated in wire centers accounting for 85 percent of the LEC's revenues from this service within an MSA. Phase II relief permits price cap LECs to file tariffs for these services on one day's notice, free from both our Part 61 rate level and our Part 69 rate structure rules.⁵⁶

26. Because our ultimate goal is to continue to foster competition and allow market forces to operate where they are present, we also seek comment in the Notice on additional pricing flexibility for common line and traffic-sensitive services. First, we consider permitting price cap LECs to deaverage rates for services in the common line and traffic-sensitive baskets in conjunction with identification and removal of implicit universal service support in interstate access charges and implementation of an explicit high cost support mechanism. We also invite parties to comment on how we should define zones for purposes of deaveraging. In addition, we seek comment on which rate elements may be deaveraged and whether deaveraging should be subject to subscriber line charge (SLC) and presubscribed interexchange carrier charge (PICC) caps or any other constraint. We also seek comment on the appropriate Phase II triggers for granting greater pricing flexibility for traffic-sensitive, common line, and the traffic-sensitive components of tandem-switched transport services.

2. Modifications to Rate Structure

27. The Notice also seeks comment on certain price cap regulation issues. Specifically, consistent with the *Access Reform First Report and Order's* efforts to reform access charges so costs are recovered in a manner that reflects how they are incurred, we seek comment on adopting a capacity-based rate structure for local switching. The local switch, which consists of an analog or digital switching system and line and trunk cards, connects subscriber lines both with other local subscriber lines and with dedicated and common interoffice trunks.⁵⁷ As discussed in more detail below, prior to the *Access Reform First Report and Order*, the interstate allocated portion of these costs was recovered entirely through per-minute charges assessed on IXCs.⁵⁸

⁵⁶ As discussed in more detail below, we eliminate the low-end adjustment mechanism for those price cap LECs qualifying for and electing to exercise either Phase I or Phase II pricing flexibility. *See* Section VI.D.2, *infra*.

⁵⁷ Line cards connect subscriber lines to the switch, and trunk ports connect interoffice trunks to the switch. *Access Reform First Report and Order*, 12 FCC Rcd 16034.

⁵⁸ 47 C.F.R. § 69.106.

28. Recognizing that a significant portion of these costs (*i.e.*, the costs associated with line cards and trunk ports) do not vary with usage, however, the Commission determined that such non-traffic-sensitive costs should be recovered on a flat-rated, rather than usage sensitive, basis.⁵⁹ Accordingly, consistent with principles of cost-causation and economic efficiency, the Commission directed price cap LECs to reassign all line-side port costs from the Local Switching rate element to the Common Line rate element and to recover these costs through the common line rate elements, including the SLC and flat-rated PICC.⁶⁰ Because the record in that proceeding was not adequate, however, to determine whether and to what extent the remaining local switching costs were traffic-sensitive or non-traffic-sensitive, LECs continue to recover these costs through traffic-sensitive charges.⁶¹

29. We take this opportunity to re-examine the local switching rate structure to determine whether it reasonably reflects the manner in which price cap LECs incur costs. In the Notice, we invite comment on whether and to what extent we should modify further our price cap rules for the traffic-sensitive basket to reflect a capacity-based local switching rate structure.⁶²

30. We also invite parties to discuss proposed revisions to our rules for the common line basket, and we consider redefining the price cap baskets and pricing bands. Specifically, we solicit comment on whether to increase the "g" factor⁶³ in the common line PCI formula and whether we should revise the baskets so that services with flat rates are not placed in the same basket as services with traffic-sensitive rates. In addition, we seek comment on our tentative conclusion that the inflation measure in the PCI formula should be consistent with the measure defined by the Bureau of Labor Statistics (BLS).

3. CLEC Access Charges

31. In the *Access Reform NPRM*, the Commission sought comment on whether CLECs have market power in the provision of terminating access services and whether to regulate these services.⁶⁴ In the *Access Reform First Report and Order*, the Commission decided to treat CLECs as non-dominant in the provision of terminating access service, because they did not

⁵⁹ *Access Reform First Report and Order*, 12 FCC Rcd at 16034.

⁶⁰ *Id.*

⁶¹ *Access Reform First Report and Order*, 12 FCC Rcd at 16040.

⁶² See Section VIII.C, *infra*.

⁶³ See Section VIII.D, *infra*.

⁶⁴ *Access Reform NPRM*, 11 FCC Rcd at 21476.

appear at that time to possess market power.⁶⁵ The Commission stated, however, that it would revisit the issue of regulating CLEC terminating access rates if there were sufficient indications that CLECs were imposing unreasonable terminating access charges.⁶⁶

32. On October 23, 1998, AT&T filed a petition for declaratory ruling requesting that the Commission confirm that, under existing Commission rules and policies, an IXC may elect not to accept service at a price chosen by the CLEC.⁶⁷ In its petition, AT&T alleges that some CLECs impose switched access charges significantly higher than those charged by the ILEC competitors in the same area.⁶⁸ AT&T points to a Commission pronouncement in the *Access Reform First Report and Order* that "terminating rates that exceed those charged by the ILEC serving the same market may suggest that a CLEC's terminating access rates are excessive," thereby warranting Commission regulation.

33. In this Order, we deny AT&T's petition. We find, however, that the record developed in response to AT&T's petition suggests the need for the Commission to revisit the issue of CLEC access rates. Accordingly, in the accompanying Notice, we initiate a rulemaking to determine the reasonableness of CLEC access rates and whether the Commission might adopt rules to address, by the least intrusive means, any failure of market forces to constrain CLEC access charges.

III. NEW SERVICES

A. Background

34. In 1983, the Commission prescribed a rate structure for switched access services in Part 69 of its rules.⁶⁹ Originally, when an incumbent LEC wanted to offer a new switched access service, and the rate element or elements for that new service did not fit into the prescribed switched access rate structure, the LEC was required to obtain a waiver of Part 69 pursuant to

⁶⁵ *Access Reform First Report and Order*, 12 FCC Rcd at 16140-41.

⁶⁶ *Id.* at 16142.

⁶⁷ AT&T Petition for Declaratory Ruling, CCB/CPD No. 98-63 (Oct. 23, 1998).

⁶⁸ We note that there are pending before the Commission several complaints concerning CLECs' terminating access charges. For instance, on October 18, 1996, Total Telecommunications Services, Inc (TTS) and Atlas Telephone Company filed a complaint against AT&T alleging that AT&T failed to compensate TTS for terminating access services provided by TTS. The complaint also alleges that AT&T wrongfully discontinued service to TTS end users in violation of section 214 of the Act. *See* Total Telecommunications Services, Inc. and Atlas Telephone Company, Inc., File No. E-97-03, Complaint (Oct. 18, 1996).

⁶⁹ 47 C.F.R. Part 69; *Access Charge Order*, 93 FCC 2d 241. The Commission has not prescribed a special access rate structure. *Access Charge Order*, 93 FCC 2d at 314-15.

Section 1.3 of the Commission's rules.⁷⁰ In 1996, the Commission adopted Section 69.4(g) of its rules, which relaxed the switched access rate structure rules for price cap LECs.⁷¹ Under Section 69.4(g), a price cap LEC is no longer required to demonstrate that "special circumstances" warrant a Part 69 waiver; instead, it need only file a petition showing that the proposed new rate element would be in the "public interest," or that another LEC previously has established the same rate element.⁷²

35. In addition, a price cap LEC filing a tariff for a new service⁷³ must comply with the new services test, which requires the LEC to show that its new service rates will recover no more than the carrier's direct costs of providing the service, plus a reasonable level of overheads, and no less than the carrier's direct costs of providing the service.⁷⁴ Those tariffs must be filed on at least fifteen days' notice.⁷⁵ Finally, the LEC is required to incorporate its new services into the appropriate price cap basket and indices within six to eighteen months after the new service tariff takes effect, in conjunction with the carrier's annual access tariff filing.⁷⁶

36. In the December 1996 *Access Reform NPRM*, the Commission invited comment on three proposals for further relaxation of its new service rules to create incentives for price cap LECs to introduce services using new technologies: (1) enabling price cap LECs to establish new switched access rate elements without prior approval; (2) eliminating the new services test; and

⁷⁰ Section 1.3 permits the Commission to grant waivers of any of its rules if "good cause therefor is shown." 47 C.F.R. § 1.3. The court has interpreted this "good cause" standard to require petitioners to show that "special circumstances warrant deviation from the general rule and such deviation will serve the public interest." *Northeast Cellular; WAIT Radio*.

⁷¹ 47 C.F.R. § 69.4(g); Price Cap Performance Review for Local Exchange Carriers, CC Docket No. 94-1, Third Report and Order, 11 FCC Rcd 21354, 21490 (1996) (*Price Cap Third Report and Order*).

⁷² 47 C.F.R. § 69.4(g).

⁷³ A "new service" is one that expands the range of service options available to a customer. The Commission expressly decided not to limit the definition of "new services" to services that employ a new technology or functional capability. *LEC Price Cap Order*, 5 FCC Rcd at 6824.

⁷⁴ See 47 C.F.R. § 61.49(f)(2); Amendments of Part 69 of the Commission's Rules Relating to the Creation of Access Charge Subelements for Open Network Architecture, CC Docket Nos. 89-79 and 87-313, Report and Order and Order on Further Reconsideration and Supplemental Notice of Proposed Rulemaking, 6 FCC Rcd 4524, 4531 (1991) (adopting the direct cost test); Amendments of Part 69 of the Commission's Rules Relating to the Creation of Access Charge Subelements for Open Network Architecture, CC Docket Nos. 89-79 and 87-313, Memorandum Opinion and Order on Second Further Reconsideration, 7 FCC Rcd 5235, 5237 (1992) (eliminating the pre-existing net revenue test as superfluous).

⁷⁵ See *Tariff Streamlining Order*, 12 FCC Rcd at 2203.

⁷⁶ 47 C.F.R. § 61.43.

(3) permitting price cap LECs to offer new services outside of price cap regulation.⁷⁷ In the *Access Reform First Report and Order*, the Commission deferred consideration of pricing flexibility issues, including these new service issues, to a future Order.⁷⁸ Bell Atlantic later proposed removing new services from price cap regulation "immediately,"⁷⁹ and the Commission invited comment on Bell Atlantic's proposal.⁸⁰ Subsequently, the Commission granted a petition to forbear from enforcing Part 69 rate structure requirements with respect to new service tariffs filed by any incumbent LEC serving more than 50,000 access lines, but less than two percent of the nation's access lines.⁸¹

B. Discussion

37. We find that the record supports permitting incumbent LECs to introduce new services on a streamlined basis. The Commission adopted price cap regulation in part to encourage price cap LECs to innovate,⁸² and to develop new services.⁸³ Thus, to the extent that our new service rules impede the introduction of new services, they undermine one of the Commission's goals in adopting price cap regulation. The new service rules clearly delay the introduction of new services, because the Commission needs time to review Section 69.4(g) public interest showings, and price cap LECs need time to prepare the cost support showing required by the new services test.⁸⁴ Moreover, it is not clear that the new services rules provide any benefits that justify such delay. By definition, a new service expands the range of service options available to consumers.⁸⁵ Thus, the introduction of a new service does not by itself compel any access customer to reconfigure its access services and so cannot adversely affect any

⁷⁷ *Access Reform NPRM*, 11 FCC Rcd at 21440-41.

⁷⁸ *Access Reform First Report and Order*, 12 FCC Rcd at 16094.

⁷⁹ Bell Atlantic *ex parte* statement of April 27, 1998, at 34.

⁸⁰ *October 5 Public Notice*, 13 FCC Rcd at 21523.

⁸¹ Petition for Forbearance of the Independent Telephone & Telecommunications Alliance, AAD File No. 98-43, Sixth Memorandum Opinion and Order, FCC 99-108 (rel. June 30, 1999) (*ITTA Forbearance Order*).

⁸² *LEC Price Cap Order*, 5 FCC Rcd at 6790.

⁸³ *Id.* at 6825.

⁸⁴ Some parties assert that meeting the Section 69.4(g) public interest standard is as burdensome or almost as burdensome as meeting the Section 1.3 waiver standard. *See, e.g.*, PacTel Comments at 23; GTE Comments at 52; Ameritech Oct. 26, 1998, Comments at 17. Petitioners seeking waiver of the Commission's rules under Section 1.3 must show that deviation from the general rule "will serve the public interest." *Northeast Cellular*, 897 F.2d at 1166. Similarly, Section 69.4(g) requires petitioners to show that establishing the new rate element "would be in the public interest."

⁸⁵ *LEC Price Cap Order*, 5 FCC Rcd at 6824-25.

access customer. Because new services may benefit some customers, and existing customers can continue to purchase existing services if they find the new service rate structure or rate level unattractive,⁸⁶ we conclude that it serves the public interest to permit price cap LECs to introduce new services on a streamlined basis.

38. In addition, the Commission adopted Part 69 before the advent of competition. Now, the delay caused by the new service rules can place price cap LECs at a competitive disadvantage. Competitive LECs that have notice of a price cap LEC's Section 69.4(g) petition may be able to begin offering the service before the incumbent LEC has been granted permission to establish new rate elements for the new service, thus diminishing the incumbent's incentives to develop and offer new services.⁸⁷ With the removal of this competitive disadvantage, price cap LECs will be better able to respond to competition from CLECs.

39. Accordingly, we revise Section 69.4 of the Commission's rules to eliminate the public interest showing required by Section 69.4(g), and to enable price cap LECs to establish any new switched access rate element, in addition to the access rate elements currently required by Section 69.4. We also eliminate the new services test in Sections 61.49(f) and (g) for all new services except loop-based services. We are concerned that new services that employ local loop facilities⁸⁸ raise cost allocation issues that the Commission has not yet addressed. In the *GTE DSL Reconsideration Order*,⁸⁹ for example, we referred to the Federal-State Joint Board for consideration in Docket No. 80-286 a petition for clarification and/or reconsideration filed by NARUC.⁹⁰ NARUC's petition sought clarification regarding the application of our Part 36 separations rules while the Joint Board considered the proper allocation of loop costs associated

⁸⁶ Bell Atlantic Comments at 46; BellSouth Comments at 37; U S West Comments at 34.

⁸⁷ Reviewing a public interest petition can be a long process. For example, the Commission needed almost a year to act on some recent petitions seeking permission to establish rate elements for Synchronous Optical Network (SONET)-based services. *See, e.g.*, Petition to Establish Part 69 Rate Elements to Offer Switched Access Rate Elements for SONET-based Service, DA 99-513 (Com. Car. Bur., Competitive Pricing Div., released March 17, 1999) (*U S West Petition*); Bell Atlantic Telephone Companies Establishment of New Rate Elements to Offer Enterprise SONET Service, DA 99-514 (Com. Car. Bur., Competitive Pricing Div., rel. March 17, 1999); BellSouth Telecommunications, Inc. Part 69.4(g)(1) Public Interest Petition to Establish New Rate Elements for Switched Access Versions of BellSouth's Smartgate Service and BellSouth SPA Managed Shared Network, DA 98-2271 (Com. Car. Bur., Competitive Pricing Div., rel. Nov. 9, 1998).

⁸⁸ For purposes of this section, we define loop-based new services in accordance with the definitions that govern jurisdictional separations. *See* 47 C.F.R. Part 36. "Loop-based" services are services that employ Subcategory 1.3 facilities. *See* 47 C.F.R. § 36.154 (Subcategory 1.3 facilities are "[s]ubscriber or common lines that are jointly used for local exchange service and exchange access for state and interstate interexchange services.")

⁸⁹ GTE Telephone Operating Cos. GTOC Transmittal No. 1148, CC Docket No. 98-79, FCC No. 99-41, Memorandum Opinion and Order (rel. February 26, 1999) (*GTE DSL Reconsideration Order*).

⁹⁰ *GTE DSL Reconsideration Order*, at ¶ 9.

with special access tariffs such as the GTE DSL tariff.⁹¹ Noting that the separations and cost allocation issues NARUC raised were beyond the scope of the limited investigation in the tariff proceeding, we stated that we would address these important issues in conjunction with the Joint Board.⁹² Until these issues are resolved, it is not appropriate to permit price cap LECs to file tariffs for new loop-based services without satisfying the cost support requirements of the new services test.

40. Bell Atlantic argues that price cap LECs should be permitted to file tariffs for new services on one day's notice.⁹³ We conclude that Bell Atlantic's request is in the public interest. The current fifteen-day notice period is no longer warranted. A primary focus of our review of new service tariffs is to determine whether the LEC complied with the new service test. By eliminating the new services test, we greatly reduce the need for reviewing LEC new service tariff filings. In addition, no customer is required to purchase the new service. Furthermore, a longer notice period would delay the introduction of new services and thus undercut the reasons for revising the price cap new service rules here.

41. We are not persuaded by the arguments advanced by parties opposing further deregulation of new services offered by price cap LECs. Some IXCs are concerned that incumbent LECs might offer new services in a manner that would make them available only to the LECs' own long distance affiliates.⁹⁴ These IXCs do not explain why or how streamlined introduction of new services would in any way affect the Commission's ability to enforce section 202 of the Act, which prohibits unreasonable discrimination.⁹⁵ Accordingly, we conclude that permitting LECs to offer new services on a streamlined basis does not increase the likelihood of unreasonable discrimination. IXCs may file complaints under section 208 of the Act,⁹⁶ should they believe that such unreasonable discrimination has occurred.

42. AT&T notes that the Commission made it easier for incumbent price cap LECs to introduce new services in the *Price Cap Third Report and Order*, and it argues that no further deregulation is necessary to encourage LECs to introduce new services.⁹⁷ Regardless of LECs' incentives to introduce new services, we conclude above that the benefits of our current new

⁹¹ *Id.* at ¶ 7.

⁹² *Id.* at ¶ 9.

⁹³ Bell Atlantic Comments at 47. *See also* USTA Oct. 26, 1998 Comments at 36 and Att. E.

⁹⁴ AT&T Comments at 81-82; MCI Comments at 63; Sprint Comments at 43.

⁹⁵ 47 U.S.C. § 202.

⁹⁶ 47 U.S.C. § 208.

⁹⁷ AT&T Comments at 81.

service rules do not justify the delay caused by those rules, and we reject AT&T's argument. Elimination of the new services rules serves the Commission's goals of streamlining our regulations, removing unnecessary regulatory barriers, and increasing consumer choice.

43. We will not, however, permit price cap LECs to offer new services outside of price cap regulation, as parties suggest.⁹⁸ MCI argues that offering new services outside of price cap regulation will encourage incumbent LECs to create "new" services that differ little from an existing service.⁹⁹ Specifically, MCI theorizes that, as access customers shift to the new service, the demand weight placed on the existing service in calculating the actual price index (API) would decrease, thus enabling the LEC to raise the price of the existing service. Subsequently, according to MCI, the LEC could increase the new service price and leave access customers with no lower-priced alternatives.¹⁰⁰ We agree with MCI that the introduction of new services outside of price caps ultimately might enable price cap LECs to raise rates for both new services and existing services to unreasonable levels. In contrast to the conditions we adopt elsewhere in this Order for removal of services from price caps,¹⁰¹ we do not predicate the new services relief we adopt here upon any showing of competition for the services at issue, thus we are not convinced by price cap LEC arguments that rates, terms, and conditions for new services will be constrained by market forces.¹⁰²

44. At this time, we revise only the new service requirements applicable to price cap LECs, not rate-of-return LECs, for several reasons. First, we have recently granted a petition to forbear from enforcing Part 69 rate structure requirements with respect to new service tariffs filed by a considerable number of rate-of-return LECs, *i.e.*, those serving more than 50,000 access lines, but less than two percent of the nation's access lines.¹⁰³ In addition, we note that the new services test is applicable only to price cap LECs, and so is irrelevant for rate-of-return LECs. Moreover, the Commission created a separate docket to consider the access reform issues specific to rate-of-return carriers.¹⁰⁴ In that proceeding, the Commission invited comment on revising the

⁹⁸ See, *e.g.*, Bell Atlantic *ex parte* statement of April 27, 1998, at 34 (suggesting immediate removal of new services from price cap regulation).

⁹⁹ MCI Comments at 62-63.

¹⁰⁰ MCI Comments at 62-63.

¹⁰¹ See, *e.g.*, Section VI *infra*.

¹⁰² See, *e.g.*, Bell Atlantic *ex parte* statement of April 27, 1998, at 34. In Section VI below, we establish a framework for granting price cap LECs greater pricing flexibility, including the ability to offer services pursuant to contract tariff and to remove services from price caps, if they satisfy certain competitive showings. In that section, we also adopt a procedure pursuant to which we will grant these types of flexibilities for new services.

¹⁰³ See *ITTA Forbearance Order*.

¹⁰⁴ *Rate of Return Access Reform NPRM*, 13 FCC Rcd 14238.

new service requirements applicable to rate-of-return LECs,¹⁰⁵ and we will address those issues on the basis of the record in that docket. Finally, we relax the new service requirements for price cap LECs in part to remove a competitive disadvantage from price cap LECs, so that they can better respond to developing competition from CLECs. Because rate-of-return LECs do not face competition to the same extent as price cap LECs, there is less need to remove any competitive disadvantage they face at this time.

IV. REMOVAL OF INTERSTATE INTER- AND INTRALATA TOLL SERVICES FROM PRICE CAP REGULATION

A. Introduction

45. The Commission currently regulates in the interexchange basket the rates that price cap LECs charge for particular interstate interexchange services.¹⁰⁶ Among the services in this basket are certain interstate interLATA toll services, called "corridor" services, and interstate intraLATA toll services.¹⁰⁷ We conclude that price cap LECs' corridor and interstate intraLATA toll services will face sufficient competition upon full implementation of inter- and intraLATA toll dialing parity¹⁰⁸ to preclude the price cap LECs from exploiting over a sustained period any individual market power they may have with respect to these services. Consequently, once a price cap LEC has implemented inter- and intraLATA toll dialing parity everywhere it provides local exchange services at the holding company level, we will allow the price cap LEC to remove all of its corridor and interstate intraLATA toll services from price cap regulation,¹⁰⁹ and subsequently to file tariffs for these services on one day's notice and without cost support.¹¹⁰ Allowing price

¹⁰⁵ *Id.* at 14269-70.

¹⁰⁶ See 47 C.F.R. § 61.42(d)(4) (creating price cap LEC basket for "interstate interexchange services that are not classified as access services for the purpose of part 69" of the Commission's rules). See also 47 C.F.R. § 61.45(b) (explaining how price cap LECs must adjust their price cap indices for various baskets of price cap services, including the interstate interexchange basket).

¹⁰⁷ See *LEC Price Cap Order*, 5 FCC Rcd at 6811, 6812. For explanations of "LATA," as well as corridor and interstate intraLATA toll services, see Section IV.B.

¹⁰⁸ See 47 C.F.R. §§ 51.205, 51.209, 51.211, 51.213; Implementation of the Local Competition Provisions in the Telecommunications Act of 1996, CC Docket No. 96-98, Second Report and Order and Memorandum Opinion and Order, 11 FCC Rcd 19392 (1996) (*Dialing Parity Order*) (implementing dialing parity requirements of 47 U.S.C. § 251), *vacated in part*, California v. FCC, 124 F.3d 934 (8th Cir. 1997), *rev'd*, AT&T v. Iowa Utils. Bd., 119 S. Ct. 721 (1999); Order, 14 FCC Rcd 5263 (1999) (*Dialing Parity Extension Order*).

¹⁰⁹ Thus, a BOC must provide inter- and intraLATA toll dialing parity throughout its region before it may remove these services from price cap regulation.

¹¹⁰ Thus, this Order addresses much of the relief Bell Atlantic sought in its 1995 petition to deregulate its provision of corridor service. See Bell Atlantic Petition for Regulation as a Nondominant Provider of Interstate

cap LECs to do so removes unnecessary regulatory constraints and enhances the operation of competitive forces where they provide corridor and interstate intraLATA toll services.¹¹¹

B. Background

46. The 1982 AT&T consent decree divided the former Bell territory into geographic units called "Local Access and Transport Areas," or "LATAs."¹¹² Most states have multiple LATAs, and LATA boundaries generally are contained within a single state. Some LATAs, however, cross state lines. With certain exceptions, the consent decree prohibited the BOCs from transporting telecommunications traffic between LATAs (*interLATA* services), but permitted them to carry traffic within a LATA (*intraLATA* services).¹¹³ Thus, at the time of divestiture, IXC's were permitted to transport interLATA traffic but BOCs generally were not.¹¹⁴ Telephone calls that do not leave customers' immediate local calling areas are intraLATA local calls and are subject only to the monthly rate that customers pay for local services. Telephone calls to destinations outside of the local calling area are toll calls subject to an additional charge. A LATA often encompasses more than one immediate local calling area, so intraLATA calls can be either local or toll calls.

47. Despite the consent decree's provisions prohibiting BOCs from providing interLATA services, it made an exception for certain interstate interLATA services, called corridor services.¹¹⁵ Corridor services are toll services that carry traffic from five counties in Northern New Jersey into New York City, from Philadelphia and its suburbs into three counties in New

InterLATA Corridor Service, Public Notice, 10 FCC Rcd 9873 (1995). We will address the provision of interstate intraLATA toll services by rate-of-return LECs in conjunction with our consideration of access reform for those carriers. *See Rate of Return Access Reform Notice*.

¹¹¹ *Compare* Competition in the Interstate Interexchange Marketplace, CC Docket No. 90-132, Report and Order, 6 FCC Rcd 5880, 5881 (1991) (*Interexchange Competition Order*) (lifting certain tariff regulation of AT&T business services on the grounds that competition for those services was "sufficiently effective," and concluding that the regulatory relief would benefit consumers).

¹¹² *See* United States v. Western Elec. Co., 569 F. Supp. 990, 993-94 (D.D.C. 1983) (*Western Elec. Co. I*). *See also* 47 U.S.C. § 153(25) (defining "LATA" as "a contiguous geographic area ... established before the date of enactment of the Telecommunications Act of 1996 by a Bell operating company such that no exchange area includes points within more than 1 metropolitan statistical area, consolidated metropolitan statistical area, or State, except as expressly permitted under the AT&T Consent Decree," or as created or modified by a BOC after the date of enactment and approved by the Commission).

¹¹³ *Western Elec. Co. I*, 569 F. Supp. at 993-94.

¹¹⁴ *Id.*

¹¹⁵ *LEC Price Cap Order*, 5 FCC Rcd at 6811, 6846 n.252.

Jersey, and from those three counties back into the Philadelphia area.¹¹⁶ At the time of the consent decree, these areas were in the Bell Atlantic and NYNEX regions. These companies have since merged.

48. BOCs and independent incumbent LECs also provide interstate intraLATA toll services. Interstate intraLATA toll calls are calls that leave an immediate local calling area and cross state lines but remain within a single LATA, such as some calls from Chicago, Illinois, to Gary, Indiana. The BOCs and independent incumbent LECs provide corridor and interstate intraLATA toll services in competition with the long-distance services of AT&T, Sprint, MCI, and many other long-distance companies.

49. Because the Commission has treated incumbent LECs as having market power in the provision of most services within their service areas, the rates that incumbent LECs may charge for corridor and interstate intraLATA toll services currently are subject to dominant carrier regulation.¹¹⁷ Dominant carriers are subject to price cap or rate-of-return regulation, must file tariffs -- on a minimum of seven days' notice and often more -- and usually with cost support data.¹¹⁸ Non-dominant carriers, on the other hand, are not subject to rate regulation and may file tariffs on one day's notice, without cost support, that are presumed lawful.¹¹⁹

50. To spur competition, section 251(b)(3) of the Act requires LECs "to provide dialing parity to competing providers of telephone exchange service and telephone toll service."¹²⁰ "Dialing parity" exists when a LEC customer can route telephone calls to at least one carrier other than that LEC without having to dial an access code.¹²¹ Pursuant to section 251(b)(3), the Commission issued an order in August 1996 requiring LECs to implement inter- and intraLATA

¹¹⁶ See *Western Elec. Co. I*, 569 F. Supp. at 1002 n.54, 1018-1024; *United States v. Western Elec. Co.*, 569 F. Supp. 1057, 1107 (D.D.C. 1983) (*Western Elec. Co. II*).

¹¹⁷ See, e.g., Policy and Rules Concerning Rates for Dominant Carriers, CC Docket No. 87-313, Order on Reconsideration, 6 FCC Rcd 2637, 2681 (1991) (observing that price cap LECs are treated as dominant providers of services in the interexchange basket).

¹¹⁸ See 47 U.S.C. §§ 203(b), 204(a)(3); 47 C.F.R. §§ 61.38, 61.41, 61.58; Implementation of Section 402(b)(1)(A) of the Telecommunications Act of 1996, CC Docket No. 96-187, Report and Order, 12 FCC Rcd 2170, 2182, 2188, 2191-92, 2202-03 (1997).

¹¹⁹ 47 C.F.R. §§ 1.773(a)(ii), 61.24(c), 61.38(a); Tariff Filing Requirements for Nondominant Carriers, CC Docket No. 93-36, Order, 10 FCC Rcd 13653, 13653-54 (1995).

¹²⁰ 47 U.S.C. § 251(b)(3).

¹²¹ See 47 U.S.C. § 153(15) (defining "dialing parity"); 47 C.F.R. § 51.5 (defining "dialing parity"); *Dialing Parity Order*, 11 FCC Rcd at 19399-19400, 19405-06, 19411.

toll dialing parity by February 8, 1999.¹²² The Commission concluded that a LEC must meet those obligations by allowing its customers to presubscribe to at least one carrier other than the LEC for intraLATA toll services, and to at least one carrier other than the LEC for interLATA toll services.¹²³

51. On August 22, 1997, the United States Court of Appeals for the Eighth Circuit vacated, on jurisdictional grounds, the Commission's intraLATA dialing parity rules as applied to intrastate intraLATA toll and interstate intraLATA local calls.¹²⁴ The United States Supreme Court, however, reversed the Eighth Circuit decision on January 25, 1999.¹²⁵ Following the Supreme Court decision, the Commission issued an order on March 23, 1999, in which it observed that intraLATA toll dialing parity had been implemented in most states.¹²⁶ Nonetheless, the Commission concluded in light of the intervening Eighth Circuit and Supreme Court decisions that a limited waiver of the intraLATA toll dialing parity deadlines and a revised implementation schedule were warranted.¹²⁷ Under the revised schedule, almost all LECs will have implemented inter- and intraLATA toll dialing parity by September 6, 1999.¹²⁸

52. Ameritech and USTA filed comments in January 1997, in response to the *Access Charge Reform NPRM*, asking the Commission to cease price cap regulation of corridor and

¹²² *Dialing Parity Order*, 11 FCC Rcd at 19400, 19401, 19409-10, 19412, 19424-26. See 47 C.F.R. §§ 51.205, 51.209.

¹²³ *Dialing Parity Order*, 11 FCC Rcd at 19400, 19412, 19414. See 47 C.F.R. § 51.209. Presubscription is a process by which a customer selects a carrier to which certain types of calls are routed automatically. See 47 C.F.R. § 51.209(b). Pursuant to the Commission's order, customers in states without LATAs -- such as Alaska and Hawaii -- must be able to presubscribe to one carrier for intrastate toll calls and the same or another carrier for interstate toll calls. *Dialing Parity Order*, 11 FCC Rcd at 19400, 19414. States that have one or more LATAs may modify the dialing parity requirement so that, like no-LATA states, customers can presubscribe to one carrier for intrastate toll calls and to the same or another carrier for interstate toll calls. *Dialing Parity Order*, 11 FCC Rcd at 19400 & n.16, 19414. See 47 C.F.R. § 51.209(d).

¹²⁴ *California v. FCC*, 124 F.3d at 934 & n.6.

¹²⁵ *AT&T v. Iowa Utils. Bd.*, 119 S. Ct. 721, 732.

¹²⁶ See *Dialing Parity Extension Order*, 14 FCC Rcd at 5266 & nn.20-21.

¹²⁷ *Id.* at 5265; 47 C.F.R. § 51.211.

¹²⁸ Under the Commission's revised implementation schedule for toll dialing parity, the implementation deadline varies among carriers, depending upon whether and when they submitted implementation plans to their relevant state commissions, and whether and when the state commissions took action. See *Dialing Parity Extension Order*, 14 FCC Rcd at 5265, 5267-68; 47 C.F.R. § 51.211. Most LECs should have implemented both intra- and interLATA toll dialing parity by September 6, 1999. See *Dialing Parity Extension Order*, 14 FCC Rcd at 5265, 5267-68; 47 C.F.R. § 51.211.

interstate intraLATA toll services.¹²⁹ Specifically, Ameritech proposed that the Commission remove these services from price cap regulation once toll dialing parity becomes available because toll dialing parity will eliminate any market power BOCs might have had.¹³⁰ Ameritech repeated its proposal regarding corridor and interstate intraLATA toll services in a 1998 *ex parte* letter.¹³¹ Bell Atlantic filed a similar letter.¹³² The Commission sought comment on the Ameritech and Bell Atlantic proposals in an October 1998 Public Notice.¹³³

C. Discussion

1. Price Cap LEC Ability to Exploit Market Power

53. A dominant carrier is "[a] carrier found by the Commission to have market power (*i.e.*, power to control prices)."¹³⁴ "Market power" is "the ability to raise prices by restricting output," or "to raise and maintain price above the competitive level without driving away so many customers as to make the increase unprofitable."¹³⁵ Pursuant to the framework outlined in the *Dominant/Non-Dominant Order*, the Commission determines whether a carrier is dominant or non-dominant by: 1) delineating the relevant product and geographic markets for examination of market power, 2) identifying firms that are current or potential suppliers in that market, and 3) determining whether the carrier under evaluation possesses individual market power in that market.¹³⁶ As a result of the competition that has developed since the consent decree and the Telecommunications Act of 1996, price cap LECs may now be non-dominant in the provision of corridor and interstate intraLATA toll services, particularly in light of the availability of inter- and intraLATA toll dialing parity. Although the record in this proceeding is insufficient for us to conduct the analysis outlined in the *Dominant/Non-Dominant Order*, we do conclude that developments in the markets for interexchange services make it unlikely that price cap LECs will

¹²⁹ See Ameritech Comments at 35; USTA Comments at 35, 38.

¹³⁰ Ameritech Comments at 35.

¹³¹ See Ameritech *ex parte* statement of June 5, 1998.

¹³² See Bell Atlantic *ex parte* statement of Apr. 27, 1998.

¹³³ *October 5 Public Notice*, 13 FCC Rcd at 21523.

¹³⁴ 47 C.F.R. § 61.3(o).

¹³⁵ Policy and Rules Concerning Rates for Competitive Common Carrier Services and Facilities Authorizations Therefor, CC Docket No. 79-252, Fourth Report and Order, 95 FCC.2d 554, 558 (1983).

¹³⁶ See Regulatory Treatment of LEC Provision of Interexchange Services Originating in the LEC's Local Exchange Area, CC Docket No. 96-149, Second Report and Order in CC Docket No. 96-149 and Third Report and Order in CC Docket No. 96-61, 12 FCC Rcd 15756, 15775, 15776, 15782 (1997) (*Dominant/Non-Dominant Order*).

be able to exploit over a sustained period any individual market power in their provision of corridor and interstate intraLATA toll services.¹³⁷

54. First, there currently exist a number of competitive alternatives to provision of these services by price cap LECs. Non-dominant IXC's such as AT&T, MCI, and Sprint already provide long-distance services in the price cap LECs' service areas. IXC's and competitive LECs not currently providing such services could do so quickly, either over their own facilities or by reselling the services of IXC's already in the market. Most customers of domestic interexchange services are sensitive to changes in price and are willing to shift their traffic if a carrier raises its prices.¹³⁸ Thus, non-dominant IXC's and competitive LECs can compete with price cap LEC provision of corridor and interstate intraLATA toll services.¹³⁹ Inter- and intraLATA toll dialing parity, which is -- or shortly will be -- available throughout the country pursuant to the March 23, 1999, *Dialing Parity Extension Order*,¹⁴⁰ will facilitate such competition.¹⁴¹ The existence of these competitive alternatives and the availability of toll dialing parity will limit the ability of price cap LECs to exploit over a sustained period any individual market power in their provision of corridor and interstate intraLATA toll services.

55. Second, some of the larger IXC's have nationwide brand identification in connection with long-distance services. This brand identification, and an IXC's ability to offer customers long-distance services that span the nation, rather than just in discrete geographies, should help offset any advantages a price cap LEC might enjoy based on its brand identification and possible integration efficiencies in the provision of local services.¹⁴² Moreover, as the Commission has noted in the past:

¹³⁷ *Compare Interexchange Competition Order*, 6 FCC Rcd at 5882 (concluding that detailed advance regulatory scrutiny of most of AT&T's business services was no longer necessary based on finding that market forces made it unlikely that AT&T would file unlawful tariffs for those services).

¹³⁸ *See Dominant/Non-Dominant Order*, 12 FCC Rcd at 15811.

¹³⁹ *See, e.g.*, Ameritech *ex parte* statement of July 26, 1999 (providing copies of web pages marketing competing services provided by AT&T, Sprint, Qwest, and MCI).

¹⁴⁰ *See Dialing Parity Extension Order*, 14 FCC Rcd at 5265, 5267-68; 47 C.F.R. § 51.211.

¹⁴¹ *See, e.g.*, Ameritech *ex parte* statement of July 26, 1999 (stating percent of lines for interstate intraLATA toll service Ameritech has lost in each of its in-region states, ranging from 9 percent of residential and 12 percent of business since implementing dialing parity in Indiana in February 1999, to 31 percent of residential and 36 percent of business since implementing dialing parity in Wisconsin in September 1996). *See also id.* (stating that Ameritech's monthly intraLATA minutes of use have dropped 26 percent from 34,143 million in January 1999 to 25,248 million in February 1999).

¹⁴² *Compare Dominant/Non-Dominant Order*, 12 FCC Rcd at 15811-12.

[a]n incumbent firm in virtually any market will have certain advantages -- including, perhaps, resource advantages, scale economies, established relationships with suppliers, ready access to capital, etc. Such advantages do not, however mean that these markets are not competitive, nor do they mean that it is appropriate for government regulators to deny the incumbent the efficiencies its size confers in order to make it easier for others to compete. Indeed, the competitive process itself is largely about trying to develop one's own advantages, and all firms need not be equal in all respects for this process to work.¹⁴³

The IXCs' nationwide brand identification and larger service areas will limit the ability of price cap LECs to exploit over a sustained period any individual market power in their provision of corridor and interstate intraLATA toll services.

2. Removal of Services from Price Caps and Relaxation of Tariff Requirements

56. In light of our determination that price cap LECs will be unable to exploit any individual market power over a sustained period in their provision of corridor and interstate intraLATA toll services, we will allow a price cap LEC to remove those services from price cap regulation on fifteen days notice,¹⁴⁴ and subsequently to file tariffs for those services on one day's notice without cost support and with a presumption of lawfulness, once it has implemented inter- and intraLATA toll dialing parity everywhere it provides local exchange services at the holding company level.¹⁴⁵ The Commission retains, however, the ability to reimpose some or all of these

¹⁴³ *Interexchange Competition Order*, 6 FCC Rcd at 5892.

¹⁴⁴ When price cap LECs remove their corridor and interstate intraLATA toll services from their interexchange baskets, we will not require them to recalibrate their interexchange basket PCI. The interexchange basket does not have service categories, thus obviating the need for an interexchange PCI recalibration. *See LEC Price Cap Order*, 5 FCC Rcd at 6811 (concluding "that the small amount of interexchange service subject to price cap regulation does not warrant the imposition of additional service categories"). When the Commission allowed AT&T to remove certain services from price cap regulation, it did require such recalibration. *See Competition in the Interstate Interexchange Marketplace*, CC Docket No. 90-132, Second Report and Order, 8 FCC Rcd 3668, 3671 (1993) (removing all services except 800 directory assistance from Basket 2) (*Interexchange Competition Second Report and Order*); Motion of AT&T Corp. to be Reclassified as a Non-Dominant Carrier, FCC 95-427, Order, 11 FCC Rcd 3271 (1995) (*AT&T Non-Dominance Order*); Re-initialization of Indexes, Memorandum Opinion and Order, 11 FCC Rcd 1201 (Com. Car. Bur. 1995) (*AT&T Non-Dominant Reinitialization Order*) (removing services except international services from Basket 1). In the AT&T cases, all the services except one service category were removed from the basket in question. Because the service band indices (SBIs) were designed to limit cross-subsidization between different types of services within a basket, and there is no danger of cross-subsidization when there is only one service category remaining in the basket, the Commission recalibrated AT&T's PCIs and APIs to eliminate the SBI for the remaining service category without affecting the headroom AT&T had previously. *Interexchange Competition Second Report and Order*, 8 FCC Rcd at 3671; *AT&T Non-Dominant Reinitialization Order*, 11 FCC Rcd at 1201.

¹⁴⁵ That date will vary among carriers, but in most cases will be by September 6, 1999. *See Dialing Parity Extension Order*, 14 FCC Rcd at 5265, 5267-68; 47 C.F.R. § 51.211. We will not allow a price cap LEC to

regulations on one or more of the price cap LECs should this prove necessary in the future.¹⁴⁶ The price cap LECs' provision of these services is also subject to Title II of the Act, enabling the Commission to continue to ensure that the rates are just, reasonable, and nondiscriminatory.¹⁴⁷

57. Because price cap LECs will be unable to exploit any individual market power over a sustained period in their provision of corridor and interstate intraLATA toll services, we find that the burdens imposed by price cap regulation of those services outweigh the little benefit such regulation might provide, especially considering the relatively *de minimis* nature of corridor and interstate intraLATA toll traffic.¹⁴⁸ We also find that the operation of market forces should make it unlikely that they will file unlawful tariffs.¹⁴⁹ Thus, upon careful consideration of the benefits and burdens of our present regulations, we conclude that more limited advance review of price cap LECs' corridor and interstate intraLATA toll service filings, when combined with mechanisms such as the complaint process and our investigation authority, is in the public interest.¹⁵⁰ We will,

remove these services from price cap regulation in some states while it remains subject to price cap regulation for the provision of these services in other states. If we were to do so, the carrier might have an incentive to shift costs to the services subject to price cap regulation to qualify for the protections of the low-end adjustment. *Cf. LEC Price Cap Order*, 5 FCC Rcd at 6819 (describing "all-or-nothing" rule, under which LEC seeking to participate in price cap regulation must convert all its cost affiliates to price cap regulation to remove incentive to shift costs from a price cap affiliate to a rate-of-return affiliate).

¹⁴⁶ *Cf. Dominant/Non-Dominant Order*, 12 FCC Rcd at 15834 (concluding that the Commission's finding that price cap LECs are non-dominant in the provision of certain domestic, interstate, interexchange services did not prevent it from reimposing such regulation on certain price cap LECs, if necessary). We note that our finding that price cap LECs will be unable to exploit any individual market power over a sustained period in their provision of corridor and interstate intraLATA toll services does not place the price cap LECs in the same position as non-dominant providers of interstate interexchange services. We previously relieved those carriers of the obligation to file certain tariffs altogether, although that order is currently subject to a stay. *See Policy and Rules Concerning the Interstate, Interexchange Marketplace*, CC Docket No. 96-61, Second Report and Order, 11 FCC Rcd 20730 (1996); *recon.*, 12 FCC Rcd 15014 (1997); *stayed sub nom. MCI Telecommunications Corp. v. FCC*, No. 96-1459 (D.C. Cir. 1997). We have made no such finding of non-dominance here. Thus, price cap LECs are still subject to tariff filing requirement -- including those pertaining to electronic filing -- even once they have removed their corridor and interstate intraLATA toll services from price cap regulation.

¹⁴⁷ *See* 47 U.S.C. §§ 201-209. *Accord* USTA Comments at 39.

¹⁴⁸ *See* Motion of AT&T Corp. to be Declared Non-Dominant for International Service, 11 FCC Rcd 17963, 17999 (1996) (stating that the economic cost of dominant carrier regulation for routes with *de minimis* traffic can impede rather than promote competitive market conditions). *See also LEC Price Cap Order*, 5 FCC Rcd at 6811 (concluding "that the small amount of interexchange service subject to price cap regulation does not warrant the imposition of additional service categories").

¹⁴⁹ *Compare Interexchange Competition Order*, 6 FCC Rcd at 5882, 5894 (concluding that detailed advance scrutiny of most of AT&T's business services was no longer necessary based on finding that market forces made it unlikely that AT&T would file unlawful tariffs for those services).

¹⁵⁰ *Compare id.* at 5881-82, 5895 (concluding "that the costs and burdens associated with detailed advance tariff review procedures for [long-distance business] services outweigh their benefits to the public").

therefore, allow price cap LECs to file tariffs for those services on one day's notice and without cost support. We do so under the authority of section 203(b)(2), which allows the Commission, "in its discretion and for good cause shown, [to] modify any requirement made by or under the authority of this section either in particular instances or by general order applicable to special circumstances or conditions."¹⁵¹ The growth in competition for long-distance services, and the availability of toll dialing parity, present just such special circumstances with regard to price cap LEC provision of corridor and interstate intraLATA toll services.

V. GEOGRAPHIC DEAVERAGING OF RATES FOR TRUNKING BASKET SERVICES

A. Background

58. Our Part 69 rules generally require that an incumbent LEC charge rates for access elements that are geographically averaged across each of its study areas.¹⁵² The Commission has developed a system of density pricing zones, however, that permits an incumbent LEC to deaverage geographically its rates for special access and switched transport services if that LEC meets certain threshold interconnection requirements.¹⁵³ The density zone pricing rules permit incumbent LECs to establish a "reasonable" number of zones, but the Commission has noted in the past that "LECs seeking to establish more than three zones shall be subject to increased scrutiny and must carefully justify the number of zones proposed in their density pricing zone plan."¹⁵⁴ In addition, incumbent LECs must show that density zones reflect cost characteristics

¹⁵¹ 47 U.S.C. § 203(b)(2). See also *Interexchange Competition Order*, 6 FCC Rcd at 5896-97 & nn. 143-145 (concluding that section 203(B)(2) authorized the Commission to change notice and cost support requirements for AT&T's business services in light of the "changed competitive situation") (quoting *Southern Motor Carriers Rate Conference v. United States*, 773 F.2d 1561, 1569, 1570 (11th Cir. 1985)).

¹⁵² 47 C.F.R. § 69.3(e)(7). A study area is a geographical segment of a carrier's telephone operations. Generally, a study area corresponds to a carrier's entire service territory within a state. Thus, carriers operating in more than one state typically have one study area for each state, and carriers operating in a single state typically have a single study area. Carriers perform jurisdictional separations at the study area level. For jurisdictional separations purposes, the Commission adopted a rule freezing study area boundaries effective November 15, 1984. Part 36 of the Commission's Rules, 47 C.F.R., Part 36, Appendix-Glossary, definition of "Study Area." See *MTS and WATS Market Structure, Amendment of Part 67 of the Commission's Rules and Establishment of a Joint Board*, CC Docket Nos. 78-72 and 80-286, 49 Fed. Reg. 48325 (Dec. 12, 1984), adopted by the Commission, 50 Fed. Reg. 939 (Jan. 8, 1985).

¹⁵³ 47 C.F.R. § 69.123. See also *Special Access Expanded Interconnection Order*, 7 FCC Rcd at 7454-56. Section 69.123(a) of the Commission's rules allows LECs to establish traffic density pricing zones in study areas in which at least one interconnector has taken a cross-connect. See 47 C.F.R. § 69.123(a).

¹⁵⁴ *Special Access Expanded Interconnection Order*, 7 FCC Rcd 7454, n.413.

such as traffic density or other measures of traffic passing through particular central offices.¹⁵⁵ The Commission sought comment in the *Access Reform NPRM* on whether to grant incumbent LECs greater flexibility to deaverage access charges.¹⁵⁶

B. Discussion

59. In this Order, we amend Section 69.123 of the Commission's rules to permit incumbent LECs to deaverage geographically their rates for access services in the trunking basket.¹⁵⁷ We will permit price cap incumbent LECs to define both the scope and number of zones, provided that each zone, except the highest-cost zone, accounts for at least 15 percent of the incumbent's trunking basket revenues in the study area, and we no longer require LECs to demonstrate that the zones reflect cost characteristics. Granting incumbent LECs more flexibility to deaverage these rates enhances the efficiency of the market for those services by allowing prices to be tailored more easily and accurately to reflect costs and, therefore, promotes competition in both urban and rural areas.

60. Since 1992, the Commission has permitted LECs to deaverage certain rates by geographic zone because of the concern that averaged rates might create a pricing umbrella for competitors that would deprive customers of the benefits of more vigorous competition.¹⁵⁸ Adoption of this policy reflected the conclusion that non-cost-based, geographically-averaged access rates could not be maintained in a market subject to increasing competition.¹⁵⁹ Deaveraged rates promote efficiency by allowing an incumbent LEC to compete for customers when it is, in fact, the lowest cost service provider and by removing support flows to the incumbent LEC's higher-cost services.¹⁶⁰ Incumbent LECs argue, however, that our current rules fail to achieve these goals for a variety of reasons. First, they argue that the "increased scrutiny" applicable to the creation of more than three pricing zones per study area discourages LECs from offering such plans.¹⁶¹ As a result, incumbent LECs argue, the zones in most zone density pricing plans are too

¹⁵⁵ *Id.*, 7 FCC Rcd 7455.

¹⁵⁶ *Access Reform NPRM* at 21433.

¹⁵⁷ We discuss deaveraging of the common line and traffic-sensitive baskets in Section VIII.A, *infra*.

¹⁵⁸ *Special Access Expanded Interconnection Order*, 7 FCC Rcd at 7454; *Switched Transport Expanded Interconnection Order*, 8 FCC Rcd at 7426.

¹⁵⁹ *See, e.g., Special Access Expanded Interconnection Order*, 7 FCC Rcd at 7454; *Switched Transport Expanded Interconnection Order*, 8 FCC Rcd 7374.

¹⁶⁰ *Special Access Expanded Interconnection Order*, 7 FCC Rcd at 7454; *Switched Transport Expanded Interconnection Order*, 8 FCC Rcd at 7426.

¹⁶¹ *See, e.g., SBC Nov. 9 Reply* at 23. Few, if any, price cap incumbent LECs have proposed to offer density zone plans with more than three density zones in a study area. Sprint argues that carriers serving a variety of

large to be of practical value.¹⁶² Finally, incumbent LECs argue that traffic density is not the most accurate means of determining appropriate geographic boundaries for deaveraging.¹⁶³

61. We agree with incumbent LECs that traffic density is not the optimal, or even an accurate, method of determining cost-based pricing zones and that LEC-designed zones are more likely to lead to efficient pricing that reflects underlying cost characteristics.¹⁶⁴ As the Commission observed in the *Access Reform NPRM*, averaging across large geographic areas distorts the operation of markets in high-cost areas because it requires incumbent LECs to offer services in those areas at prices substantially lower than their costs of providing those services.¹⁶⁵ Prices that are below cost reduce the incentives for entry by firms that could provide the services as efficiently, or more efficiently, than the incumbent LEC.¹⁶⁶ Similarly, discrepancies between price and cost may create incentives for carriers to enter low-cost areas even if their cost of providing service is actually higher than that of the incumbent LEC.¹⁶⁷

62. Given these observations, if we grant incumbent LECs practical flexibility to choose the number of zones and the criteria for establishing zone boundaries, they are more likely to establish reasonable and efficient pricing zones than if their flexibility is more constrained. Therefore, in this Order, we amend our rules to eliminate all competitive prerequisites for the deaveraging of trunking basket service rates and to permit price cap incumbent LECs to define zone pricing plans in any manner they wish, so long as each zone, except the highest-cost zone, accounts for at least 15 percent of the incumbent LEC's trunking basket revenues in the study area. This limitation ensures that incumbent LECs cannot define zones that are, for all practical purposes, specific to particular customers. As we explain in Section VI, below, we will not permit incumbent LECs to offer customer-specific contract tariffs until they satisfy certain triggers

urban, suburban, and rural areas require more than three density zones to price their services accurately relative to cost. Sprint Nov. 9 Comments at 14.

¹⁶² See, e.g., Bell Atlantic Nov. 9 Reply at 17-18.

¹⁶³ See, e.g., Ameritech Nov. 9 Reply at 9; Bell Atlantic Nov. 9 Reply at 18. Ameritech, for example, argues that, in cases where it charges identical rates in two particular zones, competitors sometimes choose to enter in the less-dense zone, suggesting that the spread between actual cost and Ameritech's price is greater there than in a denser zone and, thus, that high traffic density does not necessarily result in lower costs. Ameritech Nov. 9 Reply at 9.

¹⁶⁴ See, e.g., Ameritech Nov. 9 Reply at 9; SBC Nov. 9 Reply at 23. For example, Ameritech argues that the average length of transport facilities and the varying means by which transport facilities are deployed (aerial cables, buried cables, cable in conduits, etc.), are also significant cost drivers. Ameritech Reply in Ameritech Chicago Forbearance Proceeding, CC Docket No. 99-65, at Att. A, 16-17.

¹⁶⁵ See *Access Reform NPRM*, 11 FCC Rcd at 21434.

¹⁶⁶ See *id.* at 21434.

¹⁶⁷ See *id.*

related to the development of competition, and we are concerned that, absent a rule establishing the minimum size of a zone, incumbents might circumvent this requirement by using zone pricing as a substitute for contract tariffs. At the same time, the limit we adopt permits a maximum of seven zones, which we believe should provide the ability to adjust to any likely variation in cost conditions. We note that no incumbent LEC has requested more than five zones.¹⁶⁸ Our requirement that a zone, except the highest-cost zone, account for at least 15 percent of trunking revenues within a study area ensures that any lower rates resulting from deaveraging are enjoyed by a range of customers. Section 69.123(c)(2) of our rules, which requires transport between points located in two different zones to be priced in accordance with the higher-priced zone, also limits incumbent LECs' ability to draw pricing zones too narrowly.

63. The permissive geographic deaveraging we discuss here applies to rates for all services in the trunking basket to which density zone pricing currently applies, *i.e.*, rates for all services except for the transport interconnection charge (TIC), so long as the same zones are used for all transport elements.¹⁶⁹ We will continue to prohibit geographic deaveraging of the TIC so as not to disrupt the scheduled phase-out of that charge.¹⁷⁰ In addition, we relax the constraints on annual price increases within zones that are contained in Sections 69.123(e)(2) and 61.47(e) of our rules by raising the limit on permitted price increases within zones from five percent to 15 percent.¹⁷¹ Although such constraints limit price cap incumbent LECs' ability to implement deaveraging and rebalance rates in a manner that reflects the actual costs of providing the services at issue, some limit on the rate of price increases within zones remains desirable in order to prevent the disruptive effects of rapid and unexpected price increases. Under our price cap rules, however, deaveraging permits LECs to increase rates in one geographic zone only to the extent that they decrease rates in other geographic zones in the study area.¹⁷² As Sprint points out, particularly where demand has grown faster in high-density zones than in low-density zones, the

¹⁶⁸ Sprint, for instance, has suggested a minimum of four zones. Sprint *ex parte* statement of July 12, 1999.

¹⁶⁹ The Commission previously has imposed this requirement on geographically-deaveraged transport services. See *Switched Transport Expanded Interconnection Order*, 8 FCC Rcd at 7428.

¹⁷⁰ See *Switched Transport Expanded Interconnection Order*, 8 FCC Rcd at 7427. The TIC was intended as a temporary measure to ameliorate potential negative effects on incumbent LECs and small IXC's of transport rate structure changes made in 1992. See *Access Reform NPRM*, 11 FCC Rcd at 21402-03. We are in the process of eliminating the TIC through a combination of targeted reductions and reallocation to other access charge rate elements. See *id.*; *Access Reform First Report and Order*, 12 FCC Rcd at 16073-86.

¹⁷¹ Section 61.47(e) states, in pertinent part, "Each [pricing] band [for each service category and subcategory within a basket] shall limit the pricing flexibility of the service category, subcategory, or density zone, as reflected in the SBI, to an annual increase of [five percent]." 47 C.F.R. § 61.47(e). In this Order, although we maintain a five-percent limit on annual price increases for service category or subcategory, *on a study-area-wide basis*, we add Section 61.47(f) to our rules, which permits price cap LECs to raise prices *within a zone* by up to 15 percent, annually. See Appendix B, *infra*.

¹⁷² See 47 C.F.R. §§ 61.41-61.47.

five-percent limit on price increases sharply constrains the ability of incumbent LECs to make revenue-neutral price cuts in high-density zones.¹⁷³ Increasing to 15 percent the limit on price increases should allow more rapid movement to cost-based rates without subjecting customers in high-cost areas to rate shock. The requirement we adopt that each zone, except the highest-cost zone, account for at least 15 percent of the incumbent's trunking basket revenues in a study area should deter incumbent LECs from establishing rates for low-cost zones that are so low as to enable them to raise rates to unreasonably high levels in high-cost zones. Thus, we are not persuaded by AT&T's claims that greater geographic deaveraging flexibility will lead to predatory pricing by incumbent LECs or arguments by CPI and the Washington Commission that any further deaveraging should result only in price decreases, *i.e.*, that it be "downward only."¹⁷⁴

64. We reject the Washington Commission's argument that more liberal geographic deaveraging rules might lead to IXC violations of sections 254(b)(3) and 254(k) of the Act.¹⁷⁵ Section 254(b)(3) of the Act requires the Joint Board and the Commission to ensure that consumers in rural, insular, and high cost areas have access to telecommunications services that are available at rates that are reasonably comparable to rates charged for similar services in urban areas.¹⁷⁶ We conclude that further geographic deaveraging of trunking services that may result from this Order is unlikely to place significantly greater pressures on IXCs (purchasers of trunking services) to deaverage their rates, in part because deaveraging implies price *decreases* as well as increases. Section 254(k) prohibits a telecommunications carrier from using services that are not competitive to subsidize services that are subject to competition.¹⁷⁷ As we discuss above, however, changes in incumbent LEC pricing zones resulting from this Order are likely to *increase* the degree to which trunking service prices reflect cost and thus would decrease the likelihood of cross-subsidization.

65. We will no longer require incumbent LECs to file zone pricing plans in advance of tariff filings, as the Commission has in the past,¹⁷⁸ because we presume that market forces, along with the limitation we adopt regarding the size of zones, will result in plans that reflect cost characteristics. Parties wishing to challenge the reasonableness of incumbent LEC zone pricing plans may do so as part of the tariff approval process, pursuant to which incumbent LECs must

¹⁷³ Sprint *ex parte* statement of July 12, 1999.

¹⁷⁴ See AT&T Oct. 26 Comments at 9; CPI Oct. 26 Comments at 10; Washington Commission Oct. 26 Comments at 13.

¹⁷⁵ Washington Commission Oct. 26 Comments at 13-14.

¹⁷⁶ 47 U.S.C. § 254(b)(3).

¹⁷⁷ 47 U.S.C. § 254(k).

¹⁷⁸ See, e.g., *Special Access Expanded Interconnection Order*, 7 FCC Rcd at 7455.

file any tariffs that include both a rate increase and rate decrease upon fifteen days' notice,¹⁷⁹ or in a formal complaint under section 208 of the Act.¹⁸⁰

66. We are not persuaded by arguments made by MCI that the failure of incumbent LECs to take full advantage of the geographic deaveraging currently available under our rules is sufficient grounds for not granting incumbent LECs greater flexibility to deaverage transport services.¹⁸¹ As we discuss above, lack of flexibility in our density zone pricing rules may be responsible for incumbent LECs' current failures to take full advantage of such opportunities. We conclude above that market forces are more likely to result in efficient pricing than is regulation, and, for this reason, the greater flexibility we grant here will benefit access customers through more efficient pricing of access services.

VI. PRICING FLEXIBILITY BASED ON A COMPETITIVE SHOWING

A. Background

67. The Commission has long recognized that it should allow incumbent LECs progressively greater pricing flexibility as they face increasing competition.¹⁸² In the *Access Reform First Report and Order*, the Commission adopted a market-based approach to access charge reform, pursuant to which it would relax restrictions on incumbent LEC pricing as competition emerges, thereby ensuring that "our own regulations do not unduly interfere with the development and operation of these markets as competition develops."¹⁸³ At that time, the

¹⁷⁹ See Implementation of Section 402(b)(1)(A) of the Telecommunications Act of 1996, CC Docket No. 96-187, Report and Order, 12 FCC Rcd 2170, 2202.

¹⁸⁰ 47 U.S.C. § 208.

¹⁸¹ MCI Oct. 26 Comments at 38-39. See also Time Warner Oct. 26 Comments at 14. *Contra* Ameritech Nov. 9 Reply at 9; Bell Atlantic Nov. 9 Reply at 17-18.

¹⁸² The Commission first sought comment on a "road map" for this transition in the *Price Cap Second FNPRM*, 11 FCC Rcd 858 (1995). Later, in the *Access Reform NPRM*, the Commission noted that the parties filed pleadings in response to the *Price Cap Second FNPRM* prior to adoption of the Telecommunications Act of 1996. *Access Reform NPRM*, 11 FCC Rcd at 21428; Telecommunications Act of 1996, Pub. L. No. 104-104, 110 Stat. 154 (1996). Accordingly, the Commission refined its pricing flexibility proposals and invited parties to submit new comments. *Access Reform NPRM*, 12 FCC Rcd at 21428-48. The Commission limited the record to pleadings filed in response to the *Access Reform NPRM*, although parties were permitted to re-submit their *Price Cap Second FNPRM* comments. *Id.* at 21428.

¹⁸³ *Access Reform First Report and Order*, 12 FCC Rcd at 16094.

Commission deferred resolution of the specific timing and degree of pricing flexibility to a future Order.¹⁸⁴

68. In the previous two sections, we adopt forms of regulatory relief for price cap LECs that can be granted under current market conditions and do not require a further competitive showing. Below, we consider forms of regulatory relief which, if granted prematurely, might enable price cap LECs to (1) exclude new entrants from their markets, or (2) increase rates to unreasonable levels. Accordingly, as a condition for granting further pricing flexibility, we require incumbent LECs to show that markets are sufficiently competitive both to warrant pricing flexibility to enable incumbent LECs to respond to competition and to discourage incumbents from either excluding new entrants or raising rates to unreasonable levels. In other words, we adopt requirements that price cap LECs make "competitive showings," or satisfy "triggers," to demonstrate that market conditions in a particular area warrant the relief at issue.

69. The pricing flexibility framework we adopt consists of two phases. To obtain Phase I regulatory relief, the incumbent must show that competitors have made irreversible investments in the facilities needed to provide the services at issue, thus discouraging incumbent LECs from successfully pursuing exclusionary strategies. Phase I permits LECs to offer contract tariffs¹⁸⁵ and volume and term discounts, while requiring them to maintain their generally available price cap-constrained tariffed rates, thus protecting those customers that lack competitive alternatives. To obtain Phase II relief, which allows LECs to raise and lower rates, the incumbent must demonstrate that competitors have established a significant market presence in the provision of the services at issue. Under those market conditions, the availability of alternative providers will ensure that rates are just and reasonable. The triggers we adopt below should permit incumbent LECs to make the required showings, with a minimum of administrative burden for the industry and the Commission.

70. In Section VI.B, we define the geographic areas within which we will grant pricing flexibility. In Section VI.C.2, we establish Phase I competitive showings for (1) dedicated transport, (*i.e.*, entrance facilities, direct-trunked transport, and the dedicated component of

¹⁸⁴ *Id.* at 15989.

¹⁸⁵ A contract tariff is a tariff based on an individually-negotiated service contract. *See Interexchange Competition Order*, 6 FCC Rcd at 5897; 47 C.F.R. § 61.3(m). In order to comply with the nondiscrimination provisions of the Act, the Commission has required carriers to make all contract tariffs "generally available to similarly situated customers under substantially similar circumstances." *See Interexchange Competition Order*, 6 FCC Rcd at 5897. This requirement also will apply to contract tariffs offered by incumbent price cap LECs. We will require price cap LECs offering contract tariffs to include in those tariffs: (1) the term of the contract, including any renewal options; (2) a brief description of each of the services provided under the contract; (3) minimum volume commitments for each service; (4) the contract price for each service or services at the volume levels committed to by the customers; (5) a general description of any volume discounts built into the contract rate structure; and (6) a general description of other classifications, practices and regulations affecting the contract rate. *See* Section 61.55(c) of our rules, as set forth in Appendix B to this Order.

tandem-switched transport service) and special access services other than channel terminations,¹⁸⁶ and (2) channel terminations.¹⁸⁷ In Section VI.C.3, we adopt Phase I competitive showings for common line and traffic-sensitive services, and the traffic-sensitive components of tandem-switched transport service. We specify the regulatory relief to be afforded for all these services at Phase I in Section VI.C.4, and, in Section VI.C.5, we adopt Phase II competitive showings for dedicated transport and special access services and specify the relief that is available upon satisfaction of these showings. In the Notice accompanying this Order, we seek comment on appropriate Phase II triggers for the traffic-sensitive components of tandem-switched transport service, and for services in the traffic-sensitive and common line baskets. In Section VI.D, we revise our price cap low-end adjustment rules with respect to those price cap LECs that qualify for and elect to exercise any of the pricing flexibilities we grant in this section. We set forth the procedural requirements governing requests for pricing flexibility in Section VI.E. We base our conclusions in this section on the record developed in response to the *Price Cap Second FNPRM* and the *Access Reform NPRM*, supplemented by pleadings filed in response to the *October 5 Public Notice* and the pending forbearance petitions.¹⁸⁸ Finally, in Section VI.F, we extend by ninety days the statutory deadline applicable to U S West's pending petition for forbearance from dominant carrier regulation in Phoenix, Arizona.

B. Geographic Scope of Relief

71. *Background.* In the *Price Cap Second FNPRM*, the Commission invited comment on the geographic area that it should use for purposes of reviewing requests for pricing flexibility.¹⁸⁹ The Commission sought to define these geographic areas narrowly enough so that the competitive conditions within each area are reasonably similar, yet broadly enough to be administratively workable.¹⁹⁰ Specifically, the Commission invited comment on whether individual wire centers,¹⁹¹

¹⁸⁶ See Section II.A.1, *supra*, for a description of these services. See also Section 69.709(a) of our rules, as set forth in Appendix B to this Order.

¹⁸⁷ See Section II.A.1, *supra*, for a description of channel terminations. See also Section 69.709(a) of our rules, as set forth in Appendix B to this Order.

¹⁸⁸ The pending forbearance petitions are listed in Appendix A to this Order. Several parties recommend that we treat the forbearance petitions as *ex parte* statements in this proceeding, or consider them in the context of this proceeding. See, e.g., ALTS Comments in SBC Forbearance Proceeding, CC Docket No. 98-227, at 3; NEXTLINK Opposition to Bell Atlantic Forbearance Petition, CC Docket No. 99-24, at 3.

¹⁸⁹ *Price Cap Second FNPRM*, 11 FCC Rcd at 911-14.

¹⁹⁰ *Id.* at 911-12.

¹⁹¹ *Id.* at 914.

zone density pricing zones,¹⁹² metropolitan statistical areas (MSAs),¹⁹³ or local access and transport areas (LATAs)¹⁹⁴ are the most appropriate geographic areas within which to grant pricing flexibility. Later, in the *Access Reform NPRM*, the Commission solicited comment on using the geographic zones adopted by state public service commissions for pricing of unbundled network elements (UNEs), or the zones adopted in the Universal Service proceeding for determining high cost areas.¹⁹⁵

72. *Discussion.* We will grant pricing flexibility relief for both Phase I and Phase II on an MSA basis. We agree with those commenters that maintain that MSAs best reflect the scope of competitive entry, and therefore are a logical basis for measuring the extent of competition.¹⁹⁶ Because competitive LECs generally do not enter new markets on a state-wide basis, we reject proposals to define the geographic scope of pricing flexibility on the basis of states or study areas.¹⁹⁷ Granting pricing flexibility over such a large geographic area would increase the likelihood of exclusionary behavior by incumbent LECs by giving them flexibility in areas where competitors have not yet made irreversible investment in facilities.

73. We also decline to grant pricing flexibility on the basis of LATAs. Many LATAs include an entire state,¹⁹⁸ and in those cases, LATAs would be inappropriate for the same reasons we reject states and study areas as relevant markets. Of course, other states contain many LATAs, in which cases LATAs are similar to MSAs. In those cases, relying upon MSAs rather than LATAs should make little difference in determining whether to grant pricing flexibility.

¹⁹² *Id.*

¹⁹³ *Id.* For purposes of this Order, we use the term "MSA" to refer to MSAs as defined in Section 22.909(a) of the Commission's rules, 47 C.F.R. § 22.909(a). MSAs are listed in Common Carrier Public Mobile Services Information, Public Notice, 7 FCC Rcd 742 (1992).

¹⁹⁴ *Price Cap Second FNPRM*, 11 FCC Rcd at 911-14. The Commission also invited comment on using study areas for this purpose. *Id.* at 914. In the *Access Reform NPRM*, however, the Commission proposed not to rely on state-wide measures, because competitive conditions are likely to vary within a state. *Access Reform NPRM*, 11 FCC Rcd at 21423.

¹⁹⁵ *Access Reform NPRM*, 11 FCC Rcd at 21423.

¹⁹⁶ See USTA Oct. 26 Comments at 35 and Att. E; SBC Oct. 26 Comments at 18; Cincinnati Bell Oct. 26 Comments at 8 (supporting MSAs). See also Ameritech Oct. 26 Comments, Att. N at 2; Bell Atlantic *ex parte* statement of April 27, 1998 at 15; Ad Hoc Comments at 50-54 (supporting LATAs, which in some states are similar to MSAs).

¹⁹⁷ USTA Comments at 27; Sprint Comments at 39; Southwestern Bell Comments at 26.

¹⁹⁸ See Excel Nov. 9 Reply at 7.

74. We also reject proposals to grant pricing flexibility on the basis of wire centers or central offices.¹⁹⁹ CTSI and KMC suggest that competition may exist in only a small part of an MSA,²⁰⁰ but we believe that the triggers we establish below are sufficient to ensure that competitors have made sufficient sunk investment within an MSA. In addition, defining geographic areas smaller than MSAs would force incumbents to file additional pricing flexibility petitions, and, although these petitions might produce a more finely-tuned picture of competitive conditions, the record does not suggest that this level of detail justifies the increased expenses and administrative burdens associated with these proposals.

75. In addition, we reject proposals to permit incumbent LECs themselves to select the geographic area for which they seek pricing flexibility.²⁰¹ Determining whether the incumbent has chosen an appropriate area is likely to generate controversy, thus undermining our desire to create a framework for granting pricing flexibility, where warranted, without delay and without imposing undue burden on the industry or on Commission staff.

76. Commenters supporting MSAs have provided little if any guidance for pricing flexibility in non-MSA areas. We will grant price cap LECs pricing flexibility within the non-MSA parts of a study area²⁰² if they satisfy the triggers we adopt below throughout that area. We decline to mandate individual showings for each rural service area (RSA), as we do for MSAs, because we expect competitors to enter MSA markets first and then to extend their networks into less densely populated areas. Because rural areas by definition do not have large concentrations of population comparable to urban areas, we expect that competitive entry into rural areas will be less concentrated than in urban areas. Therefore, we do not expect that pricing flexibility will enable an incumbent to engage successfully in exclusionary pricing behavior with respect to one RSA because competitive entry is limited to another RSA. Because the danger of exclusionary pricing behavior is lessened, we place more weight on our goal of administrative ease, and permit incumbent LECs to file a single pricing flexibility petition for all the RSAs in a study area. In addition, price cap LECs report some service quality information on a non-MSA basis,²⁰³ and so it

¹⁹⁹ USTA Comments at 29; BellSouth Comments at 39; PacTel Comments at 26; California Commission Comments at 11; Pennsylvania ISPs Comments at 17-18. Aliant also would use wire centers for Phase II, but it prefers determining whether there is "substantial competition" on a statewide basis. Aliant Comments at 9.

²⁰⁰ CTSI Nov. 9 Reply at 4-5; KMC Nov. 9 Reply at 5-6.

²⁰¹ BA/NYNEX Comments at 52-53; BellSouth Comments at 39; TRA Comments at 24-25; USTA Comments at 29.

²⁰² For cellular licensing purposes, the non-MSA part of a study area comprises one or more rural service areas (RSAs), as defined in Section 22.909(b) of the Commission's rules, 47 C.F.R. § 22.909(b). RSAs are listed with MSAs in Common Carrier Public Mobile Services Information, Public Notice, 7 FCC Rcd 742 (1992). Together, MSAs and RSAs encompass all the territory included in the incumbent LECs' study areas.

²⁰³ See Policy and Rules Concerning Rates for Dominant Carriers, CC Docket No. 87-313, Memorandum Opinion and Order, 6 FCC Rcd 2974, 2989-90 (Com. Car. Bur. 1991).

should be easy for price cap LECs to collect collocation information for pricing flexibility requests in those areas.²⁰⁴

C. Phase I and Phase II Pricing Flexibility

1. General Approach

77. We will grant Phase I pricing flexibility to a price cap incumbent LEC for special access and dedicated transport services when it demonstrates either that (1) competitors unaffiliated with the incumbent LEC have established operational collocation arrangements in a certain percentage of the incumbent LEC's wire centers in an MSA, or (2) unaffiliated competitors have established operational collocation arrangements in wire centers accounting for a certain percentage of the incumbent LEC's revenues from the services in question in that MSA.²⁰⁵ In both cases, the incumbent also must show, with respect to each wire center, that at least one collocater is relying on transport facilities provided by a transport provider other than the incumbent LEC.²⁰⁶ As explained above, Phase I of our pricing flexibility framework provides incumbent LECs with regulatory relief when competitors have made irreversible investments in facilities within a given MSA. At that point, we no longer need to protect competition from exclusionary pricing behavior by incumbent LECs, because efforts to exclude competitors are unlikely to succeed. In order to protect access customers that may lack competitive alternatives, we limit the extent to which Phase I flexibility permits incumbents to raise rates, because competitors that are sufficiently entrenched to survive attempts by incumbents to exclude them from the market may not yet have a sufficient market presence to constrain prices throughout the MSA.

78. For the reasons discussed below, and based on the record before us, we conclude that a collocation-based trigger for granting pricing flexibility for special access and dedicated transport reasonably balances our two goals: (1) having a clear picture of competitive conditions in the MSA, so that we can be certain that there is irreversible investment sufficient to discourage

²⁰⁴ For purposes of the remainder of this section, we will use the term "MSA" to refer to the geographic areas on which price cap LECs may base pricing flexibility petitions: (1) MSAs and (2) the non-MSA parts of study areas.

²⁰⁵ For purposes of our triggers, the term "wire center" shall refer to any location at which an incumbent LEC is required to provide expanded interconnection for special access pursuant to § 64.1401(a) of the Commission's rules, and any location at which an incumbent LEC is required to provide expanded interconnection for switched transport pursuant to § 64.1401(b)(1) of our rules. *See* 47 C.F.R. §§ 64.1401(a), 64.1401(b)(1). For purposes of this Order, collocation by competitors refers to collocation by carriers unaffiliated with the incumbent LEC.

²⁰⁶ This requirement that at least one collocater use competitive transport facilities excludes both transport provided by the incumbent LEC pursuant to tariff and unbundled transport leased from the incumbent LEC. Henceforth in this Order, references to collocation by competitors encompass only those collocated competitors that use transport provided by a transport provider other than the incumbent LEC.

exclusionary pricing behavior; and (2) adopting an easily verifiable, bright-line test to avoid excessive administrative burdens.²⁰⁷ In Section VI.C.2, we adopt specific triggers for (1) dedicated transport and special access services other than channel terminations; and (2) channel terminations. As we explain in Section VI.C.3 below, however, we adopt a different approach to granting pricing flexibility for traffic-sensitive and common line services, by requiring price cap LECs to demonstrate the extent to which competitors offer these services over their own facilities.

79. *Irreversible Investment.* In the *Access Reform NPRM*, the Commission explained that the initial phase of pricing flexibility should enable incumbent LECs to "re-price access services in ways that respond to competitive pressure, but do not impede competitive entry."²⁰⁸ We conclude that irreversible, or "sunk," investment in facilities used to provide competitive services is the appropriate standard for determining when pricing flexibility is warranted.²⁰⁹ Phase I regulatory relief will increase the efficiency of the interstate access market and reduce prices to end-user customers; therefore, we should delay granting this relief no longer than necessary to protect the development of a competitive market. Although Phase I relief permits incumbent LECs to offer contract tariffs and expands their authority to offer volume and term discounts, it also requires LECs to maintain their existing price cap tariffed rates, thus precluding price cap LECs from abusing their market power by charging dramatically higher rates to customers that lack competitive alternatives. We are concerned, however, about the possibility that price cap LECs could use Phase I relief, which enables them to offer contract tariffs to individual customers, to engage in exclusionary pricing behavior and thereby thwart the development of competition. Economists have long noted the incentives that monopolists have to reduce prices in the short run and forgo current profits in order to prevent the entry of rivals or to drive them from the market. The monopolist then would be able to raise prices above competitive levels and earn higher profits than would have been possible if the exclusionary pricing behavior had not occurred and competitors had not exited or been deterred from entering the market.²¹⁰ Joskow and Klevorick note the conditions that increase the likelihood, and the social cost, of exclusionary pricing

²⁰⁷ See *Price Cap Second FNPRM*, 11 FCC Rcd at 908. See also USTA Oct. 26 Comments, Att. A at 31; Bell Atlantic Oct. 26 Comments, Exh. 1 at 11, 16. Bell Atlantic states that the history of transportation regulation, natural gas regulation, and Commission regulation of private lines in the 1960s and 1970s provides ample warning of the dangers inherent in relying upon myriad fact-finding processes to implement regulatory policy in markets in which there are multiple sellers. Bell Atlantic Oct. 26 Comments, Exh. 1 at 17.

²⁰⁸ *Access Reform NPRM*, 11 FCC Rcd at 21429.

²⁰⁹ See ACTA Oct. 26 Comments at 4 nn. 3, 5 (arguing that the Commission should not adopt any new pricing flexibility rules until local exchange markets are fully and "irreversibly" open to competition).

²¹⁰ See, e.g., P. Areeda & D. Turner, *Predatory Pricing and Related Practices under Section 2 of the Sherman Act*, 88 HARV. L. REV. 697 (1975); O. Williamson, *Predatory Pricing: A Strategic and Welfare Analysis*, 87 YALE L.J. 284 (1977); J. McGee, *Predatory Pricing Revisited*, 23 J. LAW & ECON. 289 (1980); F.M. SCHERER, *INDUSTRIAL MARKET STRUCTURE AND ECONOMIC PERFORMANCE* 468-479 (1990).

behavior.²¹¹ Several of these conditions, including short-run monopoly power, low elasticity of demand, and high profits in the absence of regulatory or competitive constraints, appear to characterize the interstate access market.²¹² An incumbent can forestall the entry of potential competitors by "locking up" large customers by offering them volume and term discounts at or below cost.²¹³ Specifically, large customers may create the inducement for potential competitors to invest in sunk facilities which, once sunk, can be used to serve adjacent smaller customers. To the extent the incumbent can lock in the larger business customers whose traffic would economically justify the construction of new facilities, the incumbent can foreclose competition for the smaller customers as well.²¹⁴ Consequently, we believe that pricing flexibility must be structured to prevent exclusionary pricing behavior so as to safeguard the development of competition.

80. An incumbent monopolist will engage in exclusionary pricing behavior only if it believes that it will succeed in driving rivals from the market or deterring their entry altogether. Otherwise, the reduced profits caused by exclusionary pricing behavior will not be recouped by other sales under the resulting conditions of reduced competition, and the incumbent will be worse off than if it had not engaged in exclusionary pricing behavior. Once multiple rivals have entered the market and cannot be driven out, rules to prevent exclusionary pricing behavior are no longer necessary. Investment in facilities, particularly those that cannot be used for another purpose, is an important indicator of such irreversible entry. If a competitive LEC has made a substantial sunk investment in equipment, that equipment remains available and capable of providing service in competition with the incumbent, even if the incumbent succeeds in driving that competitor from the market. Another firm can buy the facilities at a price that reflects expected future earnings and, as long as it can charge a price that covers average variable cost, will be able to compete with the incumbent LEC.²¹⁵ In telecommunications, where variable costs

²¹¹ P. Joskow & A. Klevorick, *A Framework for Analyzing Predatory Pricing Policy*, 89 YALE L.J. 213 (1979).

²¹² See J. BONBRIGHT, *PRINCIPLES OF PUBLIC UTILITY RATES* 7-11 (2d ed. 1988); C.F. Phillips, *THE REGULATION OF PUBLIC UTILITIES* 57-58 (1993).

²¹³ We recognize that using volume and term discounts may be a more profitable predatory strategy than traditional predatory pricing if the predator is subject to rate regulation but can use headroom created by the discounts to raise prices in areas, or to customers, not subject to competition. In such a case, the predator may not have to forego profits or face the usual recoupment problem.

²¹⁴ See E. Rasmusen, J.M. Ramseyer, and J.S. Wiley, *Naked Exclusion*, 81 AM. ECON. REV. 1137-45 (December 1991).

²¹⁵ See S. MARTIN, *INDUSTRIAL ECONOMICS: ECONOMIC ANALYSIS AND PUBLIC POLICY* 414-15 (1998) (the likelihood of successful predation decreases to the extent of sunk investment by new entrants); see also *Incumbent LEC Regulatory Treatment Order*, 12 FCC Rcd at 15818-19 (even if a BOC interLATA affiliate could drive one of the three large IXCs from the market, that IXC's fiber-optic transmission capacity would remain intact, and another firm could buy that capacity at a distress sale and immediately undercut the affiliate's noncompetitive prices) (citing D.F. Spulber, *Deregulating Telecommunications*, 12 YALE J. ON REG. 25, 60 (1995)).

are a small fraction of total costs,²¹⁶ the presence of facilities-based competition with significant sunk investment makes exclusionary pricing behavior costly and highly unlikely to succeed. We conclude, therefore, that our Phase I triggers should measure the extent to which competitors have made sunk investments in facilities used to compete with the incumbent LEC.

2. Phase I Triggers for Special Access and Dedicated Transport Services

a. Collocation by Competitors

81. As we explain below, collocation by competitors in incumbent LEC wire centers is a reliable indication of sunk investment by competitors. In the *Expanded Interconnection Orders*, the Commission adopted rules requiring incumbent LECs to permit competitors to collocate equipment at incumbent LEC wire centers and other LEC locations, in order to enable competitors to terminate their transmission facilities at those locations.²¹⁷ The Commission adopted these collocation rules, with only minor modifications, to implement the collocation requirements of section 251(c)(6) of the Act.²¹⁸ More recently, the Commission expanded its collocation rules to facilitate the development of competition in the advanced services market, while promoting competition in the traditional circuit-switched voice market. In particular, incumbent LECs must make available shared caged and cageless collocation arrangements, and must permit competitors to collocate all equipment used for interconnection and/or access to UNEs, even if it includes a switching or enhanced service function.²¹⁹ In many cases, a collocation arrangement indicates the existence of a competitor's transmission facilities terminating at that collocated equipment.²²⁰ Thus collocation usually represents a financial

²¹⁶ B. MITCHELL AND I. VOGELSANG, TELECOMMUNICATIONS PRICING THEORY AND PRACTICE 9 (1991).

²¹⁷ See, e.g., *Switched Transport Expanded Interconnection Order*, 8 FCC Rcd at 7377. See also Section 64.1401 of the Commission's Rules, 47 C.F.R. § 64.1401.

²¹⁸ 47 U.S.C. § 251(c)(6) (requiring incumbent LECs to provide for collocation of equipment necessary for interconnection or access to unbundled network elements); Implementation of the Local Competition Provisions in the Telecommunications Act of 1996, First Report and Order, CC Docket Nos. 96-98, 95-185, 11 FCC Rcd 15499, 15787-89 (1996) (*Local Competition Order*), *aff'd in part and vacated in part sub nom. Competitive Telecommunications Ass'n v. FCC*, 117 F.3d 1068 (8th Cir. 1997) (*CompTel*), *aff'd in part and vacated in part sub nom. Iowa Utils. Bd. v. FCC*, 120 F.3d 753 (8th Cir. 1997) (*Iowa Utils. Bd.*), *aff'd in part and rev'd in part sub nom. AT&T Corp. v. Iowa Utils. Bd.*, 119 S. Ct. 721 (1999); *Order on Reconsideration*, 11 FCC Rcd 13042 (1996); *Second Order on Reconsideration*, 11 FCC Rcd 19738 (1996); *Third Order on Reconsideration and Further Notice of Proposed Rulemaking*, 12 FCC Rcd 12460 (1997); *further recon. pending*.

²¹⁹ See *Deployment of Wireline Services Offering Advanced Telecommunications Capability*, CC Docket No. 98-147, First Report and Order and Further Notice of Proposed Rulemaking, 14 FCC Rcd 4761 (1999), *recon. pending, petitions for review pending*.

²²⁰ See *Special Access Expanded Interconnection Order*, 7 FCC Rcd 7369; *Switched Transport Expanded Interconnection Order*, 8 FCC Rcd 7374. Ameritech also notes that collocation is an indication that competitors have facilities in place to address dedicated transport demand. Ameritech Forbearance Petition at 16.

investment by a competitor to establish facilities within a wire center. We also note that competitors incur considerable expense to establish an operational collocation arrangement. The cost to a competitor of a single collocation arrangement can exceed \$300,000.²²¹ Commenters also point out that negotiating all the terms of a collocation agreement can require considerable time and effort. For example, MCI states that negotiations lasted an average of six to nine months during the period from mid-1994 to mid-1996.²²² It also seems likely that, when a competitor initially enters a market, most of these transmission facilities will be "trunk-side" facilities, *i.e.*, facilities leading from the collocated equipment to the IXC POP rather than to the customer premises. This is because competitors can use those facilities to carry highly concentrated traffic between, for example, serving wire centers and POPs, and so can use that investment to serve a number of customers.²²³ For the same reason, competitors will probably wait to invest in line-side facilities until they have all or most of their trunk-side facilities in place. In either case, the investment in transmission facilities associated with collocation arrangements is largely specific to a location; the competitive LEC's facilities cannot, for the most part, easily be removed and used elsewhere if entry does not succeed.

82. For all these reasons, we are confident that, in the past, the presence of an operational collocation arrangement in a wire center almost always implied that a competitor has installed transmission facilities to compete with the incumbent. This correlation between operational collocation arrangements and competitive transport facilities is somewhat attenuated, however, by the advent of services such as digital subscriber line (DSL) services. Competitors providing these services usually collocate in order to gain access to the incumbent's copper loops, a necessary input for DSL service, not to compete with the incumbent for the provision of transport services.

²²¹ See, *e.g.*, Comments of the Competitive Telecommunications Association, Implementation of the Local Competition Provisions in Implementation of the Local Competition Provisions in the Telecommunications Act of 1996, CC Docket No. 96-98, Second Further Notice of Proposed Rulemaking, FCC 99-70 (rel. April 16, 1999) (*UNE Remand FNPRM*), at 39. ACC notes that collocation charges can vary greatly from incumbent to incumbent and include numerous recurring and nonrecurring charges: from \$21,054 to \$50,055 under Colorado PUC-approved interim interconnection tariffs; from \$24,950 to \$72,139 under Pacific Bell's expanded interconnection tariff; and \$50,000 per collocation at a NYNEX wire center in Syracuse. ACC Comments at 6 and n.10. AT&T also maintains that collocation tariffs often include high nonrecurring charges (NRCs). AT&T Reply at 10-12 and n.30.

²²² MCI Comments at 38-39. See also AT&T Reply at 8; ACC Reply at 5. See also Application of BellSouth Corporation, BellSouth Telecommunications, Inc., and BellSouth Long Distance, Inc., for Provision of In-Region, InterLATA Services in Louisiana, CC Docket No. 98-121, Memorandum Opinion and Order, 13 FCC Rcd 20599, 20645-46 (1998) (*Second BellSouth Louisiana Order*) (finding that BellSouth had not satisfied the section 271 requirement that incumbents provide interconnection in accordance with sections 251(c)(2) and 252(d)(1) of the Act, relying in part on evidence that it can take as long as 120 to 180 days from receipt of a complete and accurate Bona Fide Firm Order for BellSouth to construct a physical collocation space).

²²³ Bell Atlantic and MCI note that competitors are particularly active in the provision of entrance facilities. Bell Atlantic *ex parte* statement of April 27, 1998, at 14; MCI Oct. 26 Comments at 55. Ameritech also relies on collocation data to demonstrate that competitors provide dedicated transport over their own facilities "where there is a significant amount of switched traffic densely aggregated." Ameritech Forbearance Petition, Att. A at 27.

DSL services often are marketed as broad-based offerings to small business and residential customers, thus requiring competitors to collocate in many, if not all, of the wire centers in an MSA, many of which may lack competitive transport facilities.²²⁴ In this case, therefore, they rely on the incumbent's transport facilities.²²⁵ Therefore, to ensure that our triggers continue to provide a clear picture of competitive conditions on a going-forward basis, we require incumbent LECs to show that at least one competitor relies on transport facilities provided by a transport provider other than the incumbent at each wire center listed in the incumbent's pricing flexibility petition as the site of an operational collocation arrangement.

83. We acknowledge that, because we will evaluate pricing flexibility requests on an MSA basis and do not require the presence of competitive facilities in every wire center in an MSA, there remains a theoretical possibility that an incumbent LEC could use pricing flexibility in a predatory manner to deter investment in competitive facilities in those wire centers where it as yet faces no competition. For the reasons given above, however, we believe the costs, particularly the administrative costs, of granting pricing flexibility on a wire center-by-wire center basis outweigh the benefits of protecting against such theoretical harms. To the extent that an incumbent LEC attempts to use pricing flexibility in a predatory manner, aggrieved parties may pursue remedies under the antitrust laws or before this Commission pursuant to section 208 of the Act.²²⁶

84. *Administrative Burdens.* The Commission has tentatively concluded that it is important to base our triggers on "objectively measurable criteria . . . so as to avoid delay caused by protracted proceedings and to minimize administrative burdens."²²⁷ We conclude here that a collocation-based trigger provides an administratively simple and readily verifiable mechanism for determining whether competitive conditions warrant the grant of pricing flexibility. In the *Price Cap Second FNPRM*, the Commission invited comment on establishing a "competitive checklist" as a test for Phase I pricing flexibility. Specifically, the Commission sought comment on eight checklist items,²²⁸ seven of which were taken from legislation pending before Congress which led

²²⁴ For example, Sprint states that it is in the midst of requesting collocation in more than 1000 incumbent LEC end offices so that it can install its own digital subscriber line access multiplexers (DSLAMs) and provide DSL service to small business and residential customers. Sprint Comments, *UNE Remand FNPRM*, at 35. Similarly, Covad explains that, when it builds a DSL network in a market, it collocates in "several dozen central offices" and relies on the incumbent LEC's transport services to connect those central offices to the two or three Covad "hubs" in that market. Covad Comments, *UNE Remand FNPRM*, at 44-45. See also Northpoint Comments, *UNE Remand FNPRM*, at 19-20.

²²⁵ See, e.g., MCI *ex parte* statement of July 7, 1999, at 8; Sprint *ex parte* statement of July 12, 1999.

²²⁶ 47 U.S.C. § 208.

²²⁷ *Access Reform NPRM*, 11 FCC Rcd at 21431.

²²⁸ Those items are as follows:

to the Telecommunications Act of 1996.²²⁹ The 1996 Act incorporated those seven criteria into the test for determining whether a Bell Operating Company (BOC) should be permitted into the market for in-region interLATA services.²³⁰ As a result of our review of several BOC 271 applications,²³¹ the Commission has found that ascertaining whether the BOC adequately has demonstrated that it is providing these checklist items on a nondiscriminatory basis is not administratively simple or easily verifiable. These applications produce voluminous records in which the parties hotly contest BOC compliance with the checklist, and resolution of these disputes within the ninety days permitted by the statute imposes considerable burdens on both industry and the Commission.

85. In order to avoid these burdensome and costly proceedings, we will rely instead on the eighth criterion -- collocation in wire centers that account for a significant portion of the incumbent LEC's business lines or interstate access revenues.²³² This approach has widespread support from diverse segments of the industry.²³³ MCI argues that, if we permit any pricing flexibility at all, we should do so only upon a showing that competitors have collocated in wire

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- a. competing providers of local switched telephone service have been authorized and become operational;
 - b. local loops and switches have become unbundled;
 - c. intrastate expanded interconnection is available through tariff or contract (physical or virtual collocation);
 - d. service provider number portability is available, *i.e.*, end users are able to switch local service providers and retain their current telephone numbers;
 - e. compensation arrangements have been established for the LEC and its competitors to complete telephone calls originated on other carriers' networks;
 - f. competitors have access to directory assistance, 911, and other databases;
 - g. intra-LATA toll dialing parity is implemented; and
 - h. competitors have implemented or announced plans to collocate, or otherwise deploy facilities, and serve customers in wire centers (or other geographic areas) that account for a significant portion of the incumbent LEC's business lines or interstate access revenues.

Price Cap Second FNPRM, 11 FCC Rcd at 906-07.

²²⁹ The Commission noted that most of these criteria were contained in legislation pending at the time of the *Price Cap Second FNPRM*. See *Price Cap Second FNPRM*, 11 FCC Rcd at 906 n.159.

²³⁰ See 47 U.S.C. §§ 271(c)(2)(A); 271(c)(2)(B)(ii), (iv), (vii), (x), (xi), (xiii).

²³¹ See, e.g., *Second BellSouth Louisiana Order*; Application of Ameritech Michigan for Provision of In-Region, InterLATA Services in Michigan, CC Docket No. 97-137, Memorandum Opinion and Order, 12 FCC Rcd 20543 (1997) (*Ameritech Michigan Order*).

²³² See *Price Cap Second FNPRM*, 11 FCC Rcd at 906-07.

²³³ Although several commenters support the use of collocation as a trigger, they propose granting regulatory relief at different percentage thresholds. We discuss these specific proposals below.

centers serving a certain percentage of the incumbent LECs' demand.²³⁴ Bell Atlantic and Ameritech also advocate granting regulatory relief when competitors have collocated in a certain percentage of wire centers in a market area,²³⁵ or in wire centers serving a certain percentage of the demand in a market area.²³⁶ We further conclude that such a collocation-based standard is administratively simple because several BOCs have provided data of this type in support of pending forbearance petitions.²³⁷

86. Finally, we have determined that it is not burdensome to require incumbent LECs to demonstrate that at least one competitor relies on transport facilities provided by a transport provider other than the incumbent at each wire center listed in the incumbent's pricing flexibility petition as the site of an operational collocation arrangement. Competitors typically must hire the incumbent to install cable from the competitors' networks to their collocated equipment.²³⁸ Thus, incumbent LECs should be able to identify those collocators providing their own transmission facilities on the basis of their billing records. Furthermore, we do not require incumbent LECs to identify *all* the competitors collocated at each wire center and providing their own transport facilities, but rather merely to identify at least one competitor providing its own transport facilities at each wire center.

87. *Other Triggers.* We conclude that none of the other triggers proposed in this record is preferable to collocation with competitive transport. Ameritech advocates granting pricing flexibility when competitors have collocated in wire centers from which they can provide service to a certain percentage of the demand for a service in the market area, measured on the basis of DS1-equivalents.²³⁹ MCI argues, however, that a "DS1 equivalent" measure overstates competitive inroads in a market by placing disproportionate weight on entrance facilities (which are usually DS3 circuits) where competitive entry has been greatest.²⁴⁰ Because the price of one

²³⁴ MCI Oct. 26 Comments at 55.

²³⁵ Bell Atlantic *ex parte* statement of April 27, 1998, at 20-21.

²³⁶ Ameritech *ex parte* statement of June 5, 1998, at 2.

²³⁷ *See, e.g.*, Petition of Bell Atlantic Telephone Companies for Forbearance from Regulation as a Dominant Carriers in Delaware; Maryland; Massachusetts; New Hampshire; New Jersey; New York; Pennsylvania; Rhode Island; Washington, D.C.; Vermont; and Virginia, CC Docket No. 99-24, Public Notice, DA 99-224 (rel. Jan. 21, 1999); SBC Reply in SBC Forbearance Proceeding, CC Docket No. 98-227, at Att 2.

²³⁸ *See* Local Exchange Carriers' Rates, Terms, and Conditions for Expanded Interconnection Through Virtual Collocation for Special Access and Switched Transport, CC Docket No. 94-97, Phase II, Order Designating Issues for Investigation, 10 FCC Rcd 11116, 11122 n.73 (1995) (brief description of cable installation services provided by incumbent LECs as part of their virtual collocation offerings).

²³⁹ Ameritech Oct. 26 Comments, Att. N at 8; Ameritech *ex parte* statement of June 5, 1998, at 2.

²⁴⁰ MCI Oct. 26 Comments at 55.

DS3 circuit is less than the price of 28 DS1 circuits,²⁴¹ even though they provide equal capacity, MCI argues that measuring competitors' market presence on the basis of revenues gives a better indication of the extent to which competitors have made significant inroads into the market in question.²⁴² We agree with MCI. Because competitors are drawn to new markets by the prospect of earning revenues, rather than merely opportunities to provide capacity, we find that revenue is a more relevant measure of market entry. Moreover, we want to adopt Phase I triggers that ensure that incumbent LECs can no longer successfully drive new entrants from the market. If we adopted a trigger based on percentage of demand measured in terms of DS1 equivalents, then an incumbent LEC might receive Phase I pricing flexibility for all dedicated transport services and all special access services other than channel terminations, even though competitive alternatives may exist only for entrance facilities.

88. In the *Access Reform NPRM*, the Commission sought comment on adopting triggers related to the degree to which local markets are open to competition, such as availability of UNEs at forward-looking economic cost, transport and termination at cost-based rates, and resale of retail services at a wholesale price.²⁴³ We find that collocation-based standards provide a better basis for Phase I triggers than standards based on availability of UNEs and resale, because availability does not indicate whether they actually have been purchased. Further, a competitor's use of UNEs or resale does not indicate that it has sunk investments in facilities in the MSA, because services provided over UNEs or through resale make use of the incumbent's facilities. Purchase of UNEs by a competitor does not, by itself, constitute the type of investment in facilities that warrants pricing flexibility for special access and dedicated transport services. UNEs, by definition, comprise incumbent LEC facilities that are leased to competitors. Because competitors have few "sunk costs" associated with UNEs, if an incumbent drives a UNE-based competitor from the market, that competitor does not leave facilities in place that another firm then can buy at a discount. Instead, a subsequent competitor would have to negotiate with the incumbent for use of those UNE facilities.²⁴⁴ As a result, such a competitor may be susceptible to an exclusionary pricing scheme. Similarly, the presence of a state-approved interconnection agreement or Statement of Generally Available Terms and Conditions, proposed as a trigger by USTA, does not by itself indicate that new market entrants have made sufficient sunk investments in facilities to resist exclusionary pricing behavior.²⁴⁵ Finally, although a transport and termination

²⁴¹ See AT&T Opposition to SBC Forbearance Petition, CC Docket No. 98-227, at 5; AT&T Opposition to U S West Phoenix Forbearance Petition, CC Docket No. 98-157, at 7; BellSouth Telecommunications, Inc., Tariff F.C.C. No. 1, 4th Revised Page 7-144.1 and 3rd Revised Page 7-145.0.1.2 (effective July 1, 1998).

²⁴² MCI Oct. 26 Comments at 55-56.

²⁴³ See *Access Reform NPRM*, 11 FCC Rcd at 21429-32.

²⁴⁴ In Section VI.C.3 of this Order, we explain why we will consider evidence of competitors' use of UNE loops as part of the required Phase I showings for other switched access services.

²⁴⁵ USTA Oct. 26 Comments, Att. E.

agreement between an incumbent and a competitor may imply that the competitor is carrying traffic over its own network, that may not provide evidence of investment in facilities used to compete with an incumbent LEC. For example, the competitor may carry wireless traffic, which may or may not be a competitive substitute for wireline connections, or the competitor may provide service over UNEs. Accordingly, we conclude that collocation arrangements are more likely than transport and termination agreements to demonstrate that competitors have invested in facilities sufficiently to resist exclusionary pricing behavior.

89. We also reject CFA's proposal to grant pricing flexibility only upon a showing of compliance with the section 271 criteria, among other things.²⁴⁶ Section 271 compliance demonstrates that a BOC has opened its local markets to competition, but it may not show the extent of competitive alternatives in the market for interstate access services. Competition may have developed to such a degree as to warrant granting pricing flexibility to such a BOC in part of a state, even if the incumbent has not satisfied the checklist, either because it is not interested in section 271 relief, or because, for example, it is working to bring its operations support systems (OSS) into compliance. Delaying pricing flexibility under these circumstances denies access customers the benefits of increased efficiency in the interstate access market. Furthermore, we determine above not to grant pricing flexibility on a state-by-state basis because competitors generally do not enter new markets on that basis. Because section 271 requires the Commission to make state-wide determinations,²⁴⁷ granting pricing flexibility upon compliance with the 14-point checklist raises the same concerns.

90. Furthermore, we will not require incumbent LECs to demonstrate that they no longer possess market power in the provision of any access services to receive pricing flexibility, for two reasons. First, as we explain in more detail below,²⁴⁸ regulation imposes costs on carriers and the public, and the costs of delaying regulatory relief outweigh any costs associated with granting that relief before competitive alternatives have developed to the point that the incumbent lacks market power. Second, non-dominance showings are neither administratively simple nor easily verifiable. As several BOCs note in their forbearance petitions, the Commission previously has based non-dominance findings on several complex criteria, including market share and supply elasticity.²⁴⁹ Market share analyses require considerable time and expense, and they generate

²⁴⁶ Specifically, CFA would require "full and sustained compliance" with sections 251, 252, 253, 271, and 272 of the Act. CFA Nov. 9 Reply at 8.

²⁴⁷ Section 271 requires, among other things, a BOC to satisfy the 14-point checklist throughout a state to obtain authority to offer in-region, interLATA services in that state. *See* 47 U.S.C. § 271(b)(1).

²⁴⁸ *See* Section VI.C.5.a, *infra*.

²⁴⁹ *See, e.g.,* Comsat Corporation, Petition Pursuant to Section 10(c) of the Communications Act of 1934, as amended, for Forbearance from Dominant Carrier Regulation and for Reclassification as a Non-Dominant Carrier, Order and Notice of Proposed Rulemaking, 13 FCC Rcd 14083, 14118-19 (1998), *cited in* U S West Phoenix Forbearance Petition at 14; U S West Seattle Forbearance Petition at 14-32; Ameritech

considerable controversy that is difficult to resolve. For example, in response to U S West's Phoenix forbearance petition, several commenters assert that U S West overstates its market share losses by treating re-sold services as services provided by competitors, even though U S West continues to provide the underlying facilities.²⁵⁰ Sprint claims that we cannot rely on U S West's market share analysis without reviewing the underlying data.²⁵¹ Measuring supply elasticity also can be controversial; a number of commenters claim, for example, that U S West underestimates its competitors' costs of extending their networks.²⁵² ALTS argues, moreover, that excess capacity in competitors' networks is generally limited to particular routes, and incumbent LECs should not, therefore, rely on that existing excess capacity to support claims regarding the elasticity of supply in the interstate access market.²⁵³

91. We do not address in this Order whether any BOC has adequately supported its market share or supply elasticity claims in its forbearance petition. Rather, we conclude here that it would be administratively burdensome to require incumbent LECs to perform and the Commission to evaluate market share or supply elasticity analyses before the LECs may obtain any regulatory relief, and so we decline to adopt such a requirement here.

92. Finally, we disagree with commenters opposing any additional pricing flexibility for price cap LECs at this time. These commenters either argue generally that price cap LECs have sufficient pricing flexibility to respond to competition under the current price cap rules,²⁵⁴ or that price cap LECs must not face meaningful competition because rates in the trunking basket are generally at the maximum permitted under the price cap rules.²⁵⁵ First, the existing rules clearly limit price cap LECs' ability to respond to competition. Price cap LECs are subject to both our Part 61 rules regarding rate levels and the mandatory rate structure rules set forth in Part 69 of our rules. Our rules precluding LECs from offering contract tariffs and limiting volume and term

Forbearance Petition at 11.

²⁵⁰ See CompTel Comments in U S West Phoenix Forbearance Proceeding at 3-4; MCI Comments in U S West Phoenix Forbearance Proceeding at 19; Sprint Comments in U S West Phoenix Forbearance Proceeding at 5-7; AT&T Comments in U S West Phoenix Forbearance Proceeding at 8; GST Comments in U S West Phoenix Forbearance Proceeding at 13-16; Qwest Comments in U S West Phoenix Forbearance Proceeding at 6.

²⁵¹ Sprint Opposition in U S West Phoenix Forbearance Proceeding at 7.

²⁵² See CompTel Comments in U S West Phoenix Forbearance Proceeding at 6-7; MCI Comments in U S West Phoenix Forbearance Proceeding at 10-13; AT&T Comments in U S West Phoenix Forbearance Proceeding at 9-10; Sprint Comments in U S West Phoenix Forbearance Proceeding at 10-11; Qwest Comments in U S West Phoenix Forbearance Proceeding at 3.

²⁵³ ALTS *ex parte* statement of June 25, 1999, at 13.

²⁵⁴ See, e.g., MCI Oct. 26 Comments at 36-37.

²⁵⁵ See, *id.* at 37-38.

discount offerings may create a price umbrella for competitors. Second, as mentioned above, delaying regulatory relief imposes costs on carriers and the public, the latter of which is deprived of the benefits of more vigorous competition. We see no public benefit in any further delay in regulatory relief, once an incumbent LEC has satisfied the triggers we adopt below. Finally, price cap LECs were required to eliminate at least some of the headroom in the trunking basket as a result of the X-Factor increase adopted in *Price Cap Fourth Report and Order*.²⁵⁶ Observing that there is no headroom in the trunking basket does not necessarily mean, therefore, that price cap LECs face no competition, because we cannot know the extent to which the X-Factor puts downward pressure on rates that the price cap LECs otherwise might have lowered in response to competition.

b. Dedicated Transport and Special Access Services, Other than Channel Terminations

93. We conclude that incumbent price cap LECs are entitled to Phase I pricing flexibility for dedicated transport services (entrance facilities, direct-trunked transport, and the flat-rated portion of tandem-switched transport) and special access services other than channel terminations upon demonstrating that competitors have collocated²⁵⁷ in 15 percent of an incumbent LEC's wire centers in the MSA, or in wire centers accounting for 30 percent of the incumbent LEC's revenues from these services. The relief granted upon satisfaction of this Phase I trigger, together with the relief we grant immediately in Sections III and V above, is comparable to much of the relief proposed by Bell Atlantic and Ameritech in their 1998 *ex parte* statements.²⁵⁸ We rely in part on the record developed in response to Bell Atlantic's and Ameritech's proposals in developing our Phase I triggers. Bell Atlantic proposes granting relief when competitors have collocated facilities, purchased UNEs, or installed their own facilities in 25 percent of the wire centers in the market area.²⁵⁹ Ameritech recommends granting relief when competitors have collocated in wire centers serving 25 percent of the demand in a market area, measured on a DS1-equivalent basis.²⁶⁰ MCI, however, recommends deferring relief until competitors account for at least 50 percent of

²⁵⁶ *Price Cap Fourth Report and Order*, 12 FCC Rcd 16642.

²⁵⁷ For purposes of this Order, we use the terms "collocation" and "collocated" to refer to operational collocation arrangements, *i.e.*, arrangements serving at least one customer. See Ameritech Forbearance Petition, Att. A at 26.

²⁵⁸ We streamline the regulation of new services in Section III, and we grant greater flexibility to deaverage rates for services in the trunking basket in Section V. In addition, upon satisfying the Phase I triggers, an incumbent LEC may offer volume and term discounts and contract tariffs under the Commission's framework. Bell Atlantic and Ameritech propose all these forms of relief, plus growth discounts, X-Factor reductions, and service band index (SBI) increases. We do not permit these flexibilities in Phase I, for reasons discussed below.

²⁵⁹ Bell Atlantic *ex parte* statement of April 27, 1998, at 20.

²⁶⁰ Ameritech *ex parte* statement of June 5, 1998, at 2.

the revenue in a market or 50 percent of the channel terminations between end offices and customer premises.²⁶¹

94. As we explain above, we conclude that it is appropriate to give incumbent LECs pricing flexibility when competitors have made irreversible, sunk investment in facilities.²⁶² For the reasons discussed above, UNEs do not represent sunk investment in facilities used to compete with incumbent LECs in the provision of special access and dedicated transport services, and so we reject Bell Atlantic's proposal that we include purchase of UNEs as a measure of competitive presence within a wire center. We also reject Bell Atlantic's proposal that we grant flexibility when competitors have collocated facilities *or* installed their own facilities in 25 percent of the wire centers in the market area.²⁶³ Although the presence of competitive facilities within a wire center may well be the best evidence of irreversible investment, this type of trigger is neither simple to administer nor easily verifiable. Our review of the records developed in response to the pending forbearance petitions indicates widespread disagreement among the parties as to the scope and reach of competitive facilities within a particular geographic area.²⁶⁴ A competitor has "installed its own facilities" within a wire center if, for example, it has laid fiber anywhere within the area served by the wire center, but a separate analysis is required to determine what proportion of the incumbent's customers the competitor can serve with those facilities. Our desire to avoid these administratively burdensome proceedings compels us to adopt collocation as a measure of competitive presence.

95. We recognize, however, that evidence of collocation may underestimate the extent of competitive facilities within a wire center, because it fails to account for the presence of competitors that do not use collocation and have wholly bypassed incumbent LEC facilities. For this reason, and because the Phase I relief we are granting is not as extensive as that sought by the incumbent LECs,²⁶⁵ we find that a threshold lower than 25 percent is warranted. Based on the

²⁶¹ MCI Oct. 26 Comments at 55.

²⁶² Our conclusions concerning whether an incumbent LEC is entitled to pricing flexibility in no way prejudice either the Commission's approach to or the outcome of the pending proceeding pertaining to the obligations of incumbent LECs to provide unbundled network elements. *See UNE Remand FNPRM*.

²⁶³ Bell Atlantic *ex parte* statement of April 27, 1998, at 20.

²⁶⁴ *See, e.g.*, U S West Phoenix Forbearance Petition in CC Docket No. 98-157, at 12-14; MCI Opposition in U S West Phoenix Forbearance Proceeding, CC Docket No. 98-157, at 8 (dispute over reach of competitive facilities in Phoenix MSA).

²⁶⁵ We explain below that we reject proposals to permit growth discounts or X-Factor reductions as forms of regulatory relief. In addition, Bell Atlantic advocates permitting incumbent LECs limited upward pricing flexibility. Bell Atlantic *ex parte* statement of April 27, 1998, at 22. We do not permit any upward pricing flexibility in Phase I.

information submitted in support of several pending petitions for forbearance,²⁶⁶ it appears that collocation in 15 percent of an incumbent's wire centers in an MSA represents significant investment in competitors' facilities. For example, Bell Atlantic reports that competitors have collocated in 17.9 percent of its wire centers in the Norfolk LATA,²⁶⁷ and that competitors have installed about 2200 miles of fiber in that LATA.²⁶⁸ In three SBC MSAs in which competitors have collocated in slightly more than 15 percent of SBC's wire centers,²⁶⁹ SBC reports that competitors' networks average at least 736 miles.²⁷⁰ This figure seems conservative because SBC reports figures for only a few of its competitors within these MSAs.²⁷¹ Because a competitor must devote significant time and expense to establish each collocation arrangement,²⁷² the extent of collocation in those three SBC MSAs indicates that competitors have made considerable investment in these MSAs. We conclude, therefore, that collocation by competitors in 15 percent of the incumbent LEC's wire centers in an MSA is the appropriate trigger for Phase I relief with respect to dedicated transport services and special access services other than channel terminations.

²⁶⁶ For the purposes of this rulemaking, we need not determine whether the studies submitted in support of the pending forbearance petitions justify the relief sought in those proceedings. The firm conducting those studies, Quality Strategies, Inc., bases its conclusions on surveys of telecommunications customers in an MSA. *See, e.g.*, SBC Forbearance Petition, Att. A at 45-46. Several commenters criticize the Quality Strategies studies as providing inadequate support for the BOCs' claims of market share loss. *See, e.g.*, Hyperion Opposition to SBC Forbearance Petition, CC Docket No. 98-27, at 4-6; KMC Opposition to SBC Forbearance Petition, CC Docket No. 98-27, at 2-4; Logix Opposition to SBC Forbearance Petition, CC Docket No. 98-27, at 3-6. Only AT&T questions Quality Strategies's data on the extent of competitors' investment, however. AT&T Opposition to SBC Forbearance Petition, CC Docket No. 98-27, at 8 n.10. In reply, SBC maintains that AT&T did not provide sufficient detail for its claims regarding the extent of competitors' investment but theorizes that the difference between the AT&T and Quality Strategies data results from differences in the size of the areas analyzed. For example, SBC claims that AT&T probably focuses on downtown Los Angeles, while Quality Strategies examined the entire Los Angeles area. SBC Reply in SBC Forbearance Proceeding, CC Docket No. 98-227, Att. 1 at 9. SBC is persuasive on this point. Therefore, without reaching the issue of whether we can base market share determinations on the Quality Strategies studies, we find that we can rely on those studies to supplement the record in this proceeding regarding where competitors have collocated or installed facilities in certain MSAs.

²⁶⁷ Bell Atlantic Forbearance Petition, Att. C at 25.

²⁶⁸ *Id.*, Exh. 10 at 2.

²⁶⁹ Those MSAs are Sacramento (8 wire centers; 21 percent); Houston (11 wire centers; 18 percent); and San Antonio (6 wire centers; 21 percent). SBC Reply in SBC Forbearance Proceeding, CC Docket No. 98-227, Att. 2.

²⁷⁰ Competitors have installed at least 400 route miles of fiber in Sacramento, at least 1228 route miles in Houston, and at least 580 miles in San Antonio. SBC Forbearance Petition, Att. A at 14, 38, 41.

²⁷¹ SBC provides route mileage data for only two of its three competitors in Sacramento, and only two of its four competitors in San Antonio. In Houston, SBC claims that TCG's network is comprised of 600 to 800 route miles. SBC Forbearance Petition, Att. A at 14, 38, 41.

²⁷² *See* Section VI.C.2.a. *supra*.

96. Our selection of this 15 percent threshold and the other thresholds we adopt below, like ratemaking issues, is not an exact science.²⁷³ Rather, the thresholds are policy determinations based on our agency expertise, our interpretation of the record before us in this proceeding,²⁷⁴ and our desire to provide a bright-line rule to guide the industry. This latter factor counsels against adoption of triggers that may provide more comprehensive measures of competition but impose heavy burdens on both industry and the Commission. Our effort to select triggers that precisely measure competition for particular services also is hampered by the lack of verifiable data concerning competitors' revenues and facilities. Unlike incumbent LECs, competitors are not subject to Commission reporting requirements, and they often are unwilling to provide this information voluntarily. Given these constraints, we adopt triggers that, in our reasoned judgment, balance both the desires for precision and simplicity and the costs to carriers and customers alike of delaying the grant of pricing flexibility.

97. In some cases, a few wire centers may account for a disproportionate share of revenues for a particular service. For instance, Bell Atlantic claims that 93 percent of its special access demand measured on a DS-1 equivalent basis is concentrated in 20 percent of its wire centers.²⁷⁵ Although, as we explained above, measuring demand on a DS-1 equivalent basis overstates competitors' presence, we nevertheless find that Bell Atlantic has shown that demand is often concentrated in particular areas. We find that collocation in wire centers representing a significant percentage of incumbent LEC revenues from a particular service also indicates meaningful investment by competitors. Accordingly, we will permit price cap LECs to satisfy the Phase I trigger on a revenue basis, as well as by showing that competitors have collocated in a percentage of incumbent LEC wire centers in an MSA.

98. We conclude that the revenue-based trigger should be higher than the trigger based on percentage of wire centers in the MSA in which competitors have collocated. If certain wire centers account for a disproportionate share of revenues, then we need to establish revenue-based thresholds higher than the percentage-based threshold to ensure that competitors have extended their networks beyond a few revenue-intensive wire centers. Ameritech recommends granting relief if competitors have collocated in wire centers providing service to 25 percent of the demand for transport services measured on the basis of DS1-equivalents.²⁷⁶ MCI advocates conditioning relief on competitors achieving a 50 percent market share in revenue terms.²⁷⁷ Based on these

²⁷³ See *United States v. FCC*, 707 F.2d 610, 618 (D.C. Cir. 1983) (*United States v. FCC*) (citing *Association of American Publishers, Inc., v. Governors of the United States Postal Service*, 485 F.2d 768, 773 (D.C. Cir. 1973)).

²⁷⁴ *United States v. FCC*, 707 F.2d at 618 (citing *Permian Basin Area Rate Cases*, 390 U.S. 747, 790 (1968); *Sun Oil Co. v. FPC*, 445 F.2d 764, 767 (D.C. Cir. 1971)).

²⁷⁵ Bell Atlantic Forbearance Petition, Att. A at 2.

²⁷⁶ Ameritech *ex parte* statement of June 5, 1998, at 2.

²⁷⁷ MCI Oct. 26 Comments at 55.

pleadings, we conclude that incumbents will qualify for Phase I relief upon demonstrating that competitors have collocated in wire centers accounting for 30 percent of the incumbent's revenues for special access (other than channel terminations) and dedicated transport services.

99. Bell Atlantic asserts that a revenue-based trigger is unworkable because the proper allocation of revenues among offices for a special access or dedicated transport services routed through multiple offices might be open to dispute.²⁷⁸ Bell Atlantic's argument is unpersuasive with respect to channel terminations because those services are not routed through intermediate offices. With respect to other special access and dedicated transport services, however, we agree that there is a revenue allocation issue. Access customers order special access and dedicated transport services to provide a transmission path between two customer-designated locations.²⁷⁹ We therefore direct any LEC seeking pricing flexibility to allocate 50 percent of the revenue from a dedicated service routed through multiple offices to the office at each end of the transmission path, unless it can make a convincing case in its petition that some other allocation would better represent the extent of competitive entry in the MSA at issue. Although a 50 percent allocation rule seems reasonable, we cannot conclude that other allocation schemes might not also be reasonable under the circumstances. Although this is not a bright-line test like we have adopted elsewhere in this Order, determining whether a petitioner has made a convincing showing on this allocation issue should not be difficult.

c. Channel Terminations

100. We conclude that pricing flexibility for channel terminations requires separate consideration of the degree of competition for channel terminations between an IXC POP and LEC serving wire center and channel terminations between a LEC end office and customer premises. Accordingly, incumbent LECs qualify for Phase I pricing flexibility with respect to channel terminations between an IXC POP and a LEC serving wire center by showing that competitors have collocated in 15 percent of the wire centers in an MSA, or in wire centers accounting for 30 percent of incumbent LEC revenues from these services. With respect to channel terminations between a LEC end office and a customer premises, incumbent LECs qualify for Phase I pricing flexibility by showing that competitors have collocated in 50 percent of incumbent LEC wire centers in the MSA, or in wire centers accounting for 65 percent of incumbent LEC revenues from these services.²⁸⁰

²⁷⁸ Bell Atlantic *ex parte* statement of May 27, 1999, at 8-9.

²⁷⁹ *See, e.g.*, Investigation of Special Access Tariffs of Local Exchange Carriers, CC Docket No. 85-166, Phase I, Tentative Decision, 8 FCC Rcd 1059, 1063-64 (1993); Investigation of Special Access Tariffs of Local Exchange Carriers, CC Docket No. 85-166, Phase I, Memorandum Opinion and Order, Tentative Decision, 12 FCC Rcd 7026, 7042 (1997).

²⁸⁰ The triggers we adopt here for granting pricing flexibility for particular services do not vary according to the technology employed. For example, the Commission found that certain digital subscriber line (DSL) services offered by incumbent LECs are special access services. *See* GTE Telephone Operating Cos. GTOC Transmittal

101. We find that channel terminations between a LEC end office and a customer premises warrant different treatment than other special access and dedicated transport services.²⁸¹ ALTS recommends treating channel terminations separately from other special access and dedicated transport services because channel terminations are not substitutes for those services.²⁸² MCI recommends granting relief in the transport market only upon a showing that competitors have captured a 50 percent market share in revenue terms, or 50 percent of the channel terminations between end offices and customer premises.²⁸³

102. We agree that pricing flexibility for channel terminations between a LEC end office and a customer premises requires a higher threshold than flexibility for other dedicated transport and special access services. Entrance facilities, direct-trunked transport, channel mileage, and the flat-rated portion of tandem-switched transport all involve carrying traffic from one point of traffic concentration to another. Thus, entering the market for these services requires less investment per unit of traffic than is required, for example, for channel terminations between an end office and customer premises. Furthermore, investment in entrance facilities enables competitors to provide service to several end users, while channel terminations between an end office and customer premises serve only a single end user. Accordingly, competitors are likely to enter the market for entrance facilities, direct-trunked transport, channel mileage, and the flat-rated portion of tandem-switched transport before they enter the market for channel terminations between a LEC end office and a customer premises.²⁸⁴ We therefore adopt a higher threshold for granting flexibility for these channel terminations than for other special access and dedicated transport services.

No. 1148, CC Docket No. 98-79, Memorandum Opinion and Order, 13 FCC Rcd 22466, 22480 (1998); Bell Atlantic Telephone Cos., *et al.*, CC Docket Nos. 98-168, 98-161, 98-167, 98-103, Memorandum Opinion and Order, 13 FCC Rcd 23667, 23675 (1998). Accordingly, we will grant LECs pricing flexibility for the provision of these services upon satisfaction of the Phase I or Phase II criteria for channel terminations between an end office and a customer's premises.

²⁸¹ See MCI Oct. 26 Comments at 57 (noting that, if a CLEC does not build to all locations using its own facilities, it must collocate in incumbent LEC wire centers and rely on incumbent LEC facilities for the path between the end office and the customer premises).

²⁸² ALTS *ex parte* statement of June 25, 1999, at 10.

²⁸³ MCI Oct. 26 Comments at 55. Upon this showing, MCI would permit incumbent LECs to offer contract tariff services. MCI Oct. 26 Comments at 48. MCI opposes any intermediate regulatory relief, arguing that our current rules afford incumbent LECs adequate pricing flexibility and that no more flexibility is warranted until incumbents can show that they face "substantial competition." MCI Oct. 26 Comments at 57-59. At most, MCI would permit incumbent LECs to increase their zone density pricing zones from three to five. MCI Oct. 26 Comments at 58-59.

²⁸⁴ See MCI Oct. 26 Comments at 55; Bell Atlantic *ex parte* statement of April 27, 1998, at 14; Ameritech Forbearance Petition, Att. A at 26-26 and exh. 2.

103. This higher threshold is warranted for another reason. As a number of parties indicate, a competitor collocating in a LEC end office continues to rely on the LEC's facilities for the channel termination between the end office and the customer premises, at least initially, and thus is susceptible to exclusionary pricing behavior by the LEC,²⁸⁵ and so collocation by competitors does not provide direct evidence of sunk investment by competitors in channel terminations between the end office and the customer premises. We recognize, therefore, the shortcomings of collocation as a measure of competition for channel terminations between end offices and customer premises, but it appears to be the best option available to us at this time. MCI's suggestion that LECs show that competitors have captured 50 percent of the market for these services²⁸⁶ is problematic because market share determinations are unreliable in the absence of verifiable data regarding competitors' revenues. The Commission has, to date, engaged only in voluntary data collection with respect to competitive providers of telecommunications services, and those efforts are not satisfactory for providing a comprehensive picture of the degree of competition in the marketplace. AT&T's most recent proposal to measure competition for channel terminations by comparing revenue represented by competitive facilities to revenue represented by incumbent LEC facilities suffers from the same deficiency.²⁸⁷ AT&T acknowledges that data used to support the revenue measure is not now available, either to the Commission or to the incumbents that would be required to satisfy any such trigger; it states that the data "would be developed by and drawn from the industry as necessary, subject to appropriate certification and verification procedures."²⁸⁸ Although we welcome suggestions from AT&T and others about the desirability of formal reporting requirements, we are not prepared to defer pricing flexibility to seek comment on those proposals.²⁸⁹

104. Despite the shortcomings of using collocation to measure competition for channel terminations, moreover, it seems likely that a new market entrant would provide channel terminations through collocation and leased LEC facilities only on a transitional basis and will eventually extend its own facilities to reach its customers. It also seems likely, therefore, that the extent to which competitors have collocation arrangements in an MSA is probative of the degree of sunk investment by competitors in channel terminations between the end office and the customer premises throughout the MSA. In addition, as we discuss above, collocation is a

²⁸⁵ See MCI Oct. 26 Comments at 64 (If a competitor relies on collocation, it cannot provide an alternative to incumbent's channel terminations between the central office and the customer premises unless the incumbent offers unbundled loops at cost-based rates).

²⁸⁶ MCI Oct. 26 Comments at 55.

²⁸⁷ See AT&T *ex parte* statement of July 29, 1999, at 2.

²⁸⁸ AT&T *ex parte* statement of July 29, 1999, at 1.

²⁸⁹ AT&T's latest proposal that the Commission collect revenue data from competitors is not reflected in the comments it submitted in response to the December 1996 *Access Reform NPRM* or in response to the *October 5 Public Notice*.

conservative measure of competition in that it does not measure competition from competitors that bypass LEC facilities altogether. Given the lack of other data in the record, therefore, we conclude that it is reasonable to rely on collocation as a proxy for irreversible, sunk investment in channel terminations between the end office and the customer premises and to set the applicable thresholds high enough to account for the limitations inherent in this trigger. Based on this reasoning, we reach two conclusions: (1) we must require incumbent LECs to make separate showings for each kind of channel termination; and (2) the thresholds for channel terminations between the end office and the customer premises must be higher than the thresholds for channel terminations between the IXC POP and the serving wire center.

105. Thus, we reject incumbent LEC recommendations to the extent that they advocate adoption of the same triggers for all channel terminations as for other dedicated transport and special access services. Instead, we adopt a trigger for channel terminations between a LEC end office and a customer premises based in part on MCI's recommendation that incumbent LECs must demonstrate that competitors have gained a 50 percent market share in revenue terms, or 50 percent of the channel terminations between end offices and customer premises. In order to avoid administratively burdensome market share determinations, however, we adopt collocation rather than market share as a measure of competitive presence. Specifically, we will permit Phase I pricing flexibility for channel terminations between an incumbent LEC's end office and customer premises when competitors have collocated in 50 percent of incumbent LEC wire centers in the MSA. Bell Atlantic reports that competitors have collocated in 50 percent of its wire centers in two LATAs, New York Metro and Philadelphia.²⁹⁰ Furthermore, Bell Atlantic states that its competitors in Philadelphia include AT&T, with a 300-mile network,²⁹¹ and MCI, with a 100-mile network.²⁹² Bell Atlantic also lists five other competitors providing service in Philadelphia.²⁹³ It seems likely that some of that investment is in channel terminations, suggesting that collocation in 50 percent of the wire centers in a geographic area correlates to sunk investment in channel terminations. Accordingly, we conclude that collocation in 50 percent of an incumbent LEC's wire centers within an MSA is an appropriate threshold for channel terminations between that LEC's end office and customer premises.

106. As we found above with respect to dedicated transport and other special access services, demand for these channel terminations may be fairly concentrated. Therefore, we also permit incumbent LECs to demonstrate that competitors have collocated in wire centers accounting for 65 percent of incumbent LEC revenues from these services. This 65 percent threshold is 15 percent higher than the trigger based on percentage of the wire centers in an MSA

²⁹⁰ Bell Atlantic Forbearance Petition, Att. C at 25.

²⁹¹ *Id.*, Exh. 7 at 2.

²⁹² *Id.*, Exh. 7 at 1.

²⁹³ Those competitors are Hyperion, Intermedia Communications, Inc., NEXTLINK, Metromedia Fiber Network, Inc., and Winstar Communications, Inc. *Id.*, Exh. 7 at 4-6.

where competitors have collocated. This 15 percent difference is consistent with the difference in the triggers we adopted for dedicated transport and other special access services, *i.e.*, wire centers accounting for 30 percent of the incumbent LEC's revenues for those services, or collocation at 15 percent of the wire centers in the MSA.

107. We also find, however, that a lower threshold is warranted for channel terminations between a LEC serving wire center and an IXC POP. As explained above, competition is likely to develop first for those services that carry traffic between points of high traffic concentration. Moreover, a competitor collocated at a LEC serving wire center provides the channel termination to an IXC POP over its *own* facilities.²⁹⁴ We conclude that incumbent LECs may demonstrate sunk investment by competitors with respect to these channel terminations if competitors have collocated in 15 percent of the wire centers in an MSA, or in wire centers accounting for 30 percent of the demand, measured by revenues, for these channel terminations in the MSA. Because these channel terminations carry traffic between points of concentration similar to the points connected by entrance facilities, we conclude that they should have the same trigger.

3. Phase I Triggers for Other Switched Access Services

108. We conclude that an incumbent price cap LEC should be allowed Phase I pricing flexibility for common line and traffic-sensitive services, and the traffic-sensitive components of tandem-switched transport service, when it demonstrates that competitors, in aggregate, offer service over their own facilities to at least 15 percent of incumbent LEC customer locations in the MSA.²⁹⁵

109. We conclude above that Phase I relief for a particular service is warranted when an incumbent LEC demonstrates that competitors have made irreversible investment in facilities used to compete with the incumbent LEC in the provision of that service. For special access and dedicated transport services, we adopt a trigger based on collocation by competitors because competitors historically have collocated in incumbent LEC wire centers in order to provide transport and special access services.²⁹⁶ Thus collocation furnishes evidence of irreversible investment in facilities in part because it indicates competitive transmission facilities terminating at

²⁹⁴ As we explained above, a competitor collocated at a LEC end office generally leases *LEC* facilities to reach end user customers.

²⁹⁵ Tandem-switched transport has three components: a per-minute charge for transport of traffic over common transport facilities between the incumbent LEC's end office and the tandem switching office; a per-minute tandem switching charge; and a flat-rated charge for transport of traffic over dedicated transport facilities between the serving wire center and the tandem switching office. 47 C.F.R. § 69.111(a)(2). For the purposes of this section, we include traffic-sensitive components of tandem-switched transport service in the term "traffic-sensitive service." We address Phase I pricing flexibility for the dedicated component of tandem-switched transport, *supra*, in Section VI.C.2.b.

²⁹⁶ See Section VI.C.2, *supra*.

the collocation site.²⁹⁷ Although we acknowledge that some competitors provide these services exclusively over their own facilities (total facilities bypass), the extent of such competition is difficult to measure. Because collocation traditionally has served as the building block for competitive transport services, we conclude that it constitutes a sufficient measure of the degree to which competitors have invested in facilities to provide these services.

110. Competition for common line and traffic-sensitive services, however, is a much more recent phenomenon, and it may not develop in this same manner. For this reason, a different approach to granting pricing flexibility for these services is warranted. For traffic-sensitive and common line services, we adopt a Phase I trigger that takes into account competitors that have wholly bypassed incumbent LEC facilities, as well as competitors that collocate in incumbents' wire centers so as to provide service over unbundled loops.

111. The 1996 Act opened the local exchange market and, hence, the market for switched access services, to competition.²⁹⁸ The Act envisions three alternatives that competitors might employ, either singly or in combination, to enter this market: total service resale, service using unbundled network elements, and service provided over the competitor's own facilities.²⁹⁹ Not all of these entry strategies, however, indicate that competitors have made irreversible investment in facilities used to compete with incumbents in the provision of switched access services. As we explain above,³⁰⁰ resold services employ only incumbent LEC facilities and thus do not indicate any irreversible investment by competitors whatsoever. Similarly, a competitor providing service solely over unbundled network elements leased from the incumbent (the so-called "UNE platform"³⁰¹) has little, if any, sunk investment in facilities used to compete with the incumbent LEC.³⁰² For these reasons we do not allow an incumbent LEC to qualify for Phase I relief as a result of competition solely from resale or unbundled network elements.

112. If, however, competitors offer switched access services either entirely over their own facilities or by combining unbundled loops with their own switching and transport, this indicates the type of irreversible investment in facilities that warrants Phase I pricing flexibility for these services. In the first case, the competitor bypasses incumbent facilities altogether; in the latter case, a competitor must collocate in an incumbent's wire center to connect the leased loops to its transport facilities. Although a trigger based solely on collocation is administratively simpler and

²⁹⁷ See Section VI.C.2.a, *supra*.

²⁹⁸ See, e.g., *Access Reform NPRM*, 11 FCC Rcd at 21358-59.

²⁹⁹ See, e.g., *Local Competition Order*, 11 FCC Rcd at 15509.

³⁰⁰ See Section VI.C.2.a, *supra*.

³⁰¹ See *Ameritech Michigan Order*, 12 FCC Rcd at 20628.

³⁰² See Section VI.C.2.a, *supra*.

more easily verified, we decline in this case to adopt such a trigger because we lack sufficient experience with competition in the local exchange and switched access markets to know the extent to which competitors might rely on either of these entry strategies. We note, for example, that the time and expense required to establish collocation arrangements³⁰³ and the difficulties associated provisioning of UNEs by incumbent LECs³⁰⁴ may encourage competition through total bypass. Because it is unclear, therefore, the extent to which competitors are pursuing UNE-based entry strategies,³⁰⁵ we conclude that data concerning total bypass may be particularly important in assessing the degree of competitive entry in the markets for switched services.

113. Rather than looking solely at collocation, therefore, we adopt a Phase I trigger for switched services that measures the extent to which competitors offer these services either exclusively or largely over their own facilities. We will grant Phase I pricing flexibility for common line and traffic-sensitive services to an incumbent LEC in an MSA if that LEC demonstrates that competitors offer service over their own facilities to 15 percent of the incumbent's customer locations in the MSA. As we explain above, a competitor provides service over its own facilities if it leases unbundled loops but provides its own switching and transport. A competitor is not, however, offering service over its own facilities to the extent it offers service through resale or exclusively through the use of unbundled network elements. We acknowledge that we have concluded, both for determining eligibility for universal service support under section 254(e) of the Act and for BOC applications under section 271 to provide in-region interLATA services, that a carrier's "own" facilities include UNEs provided by the incumbent LEC.³⁰⁶ For purposes of this Order, however, we use "own facilities" in a narrower sense, excluding UNEs provided by the incumbent LEC, except in the case of CLECs using unbundled loops in conjunction with their own switching and transport facilities.

114. We also decline at this time to permit incumbents to satisfy the Phase I trigger by showing that customer locations are served by mobile wireless competitors. Although Congress allowed the Commission to consider competition from Personal Communications Service (PCS) in the context of Bell Operating Company (BOC) applications for in-region interLATA authority

³⁰³ See *id.* See also Deployment of Wireline Services Offering Advanced Telecommunications Capability, CC Docket No. 98-147, First Report and Order and Further Notice of Proposed Rulemaking, 14 FCC Rcd 4761, 4771-93 (1999).

³⁰⁴ See, e.g., *Second BellSouth Louisiana Order*, 13 FCC Rcd at 20652-706.

³⁰⁵ INDUSTRY ANALYSIS DIVISION, COMMON CARRIER BUREAU, FCC, LOCAL COMPETITION, at Tables 3.4, 3.5 (1998) (Table 3.4 presents lines provided by large incumbent LECs to CLECs for resale, Table 3.5 presents lines provided by large incumbent LECs to CLECs as UNE loops).

³⁰⁶ See Federal-State Joint Board on Universal Service, Report and Order, 12 FCC Rcd 8776, 8862 (1997) (*Universal Service Order*); *Ameritech Michigan Order*, 12 FCC Rcd at 20598.

when PCS serves as a substitute for the BOC's services,³⁰⁷ inclusion and evaluation of such data is problematic for purposes of determining whether an incumbent LEC is entitled to Phase I pricing flexibility, primarily because it is difficult to assess whether mobile (as opposed to fixed) wireless serves as a substitute for (and thus competes with) wireline service provided by an incumbent LEC.³⁰⁸

115. In arriving at the 15 percent trigger, we note that the relief granted upon satisfaction of the Phase I trigger for common line and traffic-sensitive services, together with the relief we grant immediately in Sections III and V above, is comparable to much of the switched services relief proposed in *ex parte* submissions by Bell Atlantic,³⁰⁹ Ameritech,³¹⁰ and USTA.³¹¹

116. Bell Atlantic recommends granting relief when competitors have "demonstrated the capability" to provide service in wire centers representing, in aggregate, at least 25 percent of the demand for the service in question, *i.e.*, residential/single-line-business and multi-line business.³¹² Under Bell Atlantic's proposal, competitors have demonstrated the ability to provide service in a wire center if they provided service with their own or ported telephone numbers to any of the relevant class of customers.³¹³ Ameritech proposes granting relief when competitors have

³⁰⁷ See 47 U.S.C. § 271(c)(1)(A); *Second BellSouth Louisiana Order*, 13 FCC Rcd at 20621-25.

³⁰⁸ *Second BellSouth Louisiana Order*, 13 FCC Rcd at 20625-30.

³⁰⁹ Bell Atlantic *ex parte* statement of April 27, 1998. Bell Atlantic proposes that, upon a showing that 25 percent of wire centers are "competitive" (based on the existence of any competitor-served telephone number in the wire center), we allow incumbent LECs to deaverage common line and local switching charges; offer volume and term pricing with growth options; offer promotions; and seek approval on an expedited basis to respond to requests for proposals (RFPs). *Id.* at 27. (Bell Atlantic proposes that we grant incumbent LECs some of this relief, such as geographic deaveraging, on a lesser showing).

³¹⁰ Ameritech *ex parte* statement of June 5, 1998, at 2. Ameritech proposes that, upon a showing that competitors have collocated in incumbent LEC wire centers accounting for 25 percent of interstate local switching minutes-of-use, we allow incumbent LECs to deaverage common line and local switching charges; offer bundled service packaging, contracts, and volume and term pricing (with growth options); and provide new services on a relaxed basis. *Id.* at 2. (Ameritech proposes that we grant incumbent LECs some of this relief, such as geographic deaveraging, on a lesser showing).

³¹¹ USTA *ex parte* statement of June 1, 1999. USTA proposes that, upon a showing that 25 percent of total lines in a market have "access to" alternative facility-based local services (*i.e.*, all lines served by a wire center with operational collocation and lines located within a 1000 feet of another provider's facility), we allow incumbent LECs to deaverage subscriber line charges (SLCs) and local switching charges; offer volume and term pricing; offer contracts and promotions; and seek approval on an expedited basis to respond to RFPs. *Id.* at 1. (USTA proposes that we grant incumbent LECs some of this relief, such as geographic deaveraging, on a lesser showing).

³¹² Bell Atlantic *ex parte* statement of April 27, 1998, at 27.

³¹³ *Id.* Bell Atlantic proposes that a wire center also be classified as "competitive" if competitors use collocation and UNEs to provide service in the wire center. *Id.* Because UNE customers would be served through

collocated in wire centers serving 25 percent of the demand in a market area, measured on an interstate minutes-of-use basis.³¹⁴ USTA also proposes a 25 percent threshold, but bases it on the sum of line demand attributable to (1) wire centers in which there is operational collocation *and* competitors are taking unbundled loop or unbundled local switching UNEs and (2) lines located within 1000 feet of competitive facilities.³¹⁵

117. For the reasons we discuss above, we find that a competitor has not made irreversible investment in facilities to provide common line and/or traffic-sensitive services unless it does so through its own facilities. We therefore reject the triggers proposed by the incumbent LECs and USTA to the extent they can be satisfied by UNE platform and resale competition.³¹⁶ Given, however, that we require evidence that competitors offer service over their own facilities, and that we do not grant relief as extensive as that sought by the incumbent LECs, we adopt a trigger lower than the 25 percent threshold they propose. We will therefore grant an incumbent LEC Phase I relief for common line and traffic-sensitive services when it demonstrates that competitors, in aggregate, offer service over their own facilities to at least 15 percent of incumbent LEC customer locations in the MSA. Because competitive provision of both local switching and traffic-sensitive components of tandem switched transport service are dependent on switch ownership, we conclude that Phase I relief for these services should be tied directly to the Phase I relief for common line services.

118. We reject Bell Atlantic and USTA's proposals that we allow incumbent LECs to qualify for pricing flexibility by class-of-service, *e.g.*, for residential/single-line-business and multi-line business service,³¹⁷ because we wish to encourage competition for both high-volume business customers and residential and low-volume business customers.

119. We acknowledge that demonstrating the degree to which competitors are providing service over their own facilities is more administratively burdensome than merely measuring the extent to which competitors have collocated in incumbent LEC wire centers.³¹⁸ As discussed

CLEC-ported or "owned" telephone numbers, this test appears to be merely a subset of the telephone number test.

³¹⁴ Ameritech *ex parte* statement of June 5, 1998, at 2.

³¹⁵ USTA *ex parte* statement of June 1, 1999, at 2.

³¹⁶ Customers served via resale or the UNE platform may represent significant numbers of "owned" or "ported" telephone numbers. Similarly, evidence of competitors using unbundled local switching UNEs does not, by itself, indicate competitors' investment in facilities.

³¹⁷ Like Bell Atlantic, USTA proposes that incumbent LECs may target showings to, and therefore request relief for, residential/single-line-business or multi-line business services. USTA *ex parte* statement of June 1, 1999. USTA notes that when an incumbent LEC makes a separate showing for residential/single-line-business services, it may be appropriate to use a total bypass threshold less than 1000 feet. *Id.*

³¹⁸ See Section VI.C.2.a, *supra*.

above, however, total bypass may represent a significant portion of competition for switched access services,³¹⁹ thus we will not rely solely on collocation as a measure of competition for these services. We therefore conclude that any increased administrative burdens in measuring total facilities bypass competition are in the public interest.

120. We emphasize that incumbent LECs must demonstrate that competitors actually offer, not merely are capable of offering, common line and traffic-sensitive services to 15 percent of an incumbent LEC's customer locations within an MSA to qualify for Phase I relief. On the other hand, we are not requiring that competitors actually provide service to a specific percentage of customers. "Offering service" is an appropriate measure of competitive entry for these services because of the difficulties inherent in determining the extent to which competitors actually provide service to current or former customers of the incumbent. This constitutes sensitive competitive information that the incumbent may be unable, and a competitor unwilling, to provide. Moreover, we see no need to require this information. In contrast to special access or even dedicated transport services, competitors are likely to employ more broadly based entry strategies for common line and traffic-sensitive services. Once a competitor installs a switch in its network, it has every incentive to maximize the number of customers it serves with that switch, in order to spread the sunk switch investment over the broadest base possible. In addition, special access services may have diminished the demand among high volume users for competitive switched services, because high volume customers use special access as an alternative to switched access, an option that is not available to low volume users of switched services. Thus switched-based competitors may be more likely to seek customers through mass marketing than through highly-targeted sales.

121. We do not establish rules pertaining to how an incumbent LEC might demonstrate that competitors "offer service" over their own facilities. As we note above, competitors are likely to market switched services broadly, thus we expect that competitors will advertise their services in a variety of media. These advertisements may well be probative of the extent of competitive offerings. Furthermore, incumbents are aware, of course, of competitors' purchase of unbundled loops, and the pending forbearance petitions suggest that they possess considerable intelligence regarding the extent and location of competitive facilities.

³¹⁹ In establishing our Phase I trigger for dedicated transport and special access services, based on our experience observing the development of the market for these services, we find it reasonable to use collocation as a proxy for all forms of competition in the market for such services. As discussed, *supra*, however, we do not have such a history to evaluate in the switched access market and therefore are not as able to predict the relationship between collocation and total-facilities bypass-based entry in the switched access market.

4. Phase I Relief

a. Introduction

122. Upon satisfaction of the Phase I triggers for particular services, we will permit price cap LECs to file, on one day's notice, tariffs offering volume and term discounts for those services, and we also will permit them to file contract tariffs for those services on one day's notice. Price cap LECs must remove their contract tariff offerings from price cap regulation.³²⁰ Currently, an incumbent LEC is free to lower its access rates as much as it wants,³²¹ provided that it lowers its rates throughout the study area or density pricing zone in question.³²² Under our Phase I regulatory relief, incumbent LECs are no longer required to choose between lowering a rate throughout the area at issue or not lowering the rate at all. Price cap LECs are required to maintain generally available tariffs subject to price cap regulation for all access services, however, so that access customers can choose between obtaining services pursuant to contract tariff or generally available tariff. This ensures that no access customer will be required to pay dramatically higher access rates as a result of Phase I pricing flexibility. In this section, we explain why we conclude that these two forms of relief are warranted in Phase I.

b. Volume and Term Discounts

123. *Background.* Price cap LECs currently may offer volume and term discounts for special access services without any competitive showing.³²³ The Commission also permits incumbent LECs to offer cost-based volume and term discounts for several switched transport services³²⁴ when competitors have purchased either (1) 100 DS1-equivalent switched transport cross-connects in the incumbent LEC's "zone 1" wire centers, or (2) an average of 25 DS1-equivalent switched transport cross-connects per zone 1 wire center.³²⁵ By "cost-based"

³²⁰ Ad Hoc supports removing services offered under contract tariffs from price cap regulation. Ad Hoc Reply to U S West Phoenix Forbearance Petition, CC Docket No. 98-157, at 15-16. We address below the low-end adjustment issues raised by the removal of contract-tariff offerings from price cap regulation.

³²¹ In the *Price Cap Third Report and Order*, the Commission eliminated the lower service band indices. *Price Cap Third Report and Order*, 11 FCC Rcd at 21487-88.

³²² Section 69.3(e)(7) requires all incumbent LECs to charge uniform rates throughout each study area. See 47 C.F.R. § 69.3(e)(7). The Commission permitted incumbent LECs offering expanded interconnection to deaverage their special access and switched transport rates into three density pricing zones once demand for collocation services reached certain thresholds. *Special Access Expanded Interconnection Order*, 7 FCC Rcd at 7454; *Switched Transport Expanded Interconnection Order*, 8 FCC Rcd at 7426-27; *Virtual Collocation Order*, 9 FCC Rcd at 5196-97; 47 C.F.R. §§ 61.47(e), 69.123. We relax these rules in Section III above, however.

³²³ See *Special Access Expanded Interconnection Order*, 7 FCC Rcd at 7458-65.

³²⁴ These switched transport services are entrance facilities, interoffice mileage, and tandem-switched transport. *Switched Transport Expanded Interconnection Order*, 8 FCC Rcd at 7433-34.

³²⁵ *Switched Transport Expanded Interconnection Order*, 8 FCC Rcd at 7434-36. In the *Special Access Expanded Interconnection Order*, the Commission allowed incumbent LECs with operational expanded interconnection offerings to implement a system of traffic-density-related rate zones, to bring special access rates more in line with costs. *Special Access Expanded Interconnection Order*, 7 FCC Rcd at 7454. The Commission

discounts, the Commission meant that the discounts should be based on per-unit of capacity differences in embedded costs incurred to provide high-volume service relative to the costs of non-high-volume offerings.³²⁶ In the *Access Reform NPRM*, the Commission invited comment on expanding volume and term discount authority upon satisfaction of Phase I triggers.³²⁷

124. *Discussion.* Upon satisfaction of the Phase I triggers, we find that price cap LECs should be permitted to offer volume and term discounts to enable them to respond to competition.³²⁸ Prohibiting incumbent LECs from offering volume and term discounts when they have satisfied the Phase I triggers could distort the market for access services by preventing incumbent LECs from competing efficiently. In addition, permitting volume and term discounts creates little headroom that an incumbent could use to increase rates for other access services. For several years, the Commission has allowed volume and term discounts for certain access services in the trunking and traffic-sensitive baskets.³²⁹ There is nothing in the record before us to suggest either that the headroom resulting from those discounts has led to unreasonable rate increases for other access services in those baskets, or that headroom resulting from expanded volume and term discount authority will lead to unreasonable rate increases for other access services in those baskets in the future. Unlike contract tariffs, moreover, volume and term discounts are not tailored to individual customers, and incumbent LECs must make them available to any customer with sufficient volumes or willing to commit to a given term.³³⁰

125. Several parties do not oppose volume and term discounts in their entirety, but rather oppose allowing volume and term discounts under conditions that might enable incumbent LECs

later expanded density zone pricing to switched transport. See *Switched Transport Expanded Interconnection Order*, 8 FCC Rcd at 7426-27; *Virtual Collocation Order*, 9 FCC Rcd at 5196-97. For purposes of this Order, we use "zone 1" to refer to the zone with the heaviest traffic density.

³²⁶ See *Special Access Expanded Interconnection Order*, 7 FCC Rcd at 7463; *Switched Transport Expanded Interconnection Order*, 8 FCC Rcd at 7433.

³²⁷ *Access Reform NPRM*, 11 FCC Rcd at 21435-38.

³²⁸ See USTA Comments at 28, 49, and Att. 1 at 30-31; USTA Reply at 26-27; Citizens Comments at 17-18; PacTel Comments at 26; U S West Comments at 32-33; Ameritech Comments at 41 and Att. B at 36; BA/NYNEX Comments at 49; BA/NYNEX Reply at 23-24; BellSouth Comments at 33-34; Cincinnati Bell Comments at 18; GTE Comments at 48; SNET Comments at 18; SNET Reply at 14-15. This authority to offer volume and term discounts upon satisfaction of the Phase I triggers is in addition to the existing authority price cap LECs have to offer volume and term discounts.

³²⁹ See *Special Access Expanded Interconnection Order*, 7 FCC Rcd at 7458-65; *Switched Transport Expanded Interconnection Order*, 8 FCC Rcd at 7433-34.

³³⁰ Volume and term discounts for services in the common line basket raise issues that are not presented by volume and term discounts for services in the traffic-sensitive and trunking baskets. We address common line issues further in Section VI.D.3 of this Order, *infra*.

to lock in customers or discriminate in favor of incumbents' long distance affiliates.³³¹ The Phase I triggers we adopt above condition incumbent LEC volume and term discounts upon irreversible, sunk investment by competitors, thus making it less likely that an incumbent will try to use volume and term discounts to lock in customers. In addition, section 202 of the Act³³² and our existing enforcement procedures are adequate to address unreasonable discrimination.³³³

126. According to MCI, the Commission proposed permitting volume discounts to facilitate the development of rate structures that reflect the manner in which costs are incurred. MCI argues further that the *Access Reform First Report and Order* eliminated inefficiencies in the common line and local switching rate structures, and so volume discounts are no longer warranted for these services.³³⁴ Contrary to these arguments, however, the Commission proposed relaxing volume and term discount requirements not only to encourage incumbent LECs to develop efficient rate structures, but also to avoid distorting the market or impeding the development of effective competition.³³⁵ Therefore, the rate structure revisions adopted in the *Access Reform First Report and Order* do not obviate the need for relaxing volume discount requirements.

127. The Illinois Commission supports permitting incumbent LECs to offer volume and term discounts, but it recommends setting a price floor at total service long incremental cost (TSLRIC), or some other measure of forward-looking economic costs, below which such discounts would not be permitted because they could be anticompetitive.³³⁶ Historically, the Commission has required incumbent LECs to develop rate structures that reflect the manner in which they incur costs.³³⁷ Rate structures that are not cost-based tend to result in implicit subsidies between high-volume and low-volume users.³³⁸ We find that this concern is reduced, however, when the incumbent has met the Phase I trigger, because the existence of sunk investment by competitors limits the incentive to engage in anticompetitive pricing behavior. Furthermore, we will consider complaints filed under section 208 of the Act alleging that a rate charged pursuant to a volume discount is unreasonably low, in violation of section 201 of the

³³¹ AT&T Comments at 80-81; MCI Comments at 58-59; Sprint Comments at 43-45; ACTA Comments at 18.

³³² 47 U.S.C. § 202.

³³³ We address concerns regarding growth discounts below.

³³⁴ MCI Nov. 9 Reply at 34-35 (citing *Access Reform First Report and Order*, 11 FCC Rcd at 21437).

³³⁵ *Access Reform First Report and Order*, 11 FCC Rcd at 21437.

³³⁶ Illinois Commission Comments at 21.

³³⁷ Investigation of Interstate Access Tariff Non-Recurring Charges, CC Docket No. 85-166, Phase I, Part 3, 2 FCC Rcd 3498, 3501-02 (1987).

³³⁸ *Access Reform First Report and Order*, 12 FCC Rcd at 15998.

Act.³³⁹ Moreover, any volume or term discount that results in a below-cost offering would give rise to an antitrust claim,³⁴⁰ which provides further protection to competitors. As a result, we conclude that the benefits of permitting volume and term discounts without requiring a cost showing outweigh any possible costs. We will not require that LECs demonstrate that the volume and term discounts they may offer at Phase I are cost-based.

c. Contract Tariffs

128. Upon satisfaction of the Phase I triggers, we will permit price cap incumbent LECs to offer interstate access services pursuant to contract tariff. Access customers benefit from contract tariffs because they enable incumbent LECs to tailor services to their customers' individual needs. Incumbent LECs argue that they should be permitted to offer access services on a contract carriage basis, in part because these arrangements are common elsewhere in telecommunications and other industries.³⁴¹ We agree that, once competitors have made irreversible, sunk investments in their networks, continuing to prohibit incumbent LECs from offering services under contract tariff could reduce the efficiency of the market for access services by reducing the incumbent LECs' ability to meet customers' needs.

129. AT&T, Frontier, and MCI submit that incumbent LECs will be able to tailor contract carriage tariffs to such a point that additional customers are unlikely to select the tariff, leaving the incumbent LECs free to discriminate in favor of their affiliates.³⁴² Although any unreasonable restriction on the availability of contract tariff services would violate Section 202 of the Act,³⁴³ and any party that believes that it may be disadvantaged by an allegedly discriminatory contract tariff offering may file a complaint under section 208 of the Act,³⁴⁴ we agree that special safeguards are warranted with respect to contracts with affiliates. Permitting incumbent LECs to file contract tariffs on one day's notice provides little opportunity for the Commission or competing carriers to review the terms of the tariffs before they take effect. Issues regarding whether a particular tariff condition is unreasonably discriminatory and whether another carrier is in fact "similarly situated" may prove difficult to determine in a subsequent complaint proceeding,

³³⁹ See 47 U.S.C. §§ 201, 208.

³⁴⁰ See 15 U.S.C. § 2; *In re Air Passenger Computer Reservation Systems Antitrust Litigation*, 694 F. Supp. 1443 (C.D. Cal. 1988), *aff'd*, 948 F.2d 536 (9th Cir. 1991).

³⁴¹ USTA Comments at 49; BA/NYNEX Comments at 51; BellSouth Comments at 35-36; Ameritech Reply at 12-13; GTE Reply, App. D at 13.

³⁴² AT&T Comments at 44-45; AT&T Reply at 45; Frontier Comments at 15; MCI Comments at 62. See also ACTA Comments at 18.

³⁴³ 47 U.S.C. § 202.

³⁴⁴ 47 U.S.C. § 208.

which, in any event, takes time to resolve. We adopt, instead, a bright-line rule to address concerns about discrimination in favor of affiliates. We will not permit an incumbent LEC to offer a contract tariff to an affiliate unless and until an unaffiliated customer first purchases service pursuant to that contract.³⁴⁵

130. MCI contends that, if price cap LECs are permitted to offer contract tariffs before there is substantial competition in the market, those LECs will deter market entry through targeted rate reductions.³⁴⁶ We adopt Phase I triggers to ensure that incumbent LECs cannot drive competitors from the market through targeted rate reductions; these safeguards are adequate to address MCI's concern. Moreover, to the extent that an incumbent LEC attempts to use contract tariffs in an exclusionary manner by targeting them to specific customers, the Commission will enforce the requirement that they make contract tariffs available to all similarly situated customers.³⁴⁷

131. Intermedia argues that granting incumbent LECs contract tariff authority will result in a price squeeze with respect to facilities-based CLECs that purchase UNEs, because the Commission has adopted average variable cost as a price floor for incumbent LEC wholesale and retail rates.³⁴⁸ According to Intermedia, CLECs providing service through the use of unbundled network elements are unable to compete with incumbent LEC services priced at average variable cost, because the Commission's pricing methodology for UNEs, Total Element Long Run Incremental Cost (TELRIC), includes costs, including joint and common costs, depreciation, and a reasonable profit,³⁴⁹ that are excluded from the calculation of average variable cost.³⁵⁰ Intermedia proposes that the Commission address this price squeeze by requiring resale, at a wholesale discount, of all incumbent LEC contract tariff offerings and volume and term discounts.³⁵¹ Intermedia's concerns about potential a potential price squeeze are best addressed in the context of a complaint filed under section 208 of the Act alleging that a rate charged pursuant to a contract tariff or volume or term discount is unreasonably low and thus violates section

³⁴⁵ Once the Commission grants BOCs permission, pursuant to section 271 of the Act, 47 U.S.C. § 271, to provide in-region long distance services, they are required to offer those services through separate affiliates. *See* 47 U.S.C. § 272. Similarly, the Commission's rules require incumbent independent (non-BOC) LECs to offer in-region long distance services through separate affiliates. *See* 47 C.F.R. § 64.1903.

³⁴⁶ MCI Oct. 26 Comments at 61-62. *See also* Time Warner Oct. 26 Comments at 14-16.

³⁴⁷ *See Interexchange Competition Order*, 6 FCC Rcd at 5897.

³⁴⁸ Intermedia *ex parte* statement of July 14, 1999, at 2.

³⁴⁹ *See Local Competition Order*, 11 FCC Rcd at 15850-56.

³⁵⁰ Intermedia *ex parte* statement of July 14, 1999, at 2.

³⁵¹ *Id.* at 4-5.

201.³⁵² We note in this regard that such a complaint is not subject to dismissal merely because a given rate is at or above average variable cost; average variable cost is not necessarily a "reasonable" rate.

132. MCI and Time Warner argue that AT&T was permitted to offer contract tariff service only when the Commission found that AT&T faced "substantial competition," and that allowing incumbent LECs to offer contract carriage on a lesser showing is inconsistent with that precedent.³⁵³ We find that the precedent cited by MCI and Time Warner is not entirely on point, because, in contrast to the relief granted to AT&T, Phase I relief does not permit price cap LECs to provide services completely outside of price cap regulation.³⁵⁴ Rather, price cap LECs will be required to maintain generally tariffed access service offerings subject to price cap regulation. Because we are granting incumbent LECs much less pricing flexibility at Phase I than the Commission granted AT&T pursuant to the *Interexchange Competition Order*, we do not require price cap LECs to show that they face substantial competition.

133. Ameritech and Bell Atlantic also seek permission to respond to requests for proposals (RFPs).³⁵⁵ We find that the contract tariff authority we grant here is sufficient to enable price cap LECs to respond to RFPs, and so we need not grant any further pricing flexibility for this purpose. ALTS maintains that granting flexibility to respond to RFPs is inconsistent with a previous Commission Order terminating an investigation, in which the Commission concluded that a Southwestern Bell tariff revision designed to respond to RFPs was unreasonably discriminatory.³⁵⁶ ALTS's concern is unfounded. First, Southwestern Bell sought to respond to any RFP that indicated that the request involved a competitive situation.³⁵⁷ Unlike the Phase I triggers we adopt in this Order, Southwestern Bell's tariff did not in any way indicate whether its competitors had made irreversible investment in facilities. Second, the Commission's decision rested in part on Southwestern Bell's failure to submit adequate evidence of competition in its region at that time.³⁵⁸ The Commission did not decide, as ALTS seems to imply, that any RFP

³⁵² See 47 U.S.C. §§ 201, 208.

³⁵³ MCI Comments at 60-61; Time Warner Comments at 31-33; MCI Nov. 9 Reply at 41 (citing *Interexchange Competition Order*, 6 FCC Rcd 5880).

³⁵⁴ See *Interexchange Competition Order*, 6 FCC Rcd at 5894.

³⁵⁵ Bell Atlantic *ex parte* statement of April 27, 1998, at 22; Ameritech *ex parte* statement of June 5, 1998, at 3.

³⁵⁶ ALTS *ex parte* statement of June 25, 1999, at 25 (quoting Southwestern Bell Telephone Company, CC Docket No. 97-158, Order Concluding Investigation and Denying Application for Review, 12 FCC Rcd 19311, 19336 (1997) (*Southwestern Bell Transmittal 2633 Order*)).

³⁵⁷ See *Southwestern Bell Transmittal 2633 Order*, 12 FCC Rcd at 19317.

³⁵⁸ *Id.* at 19334-35.

authority is inherently unreasonable. Finally, the Commission noted the pendency of this rulemaking proceeding, and that the record in this proceeding might provide a basis for permitting contract tariffs or competitive response tariffs.³⁵⁹ Thus, rather than precluding consideration of this RFP issue, the *Southwestern Bell Transmittal 2633 Order* expressly contemplated addressing that issue in this Order.

d. Growth Discount

134. We reject Ameritech's and Bell Atlantic's proposal to allow incumbent LECs to offer growth discounts.³⁶⁰ Growth discounts refer to pricing plans under which incumbent LECs offer reduced per-unit access service prices to customers that commit to purchase a certain percentage above their past usage, or plans that offer reduced prices based on growth in traffic placed over an incumbent LEC's network.³⁶¹ The Commission tentatively decided not to permit growth discounts in the *Access Reform NPRM*, because they create an artificial advantage for BOC long distance affiliates with no subscribers, relative to existing IXCs and other new entrants.³⁶² The Commission also invited parties to comment on whether growth discounts would enhance the development of competitive access markets.³⁶³

135. None of the parties supporting growth discounts explains why growth discounts enhance the development of competitive access markets. Instead, Ameritech asserts that the Commission could rely on the tariff review process to ensure that any growth discounts do not unreasonably advantage the incumbent LEC's long distance affiliate.³⁶⁴ Without any affirmative benefit to growth discounts presented in the record before us, we have no basis for allowing such discounts.

e. X-Factor Reductions

136. Ameritech, Bell Atlantic, and USTA recommend reducing or eliminating the X-Factor in the price cap index (PCI) formula as competition grows.³⁶⁵ This regulatory relief is

³⁵⁹ *Id.* at 19339.

³⁶⁰ Bell Atlantic *ex parte* statement of April 27, 1998, at 21, 29; Ameritech Oct. 26 Comments, Att. N at 9-10.

³⁶¹ *Access Reform NPRM*, 11 FCC Rcd at 21437.

³⁶² *Id.* at 21437-38.

³⁶³ *Id.* at 21438.

³⁶⁴ Ameritech Oct. 26 Comments, Att. N at 9-10.

³⁶⁵ Ameritech *ex parte* statement of June 5, 1998, at 3; Bell Atlantic *ex parte* statement of April 27, 1998, at 10; USTA Oct. 26 Comments at 37 and Att. E; *see also* SBC Oct. 26 Comments at 20. In price cap regulation, the "X-Factor" limits access rate increases. Access services are grouped into "baskets," and the weighted average of

not warranted. Phase I pricing flexibility is designed to grant incumbent LECs more flexibility to lower prices for particular customers without subjecting other customers to higher rates. Because competition may not be sufficient to constrain prices throughout an MSA at Phase I, we require LECs to maintain their generally available tariffs in order to protect access customers. If we were to lower the X-Factor as competition increases, then the price cap-constrained tariffs might not be adequate to protect access customers from rate increases.

137. Ameritech maintains that the X-Factor should be eliminated in its proposed "Phase II," which is roughly analogous to our Phase I, because competitive pressures will constrain the incumbent LEC's ability to earn excessive profits.³⁶⁶ We find this reasoning unpersuasive, because the services for which the incumbent feels competitive pressure are the ones most likely to be offered under contract tariff, outside of price cap regulation. Therefore, the services that remain subject to price cap regulation are likely to be those for which the incumbent faces less competition.

138. Moreover, the Commission designed price cap regulation in part to replicate, to the extent possible, the results of a competitive market.³⁶⁷ Generally, as more competitors enter a market, supply increases, and this additional supply puts downward pressure on prices. Conversely, lowering the X-Factor decreases downward pressure on prices. Thus, lowering the X-Factor as competition increases would produce exactly the opposite result of a competitive market, thereby undercutting one of the Commission's goals in adopting price cap regulation.

f. Other Price Cap Revisions

139. We reject the proposal by several LECs to consolidate the existing price cap baskets into one basket.³⁶⁸ Ameritech states that this restructuring would permit incumbent LECs to raise prices for some services to offset reductions in prices for other services.³⁶⁹ Nothing in the record suggests that the customers facing increased prices under this kind of pricing flexibility are likely to have many competitive alternatives relative to customers that benefit from price reductions. Thus, consolidating price cap baskets would deprive access customers of protection that remains necessary at Phase I.

the rates in each basket may not exceed the price cap index (PCI). The PCI is adjusted annually by a measure of inflation minus the X-Factor. *See Price Cap Fourth Report and Order*, 12 FCC Rcd at 16647-48.

³⁶⁶ Ameritech Oct. 26 Comments, Att. N at 9-10.

³⁶⁷ *LEC Price Cap Performance Review*, 10 FCC Rcd at 9002.

³⁶⁸ Ameritech Oct. 26 Comments, Att. N at 9-10; USTA Oct. 26 Comments at 37, Att. E; SBC Oct. 26 Comments at 20.

³⁶⁹ Ameritech Oct. 26 Comments, Att. N at 9-10.

140. For similar reasons, we also decline to adopt Bell Atlantic's suggestion that we increase upper service band index (SBI) limits to 10 percent per year for transport services upon satisfaction of its proposed "Phase II" triggers, which are similar to the Commission's Phase I triggers.³⁷⁰ Increasing the upper SBI limits upon satisfaction of our Phase I triggers could enable the incumbent LEC to increase a customer's access rates before that customer has a competitive alternative.³⁷¹

5. Phase II for Special Access and Dedicated Transport

a. Introduction

141. We adopt Phase II triggers comparable to our Phase I triggers: we will grant Phase II pricing flexibility to incumbent LECs when competitors have collocated in a certain percentage of the incumbent's wire centers in an MSA, or in wire centers generating a certain percentage of an incumbent's revenues for the services at issue within the MSA. Because Phase II grants incumbent LECs considerably greater flexibility than Phase I, we adopt triggers to ensure that competitors have established a significant market presence, *i.e.*, that competition for a particular service within the MSA is sufficient to preclude the incumbent from exploiting any monopoly power over a sustained period.³⁷² Upon a Phase II showing for special access and dedicated transport services within an MSA, we will relax the price cap rules and the Part 69 rate structure requirements applicable to those services in that MSA.³⁷³

142. By significant market presence, we mean that IXCs have a competitive alternative for dedicated transport services needed to reach the majority, although not necessarily all, of their long distance customers throughout the MSA, and that almost all special access customers have a competitive alternative. We find that Phase II regulatory relief is warranted upon satisfaction of the Phase II triggers within an MSA, even though such relief might lead to higher rates for access to some parts of an MSA that lack a competitive alternative, for several reasons. First, the customers for the services we address in this section are IXCs and large businesses, not residential or small business end users. These large and sophisticated customers generate significant revenues for the incumbent and are not without bargaining power with respect to the incumbent.

143. Second, delaying Phase II regulatory relief until access customers have a competitive alternative for access to each and every end user might give competitors the ability to "game the

³⁷⁰ Bell Atlantic *ex parte* statement of April 27, 1998, at 21.

³⁷¹ See Ad Hoc Oct. 26 Comments at 30.

³⁷² As we explain further in this Order below, determining that an incumbent LEC cannot exploit monopoly power over a sustained period is not equivalent to finding that carrier to be non-dominant. See Section VI.C.4.b, *infra*.

³⁷³ Part 69 does not prescribe a rate structure for special access services.

system." In other words, competitors might be able to prevent an incumbent from obtaining pricing flexibility in an MSA simply by choosing not to enter certain parts of that MSA or to serve certain customers. We will not distort the operation of the market in this manner.

144. Finally, because regulation is not an exact science,³⁷⁴ we cannot time the grant of regulatory relief to coincide precisely with the advent of competitive alternatives for access to each individual end user. We conclude that the costs of delaying regulatory relief outweigh the potential costs of granting it before IXCs have a competitive alternative for each and every end user. The Commission has determined on several occasions that retaining regulations longer than necessary is contrary to the public interest. Almost 20 years ago, the Commission determined that regulation imposes costs on common carriers and the public, and that a regulation should be eliminated when its costs outweigh its benefits.³⁷⁵ More recently, the Commission recognized that retaining tariffing requirements for non-dominant IXCs imposes costs in the form of a less efficient market.³⁷⁶ In Section III of this Order, we conclude that the new service rules currently in effect limit incumbents' incentives to innovate. The Part 69 rate structure can impose costs on an incumbent LEC by limiting its ability to develop rate structures in response to market forces. Thus, retaining the Part 69 rate structure imposes costs on society by perpetuating inefficiencies in the market for interstate access services. The triggers we adopt for Phase II flexibility are sufficient to ensure that incumbent LECs cannot exercise any remaining monopoly power indefinitely. If an incumbent LEC charges an unreasonably high rate for access to an area that lacks a competitive alternative, that rate will induce competitive entry, and that entry will in turn drive rates down. Accordingly, we will not delay Phase II regulatory relief until access customers have a competitive alternative for access to every end user.

145. As we did in Phase I, we establish different triggers for (1) special access services (other than channel terminations) and dedicated transport services, and (2) channel terminations. In this section of the Order, we adopt triggers for each of these services and adopt specific forms of regulatory relief for Phase II. In the Notice accompanying this Order, we invite interested parties to comment on Phase II triggers for other switched access services.

³⁷⁴ *United States v. FCC*, 707 F.2d at 618.

³⁷⁵ Policy and Rules Concerning Rates for Competitive Common Carrier Services and Facilities Authorizations Therefor, CC Docket No. 79-252, First Report and Order, 85 FCC 2d 1, 3 (1980) (*Competitive Carrier First Report and Order*). The Court later overturned this Order, but only because the Commission did not have authority under the Communications Act at that time to forbear from regulation, not because it erred in determining that the costs of regulation can outweigh its benefits. *See MCI v. FCC*, 765 F.2d 1186, 1195-96 (D.C. Cir. 1985); *AT&T v. FCC*, 978 F.2d 727, 736 (D.C. Cir. 1992).

³⁷⁶ Policy and Rules Concerning the Interstate, Interexchange Marketplace, CC Docket No. 96-61, Second Report and Order, 11 FCC Rcd 20730, 20762-63 (1996).

b. Phase II Triggers

146. We note above that the regulatory relief proposed by Ameritech and Bell Atlantic for "Phase II" is analogous to our Phase I relief. Here, we find that Ameritech's and Bell Atlantic's Phase III proposals are analogous to the Phase II relief we adopt here.³⁷⁷ Therefore, we rely in part on the record developed in response to Bell Atlantic's and Ameritech's proposals in developing our Phase II triggers. Bell Atlantic proposes granting relief when competitors have collocated facilities, purchased UNEs, or installed their own facilities in 75 percent of the wire centers in the market area.³⁷⁸ Ameritech recommends granting relief when competitors have collocated in wire centers serving 75 percent of the demand in a market area, measured on a DS1-equivalent basis.³⁷⁹

147. Access customers must have competitive alternatives throughout most of an MSA before we can grant Phase II regulatory relief to an incumbent LEC. The Ameritech and Bell Atlantic proposals recognize that our Phase II triggers must be high enough to ensure that competitive alternatives for the services at issue exist in the area for which flexibility is granted. The triggers we adopt, however, differ from those recommended by these incumbent LECs in two respects: as in Phase I, (1) we base our Phase II triggers on collocation in either a certain percentage of wire centers in an MSA, or in wire centers generating a certain percentage of the revenues for the services at issue in an MSA; and (2) we conclude that different services warrant different thresholds.

148. We determined in our Phase I analysis above that evidence of collocation may underestimate the extent of competitive facilities within a wire center, because it fails to account for the presence of competitors that have wholly bypassed incumbent LEC facilities. For this reason, we adopt a threshold lower than the 75 percent recommended by Ameritech and Bell Atlantic. For dedicated transport, and for special access services other than channel terminations, we grant Phase II pricing flexibility to incumbent LECs that demonstrate that competitors have collocated in 50 percent of an incumbent LEC's wire centers in the MSA at issue. SBC has

³⁷⁷ In addition to all the forms of regulatory relief we grant immediately in Sections III and V of this Order and that we will grant upon satisfaction of Phase I triggers, in Phase II, we will (1) relax our Part 69 rate structure rules, and (2) permit price cap LECs to offer access services completely outside of price cap regulation. Ameritech and Bell Atlantic recommend removing services from price cap regulation upon demonstration that an incumbent LEC has met their Phase III criteria. Ameritech *ex parte* statement of June 5, 1998, at 3; Bell Atlantic *ex parte* statement of April 27, 1998, at 22. USTA also recommends removing services from price caps upon its Phase III showing, and recommends eliminating Part 69 rate structure requirements upon a Phase I showing. USTA Oct. 26 Comments at Att. E.

³⁷⁸ Bell Atlantic *ex parte* statement of April 27, 1998, at 21.

³⁷⁹ Ameritech *ex parte* statement of June 5, 1998, at 2.

shown that competitors have collocated in 51 percent of its wire centers in the San Diego MSA.³⁸⁰ According to SBC, competitors' networks in this MSA comprise at least 1150 route miles, and there are more than 360 buildings on those networks.³⁸¹ Similarly, competitors have collocated in 58 percent of SBC's wire centers in the Los Angeles MSA.³⁸² SBC submits that competitors' networks in this MSA comprise more than 2530 route miles, and there are more than 950 buildings on those networks.³⁸³ We explain above that establishing an operational collocation arrangement requires considerable time and expense.³⁸⁴ This evidence suggests that collocation in 50 percent of an incumbent LEC's wire centers corresponds to considerable investment by competitors in transmission facilities and the ability of competitors to serve customers in a large number of buildings.

149. As we explain in our Phase I discussion, a few wire centers may account for a disproportionate share of revenues for a particular service. For this reason, we also will grant Phase II pricing flexibility for these services upon a demonstration that competitors have collocated in wire centers accounting for 65 percent of the incumbent LEC's revenues from those services in an MSA. Similarly, we will grant Phase II pricing flexibility for channel terminations between an IXC POP and a LEC serving wire center when an incumbent demonstrates that competitors have collocated in 50 percent of its wire centers in an MSA, or in wire centers accounting for 65 percent of the incumbent's revenue for this service. As we explained in our discussion of Phase I triggers above, these services carry traffic between points of high traffic concentration and therefore warrant lower triggers than those we adopt for channel terminations between a LEC end office and a customer premises.

150. We adopt higher thresholds for channel terminations between an incumbent LEC's end office and customer premises, for the reasons we offered in our Phase I analysis. For these channel terminations, Phase II relief is available to LECs that demonstrate that competitors have collocated in 65 percent of the incumbent LEC's wire centers in the MSA at issue, or in wire centers accounting for 85 percent of the incumbent's revenues from those services in that MSA. Because these services do not carry traffic between points of high traffic concentration, and because the collocated competitors still rely on incumbent LEC facilities to reach the end user, we find that higher thresholds are warranted.

³⁸⁰ SBC Reply in SBC Forbearance Proceeding, CC Docket No. 98-227, Att. 2.

³⁸¹ SBC Forbearance Petition, Att. A at 10.

³⁸² SBC Reply in SBC Forbearance Proceeding, CC Docket No. 98-227, Att. 2. For purposes of its forbearance petition, SBC treats the Long Beach and Orange County MSAs as one MSA.

³⁸³ SBC Forbearance Petition, Att. A at 10.

³⁸⁴ Section VI.C.2, *supra*.

151. MCI argues that price cap LECs should be permitted Phase II regulatory relief, such as removal of services from price cap regulation, only when those LECs are "non-dominant," *i.e.*, no longer have market power in the provision of the services at issue.³⁸⁵ We conclude that the Phase II regulatory relief we grant below is warranted when competitors have established a significant market presence in an MSA, and we need not require a showing of non-dominance. Upon a Phase II showing, we will not grant incumbent LECs all the regulatory relief we afford to non-dominant carriers. Specifically, incumbent LECs in Phase II are still required to file generally available tariffs, while non-dominant LECs and CAPs are permitted, but not required, to file tariffs.³⁸⁶ Furthermore, our relief is limited to certain services and certain areas, and will be granted only upon satisfaction of the triggers we adopt here. Thus, Phase II relief is not tantamount to non-dominant treatment.

152. In the *Interexchange Competition Order*, the Commission allowed AT&T to remove some interexchange services from price cap regulation based on a finding of "substantial competition," but it based that finding on a more detailed analysis than the Phase II triggers we adopt here, including an examination of, *inter alia*, demand and supply elasticities, pricing behavior, and market share.³⁸⁷ We conclude that this detailed substantial competition test is not warranted for special access and dedicated transport services because we grant incumbent LECs pricing flexibility only on a MSA-by-MSA basis, while the Commission granted AT&T pricing flexibility on a nationwide basis. Furthermore, the administrative burdens of a detailed substantial competition test are magnified when done on an MSA-by-MSA basis, and we believe our collocation-based triggers are sufficient to ensure that we do not grant pricing flexibility prematurely. Accordingly, we will rely on collocation-based triggers to indicate when competitors have established a significant market presence that warrants Phase II relief for special access and dedicated transport services.³⁸⁸

c. Phase II Relief

153. Upon satisfaction of the Phase II triggers we adopt above for special access and dedicated transport services, we will no longer require price cap LECs to comply with our Part 69 rate structure rules or Part 61 price cap rules with respect to those services within an MSA. An incumbent LEC should be permitted to remove services from price cap regulation when that LEC's competitors have established a significant market presence in the provision of those

³⁸⁵ MCI Oct. 26 Comments at 48.

³⁸⁶ See Hyperion Telecommunications, Inc. Petition Requesting Forbearance, Memorandum Opinion and Order and Notice of Proposed Rulemaking, 12 FCC Rcd 8596, 8611-12 (1997).

³⁸⁷ See *Interexchange Competition Order*, 6 FCC Rcd at 5887-93.

³⁸⁸ We seek comment on Phase II relief for common line and traffic-sensitive services in the accompanying Notice.

services.³⁸⁹ A significant market presence in an MSA ensures that the incumbent will not be able to exploit any monopoly power for a sustained period. We will, however, continue to require LECs to maintain generally available tariffs, but we will permit them to file such tariffs on one day's notice. In this section, we explain why we conclude that these two forms of relief are warranted upon satisfaction of the Phase II triggers.

154. Currently, Part 69 of the Commission's rules prescribes a rate structure for all switched access services, including dedicated transport. USTA recommends eliminating the Part 69 rate structure as a form of regulatory relief.³⁹⁰ In addition, in Section III above, we eliminate rate structure requirements for new services. We agree that elimination of our Part 69 rate structure rules for existing dedicated transport services is warranted, but not until the incumbent LEC meets our Phase II requirements. As explained in more detail in Section VIII.C. below, a rate structure can create implicit subsidies if it does not reflect accurately the manner in which incumbent LECs incur the costs of providing a service. Therefore, rate structure rules are necessary in the absence of a significant market presence by competitors. Once competitors have established a significant market presence in an MSA, however, we believe it is no longer necessary to impose efficient rate structures on incumbent LECs. Therefore, we will eliminate our rate structure rules for particular services once an incumbent LEC demonstrates the development of a significant market presence by competitors for those services by satisfying the Phase II trigger. Retaining our price cap and rate structure rules until LECs are non-dominant is unwarranted because doing so would delay the action of competition in setting efficient rate levels and rate structures.

155. We recognize that the regulatory relief we grant upon a Phase II showing may enable incumbent LECs to increase access rates for some customers. We conclude that this relief nonetheless is warranted upon a Phase II showing for two reasons. First, some access rate increases may be warranted, because our rules may have required incumbent LECs to price access services below cost in certain areas. Second, we find that a Phase II showing is sufficient evidence that competitors' market presences have become significant, and that the public interest is better served by permitting market forces to govern the rates for the access services at this point. In addition, we note that these services generally are purchased by IXC's, not individual end users. IXC's are sophisticated purchasers of telecommunications services, fully capable of finding competitive alternatives where they exist and determining which competitor can best meet their needs.

³⁸⁹ In the *LEC Price Cap Order*, the Commission explained that it is unnecessary to extend the efficiency incentives of price cap regulation to services offered on a "contract-type basis." *LEC Price Cap Order*, 5 FCC Rcd at 6810.

³⁹⁰ USTA Oct. 26 Comments, Att. E.

156. We decline to adopt any other Phase II regulatory relief proposed in the *Access Reform NPRM*. Two of those proposals, elimination of price cap service categories³⁹¹ and consolidation of price cap baskets,³⁹² are not relevant because Phase II relief removes services from price cap regulation.

157. The *Access Reform NPRM* also proposed allowing incumbent LECs to charge IXCs different rates for access to different classes of end user.³⁹³ Ameritech argues that class-of-customer pricing would enable incumbent LECs to respond to competition.³⁹⁴ We find that the pricing flexibility we grant in Phase I and Phase II is sufficient to enable incumbent LECs to respond to competition. Bell Atlantic argues that class-of-customer pricing is simply another form of deaveraging.³⁹⁵ We grant price cap LECs considerable flexibility to deaverage their rates in Section V of this Order, and Bell Atlantic does not explain why deaveraging by class of customer is necessary to enable incumbent LECs to respond to competition. Thus, the record does not provide a basis for granting this relief.

D. Price Cap Issues

1. Revision of Price Cap Indices

158. We have determined that no adjustment to price cap LECs' PCIs is warranted when a LEC removes demand associated with services offered pursuant to contract tariff from a price cap basket, or when an entire service is removed from price cap regulation pursuant to a Phase II showing. When the Commission permitted AT&T to remove commercial long distance services from price cap regulation, it did not require AT&T to make any exogenous cost adjustment to the PCI for the basket from which those services were removed.³⁹⁶ Specifically, the Commission found that the removal of an individual service from a basket has no effect on the PCI, and it affects the API only by altering the base period revenue weights of the services remaining in the basket at the time a carrier revises some other rate in that basket.³⁹⁷ Thus, removing individual

³⁹¹ *Access Reform NPRM*, 11 FCC Rcd at 21445.

³⁹² *Id.* at 21447-48.

³⁹³ Specifically, the Commission proposed allowing incumbent LECs to charge an IXC different rates for local switching and transport services based on the class of end user to which the IXC provides long distance service. *Id.* at 21445-46.

³⁹⁴ Ameritech Comments at 46.

³⁹⁵ BA/NYNEX Comments at 51. *See also* USTA Comments at 28.

³⁹⁶ Revisions to Price Cap Rules for AT&T Corp., CC Docket No. 93-197, Report and Order, 10 FCC Rcd 3009, 3019 (1995) (*Commercial Services Order*).

³⁹⁷ *Commercial Services Order*, 10 FCC Rcd at 3019.

services from price cap regulation has only a *de minimis* effect on the headroom for the services remaining in the basket.³⁹⁸

159. In accordance with this precedent, we do not require incumbent LECs to make any exogenous adjustment to their PCIs to reflect the removal of demand associated with contract tariff services from price cap regulation. Although the Commission did require a "recalibration" of AT&T's PCIs when other services were removed from price cap regulation,³⁹⁹ we find that the recalibration required by those Orders is not needed for removal of contract tariff demand. In those cases, the Commission removed all the services except one service category from the basket in question. Because the service band indices (SBIs) were designed to limit cross-subsidization between different types of services within a basket, and there is no danger of cross-subsidization when there is only one service category remaining in the basket, the Commission recalibrated AT&T's PCIs and APIs to eliminate the SBI for the remaining basket without affecting the headroom AT&T had previously.⁴⁰⁰ In the case of the relief we provide here, however, incumbent LECs will remove only some demand for some services from a basket; therefore, we will retain the SBIs, and there is no need for the recalibration we required of AT&T.

2. Low-End Adjustment Mechanism

160. *Background.* In the *LEC Price Cap Order*, the Commission adopted the low-end adjustment mechanism, which permits incumbent LECs earning rates of return less than 10.25 percent in a given year to increase their PCIs to a level that would enable them to earn 10.25 percent.⁴⁰¹ The Commission decided to retain the low-end adjustment mechanism in the *Price Cap Fourth Report and Order*, to prevent confiscatory price cap rates in cases where differences in economic conditions in different price cap LECs' service regions might cause a LEC to earn a confiscatory return in a given tariff year.⁴⁰²

³⁹⁸ See also USTA *ex parte* statement of Jan. 27, 1999; U S West *ex parte* statement of Jan. 28, 1999.

³⁹⁹ *Interexchange Competition Second Report and Order*, 8 FCC Rcd at 3671 (removal of all services except 800 directory assistance from Basket 2); *AT&T Non-Dominant Reinitialization Order*, 11 FCC Rcd 1201 (removal of services except international services from Basket 1).

⁴⁰⁰ *Interexchange Competition Second Report and Order*, 8 FCC Rcd at 3671; *AT&T Non-Dominant Reinitialization Order*, 11 FCC Rcd at 1201.

⁴⁰¹ *LEC Price Cap Order*, 5 FCC Rcd at 6804.

⁴⁰² See *Price Cap Fourth Report and Order*, 12 FCC Rcd at 16691, 16704-05; *Price Cap Performance Review*, 10 FCC Rcd at 9048.

161. In its petition for reconsideration of the *Price Cap Fourth Report and Order*,⁴⁰³ AT&T questions whether it is reasonable to retain the low-end adjustment mechanism after the elimination of sharing.⁴⁰⁴ In this Order, for the reasons discussed below, we partially grant AT&T's petition on this issue. We will consider other issues raised in AT&T's petition, along with other petitions for reconsideration of the *Price Cap Fourth Report and Order*, in a future Order.

162. *Discussion.* We eliminate the low-end adjustment mechanism for price cap LECs that qualify for and elect to exercise either the Phase I or Phase II pricing flexibility we grant in this Order.⁴⁰⁵ AT&T argues that the low-end adjustment mechanism blunts efficiency incentives just as sharing does and that, therefore, retaining it is inconsistent with the Commission's decision to eliminate sharing.⁴⁰⁶ AT&T also notes that several LECs opposed retention of the low-end adjustment mechanism, and those that supported it did so only as a means to provide "symmetry" to the sharing obligation.⁴⁰⁷ AT&T requests that we eliminate the low-end adjustment mechanism or re-introduce sharing.⁴⁰⁸

163. We conclude that we should eliminate the low-end adjustment mechanism once price cap LECs qualify for and choose to exercise either the Phase I or Phase II pricing flexibility we grant in this Order. We agree with AT&T that the low-end adjustment mechanism tends to blunt efficiency incentives. We also conclude that this effect will be exacerbated by removing contract tariff services from price cap regulation, so that retention of the mechanism would be unreasonable for price cap LECs obtaining pricing flexibility. The low-end adjustment mechanism can create undesirable incentives for price cap LECs when they move some demand for some services out of price cap regulation. The low-end adjustment is a rate-of-return-based

⁴⁰³ *Price Cap Fourth Report and Order*, 12 FCC Rcd 16642. For purposes of this Section VI.D.2 of the Order, except as otherwise noted, "Petition" refers to petitions for reconsideration of the *Price Cap Fourth Report and Order* filed July 11, 1997, "Comments" refers to comments filed in response to those petitions on August 18, 1997, and "Reply" refers to replies filed in response to those petitions on September 3, 1997.

⁴⁰⁴ AT&T Petition at 13-16. When price cap regulation included sharing obligations, incumbent LECs were required to "share" half or all their earnings above specified rates of return with their access customers through lower PCIs during the following year. See *Price Cap Fourth Report and Order*, 12 FCC Rcd at 16649. The Commission eliminated sharing obligations in the *Price Cap Fourth Report and Order*, in part because the benefits derived from those obligations were reduced by the adoption of an X-Factor based on a more accurate measure of productivity growth and elimination of multiple X-Factor options. As a result, the efficiency-blunting effects of sharing began to outweigh its benefits. *Id.* at 16699-702.

⁴⁰⁵ Streamlined treatment of new services, removal of interexchange services from price caps, and geographic deaveraging of rates for services in the trunking basket do not affect a LEC's entitlement to a low-end adjustment.

⁴⁰⁶ AT&T Petition at 13-15.

⁴⁰⁷ *Id.* at 13-14; AT&T Reply at 6-7.

⁴⁰⁸ AT&T Petition at 15-16.

mechanism, and it therefore recreates some of the incentives of rate-of-return regulation, although not to the same extent as sharing obligations.⁴⁰⁹ Earnings from non-price cap services are currently not considered part of "total interstate earnings"⁴¹⁰ for purposes of calculating low-end adjustments.⁴¹¹ As a result, price cap LECs must remove the costs of non-price cap services in order to calculate interstate earnings, and they have an incentive to underallocate those costs in order to minimize measured earnings. Currently, this underallocation incentive is not a serious concern, because non-price cap services represent a very small fraction of the price cap LECs' federally tariffed activities, and so the effects of any underallocation are minimal.⁴¹² Once a LEC has removed a significant amount of demand associated with contract tariff offerings from price cap regulation, however, its incentive to underallocate the costs of non-price cap services and the effects of such underallocation will be greater.

164. Our decision to eliminate the low-end adjustment mechanism for parties obtaining pricing flexibility is consistent with a proposal made by the Ad Hoc Telecommunications Users Committee (Ad Hoc) in response to the *Access Reform NPRM*. Ad Hoc argues that incumbent LECs either should be guaranteed a just and reasonable rate of return and recovery of all of their prudent investment, or they should be permitted to pursue market opportunities and maximize their earnings, but not both.⁴¹³ Ad Hoc reasons that an incumbent LEC permitted unlimited profits under price cap regulation should not be shielded from any risk of stranded investment.⁴¹⁴ Alternatively, Ad Hoc argues that an incumbent LEC seeking some stranded investment recovery should be subject to 100 percent sharing obligations for all earning in excess of 50 basis points

⁴⁰⁹ The Commission has concluded that sharing obligations severely blunt the efficiency incentives that it sought to create when it adopted price cap regulation, by requiring price cap LECs earning more than certain rates of return to share half or all those earnings with their customers. *Price Cap Fourth Report and Order*, 12 FCC Rcd at 16699; *LEC Price Cap Performance Review*, 10 FCC Rcd at 9045-46. The low-end adjustment mechanism does not blunt efficiency incentives as much as sharing because it guarantees only a 10.25 percent rate of return, and price cap LECs should be able to achieve much greater profits by trying to increase their productivity growth.

⁴¹⁰ In the *LEC Price Cap Reconsideration Order*, the Commission explained that sharing and the low-end adjustment mechanism are based on total interstate earnings rather than basket-by-basket earnings. *LEC Price Cap Reconsideration Order*, 6 FCC Rcd at 2679-80. See also *LEC Price Cap Order*, 5 FCC Rcd at 6805. The Commission also determined that sharing and the low-end adjustment mechanism should be based on earnings from all services subject to price cap regulation, rather than earnings exclusively from access services. *LEC Price Cap Reconsideration Order*, 6 FCC Rcd at 2680-81.

⁴¹¹ See *LEC Price Cap Reconsideration Order*, 6 FCC Rcd at 2681 n.126. Earnings from services excluded from price cap regulation also are excluded from total interstate earnings for purposes of calculating low-end adjustments. *Id.* at 2681-82.

⁴¹² *LEC Price Cap Order*, 5 FCC Rcd at 6810.

⁴¹³ Ad Hoc Comments at 66-69.

⁴¹⁴ *Id.* 67-68.

over the authorized rate of return.⁴¹⁵ Although we decline to reimpose sharing obligations, we agree with Ad Hoc that an incumbent LEC seeking pricing flexibility to compete more vigorously in the marketplace should not be afforded any rate-of-return-based protection from any risk associated with its competitive ventures.⁴¹⁶

165. We have considered whether it is possible to modify the low-end adjustment mechanism to limit the undesirable incentives discussed above. For example, USTA proposed requiring price cap LECs to maintain records regarding demand for services removed from price cap regulation, but permitting them to keep that information confidential. Under USTA's proposal, a price cap LEC seeking to make a low-end adjustment would be required to re-price its removed service demand at an "average price cap tariff rate."⁴¹⁷ It would be difficult, however, for the Commission or other interested parties to verify that a price cap LEC claiming a low-end adjustment has re-priced its contract tariff demand properly. Specifically, whenever a contract tariff offering is a package of two or more access services, USTA's proposal requires the incumbent to allocate the contract rate among the services in the package. It would be difficult for the Commission to determine whether that allocation is reasonable, particularly in cases where the package includes nonregulated services and services removed from price cap regulation pursuant to a grant of pricing flexibility. Therefore, USTA's proposal would not be an adequate safeguard against cross-subsidization.

166. The other possible safeguard that we have considered would require the Commission to specify the cost allocation rules LECs would use to segregate costs and revenues from services in price cap regulation from the costs and revenues of services outside of price cap regulation. Such rules would be burdensome for carriers and the Commission and is inconsistent with the deregulatory framework envisioned by Congress when it adopted the Telecommunications Act of 1996. Indeed, we find that such cost accounting rules would make using the low-end adjustment mechanism just as burdensome as making an above-cap filing. We have retained the low-end adjustment mechanism in part to avoid costly above-cap filings.⁴¹⁸ Burdening the low-end

⁴¹⁵ *Id.* at 67.

⁴¹⁶ Courts also have held that a utility company's captive customers should bear the risk of loss of the utility's investment only if those customers also are permitted to share in the benefits resulting from that investment. *See Democratic Cent. Comm. of the Dist. of Columbia v. Washington Metro. Area Transit Comm'n*, 485 F.2d 786, 805 (D.C.Cir.1973), *cert. denied*, 415 U.S. 935 (1974); *AT&T Info. Sys., Inc. v. FCC*, 854 F.2d 1442, 1444 (D.C. Cir. 1988).

⁴¹⁷ USTA *ex parte* statement of Jan. 27, 1999, at 3-4.

⁴¹⁸ The Commission retained the low-end adjustment mechanism to help prevent price cap regulation from becoming confiscatory. *Price Cap Fourth Report and Order*, 12 FCC Rcd at 16704. The above-cap filing is the only other mechanism in price cap regulation designed explicitly to prevent confiscatory rates. Any above-cap filing must be supported by the following: (1) cost support data broken down to the lowest possible level for each relevant basket for each of the most recent four years under price cap regulation; (2) a detailed explanation of the reasons for the prices of all rate elements to which the LEC does not assign costs; (3) a comprehensive explanation

adjustment mechanism with cost allocation rules thus would undercut a major reason for retaining the low-end adjustment mechanism as part of the price cap plan. On the other hand, elimination of the low-end adjustment mechanism for an incumbent LEC might enable the Commission to relax, for that LEC, any accounting rules necessitated only by the rate-of-return-based low-end adjustment mechanism. For all these reasons, we eliminate the low-end adjustment mechanism for price cap LECs obtaining pricing flexibility.

167. Any LEC obtaining Phase I regulatory relief in any MSA will be precluded from making any low-end adjustment throughout its entire, holding-company-wide, service region, regardless of whether it files separate tariffs for each of its study areas. Permitting MSA-by-MSA low-end adjustments would require the same kind of burdensome cost allocation rules that we describe above. Furthermore, eliminating the low-end adjustment will not result in confiscatory rates, because we will continue to permit price cap LECs to make above-cap tariff filings. We also conclude that an above-cap tariff investigation provides the best forum for determining whether the above-cap tariff would implicitly force the LEC's regulated ratepayers to bear some of the risk of the LEC's competitive ventures.⁴¹⁹

168. We retain the low-end adjustment mechanism for price cap LECs that have not opted to exercise any Phase I or Phase II regulatory relief, however. As we note above, the flexibility we grant in Phase I and Phase II will exacerbate the efficiency-blunting effects of the low-end adjustment mechanism. By the same token, the inefficiencies associated with the low-end adjustment mechanism in the absence of these flexibilities are fairly minor. To be eligible for a low-end adjustment, a price cap LEC must earn less than a 10.25 percent rate of return, which would constitute a substantial earnings sacrifice for most price cap LECs. For those LECs, the benefits of the low-end adjustment mechanism would not justify such a sacrifice, because the mechanism permits only a one-time PCI adjustment to avoid back-to-back annual earnings below 10.25 percent. For this reason, we find that the benefits of retaining the low-end adjustment mechanism for those LECs that have not obtained Phase I or Phase II relief (ensuring that LECs' rates are not confiscatory without requiring above-cap filings) outweigh its effects on efficiency incentives.

3. Common Line Basket Issues

169. Above, we permit incumbent LECs to offer contract tariffs and volume and term discounts for access services once they satisfy the Phase I triggers. We also have designed our Phase I relief to limit headroom by requiring price cap LECs to remove the demand associated

of how the carrier allocated costs among rate elements in the relevant basket; and (4) an explanation of the manner in which the LEC has allocated all costs, not just exogenous costs, among baskets. *LEC Price Cap Order*, 5 FCC Rcd at 6823.

⁴¹⁹ The Commission has stated that it would probably suspend any above-cap filing for the statutory five-month period. *Id.* at 6823-24.

with contract tariff offerings from price caps, so that price cap LECs cannot use that pricing flexibility to raise access rates for those customers in the MSA that lack competitive alternatives. Phase I pricing flexibility for services in the common line basket does not raise the same concerns regarding headroom, because different price cap rules apply to the common line basket. There is no need to require price cap LECs to remove common line services offered pursuant to contract tariff from price caps, nor do we see any need for additional safeguards to prevent the creation of headroom as a result of volume and term discounts for services in the common line basket, because the current rules already preclude the creation of headroom in the common line basket. Specifically, Section 69.152(m) prohibits price cap carriers that choose to charge less than the maximum permitted end user common line charges (EUCLs) from making up any of that revenue through increases to other common line charges (primary interexchange carrier charges (PICCs) or carrier common line CCL) charges).⁴²⁰ Similarly, Section 69.153 requires incumbent LECs to base their PICC calculations on the maximum revenues permitted under the rules, rather than the actual revenues recovered.⁴²¹ Thus, our rules do not permit a LEC to charge a higher PICC for some subscriber lines simply by reducing the PICC for other lines. Finally, Section 69.154 allows price cap LECs to impose CCL charges only to the extent that their permitted common line revenues exceed the maximum amount the LECs could have recovered through EUCLs and PICCs.⁴²²

E. Procedural Issues

1. Special Access and Dedicated Transport Services

170. *Background.* In the *Access Reform NPRM*, the Commission invited comment on the procedural requirements governing requests for pricing flexibility.⁴²³ The Commission did not propose any specific pleading cycle, but it proposed establishing a deadline for Commission action of 90 days.⁴²⁴

171. *Discussion.* An incumbent LEC seeking pricing flexibility for special access or dedicated transport services under the framework we adopt in this Order may file a petition with the Commission identifying the relief it seeks and demonstrating that it has satisfied the applicable triggers. Comments on petitions will be due fifteen days after the petition is filed. Replies will be due ten days after the comments are due. The triggers established for special access and dedicated transport services are administratively simple and easy to verify. A relatively short

⁴²⁰ 47 C.F.R. § 69.152(m).

⁴²¹ 47 C.F.R. § 69.153.

⁴²² 47 C.F.R. § 69.154. Other restrictions also apply.

⁴²³ *Access Reform NPRM*, 11 FCC Rcd at 21432, 21444.

⁴²⁴ *Id.* at 21431.

pleading cycle is, therefore, sufficient to enable interested parties to examine the incumbent LEC's petition and to draft a response. We will notify interested parties of a pending pricing flexibility petition through the Competitive Pricing Division's Tariff Public Reference Log. In addition, we require incumbent LECs to submit pricing flexibility petitions through our Electronic Tariff Filing System (ETFS), so that interested parties may obtain copies of petitions through the Commission's website.

172. Incumbent LECs bear the burden of proving that they have satisfied the applicable trigger for the pricing flexibility they seek.⁴²⁵ An incumbent LEC is in the best position to present evidence of the extent of collocation in its wire centers within an MSA. We also adopt Ameritech's proposal to permit incumbent LECs to file petitions for multiple MSAs, as long as the data in those petitions are disaggregated by MSA.⁴²⁶ Specifically, to carry its burden of proof, the incumbent may show the following: (1) the total number of wire centers in the MSA; (2) the number and location of the wire centers in which competitors have collocated; (3) in each wire center on which the incumbent bases its petition, the name of at least one collocator that uses transport facilities owned by a provider other than the incumbent to transport traffic from that wire center; and (4) that the percentage of wire centers in which competitors have collocated satisfies the trigger we have adopted with respect to the pricing flexibility sought by the incumbent LEC. Alternatively, the incumbent may show the following: (1) the total base period⁴²⁷ revenues generated by the services for which the incumbent seeks relief in the MSA for which the incumbent seeks relief; (2) in each wire center on which the incumbent bases its petition, the name of at least one collocator that uses transport facilities owned by a provider other than the incumbent to transport traffic from that wire center; and (3) that the wire centers in which competitors have collocated account for a sufficient percentage of the incumbent's base period revenues generated by the services at issue within the relevant MSA or non-MSA area to satisfy the trigger we have adopted with respect to the pricing flexibility sought by the incumbent LEC. We codify these requirements in a new Section 1.774 of our rules, as set forth in Appendix B to this Order.

173. Currently, the Commission's new service rules require price cap LECs to determine the appropriate price cap basket and service band for their new services in the context of a subsequent annual access tariff filing, and to incorporate those new services into those baskets in that annual access filing.⁴²⁸ Whenever a price cap LEC can demonstrate in an annual access tariff filing that one of its new services would be properly incorporated into a basket or service band for

⁴²⁵ See Spectranet Comments at 5-6.

⁴²⁶ Ameritech Oct. 26 Comments, Att. N at 3, 5.

⁴²⁷ For price cap LECs, the "base period" is the 12-month period (*i.e.*, the calendar year) ending six months before the effective date of the LECs' annual access tariffs. See 47 C.F.R. § 61.3(e).

⁴²⁸ Specifically, price cap LECs are required to incorporate new services into a price cap basket in the annual access tariff filing effective between 6 and 18 months after the new service tariff takes effect. 47 C.F.R. § 61.42(g).

which it has been granted Phase I or Phase II regulatory relief in any MSA or MSAs, it will be granted the same relief in the same MSAs for that new service.

174. We also amend Section 0.291, listing the authority delegated to the Chief, Common Carrier Bureau (Bureau), explicitly to delegate authority to issue Orders acting on petitions for pricing flexibility involving special access and dedicated transport services. Because the pricing flexibility triggers we adopt for those services are administratively simple bright-line tests, Bureau-level review is sufficient to determine whether the incumbent LEC has satisfied the applicable test.

175. Finally, a pricing flexibility petition for special access and dedicated transport services will be deemed granted unless the Bureau denies it within 90 days of the close of the pleading cycle, as the Commission proposed in the *Access Reform NPRM*.⁴²⁹ Ameritech recommends adopting a deadline of 90 days after the filing date of the petition, rather than 90 days after the close of the pleading cycle.⁴³⁰ Although we expect our pricing flexibility thresholds to be simple to administer, it is prudent to allow more time to review pricing flexibility petitions, at least until we gain more experience. The Bureau may, of course, issue an Order before this 90-day deadline if it has completed the review. Also, if experience shows that a full 90 days is not necessary to review pricing flexibility petitions, we may consider relaxing this or other procedural requirements. The period for filing applications for review begins the day the Bureau grants or denies the petition, or the day that the petition is deemed denied.

2. Treatment of Proprietary Data

176. In the event that a price cap LEC wishes to request confidential treatment of any information contained in a pricing flexibility petition, it should follow the procedures for obtaining confidential treatment of tariff cost support information. The price cap LEC must demonstrate, by a preponderance of the evidence, that the information should be withheld from public inspection in accordance with the requirements of Section 0.459 of the Commission's rules.⁴³¹ A price cap LEC wishing to request confidential treatment of information contained in a pricing flexibility petition should demonstrate, by a preponderance of the evidence, that the information should be withheld from public inspection in accordance with the requirements of Section 0.459 of this chapter.

⁴²⁹ *Access Reform NPRM*, 11 FCC Rcd at 21431.

⁴³⁰ Ameritech Comments, Attachment N at 3, 5.

⁴³¹ See 47 C.F.R. §§ 0.459. See also Examination of Current Policy Concerning the Treatment of Confidential Information Submitted to the Commission, CC Docket No. 96-55, Report and Order, 13 FCC Rcd 24816, 24840-42 (1998) (*Treatment of Confidential Information Order*); *Tariff Streamlining Order*, 12 FCC Rcd at 2212-14.

177. In their requests for confidentiality, carriers should indicate with specificity the extent to which they believe the information they submit, such as the identity of collocators, is subject to section 222(b) of the Act concerning confidential carrier information,⁴³² and the bases for that belief. The information will be kept confidential, as appropriate, subject to Commission procedures concerning Freedom of Information Act (FOIA) requests. Although the Commission will consider any FOIA requests on a case-by-case basis, pursuant to applicable law, we note that FOIA exceptions, such as the exception for "trade secrets and commercial or financial information,"⁴³³ may prevent disclosure of such information. A price cap LEC will be required, in any event: (1) to provide collocation information to parties to the extent that the parties are the collocators upon which the price cap LEC relies in its petition, (2) to certify in its petition that it has done so, and (3) to provide to the Commission a copy of the information it provides to those parties. In such cases, the LEC may provide the data to a party in redacted form, revealing to the party only the information relating to that party.

3. Other Switched Access Services

178. We will grant Phase I pricing flexibility for common line and traffic-sensitive services, and the traffic-sensitive components of tandem-switched transport service to a price cap LEC within an MSA if the LEC demonstrates that its competitors, in aggregate, offer service over their own facilities to at least 15 percent of incumbent LEC customer locations in the MSA. For the reasons we explain in Section VI.C.3, we do not prescribe a particular method by which a LEC may demonstrate satisfaction of this trigger. As a result, petitions seeking pricing flexibility for these services will not be as routine as petitions seeking pricing flexibility for special access and dedicated transport services. Because pricing flexibility petitions for common line, traffic-sensitive, and the traffic-sensitive components of tandem-switched transport services are not subject to a bright-line rule, and will require more fact-intensive investigation, they are best addressed at the Commission level. Accordingly, we do not delegate authority to the Bureau at this time to act on petitions for pricing flexibility involving these services. A pricing flexibility petition for these services will be deemed granted unless the Commission denies it within five months of the close of the pleading cycle for that petition. Otherwise, we adopt the same procedural requirements for pricing flexibility petitions for these services as we adopt above for pricing flexibility petitions for special access and dedicated transport services. As the Commission gains experience with such petitions, it may be possible for the Commission to act in less than the full five months, or to delegate authority to the Bureau with respect to these petitions.

⁴³² See 47 U.S.C. § 222(b).

⁴³³ See 5 U.S.C. § 552(b)(4).

F. U S West Forbearance Petition

179. As we note above, several BOCs have filed petitions seeking forbearance, pursuant to section 160 of the Act,⁴³⁴ from dominant carrier regulation in the provision of certain special access and high capacity services.⁴³⁵ The first of these petitions, filed by U S West, is deemed granted if not denied by the Commission by August 24, 1999, unless the Commission extends the deadline for an additional ninety days.⁴³⁶ We conclude that such an extension is warranted here. In this Order, we adopt a comprehensive framework for granting price cap LECs such as U S West progressively greater pricing flexibility as competition develops, including much of the relief sought by U S West in its petition, and an extension of the deadline for acting on that petition will allow the Commission to consider U S West's request for relief in the context of the rules we adopt here. Accordingly, we extend the deadline for acting on U S West's petition by ninety days.

VII. CLEC ACCESS CHARGES

A. Background

180. In the *Competitive Carrier Proceeding*, the Commission established a comprehensive framework for determining whether carriers are dominant or non-dominant.⁴³⁷ Dominant carriers⁴³⁸ are carriers that possess individual market power and those without market power are non-dominant carriers.⁴³⁹ The Commission's policy since *Competitive Carrier* is that a carrier is non-dominant unless the Commission makes or has made a finding that it is dominant.⁴⁴⁰

⁴³⁴ 47 U.S.C. § 160.

⁴³⁵ See *supra* Section II.C.1.

⁴³⁶ See Petition of U S West Communications, Inc. for Forbearance from Regulation as a Dominant Carrier in the Phoenix, Arizona MSA, CC Docket No. 98-157 (filed Aug. 24, 1998); 47 U.S.C. § 160(c) (imposing one-year deadline for Commission action on forbearance petition; Commission may extend the deadline by 90 days if necessary to ensure compliance with the statutory forbearance criteria).

⁴³⁷ *Dominant/Non-Dominant Order*, 12 FCC Rcd 15766.

⁴³⁸ *Competitive Carrier First Report and Order*, 85 FCC 2d at 20-22; see also 47 C.F.R. § 61.3(o) (defining "dominant carrier").

⁴³⁹ The Commission, in the *Dominant/Non-Dominant Order*, listed a number of factors that historically have been considered in determining whether a firm possesses market power, including market share, supply and demand substitutability, the cost structure, size, and resources of the firm, and control of bottleneck facilities. See *Dominant/Non-Dominant Order*, 12 FCC Rcd at 15766. See also Implementation of Non-Accounting Safeguards of Sections 271 and 272 of the Communications Act of 1934 and Regulatory Treatment of LEC Provision of Interexchange Services Originating in the LEC's Local Exchange Area, CC Docket No. 94-149, Notice of Proposed Rulemaking, 11 FCC Rcd 18877, at 18929-38 (1996).

⁴⁴⁰ See, e.g., *Competitive Carrier First Report and Order*, 85 FCC 2d at 10-11; 47 C.F.R. § 61.3(u) (defining "non-dominant carrier").

New entrants into the exchange access market, such as competitive local exchange carriers (CLECs),⁴⁴¹ have been presumptively classified as non-dominant because the Commission has not found that they are able to exercise market power in particular service areas.⁴⁴² To date, the Commission has applied Parts 61 (Tariffs) and 69 (Access Charges) of its rules only to incumbent LECs.⁴⁴³

181. In the *Access Reform NPRM*, the Commission sought comment on whether CLECs have market power with regard to terminating access services and whether and to what extent it should regulate terminating access services provided by CLECs.⁴⁴⁴ The Commission noted that, with originating access, the calling party has the choice of service provider, the decision to place a call, and the ultimate obligation to pay for the call.⁴⁴⁵ The calling party is also the customer of the IXC that purchases the originating access service.⁴⁴⁶ As long as IXCs can influence the choice of the access provider, a LEC's ability to charge excessive originating access rates is limited, as IXCs will shift their traffic from that carrier to a competing access provider.⁴⁴⁷ The Commission noted that, with terminating access, the choice of service provider for terminating access is made by the called party.⁴⁴⁸ The decision to place the call and payment for the call lies, however, with the calling party. The calling party, or its long-distance service provider, has little or no ability to influence the called party's choice of service provider.⁴⁴⁹ Furthermore, IXCs are required by

⁴⁴¹ CLECs compete with incumbent LECs in the provision of local exchange and exchange access services.

⁴⁴² See *Tariff Filing Requirements for Non-Dominant Common Carriers*, CC Docket No. 93-36, Memorandum Opinion and Order, 8 FCC Rcd 6752, 6754 (1993) (CLECs are non-dominant carriers because they have not been previously declared dominant), *vacated and remanded in part on other grounds*, *Southwestern Bell Corp. v. FCC*, 43 F.3d 1515 (D.C. Cir. 1995); *on remand*, 10 FCC Rcd 13653 (1995).

⁴⁴³ See *Hyperion Telecommunications, Inc., Petition for Forbearance*, Memorandum Opinion and Order, 12 FCC Rcd 8596 (1997) (granting petitions seeking permissive detariffing for provision of interstate exchange access services by providers other than the incumbent LEC) (*Hyperion Order*). Concomitantly with the *Hyperion Order*, the Commission issued a Notice of Proposed Rulemaking seeking comment on mandatory detariffing for non-incumbent LEC providers of interstate exchange access services. See *Complete Detariffing for Competitive Access Providers and Competitive Local Exchange Carriers*, CC Docket No. 97-146, Notice of Proposed Rulemaking, 12 FCC Rcd 8613 (1997).

⁴⁴⁴ *Access Reform NPRM*, 11 FCC Rcd at 21476.

⁴⁴⁵ *Id.* at 21472.

⁴⁴⁶ *Id.*

⁴⁴⁷ *Id.*

⁴⁴⁸ *Id.* at 21476.

⁴⁴⁹ *Id.*

statute to charge averaged rates.⁴⁵⁰ Consequently, not only does the calling party not choose the terminating LEC, but section 254(g) requires IXCs to spread the cost of terminating access rates among all end users. Because the paying party does not choose the carrier that terminates its interstate calls, CLECs may have incentive to charge excessive rates for terminating access.⁴⁵¹ Accordingly, the Commission tentatively concluded in the *Access Reform NPRM* that terminating access may remain a bottleneck controlled by whichever LEC provides terminating access to a particular customer, even if competitors have entered the market.⁴⁵² The Commission also recognized, however, that excessive terminating access charges might encourage IXCs to enter the access market in order to avoid paying these charges.⁴⁵³

182. In the *Access Reform NPRM*, the Commission also sought comment on whether it should continue to treat incumbent LEC originating "open end" minutes, such as originating access for 800 service, as terminating minutes for access charge purposes, and whether it should extend this approach to CLECs.⁴⁵⁴ The Commission noted that, in some cases, such as 800 and 888 service, the called party, which pays for the call, is unable to influence the calling party's choice of provider for originating access services.⁴⁵⁵

183. In the *Access Reform First Report and Order*, the Commission decided not to adopt any regulations governing CLEC terminating access charges and did not address the issue of CLEC originating access charges.⁴⁵⁶ Based on the available record, the Commission decided to continue to treat non-incumbent LECs as non-dominant in the provision of terminating access

⁴⁵⁰ See 47 U.S.C. § 254(g); see also Policy and Rules Concerning the Interstate, Interexchange Marketplace, Implementation of Section 254(g) of the Communications Act of 1934, as amended, CC Docket No. 96-61, Report and Order, 11 FCC Rcd 9564 (1996) (requiring IXCs to integrate and average the rates they charge for service).

⁴⁵¹ *Access Reform NPRM*, 11 FCC Rcd at 21476 (citing JOSEPH GILLAN & PETER ROHRBACH, THE POTENTIAL IMPACT OF LOCAL COMPETITION ON TELECOMMUNICATIONS MARKET STRUCTURE: DIVERSITY OR RECONCENTRATION, 1994; ROBERT W. CRANDALL AND LEONARD WAVERMAN, TALK IS CHEAP: THE PROMISE OF REGULATORY REFORM IN NORTH AMERICAN TELECOMMUNICATIONS, 1996, at 265-265).

⁴⁵² *Access Reform NPRM*, 11 FCC Rcd at 21476.

⁴⁵³ *Id.* at 21473.

⁴⁵⁴ See *id.* at 21477. "The term open end of a call describes the origination or termination of a call that utilizes exchange carrier common line plant (a call can have no, one, or two open ends.)" 47 C.F.R. § 69.105(b)(1)(ii).

⁴⁵⁵ See *Access Reform NPRM*, 11 FCC Rcd at 21477.

⁴⁵⁶ With respect to incumbent LEC originating access charges, the Commission concluded that new entrants, by purchasing unbundled network elements or providing facilities-based competition, eventually will exert downward pressure on incumbent LEC originating access rates. *Access Reform First Report and Order*, 12 FCC Rcd at 16135-36.

service.⁴⁵⁷ Although an IXC must use the CLEC serving an end user to terminate a call, the Commission found that the record did not indicate that CLECs previously had charged excessive terminating access rates or that CLECs distinguished between originating and terminating access in their service offerings.⁴⁵⁸ The Commission concluded that it did not appear that CLECs had structured their service offerings in ways designed to exercise any market power over terminating access and that, therefore, the concerns expressed in the *Access Reform NPRM* were not substantiated by the record.

184. The Commission further observed that, as CLECs attempt to expand their market presence, the rates of incumbent LECs or other potential competitors should constrain the CLECs' terminating access rates.⁴⁵⁹ In addition, the Commission found that overcharges for terminating access could encourage access customers to take competitive steps to avoid paying unreasonable terminating access charges.⁴⁶⁰ The Commission explained that, although high terminating access charges may not create a *disincentive* for the call recipient to retain its local carrier (because the call recipient does not pay the long distance charge), the call recipient may nevertheless respond to *incentives* offered by an IXC with an economic interest in encouraging the end user to switch to another local carrier.⁴⁶¹ Thus, the Commission concluded that the possibility of competitive responses by IXCs would constrain non-incumbent LEC pricing.⁴⁶²

185. Although the Commission declined at that time to adopt any regulations governing the provision of terminating access provided by CLECs because CLECs did not appear to possess market power,⁴⁶³ it noted that it could address the reasonableness of CLEC terminating access rates in individual instances through the exercise of its authority to investigate and adjudicate

⁴⁵⁷ *Access Reform First Report and Order*, 12 FCC Rcd at 16140.

⁴⁵⁸ *Id.* The Commission noted, in fact, that the record indicated that the terminating rates of CLECs were equal to or below the tariffed rates of incumbent LECs. *Id.*

⁴⁵⁹ The Commission stated that the record indicated that long-distance carriers have established relationships with incumbent LECs for the provision of access services, and new market entrants are not likely to risk damaging their developing relationships with IXCs by charging unreasonable terminating access rates. *Id.*

⁴⁶⁰ *Id.*

⁴⁶¹ *Id.* at 16141.

⁴⁶² *Id.* at 16142. The Commission also decided to continue to treat "open end" originating minutes, such as those for 800 or 888 services, as terminating minutes for access charge purposes, recognizing, in these cases, that access customers have limited ability to influence the calling party's choice of access provider. *Id.* In order to address the potential that incumbent LECs might charge unreasonable rates for terminating access, the Commission limited price cap incumbent LEC recovery of TIC and common costs from terminating access rates for a limited period with the eventual elimination of any recovery of common line and TIC costs through terminating access charges. *Id.* at 16137.

⁴⁶³ *Id.* at 16141.

complaints under section 208.⁴⁶⁴ Moreover, the Commission stated that it would be sensitive to indications that the terminating access rates of CLECs were unreasonable.⁴⁶⁵ The Commission committed to revisit the issue of CLEC access rates if there were sufficient indications that CLECs were imposing unreasonable terminating access charges.⁴⁶⁶

B. AT&T's Petition for Declaratory Ruling

186. On October 23, 1998, AT&T filed a petition requesting that the Commission issue a declaratory ruling⁴⁶⁷ confirming that, under existing law and Commission rules and policies, IXCs may elect not to purchase switched access services offered under tariff by CLECs.⁴⁶⁸ AT&T contends that a substantial number of CLECs impose switched access charges that are significantly higher -- in some cases, by more than twenty times -- than those charged by the incumbent LEC against which the CLEC competes.⁴⁶⁹ AT&T's attempts to negotiate a resolution of this issue have stalled, it says, because many CLECs take the position that, due to the "filed tariff doctrine,"⁴⁷⁰ AT&T is obligated to accept services from the CLEC at prices chosen by the

⁴⁶⁴ 47 U.S.C. § 208.

⁴⁶⁵ *Access Reform First Report and Order*, 12 FCC Rcd at 16141-42. The Commission indicated that terminating access rates that exceed originating rates in the same market, for example, may suggest the need to revisit its regulatory approach. Similarly, the Commission noted that terminating rates that exceed those charged by the incumbent LEC serving the same market may suggest that a CLEC's terminating access rates are excessive. *Id.* at 16142.

⁴⁶⁶ *Id.*

⁴⁶⁷ See 47 C.F.R. § 1.2.

⁴⁶⁸ See *AT&T Declaratory Ruling Petition*. We note that, unless otherwise indicated, all citations to comments and replies in this section of the Order refer to comments and replies submitted in response to the *AT&T Declaratory Ruling Petition*.

⁴⁶⁹ *AT&T Declaratory Ruling Petition*, Appendix A. We note that this issue is also the subject of the Common Carrier Bureau's (Bureau) decision in *MGC Communications, Inc. v. AT&T Corp.*, File No. EAD 99-002, Memorandum Opinion and Order, DA 99-1395 (Com. Car. Bur. July 16, 1999) (*MGC Communications*).

⁴⁷⁰ In general, the "filed tariff" or "filed rate" doctrine stands for the principle that "the rate of the carrier duly filed is the only lawful charge. Deviation from it is not permitted upon any pretext . . . Ignorance or misquotation of rates is not an excuse for paying or charging either less or more than the rate filed." *Maislin Industries, U.S., Inc. v. Primary Steel, Inc.*, 497 U.S. 116, 127 (1990) (quoting *Louisville & Nashville R. Co. v. Maxwell*, 237 U.S. 94 (1915)). The filed tariff doctrine is codified at 47 U.S.C. § 203, which requires all common carriers of interstate and foreign telecommunications to file a schedule of their charges, as well as the classifications, practices, and regulations affecting such charges. A carrier may charge only the rates listed in the tariff. 47 U.S.C. § 203(c)(1). The charges, classifications, regulations or practices in the filed tariff may be changed only after notice is given to the Commission and the public. 47 C.F.R. § 203(b)(1). See also *Cincinnati Bell Telephone v. Allent Communication Services*, 17 F.3d 921, n.4 (6th Cir. 1994).

CLEC, even though AT&T did not affirmatively order access from the CLEC.⁴⁷¹ AT&T alleges that its petition is consistent with the *Access Reform First Report and Order*, in which the Commission stated that "terminating rates that exceed those charged by the ILEC serving the same market may suggest that a CLEC's terminating access rates are excessive."⁴⁷²

187. The Commission has the discretion, on a case-by-case basis, to determine whether it is best to resolve a controversy by the adoption of a general rule or by an individual ad hoc proceeding, such as a declaratory ruling.⁴⁷³ The presence or absence of factual disputes is a significant factor in deciding whether a declaratory ruling is an appropriate method for resolving a controversy.⁴⁷⁴ AT&T contends that a declaratory ruling is appropriate here because the "facts are essentially undisputed and the governing law is clear."⁴⁷⁵ Despite AT&T's allegations to the contrary, however, the facts are not undisputed here. A number of carriers assert that AT&T's calculations of CLEC originating and terminating access rates⁴⁷⁶ are either incorrect or misleading.⁴⁷⁷ In response to these assertions, AT&T addressed only one of the concerns raised

⁴⁷¹ *AT&T Declaratory Ruling Petition* at 3, n.2. AT&T does not typically place access orders, or establish direct connections, with such CLECs. *Id.* Instead, the CLEC establishes an interconnection arrangement with the incumbent LEC serving the area, and it installs trunks to the incumbent LEC's access tandem. *Id.* Calls originated from the CLEC's switch are routed to the incumbent LEC tandem, which then combines them with other traffic destined for AT&T or another IXC's network and routes that traffic to that IXC's POP. *Id.* Terminating traffic from AT&T and other IXCs similarly is routed through the incumbent LEC access tandem to the CLEC. *Id.*

⁴⁷² *Id.* at 9 (citing *Access Reform First Report and Order*, 12 FCC Rcd at 16135-42).

⁴⁷³ *See, e.g., British Caledonian Airways Ltd. v. Civil Aeronautics Board*, 584 F.2d 982, 993 (1978) (the choice made between proceeding by a general rule or by an individual ad hoc litigation is one that lies primarily in the informed discretion of the administrative agency) (*British Caledonian Airways Ltd.*).

⁴⁷⁴ *American Network, Inc. Petition for Declaratory Ruling Concerning Backbilling of Access Charges*, Memorandum Opinion and Order, 4 FCC Rcd 550, 551 (Com. Car. Bur. 1989), *recon. denied*, 4 FCC Rcd 8797 (Com. Car. Bur. 1989). We note that the factors for determining the propriety of a declaratory ruling are different in the context of a court referral under the primary jurisdiction doctrine. *See Texas & Pacific Ry. v. Abilene Cotton Oil Co.*, 204 U.S. 426 (1907) (creating "primary jurisdiction" doctrine); *United States v. Western Pacific R.R.*, 352 U.S. 59, 63-70 (1956) (explaining purpose of the doctrine); *Far East Conference v. United States*, 342 U.S. 570, 574 (1952) (same); *MCI Communications Corp. v. AT&T*, 496 F.2d 214, 220-22 (3d Cir. 1974) (applying the doctrine in the telecommunications context).

⁴⁷⁵ *AT&T Declaratory Ruling Petition* at 5.

⁴⁷⁶ *See id.* at Appendix A.

⁴⁷⁷ *See WinStar Comments* at 6; *Optel Comments* at 5; *CTSI Comments* at 10 (rates attributed to WinStar, Optel, and CTSI, respectively, are incorrect); *ALLTEL Comments* at 2 and *ALTS Comments* at 6 (AT&T's rate comparison is misleading because it does not reflect the fact that price cap carriers rates are reduced as a result of the introduction of presubscribed interexchange carrier charge); *Teligent, Inc. Comments* at 9 (AT&T fails to include an amount for transport in the rates charged by Ameritech, the local incumbent LEC, but does include an amount for transport in Teligent's rates).

by commenters.⁴⁷⁸ Without agreement by the parties on the calculation and accuracy of both the incumbent LEC and CLEC rates, it is impossible compare them.⁴⁷⁹ Nor can the Commission evaluate AT&T's claim that its request for declaratory ruling is consistent with the Commission's statements in the *Access Reform First Report and Order* that CLEC terminating access rates that exceed those of the incumbent LEC may be excessive.⁴⁸⁰

188. Moreover, the parties also dispute the applicable law. A number of opponents to AT&T's petition assert that AT&T mistakenly relies upon the *Capital Network* decision, in which the Commission found that an attempt to charge a party for a service that the party did not order would constitute an unreasonable practice within the meaning of section 201(b) of the Act, 47 U.S.C. § 201(b).⁴⁸¹ These opponents assert that AT&T failed to address the application of the constructive ordering doctrine, established in *United Artists*.⁴⁸² In *United Artists*, the Commission found that affirmative consent was unnecessary to create a carrier- customer relationship when a carrier is interconnected with other carriers in such a manner that it can expect to receive access services, and when it fails to take reasonable steps to prevent the receipt of access services and does in fact receive such services.⁴⁸³ For all the foregoing reasons, and in the exercise of our

⁴⁷⁸ AT&T states that inclusion of the presubscribed interexchange carrier charge (PICC) would not make a material difference to its calculation, but it does not address the carriers' other concerns regarding AT&T's calculations, i.e., that rates were misquoted and did not include incumbent LEC transport charges. See AT&T Reply at 4, n.10, and Appendix B, providing a recomputed comparison including the PICC.

⁴⁷⁹ In its reply, AT&T argues that its petition is not a dispute over rate calculations because it is not limited to CLECs that charge rates exceeding the corresponding ILEC levels, but also applies to CLECs that charge rates that simply mirror incumbent LEC rates. AT&T Reply at 4. AT&T asserts that both rates that exceed and rates that mirror incumbent LEC rates distort the exchange access market by establishing the incumbent LECs' purportedly above-cost charges as a benchmark for CLECs. We do not find this argument convincing. At the heart of either complaint is the fact that AT&T views itself as a captive customer forced to pay excessively high terminating rates. In order to evaluate such a complaint, all parties must agree on the method of calculating the disputed rate, e.g., whether transport fees and PICCs are included. Based on the record, it appears that the parties do not.

⁴⁸⁰ *AT&T Declaratory Ruling Petition* at 9 (citing *Access Reform First Report and Order*, 12 FCC Rcd at 1635-42).

⁴⁸¹ *AT&T Declaratory Ruling Petition* at 6-8 (citing *Capital Network Systems, Inc.*, 6 FCC Rcd 5609 (Com. Car. Bur. 1992), *application for review denied*, 7 FCC Rcd 80921 (1992), *aff'd*, *Capital Network Systems, Inc. v. FCC*, 28 F.3d 201 (D.C. Cir. 1994) (*Capital Network*)).

⁴⁸² See TRA Comments at 5; MGC Communications Comments at 13; MCI Comments at 4; Cablevision Lightpath, Inc. and Nextlink, Inc. Comments at 3. See also *United Artists Payphone Corp. v. New York Tel. Co.*, 8 FCC Rcd 5562 (1993) (*United Artists*).

⁴⁸³ *United Artists*, 8 FCC Rcd at 5565-66. See also *Capital Network*, 28 F.3d. at 204 (taking notice of the principle of constructive ordering, but finding that the principle does not apply to the billing of incomplete calls).

discretion, we decline to address AT&T's concerns regarding CLEC access charges through a declaratory ruling.⁴⁸⁴ We therefore deny AT&T's petition.

189. In the *Access Reform First Report and Order*, however, the Commission committed to review the issue of CLEC access charges if there were evidence that CLECs were imposing unreasonable terminating access charges.⁴⁸⁵ The *AT&T Petition for Declaratory Ruling*, the comments provided in support of it,⁴⁸⁶ and the Bureau's recent decision in *MGC Communications*⁴⁸⁷ suggest the need to revisit the issue of CLEC access rates.⁴⁸⁸ Accordingly, in the accompanying Notice, we initiate a rulemaking to examine CLEC originating and terminating access rates.⁴⁸⁹

VIII. NOTICE OF PROPOSED RULEMAKING

A. Geographic Deaveraging for Switched Access Services

190. In this section, we seek comment on whether to amend our Part 69 rules to permit price cap incumbent LECs to deaverage interstate common line and traffic-sensitive access charges within study areas without a competitive showing. Currently, Section 69.3(e)(7) of our rules requires an incumbent LEC to charges rates for access elements that are averaged across each of its study areas.⁴⁹⁰

⁴⁸⁴ See SBC Comments at 6-7 (requesting that the Commission issue a notice of proposed rulemaking for further comment before deciding the matter because the decision may affect other parties and practices). We note that several parties have raised a number of other substantive objections to AT&T's petition that we need not consider because we are denying the petition on procedural grounds. See, e.g., BellSouth Comments at 3; Total Telecommunication Services Comments at 4-10; MGC Communications Comments at 5; CTSI Comments at 2 (AT&T's petition violates the interconnection policies of Telecommunications Act of 1996).

⁴⁸⁵ *Access Reform First Report and Order*, 12 FCC Rcd at 16141-42.

⁴⁸⁶ See *AT&T Declaratory Ruling Petition*; Cable & Wireless Comments at 1; U S West Comments at 1; Sprint Comments at 1.

⁴⁸⁷ *MGC Communications*, File No. EAD 99-002, Memorandum Opinion and Order, DA 99-1395.

⁴⁸⁸ Although we are initiating a rulemaking into the issue of CLEC access charges, we take no position on the reasonableness of these charges at this time. We merely wish to reexamine the issue in light of the arguments filed both in support of and in opposition to the *AT&T Declaratory Ruling Petition*. For example, the comments opposing AT&T's Petition argue that CLECs may have justifiably higher access charges due to their limited geographical scope and scale and their different cost structures.

⁴⁸⁹ See, e.g., *British Caledonian Airways Ltd.*, 584 F.2d at 993.

⁴⁹⁰ 47 C.F.R. § 69.3(e)(7). A study area is a geographical segment of a carrier's telephone operations. Generally, a study area corresponds to a carrier's entire service territory within a state. Thus, carriers operating in

191. *Common Line Basket.* In the *Access Reform NPRM*, the Commission requested comment on deaveraging all interstate access rate elements except for the subscriber line charge (SLC) (and the primary interexchange carrier charge (PICC), which did not exist at the time).⁴⁹¹ At that time, however, the Commission proposed to permit deaveraging only upon a showing of the degree to which local markets are open to competition.⁴⁹² We now seek comment on whether to permit incumbent LECs to deaverage common line access elements without a competitive showing. To the extent that parties advocate conditioning deaveraging upon satisfaction of a competitive showing, we seek comment on the appropriate showing and the procedure by which evidence should be presented and evaluated.⁴⁹³

192. We also seek comment on whether to condition an incumbent LEC's authority to deaverage common line access elements on certain regulatory developments, such as deaveraging of unbundled network elements in accordance with our rules,⁴⁹⁴ or establishment of explicit universal service high cost support mechanisms, and, if so, how. Should we impose these conditions in addition to any competitive showing that we may require? We note that, where unbundled network elements are deaveraged, continuing to require incumbents to charge access rates that are averaged across the study area may foreclose the incumbent LEC from meeting competition from unbundled network elements in low-cost areas. Similarly, an incumbent LEC's

more than one state typically have one study area for each state, and carriers operating in a single state typically have a single study area. Carriers perform jurisdictional separations at the study area level. For jurisdictional separations purposes, the Commission adopted a rule freezing study area boundaries effective November 15, 1984. Part 36 of the Commission's Rules, 47 C.F.R., Part 36, Appendix-Glossary, definition of "Study Area." See *MTS and WATS Market Structure, Amendment of Part 67 of the Commission's Rules and Establishment of a Joint Board*, CC Docket Nos. 78-72 and 80-286, 49 Fed. Reg. 48325 (Dec. 12, 1984), adopted by the Commission, 50 Fed. Reg. 939 (Jan. 8, 1985). Section 69.123 permits incumbents to deaverage rates for services in the trunking basket except for the transport interconnection charge (TIC). In Section V, *supra*, we grant incumbent LECs greater flexibility to deaverage rates for these services.

⁴⁹¹ *Access Reform NPRM*, 11 FCC Rcd at 21433.

⁴⁹² For further discussion and analysis of this proposal, see Section VI.C.1, *supra*.

⁴⁹³ We note that, if we permit incumbent LECs to deaverage common line and/or traffic-sensitive charges, IXCs may face significantly differing access costs within LEC study areas. This may increase pressure on IXCs to deaverage interstate interexchange service rates in a manner that conflicts with section 254(g) of the Act, which requires IXCs to charge subscribers in rural and high cost areas rates no higher than rates charged to subscribers in urban areas and to charge subscribers in each state rates no higher than rates charged in any other state. 47 U.S.C. § 254(g). See also MCI Oct. 26 Comments at 32.

⁴⁹⁴ See 47 C.F.R. § 51.507(f) (requiring states to deaverage UNEs across at least three geographic zones); ALTS Oct. 26 Comments at 9. We recently issued a *sua sponte* stay of Section 51.507(f) that will remain in effect until six months after the Commission issues its order in CC Docket No. 96-45, finalizing and ordering implementation of high-cost universal service support for non-rural local exchange carriers under section 254 of the Act. See *Implementation of the Local Competition Provisions of the Telecommunications Act of 1996*, CC Docket No. 96-98, FCC No. 99-86, Stay Order (rel. May 7, 1999).

averaged rates will be below that LEC's cost in high-cost areas, thus discouraging competitive entry in those areas. We also seek comment on whether incumbent LECs should be required, as opposed to merely permitted, to deaverage certain or all common line access rate elements based on any conditions, such as the deaveraging of unbundled network element rates in a state.

193. Currently, incumbent LECs recover interstate common line costs through the SLC, PICC, and carrier common line charge (CCLC). The SLC and PICC are flat-rated charges that vary by class of customer, *e.g.*, multi-line business, single-line business, primary residential line, and additional residential lines, subject to various caps.⁴⁹⁵ The CCLC is a per-minute charge that does not vary by class of customer.⁴⁹⁶ The SLC is assessed directly on end users while the PICC and CCLC are assessed on IXCs. Incumbent LECs are required to recover their interstate-allocated common line costs first through SLCs (subject to caps), then from PICCs (again, subject to caps), and finally from the CCLC. As the SLC and PICC caps rise,⁴⁹⁷ the CCLC gradually decreases and will someday be eliminated.

194. Parties supporting the deaveraging of interstate common line access charges should comment on the appropriate means of distributing deaveraged cost recovery among such charges. We request comment on whether any deaveraging of the SLC and PICC should be subject to current caps on those charges. At present, our rules provide that, to the extent the SLC caps on all lines and the PICC ceilings on primary residential and single-line business (SLB) lines prevent recovery of the full common line revenues permitted by our price cap rules, incumbent LECs may recover the shortfall through non-primary residential (NPR) and multi-line business (MLB) PICCs.⁴⁹⁸ Thus, if primary residential and SLB SLCs and PICCs have reached their caps, NPR and MLB PICCs may be funding at least part of this shortfall, *i.e.*, subsidizing residential and SLB PICCs. This subsidy will decrease over time as the caps on the primary-residential and single-line business SLCs rise. To what degree should we condition deaveraging of common line rate elements on developments such as the elimination of the MLB PICC? What constraints, if any, should we place on the means by which certain foregone revenue may be recovered? For example, should we permit deaveraging only within a customer class and for a particular type of charge, *e.g.*, prohibit incumbent LECs from recovering foregone SLC revenue through the CCLC or prohibit incumbent LECs from raising the NPR SLC to fund lower MLB SLCs?

195. Further, we seek comment on the means of recognizing any geographic variation in common line costs, *i.e.*, methods of defining geographic pricing zones. Many states have defined at least three geographic zones for the pricing of unbundled loops pursuant to section 252(d)(1)

⁴⁹⁵ 47 C.F.R. §§ 69.152, 69.153.

⁴⁹⁶ 47 C.F.R. § 69.154.

⁴⁹⁷ *See* 47 C.F.R. §§ 69.152(k), 69.153.

⁴⁹⁸ 47 C.F.R. § 69.153(d).

of the Act.⁴⁹⁹ Universal service reform also may require defining zones to reflect different cost characteristics.⁵⁰⁰ We seek comment on whether geographic pricing zones for common line charges should be based on UNE or universal service zones or, perhaps, trunking basket service zones.⁵⁰¹ Parties are invited to suggest additional bases for establishing geographic zones. For example, should we require LECs to establish identical geographic pricing zones for all access elements?

196. We seek comment on whether to permit incumbent LECs to define their own zones. If so, should we place any constraints on incumbent LEC zone pricing plans for common line service? For example, must an incumbent LEC demonstrate that such zones are based on cost? If so, how? Should there be a limit on the number or size of such zones? We note, for example, that in the accompanying Order we grant incumbent LECs greater flexibility to deaverage rates for services in the trunking basket, but we require each zone, except the highest-cost zone, to account for at least 15 percent of the incumbent's trunking basket revenues in the study area.⁵⁰²

197. In addition, we seek comment on the procedures by which the Commission might permit incumbent LECs to define common line access charge zones. Should we require parties to submit for prior approval such zone pricing plans in advance of tariff filings, as we initially required for special access and switched transport zone pricing plans?⁵⁰³ If so, what information should we require parties to submit?

198. We also seek comment on whether the use of different zones for unbundled network elements, universal service, and access charges would create inefficiencies and arbitrage

⁴⁹⁹ See, e.g., Consolidated Petition of AT&T Communications, Inc., and MCI Telecomms. Corp. and Affiliates for Arbitration with Southwestern Bell Tel. Co., Case Nos. TO-97-40 and TO-97-67, at 35-36 (Mo. P.S.C. Dec. 11, 1996); Petition of AT&T Communications, Inc. for Arbitration with GTE Hawaiian Tel. Co., Docket No. 96-0329, Decision No. 15528 at 36 (Haw. P.U.C. Apr. 18, 1997). Section 51.507(f) requires states to create at least three geographic rate zones for unbundled network elements. 47 C.F.R. § 51.507(f). We note that despite the fact that Section 51.507(f) of our rules was ineffective when most states determined whether to deaverage geographically unbundled network element rates, many states, such as those listed here, chose to do so.

⁵⁰⁰ Federal-State Joint Board on Universal Service, CC Docket 96-45, Forward-Looking Mechanism for High Cost Support for Non-Rural LECs, CC Docket No. 97-160, Access Charge Reform, CC Docket No. 96-262, Seventh Report and Order and Thirteenth Order on Reconsideration in CC Docket No. 96-45 and Fourth Report & Order in CC Docket No. 96-262, 14 FCC Rcd 8078, 8126-30 (1999) (*Universal Service Seventh Report and Order*).

⁵⁰¹ See, e.g., *id.* We relax our rules concerning zone pricing of trunking basket services in Section V, *supra*.

⁵⁰² See Section V, *supra*. We adopt that requirement to ensure that incumbent LECs cannot define zones that are, for all practical purposes, specific to particular customers.

⁵⁰³ See, e.g., *Special Access Expanded Interconnection Order*, 7 FCC Rcd at 7456-57.

opportunities.⁵⁰⁴ We seek comment on alternative approaches for ensuring that the zones for these different purposes are compatible and that geographic zones generally reflect cost differences.⁵⁰⁵

199. *Traffic-sensitive basket.* The traffic-sensitive basket includes local switching, information, data base access services, billing name and address, local switching trunk ports, and signaling transfer point port termination.⁵⁰⁶ In the past, parties have argued that traffic-sensitive service costs vary little, if at all, within study areas.⁵⁰⁷ Furthermore, we are unaware of any state commission that has deaveraged an incumbent LEC's rates for unbundled local switching. We invite parties to submit further evidence regarding the degree to which costs of traffic-sensitive services may vary geographically within incumbent LEC study areas and whether any such variance warrants permitting incumbent LECs to deaverage traffic-sensitive charges. We seek comment on whether we should establish similar or identical rules concerning any deaveraging of traffic-sensitive elements as we may establish for common line elements. For example, should we establish similar or identical rules regarding the methods and procedures for establishing rate zones for traffic-sensitive services, to the extent that they should differ from common line or transport zones? In Section VIII.C, *infra*, we seek comment on replacing the existing per-minute or per-call local switching rate structure rules with a capacity-based rate structure. How might deaveraging of traffic-sensitive charges be affected by such changes in the switching rate structure?

B. Phase II Pricing Flexibility for Switched Service

200. In this section, we seek comment on Phase II pricing flexibility for common line and traffic-sensitive services, and the traffic-sensitive components of tandem-switched transport services offered by price cap incumbent LECs.⁵⁰⁸ We seek comment on the appropriate triggers for such relief and how Phase II relief for common line and traffic-sensitive services might differ

⁵⁰⁴ See *Universal Service Seventh Report and Order*, 14 FCC Rcd at 8128-29.

⁵⁰⁵ For example, different geographic zones may work for these purposes so long as the results are not widely disparate in any particular location.

⁵⁰⁶ 47 C.F.R. § 61.42(e)(2).

⁵⁰⁷ See, e.g., MCI Nov. 5 Reply Comments at 31-32, 36-37; Time Warner Oct. 26 Comments at 14.

⁵⁰⁸ As in our discussion of Phase I triggers for common line service, traffic-sensitive service, and traffic-sensitive components of tandem-switched transport service in Section VI.C.3, *supra*, references to "traffic-sensitive service" in this section include the traffic-sensitive components of tandem-switched transport service. The elements of tandem-switched transport are discussed in Section VI.C.3, *supra*. See also 47 C.F.R. § 69.111. We address Phase II pricing flexibility for the dedicated portion of tandem switched transport in Section VI.C.2, *supra*.

from Phase II relief for dedicated transport and special access services that we establish in the Order accompanying this Notice.⁵⁰⁹

1. Triggers

201. As we discuss in the Order, Phase II relief is warranted when an incumbent LEC demonstrates that competitors have established a significant market presence, *i.e.*, that competition for a particular service within a geographic area is sufficient to preclude the incumbent from exploiting any monopoly power over a sustained period.⁵¹⁰ In the Order, we conclude that an incumbent price cap LEC is entitled to Phase I pricing flexibility for common line and traffic-sensitive services in an MSA when it demonstrates that competitors, in aggregate, offer service over their own facilities to at least 15 percent of incumbent LEC customer locations in the MSA.⁵¹¹ We seek comment on whether we should predicate Phase II relief for these services on a similar showing that competitors offer these services over their own facilities but adopt a threshold higher than 15 percent, and, if so, what this threshold should be. If a different approach is warranted for Phase II relief, what should the relevant test(s) be?

202. In the Order, we decline to include customer locations served by mobile wireless competitors toward satisfaction of the Phase I trigger, due to the administrative burdens of determining when mobile wireless serves as a substitute for incumbent LEC wireline service.⁵¹² Should we exclude mobile wireless service from the Phase II trigger, as well? Are there reasons to believe that mobile wireless substitution will be easier or more important to measure in the context of requests for Phase II relief?

203. Some parties, such as Bell Atlantic and USTA, have proposed that we allow incumbent LECs to seek pricing flexibility for these services with respect to certain classes of customer, such as multi-line business customers, based on meeting triggers applicable only to a particular class of customers.⁵¹³ We conclude, above, that we should not allow such separate showings for Phase I relief because we wish to encourage competition for both high-volume business customers and residential and low-volume business customers.⁵¹⁴ Should we decline to permit such separate showings for Phase II pricing flexibility for common line and traffic-sensitive services?

⁵⁰⁹ See Section VI.C.5.c, *supra*.

⁵¹⁰ See Section VI.C.5, *supra*.

⁵¹¹ See Section VI.C.3, *supra*.

⁵¹² See *id.*

⁵¹³ Bell Atlantic *ex parte* statement of April 27, 1998, at 27; USTA *ex parte* statement of June 1, 1999, at 2.

⁵¹⁴ See Section VI.C.3, *supra*.

2. Relief

204. In the Order, we conclude that an incumbent LEC that qualifies for Phase II relief for dedicated transport and special access services need not comply with Part 69 rate structure rules with respect to these services, may remove these services from price caps, and may file tariffs for these services on one day's notice (so long as such tariffs are made generally available).⁵¹⁵ Should we grant similar Phase II relief for common line and traffic-sensitive service? If not, what relief is warranted upon satisfaction of the Phase II triggers for these services?

205. We also seek comment on whether we should impose certain safeguards with respect to Phase II relief for common line and traffic-sensitive services that we do not impose with respect to dedicated transport and special access services. Currently, incumbent LECs recover some of their common line costs through the SLC, which is assessed directly on the end user. As a condition of granting Phase II relief for common line services, should we require price cap incumbent LECs to charge some or all of the common line charge directly to the end user? If only some of the costs should be charged directly to the end user, on what basis should we establish a limit? What are the advantages and disadvantages of prohibiting some or all common line cost recovery from IXCs? What additional safeguards might we require? For example, should we limit in any way the extent to which incumbent LECs recover local switching costs from IXCs, as opposed to end users?

206. We also seek comment on the relationship between granting price cap LECs Phase II pricing flexibility for common line and traffic-sensitive services and their receipt of universal service support with respect to these services. If, for example, a price cap LEC is entitled to universal service support for a line if its costs⁵¹⁶ exceed a particular benchmark, should we prohibit the LEC from charging a rate above that benchmark? Similarly, if eligibility for high cost support were determined on the basis of a revenue benchmark, should common line charges be limited by that benchmark? In what other ways should Phase II pricing flexibility for common line and traffic sensitive-services be affected or limited by universal service concerns?

⁵¹⁵ See Section VI.C.4.c, *supra*.

⁵¹⁶ Cost could be determined in a number of ways, including, but not limited to, costs associated with a particular line or a price cap LEC's average cost per line in a study area. See, e.g., *Universal Service Seventh Report and Order*, 14 FCC Rcd at 8126-30.

C. Switching Issues

1. Local Switching

a. Introduction

207. We solicit comment on replacing the existing per-minute or per-call local switching rate structure rules with a capacity-based rate structure.⁵¹⁷ Specifically, should we require price cap LECs to charge for local switching on the basis of the number of trunks connected to a given end office switch? Below, we seek comment on a capacity-based local switching rate structure. We then consider adding a factor to the traffic-sensitive PCI formula, designed to serve a function similar to the "g" factor in the common line PCI formula, in order to give access customers a reasonable portion of the benefits of demand growth. Finally, we seek comment on whether to require LECs to decrease their traffic-sensitive PCIs, so that LECs would not retain the benefits of past demand growth on a going-forward basis.

b. Background

208. The Commission's long-standing policy is to require, to the extent possible, rate structures to reflect the manner in which carriers incur costs. Inefficient rate structures lead to inefficient and undesirable economic behavior, and create an implicit subsidy between high-volume users and low-volume users.⁵¹⁸ For example, a rate structure that recovers non-traffic-sensitive costs through traffic-sensitive access rates increases the per-minute rates paid by IXCs and long-distance companies, thereby artificially suppressing demand for interstate long-distance services, and requiring high-volume customers to pay charges in excess of the costs of providing their service. Meanwhile, low-volume customers pay rates that are less than the cost of the dedicated equipment.⁵¹⁹

209. The Part 69 rules require incumbent LECs to charge per-minute rates for local switching,⁵²⁰ based on the Commission's 1983 finding that local switching services were traffic-sensitive.⁵²¹ In the *Access Reform First Report and Order*, the Commission recognized that the local switching costs associated with line cards and trunk ports are non-traffic-sensitive,⁵²² and revised the access charge rate structure to require incumbent LECs to recover those costs through

⁵¹⁷ We address tandem switching issues later in this Order. We do not consider revising Section 69.125, the rate structure rules for dedicated signalling transport services, or Section 69.129, the rate structure rules for signalling for tandem switching. We reviewed our SS7 signalling rate structure rules in the *Access Reform First Report and Order*, 12 FCC Rcd at 16089-91, and we see no reason to re-open those issues at this time.

⁵¹⁸ *Access Reform First Report and Order*, 12 FCC Rcd at 15995-96, 15998; Investigation of Interstate Access Tariff Non-Recurring Charges, CC Docket No. 85-166, Phase I, Part 3, 2 FCC Rcd 3498, 3501-02 (1987).

⁵¹⁹ See *Access Reform First Report and Order*, 12 FCC Rcd at 15996, 16008.

⁵²⁰ See, e.g., 47 C.F.R. § 69.106; *Access Charge Order*, 93 FCC 2d at 304 (1983) (*Access Charge Order*).

⁵²¹ *Access Charge Order*, 93 FCC 2d at 304-05.

⁵²² Line cards connect subscriber lines to the switch, and trunk ports connect interoffice trunks to the switch. *Access Reform First Report and Order*, 12 FCC Rcd at 16034.

non-traffic-sensitive rates.⁵²³ The Commission also concluded that the record at that time was not adequate to determine whether or to what extent the remaining local switching costs were traffic-sensitive or non-traffic-sensitive, and maintained the requirement that LECs recover those costs through traffic-sensitive rates.⁵²⁴ The Commission did, however, revise the local switching rate structure to permit, but not require, incumbent LECs to establish per-call local switching charges, in addition to per-minute rates.⁵²⁵

210. The Commission also considered the nature of switching costs in the *Local Competition Order*, in the context of establishing pricing rules for local switching unbundled network elements (UNEs). At least one party to that proceeding, the Washington Utilities and Transportation Commission, advocated a rate structure based on peak usage for local switching in 1996, arguing that a flat rate based upon the cost of providing capacity at peak load is possibly the most economically correct pricing mechanism.⁵²⁶ In the *Local Competition Order*, the Commission concluded that shared local switching costs, *i.e.*, local switching costs other than the costs of line cards and trunk ports, could be reasonably recovered through either flat or per-minute rate structures, and permitted state public service commissions to adopt either traffic-sensitive or non-traffic-sensitive rate structures for local switching unbundled network elements (UNEs).⁵²⁷

c. Capacity-based Local Switching Rate Structure

211. If costs are driven by peak demand, as suggested by the Washington Utilities and Transportation Commission, then local switching costs do not vary directly with total switched minutes in most cases. In the *Access Reform First Report and Order*, however, the Commission considered and rejected a proposal to require incumbent LECs to develop peak and off-peak rates for local switching, because the Commission concluded that LECs would have difficulty determining peak and off-peak hours with any degree of certainty, due to geographic, user-type, and service considerations. In addition, charging different prices for calls made during different times of the day may cause customers to shift their calling to less expensive times, thereby resulting in different peak times.⁵²⁸ We know of no reason to revisit our conclusion to reject peak

⁵²³ *Id.* at 16035-36.

⁵²⁴ *Id.* at 16040.

⁵²⁵ *Id.* at 16041-46.

⁵²⁶ See Washington Utilities and Transportation Commission Comments in CC Docket No. 96-98, at 29-30, summarized in *Local Competition Order*, 11 FCC Rcd at 15900.

⁵²⁷ *Local Competition Order*, 11 FCC Rcd at 15878-79, 15905.

⁵²⁸ *Access Reform First Report and Order*, 12 FCC Rcd at 16046-47. See also *Interconnection Between Local Exchange Carriers and Commercial Mobile Radio Service Providers*, CC Docket No. 95-185, Notice of Proposed

and off-peak rates for local switching. Instead, we consider adopting a capacity-based local switching rate structure. If an increase in total minutes or total number of calls would lead to a measurable increase in local switching costs only when the increase at times of peak demand is so great as to require an expansion of switch capacity, then a capacity-based rate structure may reflect the manner in which incumbent LECs incur local switching costs better than the existing rate structure, without the difficulties raised by determining peak and off-peak hours.

212. A capacity-based local switching rate structure may offer other benefits. Most notably, if IXCs purchased a greater portion of their access services through non-traffic-sensitive rates, they would have an incentive to develop off-peak pricing plans to encourage long distance consumers to make more or longer off-peak calls. This, in turn, would encourage more efficient use of the public switched network. Such pricing plans are also likely to extend a greater share of the benefits of access cost reductions to residential long distance customers, because they are more likely than business customers to be off-peak users.

213. Accordingly, we seek comment on revising Section 69.106(f)(2) of the Commission's Rules to require price cap LECs to develop capacity-based local switching charges rather than per-minute charges. For example, should we require price cap LECs to calculate a capacity-based local switching charge by considering the aggregate number of trunks switched by the LEC? If local switching rates are based on number of trunk-side connections, how should we treat local switching access services with line-side connections, such as Feature Group A?⁵²⁹

214. We also invite comment on the level of detail that we should specify in our local switching rate structure rules. Specifically, should Section 69.106 require incumbent LECs to charge for local switching based on the DS-1 equivalent capacity of an access customer's trunks connected to a particular end office switch, so that the DS-3 charge would be 28 times the DS-1 charge? Should we instead establish some initial rate relationship between DS-1 and DS-3, as the Commission did for transport?⁵³⁰ Is there some other rate structure we could prescribe that would better reflect how local switching costs vary with increases in peak demand that necessitate expansion of switch capacity? Alternatively, should we permit LECs to develop their own capacity-based local switching rate structures, and examine the reasonableness of those structures in the tariff review process?

Rulemaking, 11 FCC Rcd 5020, 5042 (1996).

⁵²⁹ For purposes of this Order, Feature Group A is line side access to telephone company end office switches with an associated seven digit telephone number for the customer's use in originating communications from and terminating communications to an IXC's interstate service or a customer-provided interstate communications capability. *See* Contel of Indiana, Inc., Memorandum Opinion and Order, 3 FCC Rcd 4298, 4303 n.5 (Com. Car. Bur., 1988) (*citing* Exchange Carrier Association Tariff F.C.C. No. 1, pp. 157-59).

⁵³⁰ The Commission adopted a presumption of reasonableness for initial transport rates if incumbent LECs developed DS-3 and DS-1 rates with a ratio of 9.6-to-1. *See* 47 C.F.R. § 69.108, Transport Rate Structure and Pricing, CC Docket No. 91-213, First Reconsideration Order, 8 FCC Rcd 5370 (1993).

215. We tentatively conclude that a capacity-based local switching rate structure, if it indeed reflects cost causation, would not artificially disadvantage smaller IXCs in the market for long distance services. As the Commission concluded in its decision to eliminate the unitary rate structure for tandem-switched transport, rules that protect small IXCs in competition with AT&T, or other large IXCs, are unnecessary because the long-distance market is competitive.⁵³¹ We seek comment on this conclusion.

216. In addition, we invite parties to comment on whether permitting volume and term discounts for switched access services, as we propose above, would exacerbate any negative impact for smaller IXCs. We invite comment on whether a resale market for local switching services is likely to develop, and whether such a development would mitigate any negative impact that smaller IXCs might face. We note that the Commission already has a policy prohibiting carriers from placing restrictions on resale in their tariffs.⁵³² We invite comment on whether any further resale protection is necessary. Alternatively, we invite comment on whether we should permit or require incumbent LECs to retain existing per-minute or per-call local switching charges concurrently with non-traffic-sensitive charges. Finally, we invite parties to make other proposals.

d. Revision of Traffic-Sensitive PCI Formula

217. In the *LEC Price Cap Order*, the Commission concluded that it needed to adopt a formula for the common line basket PCI different from the PCI formula for the other baskets, to reflect that carrier common line rates are traffic-sensitive even though common line costs are non-traffic-sensitive.⁵³³ Accordingly, the Commission included a "g" factor in the common line PCI formula, where g represents per-minute growth per access line.⁵³⁴ The Commission found that including g would give all the benefits of demand growth to IXCs, while excluding g would give all the benefits of demand growth to LECs.⁵³⁵ The Commission incorporated g/2 as a

⁵³¹ *Access Reform First Report and Order*, 12 FCC Rcd at 16060.

⁵³² *Resale and Shared Use of Common Carrier Services and Facilities*, 60 FCC 2d 261 (1976), *cited in, e.g.*, *Metro Communications, Inc., v. Ameritech Mobile Communications, Inc.*, 12 FCC Rcd 13083, 13092 (Wireless Tel. Bur., 1996).

⁵³³ *LEC Price Cap Order*, 5 FCC Rcd at 6793.

⁵³⁴ *Id.* at 6794. The g factor is defined as "the ratio of minutes of use per access line during the base period, to minutes of use per access line during the previous base period, minus 1." *See* Section 61.45(c)(1) of the Commission's Rules, 47 C.F.R. § 61.45(c)(1).

⁵³⁵ *LEC Price Cap Order*, 5 FCC Rcd at 6794. Setting g at zero would mean that the common line PCI is unaffected by demand growth. In this case, the LEC would keep all the increased revenue resulting from that demand growth. Alternatively, incorporating a "full g" into the common line PCI would require LECs to reduce their common line PCIs to reflect all demand growth. In this case, the IXC would receive all the benefits of demand growth in the form of lower common line rates.

compromise, because it found that both IXCs and LECs contribute to demand growth.⁵³⁶ The Commission did not attempt to measure at that time the relative contributions to demand growth made by IXCs and LECs, and expressly stated that a 50-50 split was not a precise reflection of the LECs' ability to influence usage.⁵³⁷

218. If we decide to adopt a capacity-based local switching rate structure, it may be appropriate to include a factor in the traffic-sensitive PCI formula similar to the g factor currently in the common line PCI formula. Although, as discussed above, it is possible that a capacity-based local switching rate structure reflects costs better than a per-minute rate structure, capacity-based rates may not reflect local switching costs perfectly. More specifically, an increase in the number of trunks at a switch may not lead to a proportional increase in local switching costs. Rather, such an increase in trunks may lead to a measurable increase in local switching costs only when the increase of peak demand is so great as to require an expansion of switch capacity. If this is the case, then local switching costs may not vary directly with changes in per-trunk demand. We tentatively conclude that it would not be reasonable to permit incumbent LECs to retain all the benefits of trunk growth if they are not exclusively responsible for encouraging that growth. Accordingly, we invite parties to discuss whether the traffic-sensitive PCI formula should include a "q" factor, similar to the "g" factor in the common line PCI formula, to incorporate growth in number of trunks into the traffic-sensitive PCI formula. We also invite comment on whether to adopt a q factor if we decide not to revise the local switching rate structure as proposed above, or if we permit or require LECs to offer both usage-sensitive and capacity-based local switching rates.

219. We also request comment on the definition of this q factor if we decide to adopt it. For example, should it be based on the change in DS-1 equivalent capacity? Should price cap LECs measure changes in DS-3 equivalent capacity on some basis other than DS-1 equivalents? We intend to base any q factor we adopt on data that price cap LECs currently collect, or data that price cap LECs could collect at little or no additional cost. We therefore invite any party proposing a q factor definition to discuss whether and to what extent its definition would affect price cap LECs' data collection costs.

220. We also invite comment on the relationship between any q factor we add to the traffic-sensitive PCI formula and the g factor in the common line PCI formula. Specifically, the common line PCI formula currently includes "g/2", because the Commission found in the *LEC Price Cap Order* that both LECs and IXCs contribute to demand growth, and that "g/2" gives both IXCs and LECs a reasonable share of the benefits of per-minute demand growth.⁵³⁸ We note that we invite comment below on increasing the g factor in the common line PCI formula from g/2

⁵³⁶ *Id.* at 6795.

⁵³⁷ *Id.*

⁵³⁸ *Id.*

to a full g.⁵³⁹ We therefore invite comment on whether any q factor we adopt for the traffic-sensitive PCI formula should be consistent the common line g factor, as revised in this proceeding. Alternatively, we invite comment on whether we should base the q factor in the traffic-sensitive basket on a different fraction than the common line g factor, because local switching does not make up all of the traffic-sensitive basket.⁵⁴⁰

e. Adjustment to Traffic-Sensitive PCIs

221. In the *LEC Price Cap Order*, the Commission concluded that failing to include a "g" factor in the common line PCI formula would not give IXCs any incentive to become more productive through encouraging demand growth.⁵⁴¹ In other words, failure to include "g" would have created an imbalance between the interests of IXC customers and LEC stockholders. This imbalance would have been substantially similar to the imbalance found by the Commission in the 1995 *LEC Price Cap Performance Review Order*. In that Order, the Commission found that it had previously set the X-Factor lower than it intended, due to the inclusion of 1984-85 data in one of the original X-Factor studies.⁵⁴² The Commission observed that LECs were supposed to become more efficient to earn more than would have been permitted under rate-of-return regulation, and ratepayers were to benefit from rates reduced to the level that would provide this challenge.⁵⁴³ The Commission then concluded that some portion of the LECs' earnings were obtained without any productivity improvements, and rates were not as low as the Commission intended.⁵⁴⁴

222. If we find that local switching costs are more appropriately recovered through capacity-based charges, then permitting LECs to charge per-minute local switching rates since LEC price cap regulation was adopted in 1991, without including a q factor in the traffic-sensitive PCI formula, may have created an imbalance between the interests of IXC customers and LEC stockholders, similar to the imbalance found in the *LEC Price Cap Performance Review Order*

⁵³⁹ See Section VIII.D.1, *infra*.

⁵⁴⁰ The services other than local switching in the traffic-sensitive basket are: (1) information; (2) database access services; (3) billing name and address (BNA); (4) trunk ports; and (5) signalling transfer point port termination. See Section 61.42(e)(1) of the Commission's Rules, 47 C.F.R. § 61.42(e)(1). These services generate less revenue than local switching. Local switching generally makes up about 2/3 or 3/4 of the revenues associated with the traffic-sensitive basket.

⁵⁴¹ *LEC Price Cap Order*, 5 FCC Rcd at 6795.

⁵⁴² *LEC Price Cap Performance Review Order*, 10 FCC Rcd at 9069.

⁵⁴³ *Id.* at 9070.

⁵⁴⁴ *Id.*

resulting from the 1984-85 data discussed above.⁵⁴⁵ The existing per-minute rate structure provides the incumbent LEC with more revenue whenever per-minute demand increases, regardless of whether the LEC's costs have increased. This revenue increase results in higher earnings for the LEC, regardless of whether it has become more productive in its provision of local switching. This could explain, at least in part, why overall LEC earnings have increased in recent years, even though the Commission increased the X-Factor in 1995 and 1997. Furthermore, such an imbalance would remain embedded in the incumbent LECs' traffic-sensitive PCIs, regardless of whether we correct it by revising the local switching rate structure or including a q factor in the traffic-sensitive PCI formula on a forward-looking basis. Moreover, using per-minute charges without simultaneously using a q factor may have exacerbated this imbalance. Accordingly, we seek comment on whether to require a one-time downward adjustment of the LECs' traffic-sensitive PCIs to correct for any imbalance on a going-forward basis, similar to the adjustment required in the *Price Cap Performance Review Order*.⁵⁴⁶ Specifically, price cap LECs were required to reduce their PCIs to the levels that would have resulted had the Commission excluded the 1984 data point in its 1990 X-Factor determination. In this proceeding, we invite comment on whether price cap LECs should be required to reduce their traffic-sensitive PCIs to the levels that would have resulted had the Commission incorporated a q factor in the traffic-sensitive PCI formula that took effect in 1991. Alternatively, we invite comment on basing this PCI adjustment on a more recent year.

2. Tandem-Switched Transport

223. We solicit comment on whether we should revise the rate structure for tandem-switched transport, for the same reasons we consider revising the local switching rate structure discussed above.⁵⁴⁷ We also invite comment on all the issues we discussed in this section above, to the extent that they are relevant to tandem switching. Is tandem-switched transport different from local switching, such that capacity-based tandem switching rates are inappropriate? If capacity-based tandem switching rates are appropriate, how would they be developed? For example, they could be established based on the number of trunks between the IXC POP and the tandem switch.

224. If the tandem switching rate structure should remain usage-based, how could we prevent larger IXCs from maintaining an inadequate number of trunks to the LEC switch, and using tandem switching as inexpensive overflow? Could LECs establish a rate for IXCs that only use tandem-switched transport, and recover a higher rate for overflow from local switching? If so, we recognize that IXCs rely exclusively on tandem switching for certain routes, and so we

⁵⁴⁵ See AT&T *ex parte* statement of Feb. 19, 1999, at 6 (alleging a 45 percent rate of return for all price cap LECs in the traffic-sensitive basket).

⁵⁴⁶ *Price Cap Performance Review Order*, 10 FCC Rcd at 9069-73. See also *Bell Atlantic v. FCC*, 79 F.3d at 1204-05 (affirming *Price Cap Performance Review Order* on this issue).

⁵⁴⁷ See Section VIII.C.1.c, *supra*.

believe that an overflow rate should be applied only on routes for which an IXC also has trunks to the local switch.

225. In addition, we invite parties to discuss whether we should add a q factor to the trunking basket PCI, if we conclude that tandem switching costs are more appropriately recovered through capacity-based rates. If so, how should that q factor be defined? Parties may also discuss whether we should adjust the trunking basket PCI to reflect that price cap LECs have recovered essentially flat costs through traffic-sensitive rates since LEC price cap regulation took effect in 1991, similar to the traffic-sensitive PCI adjustment we propose above.

D. Price Cap Issues

1. Common Line Issues

a. G Factor

226. The Commission proposed revisions to the common line formula in the *Price Cap Fourth FNPRM*, which established part of the record for the *Price Cap Fourth Report and Order*.⁵⁴⁸ The Commission decided against revising the common line formula in the *Price Cap Fourth Report and Order*, however, because it expected the common line PCI formula to be eliminated when per-minute CCL charges were eliminated, as a result of rules adopted in the *Access Reform First Report and Order*.⁵⁴⁹ The transition away from per-minute CCL charges, however, is progressing slowly for certain incumbent LECs. Accordingly, we take this opportunity to review some of the common line issues addressed in the *Price Cap Fourth Report and Order*.

227. Above, we explain why the Commission included a "g/2" term in the common line formula when it adopted LEC price cap regulation.⁵⁵⁰ Later, in 1995, the Commission found evidence that IXCs influence per-minute demand growth more than LECs, and considered increasing the g factor to reflect the IXCs' greater contribution to demand growth.⁵⁵¹ The Commission did not revise the common line formula at that time, however, because it found that the separate common line formula could be eliminated completely if it adopted a moving average TFP-based X-Factor. The moving average X-Factor would incorporate the effects of growth into

⁵⁴⁸ *Price Cap Fourth FNPRM*, 10 FCC Rcd at 13680-81.

⁵⁴⁹ *Price Cap Fourth Report and Order*, 12 FCC Rcd at 16710 (citing *Access Reform First Report and Order*, 12 FCC Rcd at 16027). In the *Access Reform First Report and Order*, the Commission adopted rules to phase out per-minute CCL charges through imposition of PICCs, and to replace the current common line PCI formula with the formula used for other PCI baskets when per-minute CCL charges are eliminated. *Access Reform First Report and Order*, 12 FCC Rcd at 16027-28).

⁵⁵⁰ Section VIII.C.1.d, *supra*.

⁵⁵¹ *LEC Price Cap Performance Review Order*, 10 FCC Rcd at 9078-80.

the PCI, and a separate g factor would no longer be necessary.⁵⁵² Although the Commission did not adopt a moving average-based X-Factor in the 1997 *Price Cap Fourth Report and Order*, it nevertheless decided against revising the common line formula, because the Commission expected per-minute CCL rates and the separate common line formula to be phased out relatively quickly as a result of common line rule revisions adopted concurrently in the *Access Reform First Report and Order*.⁵⁵³ Our access reform rules have not eliminated per-minute CCL charges for some companies as quickly as the Commission had anticipated. As a result, this issue warrants re-examination. We invite comment on whether the g factor in the common line PCI formula should be increased, and if so, whether it should be increased to a full "g." Increasing the "g" factor would cause the common line PCI to decrease more quickly, which in turn would cause the per-minute CCL rate to decrease more quickly. The g factor would still be eliminated when the CCL is eliminated in the access reform transition. Parties advocating a "g" factor between g/2 and g should specify what fraction of g they believe should be included in the common line PCI formula, and explain their reasons.⁵⁵⁴

b. Reflection of Revised Common Line Rate Structure in Common Line Formula

228. We have determined that as long as the multi-line business PICC exists, to the extent that the ratio of primary residential and single line business lines to non-primary residential and multiline business lines changes, the common line formula may create a windfall or shortfall for some LECs. Accordingly, we seek comment on revising the common line PCI rules to eliminate any such windfall or shortfall.

229. Prior to the *Access Reform First Report and Order*, price cap LECs recovered all their common line revenues through two charges: (1) flat monthly end user common line charges (EUCL), also known as SLCs, imposed on end users; and (2) per-minute CCLs imposed on IXCs.⁵⁵⁵ In the *Access Reform First Report and Order*, the Commission prescribed new flat common line rate elements, called PICCs, to be imposed on IXCs in most cases.⁵⁵⁶ PICC charges

⁵⁵² *Id.* at 9079-80.

⁵⁵³ *Price Cap Fourth Report and Order*, 12 FCC Rcd at 16709-10; *Access Reform First Report and Order*, 12 FCC Rcd at 16027-28.

⁵⁵⁴ The current rules require price cap LECs to replace the current common line PCI formula with the formula used for other PCI baskets when they eliminate per-minute CCL charges. *Access Reform First Report and Order*, 12 FCC Rcd at 16027-28; Section 61.45(c)(2) of the Commission's Rules, 47 C.F.R. § 61.45(c)(2). We do not contemplate revising the rules to permit or require price cap LECs to use the separate common line PCI formula after they have eliminated per-minute CCL charges.

⁵⁵⁵ *See Access Reform First Report and Order*, 12 FCC Rcd at 16018.

⁵⁵⁶ *Id.* at 16019-26. Incumbent LECs are permitted to impose PICC charges directly on end users that do not select a presubscribed interexchange carrier (PIC). *Id.* at 16019.

were designed to recover some of the revenues formerly recovered through per-minute CCL charges, and to annually increase until the per-minute CCL charge is phased out.⁵⁵⁷

230. PICCs on single-line business and primary residential lines were set initially so that the sum of the PICC and SLC applicable to each of these lines was less than the average revenue per line permitted under the price cap rules.⁵⁵⁸ Those PICCs will increase until the sum of the applicable PICC and SLC is equal to the maximum permitted revenue per line.⁵⁵⁹ During the interim, price cap LECs are allowed to recover this shortfall through PICCs on multiline business lines. As a result, during this interim period, single-line business and primary residential lines receive an explicit subsidy from multiline business lines.⁵⁶⁰

231. The growth rate of the amount received through this PICC subsidy ideally should be equivalent to the growth rate of primary residential and single-line business lines. The PICC subsidy, however, will grow too quickly or too slowly whenever the lines giving subsidy, multiline business lines,⁵⁶¹ grow at a different rate than the lines receiving subsidy, single-line business and residential lines. This subsidy increases disproportionately if multiline business lines grow more quickly than single-line business and primary residential lines. This subsidy fails to keep up with line growth if multiline business lines grow less quickly than single-line business and primary residential lines.

232. For example, assume that the average permitted revenue per line in Year 1 is \$6, and that the LEC provides 50 residential lines and 50 multiline business lines. Thus, the LEC is permitted \$300 in revenue for residential lines (50*6), and \$300 in multiline business lines (50*6). Assume also that the caps on SLCs and PICCs permit the LEC to collect \$4 for each residential line, and \$8 for each multiline business line. In this case, residential line charges recover only \$200 in revenue, and so need \$100 in subsidy. Multiline business lines recover \$400 of revenue, and so generate \$100 in subsidy. In this case, there is no windfall or shortfall in subsidy, and the LEC recovers an average of \$6.00 per line. Now assume that, in Year 2, multiline business lines grow from 50 to 70, while residential lines remain at 50, and everything else in Year 1 remains the

⁵⁵⁷ *Id.* at 16023.

⁵⁵⁸ *Id.* at 16020-21.

⁵⁵⁹ *Id.*

⁵⁶⁰ *Id.* at 16022. In some study areas, some or all of the non-primary residential PICC may also subsidize primary residential lines, depending, among other things, upon the relationship of the carrier common line revenues per line and the cap on the non-primary residential SLC. In addition, if PICCs on multiline business lines still do not enable a price cap LEC to recover all its permitted common line revenue, the LEC may recover those residual revenues through per-minute CCL charges assessed on originating minutes. *Id.*

⁵⁶¹ As discussed above, non-primary residential lines also provide subsidy in some cases, and so the growth rate of non-primary residential lines also affects this subsidy.

same. In this case, residential lines still require \$100 in subsidy. The LEC, however, would collect \$560 in revenue from each multiline business line (70*8). As a result, multiline business charges generate \$160 in subsidy. Because the LEC's residential lines require only \$100 in subsidy, the LEC receives a windfall of \$60 in this example, and would recover an average of \$6.33 per line. Thus, under our current rules, when calculating common line permitted revenue for the following year, the incumbent LEC would base those calculations on \$6.33 per line rather than \$6.00 per line.

233. If we permitted common line revenues to increase with the average growth rate of all common lines, we would eliminate the windfall or shortfall that now occurs whenever multiline business lines grow faster or slower than primary residential and single-line business lines. Accordingly, we invite comment on revising the formula in Section 61.46(d)(1) so that permitted common line revenues increase with the average growth rate of all common lines. We also invite interested parties to propose specific revisions to this formula. Finally, we solicit comment on whether any disproportionate increase or decrease in common line subsidy has created an imbalance between ratepayer and stockholder interests, of the kind we discussed at length in the *LEC Price Cap Performance Review Order*⁵⁶² and in this Section of this Order. If so, should we require price cap LECs to make exogenous adjustments to their common line PCIs to correct this imbalance on a going-forward basis?

2. Reorganization of Baskets and Bands

234. In the *Access Reform First Report and Order*, the Commission revised the local switching rate structure to require LECs to charge flat charges for dedicated trunk ports.⁵⁶³ Price cap LECs established these new rate elements in tariffs that took effect on January 1, 1998. Because of the relative levels of demand for trunk ports and local switching, a price cap LEC could, in subsequent tariff filings, reduce its flat trunk port charges substantially, and make up that revenue through a relatively small increase in its per-minute local switching charge. Some price cap LECs did in fact reduce their recently-created flat trunk port charges substantially in their 1998 annual access filings, and some carriers have eliminated those charges in some study areas in their 1999 annual access filings.⁵⁶⁴ We invite comment on whether we should modify our price cap rules to place flat charges and traffic-sensitive charges in separate baskets, to prevent LECs from eliminating their existing flat trunk port charges, and thereby circumventing the local switching rate structure rules we adopted in the *Access Reform First Report and Order*. In addition, we invite parties to propose specific services to be included in each basket, if we decide that any modifications to the basket configurations are warranted. Alternatively, we invite comment on whether adopting a capacity-based local switching rate structure would be sufficient

⁵⁶² *LEC Price Cap Performance Review Order*, 10 FCC Rcd at 9069-70.

⁵⁶³ *Access Reform First Report and Order*, 12 FCC Rcd at 16035-36.

⁵⁶⁴ Sprint eliminated its trunk port charges in its Arizona study area, and GTE eliminated these charges in its Northern California, Montana, and Minnesota study areas.

to preclude LECs from entirely circumventing the local switching rate structure rules adopted in the *Access Reform First Report and Order*.

3. Inflation Measure

235. Currently, the inflation measure in the PCI formula is the "Fixed Weight Price Index for Gross Domestic Product, 1987 Weights."⁵⁶⁵ The Bureau of Labor Statistics (BLS) now measures inflation with a chain-weighted GDP-PI, which bases weights for the current year's index on the prior year. We also note that the Commission used chain-weighted price indices in its calculation of a new X-Factor based on total factor productivity.⁵⁶⁶ We tentatively conclude that we should make the inflation measure in the PCI formula consistent with BLS's measure and with that used in setting the X-Factor. We seek comment on this tentative conclusion.

E. CLEC Access Charges

1. Background

236. As we discuss above,⁵⁶⁷ the Commission requested comment in the *Access Reform NPRM* on the regulation of terminating access charges of both incumbent LECs and CLECs. The Commission noted that, with originating access, the calling party has the choice of service provider, the decision to place a call, and the ultimate obligation to pay for the call.⁵⁶⁸ The calling party also is the customer of the IXC that purchases the originating access service.⁵⁶⁹ The Commission noted that, unlike originating access, the choice of an access provider for terminating access is made by the recipient of the call. It suggested that, because neither the originating caller nor its long-distance service provider can exert substantial influence over the called party's choice of terminating access provider, the terminating end of a long-distance call may remain a bottleneck, controlled by the LEC providing access to a particular customer. The Commission also sought comment on the continued treatment of incumbent LEC originating "open end" minutes as terminating minutes for access charge purposes, and whether to extend that approach to CLECs.⁵⁷⁰ The Commission noted that, in some cases, such as 800 and 888 service, the called

⁵⁶⁵ Section 61.3(q) of the Commission's Rules, 47 C.F.R. § 61.3(q).

⁵⁶⁶ *See, e.g., Price Cap Fourth Report and Order*, 12 FCC Rcd at 16784 (App. D).

⁵⁶⁷ *See* Section VII.A, *supra*.

⁵⁶⁸ *Access Reform NPRM*, 11 FCC Rcd at 21472.

⁵⁶⁹ *Id.*

⁵⁷⁰ *See id.* at 21477. "The term open end of a call describes the origination or termination portion of a call that utilizes exchange carrier common line plant (a call can have no, one, or two open ends)." 47 C.F.R. § 69.105(b)(1)(ii).

party, which pays for the call, is unable to influence the calling party's choice of provider for originating access services.⁵⁷¹

237. Based on the record submitted in response to the *Access Reform NPRM*, the Commission concluded that non-incumbent LECs should be treated as non-dominant in the provision of terminating access.⁵⁷² The Commission found that there was insufficient evidence in the record to determine that CLECs had the ability to exercise market power in the provision of terminating access.⁵⁷³ The Commission further concluded that, as CLECs attempt to expand their market presence, the rates of incumbent LECs or other potential competitors would constrain the CLECs' terminating access rates.⁵⁷⁴ The Commission decided, therefore, not to adopt any regulations at that time governing the provision of terminating access provided by CLECs because CLECs did not appear to possess market power.⁵⁷⁵ The Commission indicated, however, that it would revisit the issue if there were sufficient indications that CLECs were imposing unreasonable terminating access charges.⁵⁷⁶ Although the Commission did not address the issue of CLEC originating access, it indicated, in the context of incumbent LEC originating access, that it believed that new entrants would eventually exert downward pressure on originating access rates.⁵⁷⁷ The Commission also concluded that the continued treatment of "open end" originating minutes, such as those for 800 or 888 services, as terminating minutes for access charge purposes was appropriate because the called party, which pays for the 800 or 888 calls, has limited ability to influence the calling party's choice of access provider.⁵⁷⁸

⁵⁷¹ See *id.*

⁵⁷² See *Access Reform First Report and Order*, 12 FCC Rcd at 16140; see also Section VII.A, *supra* for a definition of non-dominant carrier and a detailed discussion of the Commission's conclusions.

⁵⁷³ See *Access Reform First Report and Order*, 12 FCC Rcd at 16140; see also Section VII.A. *supra*.

⁵⁷⁴ See *Access Reform First Report and Order*, 12 FCC Rcd at 16140; see also Section VII.A. *supra*.

⁵⁷⁵ See *Access Reform First Report and Order*, 12 FCC Rcd at 16141-42; see also Section VII.A, *supra*.

⁵⁷⁶ See *Access Reform First Report and Order*, 12 FCC Rcd at 16140 (noting that CLEC terminating access rates exceeding originating rates in the same market may suggest the need to revisit the regulatory approach; similarly, CLEC rates that exceed incumbent LEC terminating rates in the same market may suggest that a CLEC's terminating access rates are excessive).

⁵⁷⁷ The Commission concluded that new entrants, by purchasing unbundled network elements or providing facilities-based competition, eventually will exert downward pressure on incumbent LEC originating access rates. *Id.* at 16135-36.

⁵⁷⁸ *Id.* at 16140. The Commission noted that incumbent LEC access charges for "open end" minutes would be governed by the same requirements applicable to terminating access provided by incumbent LECs. *Id.* at 16142. In order to address the potential that incumbent LECs might charge unreasonable rates for terminating access, the Commission limited the price cap incumbent LEC recovery of TIC and common costs from terminating access rates for a limited period with the eventual elimination of any recovery of common line and TIC costs through

238. Since that time, however, we have received indications that the Commission may have overestimated the ability of the marketplace to constrain CLEC access rates. In particular, IXCs allege that a substantial number of CLECs impose switched access charges that are significantly higher than those charged by the incumbent LECs with which they compete,⁵⁷⁹ suggesting that the Commission may need to revisit the issue of CLEC access rates. If market forces fail to constrain CLEC access rates, requiring IXCs to pay access charges set unilaterally by CLECs is not economically efficient and does not further the goals of the Telecommunications Act of 1996. We are reluctant, however, to regulate rates charged by competitive entrants to the local exchange and exchange access markets and prefer instead to seek a marketplace solution that might constrain CLEC access rates.

2. Discussion

239. Throughout the *Access Reform* proceeding, the Commission has questioned whether CLECs possess market power over terminating access service and whether such power precludes market forces from ensuring that terminating access charges are just and reasonable. In the *Access Reform NPRM*, the Commission invited parties to comment on whether CLECs have market power over IXCs that need to terminate long-distance calls to CLEC customers, and, if so, whether the Commission should subject CLEC terminating access rates to some form of regulation.⁵⁸⁰ Given the rapidly evolving telecommunications industry, we again invite parties to comment on this issue.

240. In particular, in response to the *Access Reform NPRM*, USTA challenges the fundamental premise that, because the called party is not paying for the call, terminating access charges are shielded from downward market pressures.⁵⁸¹ According to USTA, if a LEC overprices terminating access relative to originating access, a pair of callers in repeated communications would have an incentive to alter their pattern of calls to favor the lower-priced alternative.⁵⁸² In the *Access Reform First Report and Order*, the Commission stated that it was not convinced that a significant competitive impact would result from changes in calling patterns

terminating access charges. *Id.*

⁵⁷⁹ *AT&T Declaratory Ruling Petition*, Appendix A (alleging that a number of CLECs impose charges that are in some cases more than twenty times higher than those charged by incumbent LECs with which they compete); see also Sprint Reply at 3; Cable & Wireless Comments at 2. Unless otherwise indicated, all citations to comments and replies in this section of the Notice refer to comments and replies submitted in response to the *AT&T Declaratory Ruling Petition*.

⁵⁸⁰ See *Access Reform NPRM*, 11 FCC Rcd at 21476.

⁵⁸¹ USTA *Access Reform NPRM* Comments, Attachment 3 at 12.

⁵⁸² *Id.*; see also TCI *Access Reform NPRM* Reply at 32 (the Commission's analysis of a calling party's incentives does not consider the incentives that called parties have because of the value they place on receiving calls as well as originating them).

between pairs of callers.⁵⁸³ Based on their experiences since the *Access Reform First Report and Order*, we ask parties to comment on USTA's hypothesis. In addition, in response to the *Access Reform NPRM*, TCI disputes the premise that CLECs may possess market power. TCI asserts that CLECs do not have market power because IXCs can exercise bargaining power in negotiating terminating access charges with CLECs.⁵⁸⁴ TCI argues that the absence of an agreement will not prevent an IXC from completing many calls; instead, the IXC simply will have to pay terminating access to a different carrier.⁵⁸⁵ The absence of an agreement would be very costly to a CLEC, however, because it is quite possible that switched local service would not be a viable business without interconnection agreements with all the major IXCs.⁵⁸⁶ We ask parties to comment on TCI's hypothesis.

241. TCI's comments also raise the fundamental question of an IXC's obligation to accept or deliver traffic from or to a LEC. The Bureau recently released an order in which it found that AT&T had failed to take reasonable and necessary steps to terminate its access service arrangement with MGC, a CLEC.⁵⁸⁷ The Bureau also found, however, that MGC had failed to identify a legal impediment to an IXC declining to purchase a particular LEC's access service,⁵⁸⁸ but it emphasized that its holding was limited to the specific factual record⁵⁸⁹ and the arguments raised by the parties.⁵⁹⁰ The Bureau stated that:

by holding that none of the obligations we discuss above prevents AT&T from declining MGC's originating access service, we do not imply that AT&T is entirely without constraint in determining where, how, or whom it will provide its long distance services. Naturally, in providing those services, AT&T remains subject to a broad variety of statutory and regulatory

⁵⁸³ *Access Reform First Report and Order*, 12 FCC Rcd at 16136.

⁵⁸⁴ Although TCI's point is limited to terminating access charges, presumably it also could apply to originating access charges.

⁵⁸⁵ TCI *Access Reform NPRM* Reply, Attachment A at 8.

⁵⁸⁶ *Id.* TCI appears to assume that an IXC is not obligated to deliver traffic to a terminating access provider if the IXC believes the rates are too high. We note that this issue is raised by AT&T's Declaratory Ruling Petition that we denied in this Order and addressed in the Bureau's decision in *MGC Communications*.

⁵⁸⁷ *MGC Communications* at ¶ 16.

⁵⁸⁸ *Id.* at ¶ 8.

⁵⁸⁹ At the hearing, MGC appeared to concede that, under its tariff, an IXC prospectively may refuse to accept a LEC's originating access traffic. *MGC Communications* at ¶ 8. MGC also argued, however, that the equal access, dialing parity, and payphone provisions of the Act obligate IXCs to accept CLEC traffic. *Id.* The Bureau rejected these arguments. *Id.* at ¶ 12.

⁵⁹⁰ *Id.* at ¶ 12.

constraints that are too numerous to list here, but which include, without limitations, sections 201, 202, 203, and 214 of the Act and section 63.71 of the Commission's rules.⁵⁹¹

242. We now solicit comment on the issue the Bureau explicitly did not reach: whether any statutory or regulatory constraints prevent an IXC from declining a CLEC's access service. Commenters should identify any such constraints with particularity. If there are circumstances in which an IXC may decline to purchase a CLEC's access service, what are the ramifications for the customer of the CLEC? How would such a customer make or receive long-distance calls? Is such a regime consistent with the goals of section 254 of the Act that consumers in all regions of the nation have access to telecommunications services, including interexchange services?⁵⁹² Provided that an IXC may refuse a CLEC's access traffic, is this a market-based solution to excessive CLEC rates that obviates the need for any regulatory action by the Commission?

243. If an IXC may refuse a CLEC's access service, we also solicit comment on whether an IXC can refuse to accept traffic from an incumbent LEC when there are no competitive alternatives to the LEC, *e.g.*, a rural area with only one local exchange provider.⁵⁹³ We note that the Commission regulates incumbent LEC access charges.⁵⁹⁴ If an incumbent LEC's rates are within the Commission's mandates, should they be presumed to be just and reasonable? If so, should an IXC be allowed to refuse an incumbent LEC's access service despite the fact that the LEC's access rates are just and reasonable? What are the ramifications for the customer in that case? If there are no competitive alternatives, how would the end user of the LEC receive long-distance service if the IXC refused the LEC's access service? If in fact an IXC may refuse a LEC's access service, we also solicit comment on whether an IXC can accept traffic from incumbent LECs but refuse to accept traffic from CLECs. What are the ramifications for both the end users of the CLEC and the incumbent LEC? Would this lead to confusion on the part of the calling party who would not be aware until it placed its call, and the call did not go through, that the called party was served by a CLEC? Should an IXC's obligations to accept or deliver traffic from or to a CLEC differ for originating and terminating access services?

244. We acknowledge that CLEC access rates may, in fact, be higher due to the CLECs' high start-up costs for building new networks, their small geographical service areas, and the

⁵⁹¹ *Id.* See also 47 U.S.C. §§ 201, 202, 203, and 214; 47 C.F.R. § 63.71 (establishing procedures for discontinuance or impairment of service by domestic, non-dominant carriers).

⁵⁹² 47 U.S.C. § 254(b)(3).

⁵⁹³ We note that AT&T did not address the issue of incumbent LEC access services. *AT&T Declaratory Ruling Petition* at n.4.

⁵⁹⁴ See *Access Reform First Report and Order*, 12 FCC Rcd at 16135-38.

limited number of subscribers over which CLECs can distribute costs.⁵⁹⁵ Requiring IXCs to bear these costs, however, may impose unfair burdens on IXC customers that pay rates reflecting these CLEC costs even though the IXC customers may not subscribe to the CLEC. IXCs currently spread their access costs among all their end users. We solicit comments on solutions to this problem. Might the problem of excessive CLEC access rates be solved if IXCs charged different rates to end users *within the same geographic area* based upon the level of access charges levied by the end user's local exchange company? Because their long-distance bills would fluctuate based on the level of access charges, end users presumably would switch to LECs that charged lower access charges in order to reduce their long-distance bills. Is this a market-based solution to the issue of CLEC access rates?

245. If it is a market-based solution, we solicit comments on whether section 254(g) permits IXCs to charge different rates to end users *within the same geographic area* based upon the level of access charges levied by the end user's local exchange company.⁵⁹⁶ The legislative history of section 254(g) indicates that it is intended to ensure that rates *between geographic areas* are equal.⁵⁹⁷ If section 254(g) permits IXCs to charge different rates to end users *within the same geographic area* based upon the level of access charges levied by the end user's local exchange company, what practical difficulties might that raise with respect to ensuring that urban and rural rates are comparable? How, for example, might one compare urban and rural rates if IXCs charge different rates within an urban area?

246. We also seek comment on whether mandatory detariffing of CLEC interstate access charges might address any market failure to constrain terminating access rates. Mandatory detariffing would eliminate the CLECs' ability unilaterally to set terminating access rates by filing a tariff and to avoid negotiating those rates in the marketplace by relying on the filed tariff

⁵⁹⁵ See, e.g., Cox Comments at 5 (a CLEC that primarily serves residential customers will have a low volume of access traffic (and hence higher per minute costs) relative to a CLEC of equal size that primarily serves businesses); OpTel Comments at 5 (CLECs' higher access rates often reflect the higher cost structure of a facilities-based CLEC in the process of building a new network relative to the cost structure of an incumbent LEC with an established network).

⁵⁹⁶ See 47 U.S.C. § 254(g) (The Commission shall adopt rules to require that the rates charged by providers of interexchange telecommunications services to subscribers in rural and high cost areas shall be no higher than the rates charged by each such provider to its subscribers in urban areas. Such rules shall also require that a provider of interstate interexchange services shall provide such services to its subscribers in each State at rates no higher than the rates charged to its subscribers in any other State); see also 47 C.F.R. § 64.1801.

⁵⁹⁷ In the Joint Explanatory Statement, the conferees stated that: "[n]ew section 254(g) is intended to incorporate the policies of geographic rate averaging and rate integration of interexchange services in order to ensure that subscribers in rural and high cost areas throughout the Nation are able to continue to receive both intrastate and interstate interexchange services at rates no higher than those paid by urban subscribers." S. Rep. No. 230, 104th Cong., 2nd Sess. at 132 (1996) (Joint Explanatory Statement).

doctrine.⁵⁹⁸ To the extent that detariffing encourages parties to negotiate rates for terminating access, is it a market-based solution to excessive terminating access charges? We note, however, that our decision to require mandatory detariffing by IXCs has been stayed by the court of appeals,⁵⁹⁹ and the court's ultimate decision likely will implicate our ability to impose mandatory detariffing on CLECs. Finally, we seek comment on whether the adoption of any other solution should serve only as a "stopgap" measure until such time as we may be able to require detariffing.

247. We strongly prefer to rely upon a marketplace solution, such as those discussed above, to constrain CLEC access rates. Nonetheless, in the event that we conclude that legal or other impediments preclude adoption of a market-based solution, we also seek comment on a regulatory backstop to constrain CLEC access rates. In the *Access Reform NPRM*, the Commission invited parties to address whether the incumbent LECs' terminating access charges should serve as a benchmark to evaluate the reasonableness of CLECs' terminating rates. It suggested that a CLEC's terminating access charges might be presumptively just and reasonable if they were less than or equal to the terminating access charges of the incumbent LEC with which the CLEC competes.⁶⁰⁰ If, on the other hand, the CLEC's terminating access charges exceed the incumbent LEC's charges, the CLEC could be required to provide cost support for its charges or, alternatively, it might be required to collect the difference from its end users, rather than IXCs.⁶⁰¹ We again seek comment on these proposals and whether they also should apply to originating access rates. Should access rates below a particular benchmark be presumed just and reasonable, thus providing CLECs with a defense in the context of a section 208 complaint?⁶⁰² We seek comment on what rates to use as a benchmark, *e.g.*, the incumbent LEC rate in the area served by the CLEC, or some other terminating access rate.⁶⁰³

⁵⁹⁸ In its declaratory ruling petition, AT&T alleges that its attempts to negotiate terminating access charges have stalled because many CLECs take the position that, due to the "filed tariff doctrine," AT&T is obligated to accept services from the CLEC at prices chosen by the CLEC. *AT&T Declaratory Ruling Petition* at 3, n. 2; see Section VII.B. for a discussion of the filed tariff doctrine.

⁵⁹⁹ See Policy and Rules Concerning the Interstate, Interexchange Marketplace, CC Docket No. 96-61, Second Report and Order, 11 FCC Rcd 20730, 20741-43 (1996) (*Tariff Forbearance Order*), *stay granted*, MCI Telecommunications Corp. v. FCC, No. 96-1459 (D.C. Cir. filed Feb. 13, 1997).

⁶⁰⁰ *Access Reform NPRM*, 11 FCC Rcd at 21476.

⁶⁰¹ *Id.*

⁶⁰² 47 U.S.C. § 208.

⁶⁰³ Commenters provide a number of suggestions on what rate to use as a benchmark. For example, Cox asserts that, if the Commission is going to use a benchmark, it should use the rates of smaller, more geographically dispersed non-price cap incumbent LECs, such as the incumbent LECs participating in the NECA tariff. Cox *Access Reform NPRM* Comments at 6. Although MCI does not believe that the interstate access rates charged by NECA member companies are just and reasonable, it suggests that NECA rates levels may be a useful starting point in setting a benchmark because they are supposed to be set at a level equal to the national averaged rate had all incumbent LECs remained in the NECA pool. MCI *Access Reform NPRM Reply Comments* at 6 and n.24.

248. We also seek comment on whether any benchmark should vary depending on various criteria, such as, for example, whether the CLEC serves high cost areas or low cost areas. Alternatively, should any benchmark take the form of a sliding scale that declines as the number of access minutes per CLEC switch increases? Would it be appropriate to estimate this benchmark using incumbent LEC data? If parties believe that the benchmark should vary depending on various criteria, we solicit comment on these criteria, on what methodology we should use to establish alternative benchmarks, and what criteria we should use to determine which benchmark should apply to an individual CLEC.

249. Assuming we were to employ some form of a benchmark, we seek comment on whether to provide an "escape valve" that would allow CLECs wishing to charge more than the benchmark to collect those charges from end users (either the called party or calling party).⁶⁰⁴ In particular, we seek comment on an "end party pays" proposal that would require CLECs to collect the difference between the benchmark terminating access rate and the CLEC terminating access rate from end users (either the calling or called party) rather than from the IXC.⁶⁰⁵ We note that this "end party pays proposal" would resolve the problems associated with IXC averaging requirements,⁶⁰⁶ by in essence, "deaveraging" terminating access by charging the end user, rather than the IXC, for the terminating access.

250. In particular, if the *called* party pays, the person receiving the call would be charged the difference between the CLEC terminating access rate and the benchmark terminating access rate. We ask parties to comment on whether charging the called party would yield an increase in the number of uncompleted calls due to the called parties' refusal to accept the charges. In the *Access Reform First Report and Order*, the Commission found that a "called party pays" proposal may be disruptive to wireline services.⁶⁰⁷ Given the increasing popularity of wireless services and that most wireless companies charge the called parties for receiving calls, we seek comment on the continued validity of the Commission's concerns that consumers would be adverse to a "called

Sprint states that, although it has no objection to paying NECA level terminating access charges to CLECs that serve high costs areas also served by NECA carriers, there is no justification for using NECA rates as a benchmark for CLEC rates in the low cost high-density metropolitan areas. Sprint Access Reform NPRM Reply Comments at 7.

⁶⁰⁴ See, e.g., *Access Reform NPRM*, 11 FCC Rcd at 21476.

⁶⁰⁵ See, e.g., *id.*

⁶⁰⁶ See Section VII.A. *supra* for a discussion of IXC averaging requirements.

⁶⁰⁷ See *Access Reform First Report and Order*, 12 FCC Rcd at 16138. We note that, in response to the Access Reform NPRM, the California Commission indicated that it opposed any "called party pays" proposal because customers most likely would not understand why they were paying to receive a call and some customers would refuse to accept calls if they knew that doing so would mean incurring a charge. California Commission *Access Reform NPRM* Comments at 18.

party pays" proposal in the context of wireline services. In addition, we invite parties to address how to accomplish charging the customer receiving the call for terminating access.

251. If, conversely, the calling party pays, the person making the call, rather than the IXC, would be charged the difference between the CLEC terminating access rate and the benchmark terminating access rate. We seek comment on whether wireline consumers would be adverse to a "calling party pays" regime. We note that such a regime is offered widely by wireless providers abroad, and on a much more limited basis by some providers of cellular, paging and Personal Communications Service (PCS) in the United States.⁶⁰⁸ Further, we seek comment on whether requiring called or calling parties to pay for a portion of terminating access might encourage competition for terminating access. In addition, we question whether these "end party pays" proposals should be limited only to CLECs, and if so, whether this would result in confusion on the part of end users, *i.e.*, incumbent LEC end users would not be charged for terminating access but CLEC end users would be.

252. Adoption of a "calling party pays" regime would require notification to the party making the call that it would be responsible for terminating access charges in addition to a long distance charge from its IXC. We seek comment on the development of a notification system. In particular, we seek comment on a proposal that the notification be developed in cooperation with the States and include: (1) notice that the calling party will be responsible for the terminating access charges; (2) the terminating access rates that the calling party incurs will be charged by the terminating LEC provider; and (3) notice that the calling party may terminate the call prior to incurring any charges. If we were to adopt a "called party pays" proposal, the *called party* would be notified at the time it signed up for service from a CLEC that it would have to pay terminating access charges for incoming long-distance calls. Accordingly, for the "called party pays proposal," we seek comment on the development of a more limited notification that merely delineates local calls from "called party pays" calls.

253. In response to *AT&T's Declaratory Ruling Petition*, Bell Atlantic proposes that the Commission link the terminating access rates of all local carriers, both CLECs and incumbent LECs, to originating access rates.⁶⁰⁹ Bell Atlantic argues that originating rates are not excessive

⁶⁰⁸ See *Access Reform NPRM*, 11 FCC Rcd at 21474. In the context of wireless services, the Commission recently adopted a declaratory ruling that clarified that calling party pays, a service whereby the party placing the call to a wireless customer pays the wireless airtime charges, is a commercial mobile radio service offering. See *Calling Party Pays Service Offerings in the Commercial Mobile Radio Services*, WT Docket No. 97-207, Declaratory Ruling and Notice of Proposed Rulemaking, FCC 99-137 (rel. July 7, 1999). In the same proceeding, the Commission also initiated a rulemaking requesting comments on a uniform notification requirement, the effect of competitive pressures on calling party pays rates, and whether it could and should require LECs to bill and collect for a CMRS carrier's calling party service. See *id.*

⁶⁰⁹ Bell Atlantic Comments at 2. See also Spectranet Access Reform NPRM Comments at 10 (supporting requiring that all LECs (both CLEC and incumbent LECs) price terminating access the same as originating access in each applicable geographic market).

because competitive forces keep them in check.⁶¹⁰ It hypothesizes that, if the Commission required every carrier to set terminating rates at a level no higher than its originating rates, those competitive forces would constrain terminating access rates as well.⁶¹¹ We seek comment on Bell Atlantic's proposal. In order to address the potential that incumbent LECs might charge unreasonable rates for terminating access, the Commission limited price cap incumbent LEC recovery of TIC and common line costs from terminating access rates for a limited period, with the eventual elimination of any recovery of common line and TIC costs through terminating access charges.⁶¹² Furthermore, the Commission declined at that time to link terminating rates to originating rate levels because that approach would not substantially affect terminating access rates where originating access rates were not subject to competitive pressures.⁶¹³ The Commission also found that linking an incumbent LEC's terminating access rates to its originating access rate might reduce the incumbent LEC's incentive to lower its originating access rates.⁶¹⁴ We now seek comment on whether we should link the rates that all local carriers, both CLECs and incumbent LECs, charge for terminating access to originating access rates. We also seek comment on the possible effects on competition between incumbent LECs and CLECs if we were to adopt Bell Atlantic's proposal, but limit it to CLECs.

254. Some commenters have suggested that CLECs are charging excessive originating access rates.⁶¹⁵ In the *Access Reform NPRM*, the Commission stated that as long as IXCs can influence the choice of the access provider, a LEC's ability to charge excessive originating access rates is limited, as IXCs will shift their traffic from that carrier to a competing access provider.⁶¹⁶ In the *Access Reform First Report and Order*, the Commission did not specifically address the issue of CLEC originating access rates. Instead, in the context of incumbent LEC originating access rates, the Commission concluded that new entrants, by purchasing unbundled network elements or providing facilities-based competition, would eventually exert downward pressure on originating access rates.⁶¹⁷ Given the complaints by AT&T and others regarding excessive CLEC originating access rates,⁶¹⁸ we seek comment on a marketplace solution that would constrain

⁶¹⁰ *Id.*

⁶¹¹ *Id.*

⁶¹² *Access Reform First Report and Order*, 12 FCC Rcd at 16136.

⁶¹³ *Id.* at 16137.

⁶¹⁴ *Id.*

⁶¹⁵ *AT&T Declaratory Ruling Petition* at 2; Sprint Reply at 3; Cable & Wireless Comments at 2.

⁶¹⁶ *Access Reform NPRM*, 11 FCC Rcd at 21472.

⁶¹⁷ *Id.* at 16136.

⁶¹⁸ *AT&T Declaratory Ruling Petition* at 2; Sprint Reply at 3; Cable & Wireless Comments at 2.

CLEC originating access rates. In particular, we seek comment on whether any of the terminating access proposals discussed above also may apply to originating access rates. Finally, we seek comment on whether an entirely separate solution is necessary to resolve the issue of originating access charges. If a separate solution is necessary, we solicit comments on what that solution should be.

255. In the case of both originating access associated with "open end" services, such as 800 or 888 calls, and terminating access, the party paying for the call does not choose the access provider. We invite parties to comment on whether, therefore, to treat CLEC "open end" originating minutes the same as CLEC terminating minutes for access charge purposes.⁶¹⁹ Assuming "open end" minutes are treated the same as terminating minutes for access charge purposes, we seek comment on whether the calling party and called party pays proposals set forth above also might work for "open end" minutes, or whether modifications are needed for "open end" minutes. For instance, if we were to adopt a *calling party pays* proposal for originating "open end" minutes, we might require the calling party to pay the portion of the access charges that exceed the benchmark for 800 or 888 calls, because it is the caller, in that instance, that makes the choice of provider for originating access. Finally, we seek comment on whether an entirely separate solution is necessary to resolve the issue of "open end" originating access charges. If a separate solution is necessary, we solicit comments on what that solution should be.

256. We strongly prefer not to intervene in the marketplace, particularly with respect to competitive new entrants, unless intervention is necessary to fulfill our statutory obligation to ensure just and reasonable rates. If market forces are not operating to constrain CLEC access charges, we seek the least intrusive means possible to correct any market failures.

257. Finally, in the *Access Reform NPRM*, the Commission sought comment on any less intrusive methods of ensuring that a CLEC's originating and terminating access charges are just and reasonable.⁶²⁰ We do so again. We further invite parties to comment on how small business entities, including small incumbent LECs and new entrants, will be affected by the proposals above regarding CLEC access charges.

⁶¹⁹ We note that, in response to the *Access Reform NPRM*, TCI argued that originating "open end" minutes do not constitute a bottleneck, and, thus should not be treated as terminating access minutes, because originating "open end" access rates will respond to the market. See TCI *Access Reform NPRM* Reply at 34 (An access provider with high originating access charges would discourage businesses from making open end services available. In such situations, the calling party would lose the benefit of that service and change to an access provider with lower originating access rates.) In making its argument that "open end" minutes should not be treated as terminating minutes for access charge purposes, TCI assumes that terminating access rates are regulated.

⁶²⁰ *Access Reform NPRM*, 11 FCC Rcd at 21476.

IX. PROCEDURAL ISSUES

A. Final Regulatory Flexibility Analysis

258. As required by the Regulatory Flexibility Act (RFA),⁶²¹ an Initial Regulatory Flexibility Analysis (IRFA) was incorporated in *Access Reform NPRM*.⁶²² The Commission sought written comments on the proposals in the *Access Reform NPRM*, including the IRFA. The Commission's Final Regulatory Flexibility Analysis (FRFA) in this Order conforms to the RFA, as amended.⁶²³ To the extent that any statement contained in this FRFA is perceived as creating ambiguity with respect to our rules or statements made in preceding sections of this Order, the rules and statements set forth in those preceding sections shall be controlling.

1. Need for and Objectives of this Report and Order

259. This proceeding is being conducted to advance the pro-competitive, de-regulatory national policies embodied in the Telecommunications Act of 1996. The Commission continues the process it began in 1997 with the Access Reform First Report and Order to reform regulation of interstate access charges in order to accelerate the development of competition in all telecommunications markets and to ensure that our own regulations do not unduly interfere with the operation of these markets as competition develops.

2. Summary of Significant Issues Raised by the Public Comments in Response to the IRFA

260. We have already addressed the general concerns raised by Rural Telephone Coalition that this proceeding may "prejudge and prejudice" a later rulemaking for non-price cap LECs, and that the delay in implementing that rulemaking may injure non-price cap LECs.⁶²⁴ Otherwise, the comments filed do not address the specific issues contained in this Order.⁶²⁵

⁶²¹ See 5 U.S.C. § 603.

⁶²² Access Charge Reform, CC Docket No. 96-262, Notice of Proposed Rulemaking, 11 FCC Rcd 21354 (1996) (*Access Reform NPRM*).

⁶²³ See 5 U.S.C. § 604. The Regulatory Flexibility Act, 5 U.S.C. § 601 *et. seq.*, was amended by the "Small Business Regulatory Enforcement Fairness Act of 1996" (SBREFA), which was enacted as Title II of the Contract With America Advancement Act of 1996, Pub.L. No. 104-121, 110 Stat. 847 (1996) (CWAAA).

⁶²⁴ See *Access Reform First Report and Order*, 12 FCC Rcd at 16161-62.

⁶²⁵ See USTA Comments at 16-17, 56-57; SNET Comments at 29; Rural Telephone Coalition Comments at 2-3, 10-13, 15; Frontier Comments at 5-6.

3. Description and Estimate of the Number of Small Entities to which the Rules Will Apply:

261. The RFA directs agencies to provide a description of and, where feasible, an estimate of the number of small entities that may be affected by the proposed rules, if adopted.⁶²⁶ The RFA generally defines the term "small entity" as having the same meaning as the terms "small business," "small organization," and "small governmental jurisdiction."⁶²⁷ In addition, the term "small business" has the same meaning as the term "small business concern" under the Small Business Act.⁶²⁸ A small business concern is one which: (1) is independently owned and operated; (2) is not dominant in its field of operation; and (3) satisfies any additional criteria established by the Small Business Administration (SBA).⁶²⁹ The Small Business Administration has defined a small business for Standard Industrial Classification (SIC) category 4813 (Telephone Communications, Except Radiotelephone) to be a small entity that has no more than 1500 employees.⁶³⁰

Total Number of Telephone Companies Affected:

262. We have included small incumbent LECs in this present RFA analysis. As noted above, a "small business" under the RFA is one that, *inter alia*, meets the pertinent small business size standard (*e.g.*, a telephone communications business having 1,500 or fewer employees), and "is not dominant in its field of operation."⁶³¹ The SBA's Office of Advocacy contends that, for RFA purposes, small incumbent LECs are not dominant in their field of operation because any such dominance is not "national" in scope.⁶³² We have therefore included small incumbent LECs

⁶²⁶ 5 U.S.C. § 603(b)(3).

⁶²⁷ *Id.* § 601(6).

⁶²⁸ 5 U.S.C. § 601(3) (incorporating by reference the definition of "small business concern" in 15 U.S.C. § 632). Pursuant to the RFA, the statutory definition of a small business applies "unless an agency, after consultation with the Office of Advocacy of the Small Business Administration and after opportunity for public comment, establishes one or more definitions of such term which are appropriate to the activities of the agency and publishes such definition(s) in the Federal Register." 5 U.S.C. § 601(3).

⁶²⁹ Small Business Act, 15 U.S.C. § 632 (1996).

⁶³⁰ 13 C.F.R. § 121.201.

⁶³¹ 5 U.S.C. § 601(3).

⁶³² Letter from Jere W. Glover, Chief Counsel for Advocacy, SBA, to William E. Kennard, Chairman, FCC (May 27, 1999). The Small Business Act contains a definition of "small business concern," which the RFA incorporates into its own definition of "small business." See 15 U.S.C. § 632(a) (Small Business Act); 5 U.S.C. § 601(3) (RFA). SBA regulations interpret "small business concern" to include the concept of dominance on a national basis. 13 C.F.R. § 121.102(b). Since 1996, out of an abundance of caution, the Commission has included small incumbent LECs in its regulatory flexibility analyses. *Implementation of the Local Competition Provisions*

in this RFA analysis, although we emphasize that this RFA action has no effect on FCC analyses and determinations in other, non-RFA contexts.

263. *Price Cap Local Exchange Carriers.* The rulemaking contained in this Order applies only to price cap LECs. We do not have data specifying the number of these carriers that are either dominant in their field of operations, are not independently owned and operated, or have more than 1,500 employees, and thus are unable at this time to estimate with greater precision the number of price cap LECs that would qualify as small business concerns under the SBA's definition. However, there are only 13 price cap LECs. Consequently, we estimate that significantly fewer than 13 providers of local exchange service are small entities or small price cap LECs that may be affected by these proposals.

4. Summary Analysis of the Projected Reporting, Recordkeeping, and Other Compliance Requirements

264. In this Report and Order, we adopt changes in pricing flexibility to price cap LECs in the form of streamlined introduction of new services, geographic deaveraging of rates for services in the trunking basket, and removal of interexchange services from price cap regulation. These changes will affect all price cap LECs, including small price cap LECs, and will require small price cap LECs to make one or more tariff filings should they desire to obtain the additional pricing flexibility, which will involve the usage of legal skills, and possibly accounting, economic, and financial skills.

5. Burdens on Small Entities, and Significant Alternatives Considered and Rejected

265. In Sections III, IV, and V, we adopt forms of regulatory relief for price cap LECs that can be granted under current market conditions and do not require a further competitive showing. Price cap LECs each will have to file at least one tariff to implement this relief, but the administrative burdens they will face in future filings will diminish as a result. In Section VI, we grant additional pricing flexibility to price cap LECs that make "competitive showings," or satisfy "triggers," to demonstrate that market conditions in particular areas warrant the relief at issue. In order to minimize the administrative burdens on price cap LECs, we base our triggering mechanisms on objectively measurable criteria.

266. We considered and rejected alternative triggers and granting a different amount of pricing flexibility. In setting the triggers and relief in the manner we did, we attempted to balance the interests of price cap LECs in being able to gain regulatory relief, with our interest in protecting ratepayers from unreasonable rate levels and new entrants from anti-competitive actions.

of the Telecommunications Act of 1996, CC Docket, 96-98, First Report and Order, 11 FCC Rcd 15499, 16144-45 (1996).

6. Report to Congress

267. The Commission will send a copy of this Report and Order, including this FRFA, in a report to be sent to Congress pursuant to the Small Business Regulatory Enforcement Fairness Act of 1996.⁶³³ In addition, the Commission will send a copy of this Report and Order, including FRFA, to the Chief Counsel for Advocacy of the Small Business Administration. A copy of this Report and Order and FRFA (or summaries thereof) will also be published in the Federal Register.⁶³⁴

B. Initial Regulatory Flexibility Act Analysis

268. As required by the Regulatory Flexibility Act (RFA),⁶³⁵ the Commission has prepared this present Initial Regulatory Flexibility Analysis (IRFA) of the possible significant economic impact on small entities by the policies and rules proposed in this Further Notice of Proposed Rulemaking (Further Notice). Written public comments are requested on this IRFA. Comments must be identified as responses to the IRFA and must be filed by the deadlines for comments on the Further Notice provided below in Section IX.D. The Office of Public Affairs will send a copy of the Further Notice, including this IRFA, to the Chief Counsel for Advocacy of the Small Business Administration.⁶³⁶ In addition, the Further Notice and IRFA (or summaries thereof) will be published in the Federal Register.⁶³⁷

269. Need for, and objectives of, the proposed rules. Consistent with the Telecommunications Act of 1996, the Commission has revised its interstate access charges to facilitate competition in the provision of interstate access services. These proposals attempt to effect additional regulations reflective of the competitive marketplace. In Sections VIII.A and VIII.B we seek to establish additional pricing flexibilities for price cap incumbent LECs, while at the same time limit use of those flexibilities to deter entry, to drive existing competitors from the market, or to increase rates for those customers that lack competitive alternatives. In Section VIII.C, we seek to modify the common line rate structure should we determine that a capacity-based rate structure reflects the manner in which price cap LECs incur their costs better than the current traffic-sensitive rate structure. In Section VIII.D, we seek to refine several of our price cap rules to better reflect the manner in which price cap incumbent LECs costs are incurred. In

⁶³³ 5 U.S.C. § 801(a)(1)(A).

⁶³⁴ See 5 U.S.C. § 604(b).

⁶³⁵ 5 U.S.C. § 603. The RFA, see 5 U.S.C. § 601 *et seq.*, has been amended by the Contract With America Advancement Act of 1996, Pub. L. No. 104-21, 110 Stat. 847 (1996) (CWAAA). Title II of the CWAAA is the "Small Business Regulatory Enforcement Fairness Act of 1996" (SBREFA).

⁶³⁶ 5 U.S.C. § 603(a).

⁶³⁷ See *id.*

Section VIII.E, we seek to prevent CLECs from charging unreasonable rates for terminating access service.

270. Legal Basis. The proposed action is supported by Sections 4(i), 4(j), 201-205, 208, 251, 252, 253 and 403 of the Communications Act of 1934, as amended, 47 U.S.C. §§ 154(i), 154(j), 201, 205, 208, 251, 252, 253, 403.

271. Description, potential impact and number of small entities affected. The RFA directs agencies to provide a description of and, where feasible, an estimate of the number of small entities that may be affected by the proposed rules, if adopted.⁶³⁸ The RFA generally defines the term "small entity" as having the same meaning as the terms "small business," "small organization," and "small governmental jurisdiction."⁶³⁹ In addition, the term "small business" has the same meaning as the term "small business concern" under the Small Business Act.⁶⁴⁰ A small business concern is one which: (1) is independently owned and operated; (2) is not dominant in its field of operation; and (3) satisfies any additional criteria established by the Small Business Administration (SBA).⁶⁴¹ The Small Business Administration has defined a small business for Standard Industrial Classification (SIC) category 4813 (Telephone Communications, Except Radiotelephone) to be a small entity that has no more than 1500 employees.⁶⁴²

Total Number of Telephone Companies Affected:

272. We have included small incumbent LECs in this present RFA analysis. As noted above, a "small business" under the RFA is one that, *inter alia*, meets the pertinent small business size standard (*e.g.*, a telephone communications business having 1,500 or fewer employees), and "is not dominant in its field of operation."⁶⁴³ The SBA's Office of Advocacy contends that, for RFA purposes, small incumbent LECs are not dominant in their field of operation because any

⁶³⁸ 5 U.S.C. § 603(b)(3).

⁶³⁹ *Id.* § 601(6).

⁶⁴⁰ 5 U.S.C. § 601(3) (incorporating by reference the definition of "small business concern" in 15 U.S.C. § 632). Pursuant to the RFA, the statutory definition of a small business applies "unless an agency, after consultation with the Office of Advocacy of the Small Business Administration and after opportunity for public comment, establishes one or more definitions of such term which are appropriate to the activities of the agency and publishes such definition(s) in the Federal Register." 5 U.S.C. § 601(3).

⁶⁴¹ Small Business Act, 15 U.S.C. § 632 (1996).

⁶⁴² 13 C.F.R. § 121.201.

⁶⁴³ 5 U.S.C. § 601(3).

such dominance is not "national" in scope.⁶⁴⁴ We have therefore included small incumbent LECs in this RFA analysis, although we emphasize that this RFA action has no effect on FCC analyses and determinations in other, non-RFA contexts.

273. *Price Cap Local Exchange Carriers.* The proposals in Section VIII.A-D apply only to price cap LECs. We do not have data specifying the number of these carriers that are either dominant in their field of operations, are not independently owned and operated, or have more than 1,500 employees, and thus are unable at this time to estimate with greater precision the number of price cap LECs that would qualify as small business concerns under the SBA's definition. However, there are only 13 price cap LECs. Consequently, we estimate that significantly fewer than 13 providers of local exchange service are small entities or small price cap LECs that may be affected by these proposals.

274. *Competitive Local Exchange Carriers.* The proposals in Section VIII.E apply only to competitive LECs. Neither the Commission nor the Small Business Administration has developed a definition of small providers of local exchange service. The closest applicable definition under Small Business Administration rules is for telephone telecommunications companies other than radiotelephone (wireless) companies.⁶⁴⁵ The most reliable source of information regarding the number of competitive LECs nationwide of which we are aware appears to be the data that we collect annually in connection with the Telecommunications Relay Service (TRS). According to our most recent data, 129 companies reported that they were engaged in the provision of either competitive access provider services or competitive local exchange carrier services.⁶⁴⁶ We do not have data specifying the number of these carriers that are either dominant in their field of operations, are not independently owned and operated, or have more than 1,500 employees, and thus are unable at this time to estimate with greater precision the number of competitive LECs that would qualify as small business concerns under the SBA's definition. Consequently, we estimate that fewer than 129 providers of local exchange service are small entities or small competitive LECs that may be affected by these proposals.

⁶⁴⁴ Letter from Jere W. Glover, Chief Counsel for Advocacy, SBA, to William E. Kennard, Chairman, FCC (May 27, 1999). The Small Business Act contains a definition of "small business concern," which the RFA incorporates into its own definition of "small business." See 15 U.S.C. § 632(a) (Small Business Act); 5 U.S.C. § 601(3) (RFA). SBA regulations interpret "small business concern" to include the concept of dominance on a national basis. 13 C.F.R. § 121.102(b). Since 1996, out of an abundance of caution, the Commission has included small incumbent LECs in its regulatory flexibility analyses. *Implementation of the Local Competition Provisions of the Telecommunications Act of 1996*, CC Docket, 96-98, First Report and Order, 11 FCC Rcd 15499, 16144-45 (1996).

⁶⁴⁵ Standard Industrial Classification (SIC) Code 4813.

⁶⁴⁶ FCC, Common Carrier Bureau, *Carrier Locator: Interstate Service Providers*, Figure 1 (number of carriers paying into the TRS Fund by type of carrier) (Jan. 1999).

275. Reporting, record keeping and other compliance requirements. We expect that, on balance, the proposals in this Further Notice will slightly increase price cap LECs' administrative burdens. The proposals in Section VIII.A would require at least one additional tariff filing, and may require additional showings. The proposals in Section VIII.B will require a price cap LEC, to the extent that it chooses to avail itself of the additional flexibility, to file a petition demonstrating that it has met the triggers, and make an initial tariff filing. We expect that the proposals in Sections VIII.C and VIII.D would establish new methodologies that price cap LECs would need to apply in their tariff filings, but otherwise should not affect their administrative burdens.

276. We expect that the proposals in Section VIII.E will have no effect on the administrative burdens of competitive LECs, because they would have no additional filing requirement. They would only be required to respond to complaints.

277. Steps taken to minimize significant economic impact on small entities, and significant alternatives considered. In this Notice, we sought comment on how a number of proposals would affect small entities. We believe that overall, these proposals should have a positive economic impact on small price cap LECs. The proposals in Sections VIII.A, VIII.B, and VIII.C should enable small price cap LECs to price their regulated services in a manner that is more reflective of the underlying costs of these services. In Sections VIII.C, we have also sought comment on whether small interexchange carriers would be artificially disadvantaged if we adopt a capacity-based local switching rate structure. The proposals in Sections VIII.D and VIII.E should not have a significant economic impact on small entities. We seek comment on these proposals and urge that parties support their comments with specific evidence and analysis.

278. Federal rules which overlap, duplicate or conflict with this proposal. None.

C. Paperwork Reduction Act

279. On April 1, 1997, the Office of Management and Budget (OMB) approved all of our proposed information collection requirements in accordance with the Paperwork Reduction Act.⁶⁴⁷ The OMB made one recommendation, suggesting that we try "to minimize the number of new filings that firms must create in order to be compliant with the rules adopted" We have carefully considered the recommendation of OMB, and in the course of preparing this Order, we have decided to modify several of the collection requirements proposed in the *Access Reform NPRM*.⁶⁴⁸ This Order has greatly reduced the number of filings a price cap LEC will have to submit to receive pricing flexibility. In addition, many of the filings should take less time to make than was originally proposed. For example, we estimate that based on the competitive triggers we

⁶⁴⁷ Notice of Office Management and Budget Action, OMB No 3060-0760 (Apr. 1, 1997).

⁶⁴⁸ Access Charge Reform, CC Docket No. 96-262, Notice of Proposed Rulemaking, 11 FCC Rcd 21354 (1996) (*Access Reform NPRM*).

adopted, it should only take five hours each to make two Phase II showings per MSA for all special access and dedicated transport services, whereas the original filing to OMB estimated that each Phase II showing would take approximately 300 hours.

280. The Further Notice of Proposed Rulemaking contains either a proposed or modified information collection. As part of its continuing effort to reduce paperwork burdens, we invite the general public and the OMB to take this opportunity to comment on the information collections contained in the Further Notice of Proposed Rulemaking, as required by the Paperwork Reduction Act of 1995, 44 U.S.C. §§ 3501-3520. Public and agency comments are due at the same time as other comments on the Further Notice of Proposed Rulemaking; OMB comments are due 60 days from date of publication of the Further Notice of Proposed Rulemaking in the Federal Register. Comments should address: (a) whether the proposed collection of information is necessary for the proper performance of the functions of the Commission, including whether the information shall have practical utility; (b) the accuracy of the Commission's burden estimates; (c) ways to enhance the quality, utility, and clarity of the information collected; and (d) ways to minimize the burden of the collection of information on the respondents, including the use of automated collection techniques or other forms of information technology.

D. Filing Comments

281. Pursuant to Sections 1.415 and 1.419 of the Commission's rules, 47 C.F.R. §§ 1.415, 1.419, interested parties may file comments on or before October 29, 1999, and reply comments on or before November 29, 1999. Comments may be filed using the Commission's Electronic Comment Filing System (ECFS) or by filing paper copies. *See Electronic of Documents in Rulemaking Proceedings*, 63 Fed. Reg. 24,121 (1998).

282. Comments filed through the ECFS can be sent as an electronic file via the Internet to <<http://www.fcc.gov/e-file/ecfs.html>>. Generally, only one copy of an electronic submission must be filed. If multiple docket or rulemaking numbers appears in the caption of this proceeding, however, commenters must transmit one electronic copy of the comments to each docket or rulemaking number referenced in the caption. In completing the transmittal screen, commenters should include their full name, Postal Service mailing address, and the applicable docket or rulemaking number. Parties may also submit an electronic comment by Internet e-mail. To get filing instructions for e-mail comments, commenters should send an e-mail to ecfs@fcc.gov, and should include the following words in the body of the message, "get form <your e-mail address>." A sample form and directions will be sent in reply.

283. Parties who choose to file by paper must file an original and four copies of each filing. If more than one docket or rulemaking number appear in the caption of this proceeding, commenters must submit two additional copies for each additional docket or rulemaking number. All filings must be sent to the Commission's Secretary, Magalie Roman Salas, Office of the

Secretary, Federal Communications Commission, 445 Twelfth St., S.W., Room TW-A325, Washington, DC 20554.

X. ORDERING CLAUSES

284. Accordingly, IT IS ORDERED, pursuant to sections 1, 4(i), 4(j), 201-205, 303(r), and 403 of the Communications Act of 1934, as amended, 47 U.S.C. §§ 151, 154(i), 154(j), 201-205, 303(r), 403, and section 553 of Title 5, United States Code, that revisions to Parts 1, 61, and 69 of the Commission's rules, 47 C.F.R. Parts 1, 61, 69, ARE ADOPTED as set forth in Appendix B.

285. IT IS FURTHER ORDERED that the rule revisions adopted in this Order will be effective 30 days after publication of this Order in the Federal Register. The collections of information contained within are contingent upon approval by the Office of Management and Budget.

286. IT IS FURTHER ORDERED that, pursuant to section 10(c) of the Communications Act of 1934, 47 U.S.C. § 160(c), the period for review by the Commission of the petition for forbearance filed by U S West Communications, Inc., CC Docket No. 98-157, IS EXTENDED by 90 days.

287. IT IS FURTHER ORDERED that the petition for declaratory ruling filed by AT&T, CCB/CPD File No. 98-63, IS DENIED.

288. IT IS FURTHER ORDERED that NOTICE IS HEREBY GIVEN OF the rulemaking described above and that COMMENT IS SOUGHT on these issues.

289. IT IS FURTHER ORDERED that the Commission's Office of Public Affairs, Reference Operations Division, SHALL SEND a copy of the Further Notice of Proposed Rulemaking, including the Regulatory Flexibility Act analysis, to the Chief Counsel for Advocacy of the Small Business Administration.

FEDERAL COMMUNICATIONS COMMISSION

Magalie Roman Salas
Secretary

APPENDIX A**Parties Filing Pleadings****I. Price Cap Second FNRPM****A. Comments**

1. Ad Hoc Telecommunications Users Group (Ad Hoc)
2. Ameritech
3. Association for Local Telephone Services (ALTS)
4. AT&T Corp. (AT&T)
5. Bell Atlantic Telephone Companies (Bell Atlantic)
6. BellSouth Telecommunications, Inc. (BellSouth)
7. California Cable Television Association (CCTA)
8. Cincinnati Bell Telephone Co. (Cincinnati Bell)
9. Comcast Corp. (Comcast)
10. Competitive Telecommunications Association (CompTel)
11. Cox Enterprises, Inc. (Cox)
12. General Services Administration (GSA)
13. GTE Service Corp. (GTE)
14. ICG Access Services, Inc. (ICG)
15. Information Industry Association (IIA)
16. LCI International, Inc. (LCI)
17. LDDS WorldCom (LDDS)
18. Lincoln Telephone and Telegraph Co. (Lincoln)
19. MCI Telecommunications Corp. (MCI)
20. Metropolitan Fiber Systems (MFS)
21. National Telephone Cooperative Association (NTCA)
22. NYNEX Telephone Companies (NYNEX)
23. Organization for the Protection and Advancement of Small Telephone Companies (OPASTCO)
24. Pacific Bell and Nevada Bell (together, Pacific Bell)
25. Southern New England Telephone Co. (SNET)
26. Southwestern Bell Telephone Co. (SBC)
27. Sprint Corporation (Sprint)
28. Sprint Telecommunications Venture
29. Tele-Communications Association (TCA)
30. Telecommunications Resellers Association (TRA)
31. Teleport Communications Group Inc. (Teleport)
32. Time Warner Communications Holdings, Inc., (Time Warner)

33. U S West Communications, Inc. (U S West)
34. United States Telephone Association (USTA)

B. Replies

1. Ad Hoc
2. Ameritech
3. Association for Local Telecommunications Services (ALTS)
4. AT&T
5. Bell Atlantic
6. BellSouth
7. Cincinnati Bell
8. Comcast
9. Competitive Telecommunications Association (CompTel)
10. Cox
11. Frontier
12. General Services Administration (GSA)
13. GTE
14. LDDS
15. MCI
16. MFS
17. National Cable Television Association, Inc. (NCTA)
18. NYNEX
19. Pacific Bell
20. Southwestern Bell (SBC)
21. Sprint
22. Sprint Telecommunications Venture
23. Teleport
24. Time Warner
25. TRA
26. U S West
27. USTA

II. *Access Reform NPRM*

A. Comments

1. ACC Long Distance
2. Ad Hoc Telecommunications Users Committee (Ad Hoc)
3. AirTouch Communications, Inc. (AirTouch)
4. Alabama Public Service Commission (Alabama Commission)
5. Alaska Telephone Association

6. Aliant
7. Alliance for Public Technology
8. Allied Communications Group, Inc. (Allied)
9. ALLTEL Telephone Services Corporation (ALLTEL)
10. America On-Line
11. American Association for Adult and Continuing Education, et al.
12. American Association for Retired Person, Consumer Federation of America, and Consumers Union (AARP, et al.)
13. American Library Association
14. American Petroleum Institute (API)
15. America's Carriers Telecommunication Association (ACTA)
16. Ameritech
17. Association for Local Telecommunications Services (ALTS)
18. AT&T
19. Bankers Clearinghouse, et al.
20. Bell Atlantic Telephone Companies and NYNEX (BA/NYNEX)
21. BellSouth Corporation, BellSouth Telecommunications, Inc. (BellSouth)
22. California Cable Television Association (CCTA)
23. (People of the State of) California and the Public Utility Commission of the State of California (California Commission)
24. Cathey, Hutton & Associates
25. Centennial Cellular Corp.
26. Cincinnati Bell Telephone Company (Cincinnati Bell)
27. Citizens for a Sound Economy Foundation (CSE)
28. Citizens Utilities Company (Citizens)
29. Commercial Internet Exchange Association (CIX)
30. Communications Workers of America (CWA)
31. Competition Policy Institute (CPI)
32. Competitive Telecommunications Association (CompTel)
33. Compuserve, Inc. and Prodigy Services Corp. (Compuserve)
34. Consumer Project on Technology (Consumer Project)
35. District of Columbia Public Service Commission (District of Columbia Commission)
36. Evans Telephone Company, et al. (Small Western LECs)
37. Excel Telecommunications, Inc. (Excel)
38. Florida Public Service Commission (Florida Commission)
39. Frederick & Warinner, L.L.C.
40. Frontier Corporation (Frontier)
41. General Communication, Inc. (GCI)
42. General Services Administration/Department of Defense (GSA/DOD)
43. Gray Panthers
44. GTE Service Corp. (GTE)
45. GVNW Inc./Management (GVNW)

46. Harris, Skrivan & Associates, LLC
47. ICG Telecom Group, Inc. (ICG)
48. Illinois Commerce Commission (Illinois Commission)
49. Illuminet
50. Independent Telephone and Telecommunications Alliance (ITTA)
51. Information Industry Association (IIA)
52. Interactive Services Association
53. International Communications Association (ICA)
54. Internet Access Coalition
55. ITCs, Inc.
56. IXC Long Distance, Inc.
57. John Staurulakis, Inc. (Staurulakis)
58. Kansas Corporation Commission (Kansas Commission)
59. LCI International Telecom Corp. (LCI)
60. MCI
61. Media Access Project, et al.
62. Microsoft Corporation (Microsoft)
63. Minnesota Independent Coalition (Minnesota Independent Coalition)
64. Missouri Public Service Commission (Missouri Commission)
65. National Association of Regulatory Utility Commissioners (NARUC)
66. National Cable Television Association, Inc. (NCTA)
67. National Exchange Carrier Association, Inc. (NECA)
68. New York State Department of Public Service (New York Commission)
69. Northern Arkansas Telephone Company
70. Northern Marianna Islands (Commonwealth of)
71. Ohio Consumers' Counsel (Ohio Consumers' Counsel)
72. Ohio Public Utilities Commission (Ohio Commission)
73. Ozarks Technical Community College
74. Pacific Telesis Group (PacTel)
75. Pennsylvania Internet Service Providers (Pennsylvania ISPs)
76. Personal Communications Industry Association (PCIA)
77. Public Utilities Commission of Texas (Texas Commission)
78. Public Utility Commission of Oregon (Oregon Commission)
79. Puerto Rico Telephone Company (PRTC)
80. Jon Radoff
81. Roseville Telephone Company (Roseville)
82. Rural Telephone Coalition (RTC)
83. Rural Telephone Finance Cooperative
84. Rural Utilities Service (RUS)
85. SDN Users Association, Inc.
86. Service-oriented Open Network Technologies, Inc. (SONETECH)
87. South Dakota Public Utilities Commission (South Dakota Commission)
88. Southern New England Telephone Co. (SNET)

89. Southwestern Bell (SBC)
90. Spectranet Interactive, Inc. (Spectranet)
91. Sprint
92. State Consumer Advocates
93. TCA, Inc. (TCA)
94. TDS Telecommunications Corporation (TDS)
95. Telco Communications Group, Inc.
96. Telecommunications Resellers Association (TRA)
97. Tele-Communications, Inc. (TCI)
98. Teleport
99. Tennessee Regulatory Authority (Tennessee Commission)
100. Texas Office of Public Utility Counsel (Texas Public Utility Counsel)
101. Time Warner Communications Holdings, Inc. (Time Warner)
102. U S West
103. USTA
104. Washington Independent Telephone Association (WITA)
105. Washington Utilities and Transportation Commission (Washington Commission)
106. Lyman C. Welch
107. Western Alliance
108. WinStar Communications, Inc. (WinStar)
109. WorldCom, Inc. (WorldCom)

B. Replies

1. ACC Long Distance
2. Ad Hoc
3. Alarm Industry Communications Committee
4. State of Alaska (Alaska Commission)
5. Aliant
6. Alliance for Public Technology
7. ALLTEL Telephone Services Corporation (ALLTEL)
8. America On-Line
9. American Association for Adult and Continuing Education, et al.
10. American Association for Retired Person, Consumer Federation of America, and Consumers Union, and Texas Office of Public Utility Counsel (AARP, et al.)
11. American Communications Services, Inc.
12. Ameritech
13. API
14. Arch Communications Group
15. Association for Local Telecommunications Services (ALTS)
16. AT&T

17. Bankers Clearinghouse, et al.
18. Bell Atlantic Telephone Companies and NYNEX (BA/NYNEX)
19. BellSouth Corporation, BellSouth Telecommunications, Inc. (BellSouth)
20. (People of the State of) California and the Public Utility Commission of the State of California (California Commission)
21. Colorado Library Education and Healthcare Telecommunications Coalition
22. Commercial Internet Exchange Association (CIX)
23. Competitive Telecommunications Association (CompTel)
24. Compuserve
25. Consumer Project on Technology (Consumer Project)
26. Cox
27. General Communication, Inc. (GCI)
28. General Services Administration/Department of Defense (GSA/DOD)
29. Consumers' Utility Counsel Division, [Georgia] Governor's Office of Consumer Affairs (Georgia Consumers' Utility Counsel)
30. Georgia Public Service Commission (Georgia Commission)
31. GTE Service Corp. (GTE)
32. GVNW Inc./Management (GVNW)
33. State of Hawaii (Hawaii)
34. ICG Telecom Group, Inc. (ICG)
35. Internet Access Coalition
36. IXC Long Distance, Inc.
37. LCI International Telecom Corp. (LCI)
38. Maine Public Utilities Commission (Maine Commission)
39. MCI
40. Media Access Project, et al.
41. Minnesota Independent Coalition (Minnesota Independent Coalition)
42. Minnesota Internet Services Trade Association
43. National Cable Television Association, Inc. (NCTA)
44. National Exchange Carrier Association, Inc. (NECA)
45. Ohio Consumers' Counsel (Ohio Consumers' Counsel)
46. Ohio Public Utilities Commission (Ohio Commission)
47. Pacific Telesis Group (PacTel)
48. Personal Communications Industry Association (PCIA)
49. PSINet, Inc. (PSINet)
50. Puerto Rico Telephone Company (PRTC)
51. Roseville Telephone Company (Roseville)
52. Rural Telephone Coalition (RTC)
53. Southern New England Telephone Co. (SNET)
54. Southwestern Bell Telephone Company (SBC)
55. Sprint Corporation (Sprint)
56. State Consumer Advocates
57. TDS Telecommunications Corporation (TDS)

58. Telco Communications Group, Inc.
59. Tele-Communications, Inc. (TCI)
60. Teleport Communications Group Inc. (Teleport)
61. Texas Association of Broadcasters
62. Texas Office of Public Utility Counsel (Texas Public Utility Counsel)
63. The Gallegos Family Network
64. Time Warner Communications Holdings, Inc. (Time Warner)
65. U S West
66. USTA
67. WorldCom, Inc. (WorldCom)

III. *October 5 Public Notice*

A. Comments

1. Ad Hoc
2. America's Carriers Telecommunication Association (ACTA)
3. Ameritech
4. API
5. Association for Local Telecommunications Services (ALTS)
6. AT&T
7. Bell Atlantic
8. BellSouth
9. Cable & Wireless (Cable & Wireless)
10. Cincinnati Bell
11. CompTel
12. Consumer Federation of America (CFA)
13. Consumers Union
14. CoreComm Newco, Inc. (CoreComm)
15. CPI
16. CTSI, Inc. (CTSI)
17. CWA
18. ENTUA
19. Excel Telecommunications, Inc. (Excel)
20. General Services Administration (GSA)
21. GTE
22. KMC Telecom, Inc. (KMC)
23. MCI WorldCom, Inc. (MCI)
24. MediaOne Group, Inc. (MediaOne)
25. NEXTLINK Communications, Inc. (NEXTLINK)
26. Operator Communications, Inc. (OCI)
27. RCN Telecom Services, Inc. (RCN)

28. SBC (SBC)
29. United States Small Business Administration (SBA)
30. Small Business Survival Committee
31. Sprint
32. Time Warner
33. TRA
34. U S West
35. USTA
36. Washington Utilities and Transportation Commission (Washington Commission)
37. Western Wireless Corporation (Western Wireless)

B. Replies

1. Ad Hoc
2. Ameritech
3. API
4. AT&T
5. Bell Atlantic
6. BellSouth
7. CFA
8. Cincinnati Bell
9. CompTel
10. CTSI
11. Excel
12. General Services Administration (GSA)
13. GST Telecom Inc. (GST)
14. GTE
15. ITTA
16. KMC
17. MCI WorldCom, Inc. (MCI)
18. NEXTLINK
19. RCN Telecom Services, Inc. (RCN)
20. SBC (SBC)
21. Sprint
22. TRA
23. U S West
24. USTA

IV. *AT&T Petition for Declaratory Ruling*

A. Comments

1. ALLTEL Communications
2. Ameritech
3. Association for Local Telecommunications Services (ALTS)
4. BellSouth Telecommunications, Inc. (BellSouth)
5. Cable & Wireless USA, Inc. (Cable & Wireless)
6. Cablevision Lightpath, Inc. and NEXTLINK Communications, Inc.
7. Cox Communications (Cox)
8. CTSI, Inc. (CTSI)
9. Freedom Ring Communications
10. Frontier Corp. (Frontier)
11. GTE Service Corp (GTE)
12. GVNW Inc./Management (GVNW)
13. Heart of Iowa Communications, Inc.
14. MCI WorldCom, Inc. (MCI)
15. MediaOne Group, Inc. (MediaOne)
16. MGC Communications, Inc.
17. Optel, Inc.
18. Rainer Cable, Inc.
19. SBC Communications (SBC)
20. Sprint Communications Co., L.P. (Sprint)
21. Telecommunications Resellers Association (TRA)
22. Teligent, Inc.
23. The Orlando Telephone Company
24. Time Warner Telecom (Time Warner)
25. Total Telecommunications Services, Inc.
26. U S West Communications, Inc. (U S West)
27. WinStar Communications, Inc. (WinStar)

B. Replies

1. Ameritech
2. Association for Local Telecommunications Services (ALTS)
3. AT&T Corp. (AT&T)
4. Bell Atlantic
5. CTSI, Inc. (CTSI)
6. MCI WorldCom, Inc. (MCI)
7. MGC Communications, Inc.
8. NEXTLINK Communications, Inc. (NEXTLINK)
9. SBC Communications, Inc. (SBC)

10. Sprint Communications Co., L.P. (Sprint)
11. Total Telecommunications Services, Inc.
12. WinStar Communications, Inc. (WinStar)

V. Forbearance Petitions

1. U S West, Phoenix MSA

a. Comments

1. Ameritech Operating Companies (Ameritech)
2. AT&T Corp. (AT&T)
3. BellSouth Telecommunications, Inc. (BellSouth)
4. Competitive Telecommunications Association (CompTel)
5. GST Telecom Inc.
6. GTE Service Corp. (GTE)
7. MCI WorldCom, Inc. (MCI)
8. Qwest Communications Corp. (Qwest)
9. SBC Communications, Inc. (SBC)
10. Sprint Corporation (Sprint)
11. TSR Wireless LLC (TSR)
12. United States Telephone Association (USTA)

b. Replies

1. Ad Hoc Telecommunications Users Committee (Ad Hoc)
2. AT&T Corp. (AT&T)
3. Bell Atlantic Telephone Companies (Bell Atlantic)
4. GST Telecom Inc.
5. MCI WorldCom, Inc. (MCI)
6. U S West Communications, Inc. (U S West)

2. SBC, Fourteen SBC MSAs

a. Comments

1. Ameritech Operating Companies (Ameritech)
2. Association for Local Telecommunications Services (ALTS)
3. AT&T Corp. (AT&T)
4. Competitive Telecommunications Association (CompTel)
5. GST Telecom Inc.
6. Hyperion Telecommunications, Inc. (Hyperion)

7. KMC Telecom, Inc. (KMC)
8. Logix Communications Corporation.
9. MCI WorldCom, Inc. (MCI)
10. MediaOne Group, Inc. (MediaOne)
11. Network Access Solutions, Inc.
12. NEXTLINK Communications, Inc.
13. Sprint Corporation (Sprint)
14. Telecommunications Resellers Association (TRA)
15. Time Warner Communications Holdings, Inc. d/b/a Time Warner (Time Warner)
16. U S West Communications, Inc. (U S West)
17. United States Telephone Association (USTA)
18. UTC, The Telecommunications Association

b. Replies

1. Ad Hoc Telecommunications Users Committee (Ad Hoc)
2. Bell Atlantic Telephone Companies (Bell Atlantic)
3. Hyperion Telecommunications, Inc. (Hyperion)
4. KMC Telecom, Inc. (KMC)
5. Level 3 Communications Inc.
6. Logix Communications, Corporation
7. NEXTLINK Communications, Inc. (NEXTLINK)
8. SBC Communications, Inc. (SBC)
9. Telecommunications Resellers Association (TRA)

3. U S West, Seattle MSA

a. Comments

1. Association for Local Telephone Services (ALTS)
2. AT&T Corp. (AT&T)
3. Competitive Telecommunications Association/America's Carriers Telecommunications Association (CompTel)
4. Ms. Sue Conachan
5. Ms. Kathryn Fancher
6. Focal Communications, Inc. (Focal)
7. General Services Administration (GSA)
8. GST Telecom Inc.
9. Hyperion Telecommunications, Inc. (Hyperion)
10. MCI WorldCom, Inc. (MCI)
11. Network Access Solutions, Inc.

12. NEXTLINK Communications Inc. and Electric Lightwave, Inc. (NEXTLINK)
13. SBC Communications (SBC)
14. Sprint Corporation (Sprint)
15. Telecommunications Resellers Association (TRA)
16. Washington Association of Internet Service Providers
17. WGHT Pompton Lakes NJ

b. Replies

1. Bell Atlantic Telephone Companies (Bell Atlantic)
2. General Services Administration (GSA)
3. Qwest Communications Corp. (Qwest)
4. U S West Communications, Inc. (U S West)

4. Bell Atlantic, Twelve Bell Atlantic Study Areas

a. Comments

1. Association for Local Telecommunications Services (ALTS)
2. AT&T Corp. (AT&T)
3. Cablevision Lightpath, Inc
4. Capital One Financial Services
5. CBS Broadcasting Corporation, National Broadcasting Company, Turner Broadcasting System, Inc., and The Walt Disney Corporation
6. Competitive Telecommunications Association/America's Carriers Telecommunications Association (CompTel)
7. CTSI, Inc & RCN Telecom
8. General Services Administration (GSA)
9. Hyperion Telecommunications, Inc. (Hyperion)
10. Mr. Marcel Kates
11. KMC Telecom, Inc
12. Marriott Corporation (Marriott)
13. MCI WorldCom, Inc. (MCI)
14. MediaOne Group (MediaOne)
15. Network Access Solutions, Inc.
16. Network Plus, Inc.
17. NEXTLINK Communications, Inc. (NEXTLINK)
18. Sprint Corporation (Sprint)
19. Telecommunications Resellers Association
20. Mr. Jerry Thompson

21. Time Warner Communications Holdings, Inc. d/b/a Time Warner (Time Warner)
22. United States Telephone Association (USTA)
23. xDSL Networks, Inc.

b. Replies

1. Bell Atlantic Telephone Companies (Bell Atlantic)
2. General Services Administration (GSA)

5. Ameritech, Chicago LATA

a. Comments

1. Association for Local Telephone Services (ALTS)
2. AT&T Corp. (AT&T)
3. Competitive Telecommunications Association (CompTel)
4. Core Comm, Ltd. (CoreComm)
5. Focal Communications Corporation and KMC Telecom, Inc.
6. MCI WorldCom, Inc. (MCI)
7. McLeod USA Telecommunications Services, Inc.
8. NEXTLINK Communications, Inc. (NEXTLINK)
9. SBC Communications, Inc. (SBC)
10. Sprint Corporation (Sprint)
11. Telecommunications Resellers Association (TRA)
12. United States Telephone Association (USTA)

b. Replies

1. Ameritech Operating Companies (Ameritech)

APPENDIX B

AMENDMENTS TO THE CODE OF FEDERAL REGULATIONS

PART 0 -- COMMISSION ORGANIZATION

1. The authority citation continues to read as follows:

Authority: Sec. 5, 48 Stat. 1068, as amended; 47 U.S.C. 155.

2. Revise § 0.291 by adding paragraph (i) to read as follows:

§ 0.291 Authority delegated.

* * * * *

(i) *Authority concerning petitions for pricing flexibility.*

(1) The Chief, Common Carrier Bureau, shall have authority to act on petitions filed pursuant to Part 69, Subpart H, of this chapter for pricing flexibility involving special access and dedicated transport services. This authority is not subject to the limitation set forth in paragraph (a)(2) of this section.

(2) The Chief, Common Carrier Bureau, shall not have authority to act on petitions filed pursuant to Part 69, Subpart H, of this chapter for pricing flexibility involving common line and traffic sensitive services.

PART 1 -- PRACTICE AND PROCEDURE

3. The authority citation continues to read as follows:

Authority: 15 U.S.C. 79 *et seq.*, 47 U.S.C. 151, 154(i), 154(j), 155, 225, and 303(r).

4. Revise § 1.773 by adding paragraph (a)(1)(v), to read as follows:

(v) For the purposes of this section, any tariff filing by a price cap LEC filed pursuant to the requirements of Section 61.42(d)(4)(ii) of this chapter will be considered *prima facie* lawful, and will not be suspended by the Commission unless the petition requesting suspension shows each of the following:

- (A) That there is a high probability the tariff would be found unlawful after investigation;
- (B) That any unreasonable rate would not be corrected in a subsequent filing;
- (C) That irreparable injury will result if the tariff filing is not suspended; and
- (D) That the suspension would not otherwise be contrary to the public interest.

5. Add § 1.774 to read as follows:

§ 1.774 Pricing flexibility

(a) *Petitions.*

(1) A petition seeking pricing flexibility for specific services pursuant to Part 69, Subpart H, of this chapter, with respect to a metropolitan statistical area (MSA), as defined in Section 22.909(a) of this chapter, or the non-MSA parts of a study area, must show that the price cap LEC has met the relevant thresholds set forth in Part 69, Subpart H, of this chapter.

(2) The petition must make a separate showing for each MSA for which the petitioner seeks pricing flexibility, and for the portion of the study area that falls outside any MSA.

(3) Petitions seeking pricing flexibility for services described in Sections 69.709(a) and 69.711(a) of this chapter must include:

(i) the total number of wire centers in the relevant MSA or non-MSA parts of a study area, as described in Section 69.707 of this chapter;

(ii) the number and location of the wire centers in which competitors have collocated in the relevant MSA or non-MSA parts of a study area, as described in Section 69.707 of this chapter;

(iii) in each wire center on which the price cap LEC bases its petition, the name of at least one collocator that uses transport facilities owned by a provider other than the price cap LEC to transport traffic from that wire center; and

(iv)(A) the percentage of the wire centers in the relevant MSA or non-MSA area, as described in Section 69.707 of this chapter, in which competitors have collocated and use transport facilities owned by a provider other than the price cap LEC to transport traffic from that wire center; or

(B) the percentage of total base period revenues generated by the services at issue in the petition that are attributable to wire centers in the relevant MSA or non-MSA area, as described in Section 69.707 of this chapter, in which competitors have collocated and use transport facilities owned by a provider other than the price cap LEC to transport traffic from that wire center.

(4) Petitions seeking pricing flexibility for services described in Section 69.713(a) of this chapter must make a showing sufficient to meet the relevant requirements of Section 69.713.

(b) *Confidential treatment* A price cap LEC wishing to request confidential treatment of information contained in a pricing flexibility petition should demonstrate, by a preponderance of the evidence, that the information should be withheld from public inspection in accordance with the requirements of Section 0.459 of this chapter.

(c) *Oppositions.* Any interested party may file comments or oppositions to a petition for pricing flexibility. Comments and oppositions shall be filed no later than 15 days after the petition is filed. Time shall be computed pursuant to Section 1.4 of this part.

(d) *Replies.* The petitioner may file a reply to any oppositions filed in response to its petition for pricing flexibility. Replies shall be filed no later than 10 days after comments are filed. Time shall be computed pursuant to Section 1.4 of this part.

(e) *Copies, service.*

(1)(i) Any price cap LEC filing a petition for pricing flexibility must submit its petition pursuant to the Commission's Electronic Tariff Filing System (ETFS), following the procedures set forth in Section 61.14(a) of this chapter.

(ii) The price cap LEC must provide to each party upon which the price cap LEC relies to meet its obligations under paragraph (a)(3)(iii) of this section, the information it provides about that party in its petition, even if the price cap LEC requests that the information be kept confidential under paragraph (b) of this section.

(A) The price cap LEC must certify in its pricing flexibility petition that it has made such information available to the party.

(B) The price cap LEC may provide data to the party in redacted form, revealing only that information to the party that relates to the party.

(C) The price cap LEC must provide to the Commission copies of the information it provides to such parties.

(2)(i) Interested parties filing oppositions or comments in response to a petition for pricing flexibility may file those comments through ETFS.

(ii) Any interested party electing to file an opposition or comment in response to a pricing flexibility petition through a method other than ETFS must file an original and four copies of each opposition or comment with the Commission, as follows: the original and three copies of each pleading shall be filed with the Secretary, FCC, Room CY-A257, 445 Twelfth St. S.W., Washington, D.C., 20554; one copy must be delivered directly to the Commission's copy contractor, International Transcription Service, Inc., 1231 Twentieth St. N.W., Washington, D.C. 20036. Additional, separate copies shall be served simultaneously upon the Chief, Common Carrier Bureau; the Chief, Competitive Pricing Division; and the Chief, Tariff and Pricing Analysis Branch of the Competitive Pricing Division.

(iii) In addition, oppositions and comments shall be served either personally or via facsimile on the petitioner. If an opposition or comment is served via facsimile, a copy of the opposition or comment must be sent to the petitioner via first class mail on the same day as the facsimile transmission.

(3) Replies shall be filed with the Commission through ETFS. In addition, petitioners choosing to file a reply must serve a copy on each party filing an opposition or comment, either personally or via facsimile. If a reply is served via facsimile, a copy of the reply must be sent to the recipient of that reply via first class mail on the same day as the facsimile transmission.

(f) *Disposition.*

(1) A petition for pricing flexibility pertaining to special access and dedicated transport services shall be deemed granted unless the Chief, Common Carrier Bureau, denies the petition no later than 90 days after the close of the pleading cycle. The period for filing applications for review begins the day the Bureau grants or denies the petition, or the day that the petition is deemed denied. Time shall be computed pursuant to Section 1.4 of this part.

(2) A petition for pricing flexibility pertaining to common-line and traffic-sensitive services shall be deemed granted unless the Commission denies the petition no later than five months after the close of the pleading cycle. Time shall be computed pursuant to Section 1.4 of this part.

PART 61 -- TARIFFS

6. The authority citation continues to read as follows:

Authority: Secs. 1, 4(i), 4(j), 201-205, and 403 of the Communications Act of 1934, as amended; 47 U.S.C. 151, 154(i), 154(j), 201-205, and 403, unless otherwise noted.

7. Amend § 61.3 by revising paragraph (m) and adding paragraphs (nn), (oo), and (pp), to read as follows:

§ 61.3 Definitions.

* * * * *

(m) *Contract-based Tariff.* A tariff based on a service contract entered into between a non-dominant carrier and a customer, or between a customer and a price cap local exchange carrier which has obtained permission to offer contract-based tariff services pursuant to Part 69, Subpart H, of this chapter.

* * * * *

(nn) *Corridor service.* "Corridor service" refers to interLATA services offered in the "limited corridors" established by the District Court in *United States v. Western Electric Co., Inc.*, 569 F. Supp. 1057, 1107 (D.D.C. 1983).

(oo) *Toll dialing parity.* "Toll dialing parity" exists when there is dialing parity, as defined in Section 51.5 of this chapter, for toll services.

(pp) *Loop-based services.* Loop-based services are services that employ Subcategory 1.3 facilities, as defined in Section 36.154 of this chapter.

8. Amend § 61.42 by redesignating paragraph (d)(4) as (d)(4)(i), and adding paragraph (d)(4)(ii), to read as follows:

§ 61.42 Price cap baskets and service categories.

* * * * *

(d) * * *

(4) * * *

(ii) If a price cap carrier has implemented interLATA and intraLATA toll dialing parity everywhere it provides local exchange services at the holding company level, that

price cap carrier may file a tariff revision to remove corridor and interstate intraLATA toll services from its interexchange basket.

9. Amend § 61.45 by revising paragraph (d)(1)(vii), to read as follows:

§ 61.45 Adjustments to the PCI for local exchange carriers.

* * * * *

(d) * * *

(1) * * *

(vii) Retargeting the PCI to the level specified by the Commission for carriers whose base year earnings are below the level of the lower adjustment mark, subject to the limitation in Section 69.731 of this chapter.

10. Amend § 61.46 to add paragraph (i) to read as follows:

§ 61.46 Adjustments to the API.

* * * * *

(i) In no case shall a price cap local exchange carrier include data associated with services offered pursuant to contract tariff in the calculations required by this section.

11. Amend § 61.47 to revise paragraphs (a) and (e)(1), and to add paragraphs (f) and (k), to read as follows:

§ 61.47 Adjustments to the SBI; pricing bands.

(a) In connection with any price cap tariff filing proposing changes in the rates of services in service categories, subcategories, or density zones, the carrier must calculate an SBI value for each affected service category, subcategory, or density zone pursuant to the following methodology: * * *

* * * * *

(e) Pricing bands shall be established each tariff year for each service category and subcategory within a basket. Each band shall limit the pricing flexibility of the service category,

subcategory, as reflected in the SBI, to an annual increase of a specified percent listed in this paragraph below, relative to the percentage change in the PCI for that basket, measured from the levels in effect on the last day of the preceding tariff year. For local exchange carriers subject to price cap regulation as that term is defined in Section 61.3(x) of this part, there shall be no lower pricing band for any service category or subcategory.

(1) Five percent:

- (i) Local switching (traffic sensitive basket)
- (ii) Information (traffic sensitive basket)
- (iii) Database Access services (traffic sensitive basket)
- (iv) 800 Database Vertical Services subservice (traffic sensitive basket)
- (v) Billing Name and Address (traffic sensitive basket)
- (vi) Local switching trunk ports (traffic sensitive basket)
- (vii) Signalling Transfer Point Port Termination (traffic sensitive basket)
- (viii) Voice grade (trunking basket)
- (ix) Audio/Video (trunking basket)
- (x) Total High Capacity (trunking basket)
- (xi) DS1 subservice (trunking basket)
- (xii) DS3 subservice (trunking basket)
- (xiii) Wideband (trunking basket)

* * *

(f) A local exchange carrier subject to price cap regulation may establish density zones pursuant to the requirements set forth in Section 69.123 of this chapter, for any service in the trunking basket, other than the interconnection charge set forth in Section 69.124 of this chapter. The pricing flexibility of each zone shall be limited to an annual increase of 15 percent, relative to the percentage change in the PCI for that basket, measured from the levels in effect on the last day of the preceding tariff year. There shall be no lower pricing band for any density zone.

* * * * *

(k) In no case shall a price cap local exchange carrier include data associated with services offered pursuant to contract tariff in the calculations required by this section.

12. In § 61.49, revise paragraphs (f)(2) and (g), and add (f)(3) and (f)(4), to read as follows:

§ 61.49 Supporting information to be submitted with letters of transmittal for tariffs of carriers subject to price cap regulation.

* * * * *

(f) * * *

(2) Each tariff filing submitted by a price cap LEC that introduces a new loop-based service, as defined in Section 61.3(pp) of this part -- including a restructured unbundled basic service element (BSE), as defined in Section 69.2(mm) of this chapter, that constitutes a new loop-based service -- that is or will later be included in a basket, must be accompanied by cost data sufficient to establish that the new loop-based service or unbundled BSE will not recover more than a just and reasonable portion of the carrier's overhead costs.

(3) A price cap LEC may submit without cost data any tariff filings that introduce new services, other than loop-based services.

(4) A price cap LEC that has removed its corridor or interstate intraLATA toll services from its interexchange basket pursuant to Section 61.42(d)(4)(ii) of this part, may submit its tariff filings for corridor or interstate intraLATA toll services without cost data.

(g) Each tariff filing submitted by a local exchange carrier subject to price cap regulation that introduces a new loop-based service or a restructured unbundled basic service element (BSE), as defined in Section 69.2(mm) of this chapter, that is or will later be included in a basket, or that introduces or changes the rates for connection charge subelements for expanded interconnection, as defined in Section 69.121 of this chapter, must also be accompanied by:

* * *

13. Add § 61.55 to read as follows:

§ 61.55 Contract-based tariffs.

(a) This section shall apply to price cap LECs permitted to offer contract-based tariffs under Section 69.727(a) of this chapter.

(b) Composition of contract-based tariffs shall comply with Sections 61.54(b) through (i) of this part.

(c) Contract-based tariffs shall include the following:

- (1) The term of contract, including any renewal options;
- (2) A brief description of each of the services provided under the contract;
- (3) Minimum volume commitments for each service;

(4) The contract price for each service or services at the volume levels committed to by the customers;

(5) A general description of any volume discounts built into the contract rate structure; and

(6) A general description of other classifications, practices, and regulations affecting the contract rate.

14. Amend § 61.58 to revise paragraphs (b) and (c), and add (d), to read as follows:

§ 61.58 Notice requirements.

* * * * *

(b) Tariffs for new services filed by price cap local exchange carriers shall be filed on at least one day's notice.

(c) Contract-based tariffs filed by price cap local exchange carriers pursuant to Sections 69.727(a) of this chapter shall be filed on at least one day's notice.

(d)(1) A local exchange carrier that is filing a tariff revision to remove its corridor or interstate intraLATA toll services from its interexchange basket pursuant to Section 61.42(d)(4)(ii) of this part shall submit such filing on at least fifteen days' notice.

(2) A local exchange carrier that has removed its corridor and interstate intraLATA toll services from its interexchange basket pursuant to Section 61.42(d)(4)(ii) of this part shall file subsequent tariff filings for corridor or interstate intraLATA toll services on at least one day's notice.

PART 69 -- ACCESS CHARGES

15. The authority citation continues to read as follows:

Authority: 47 U.S.C. 154, 201, 202, 203, 205, 218, 220, 254, 403.

16. Amend § 69.4 by revising subparagraph (e)(7) to read as follows:

§ 69.3 Filing of Access Service Tariffs

* * * * *

(7) Such a tariff shall not contain charges for any access elements that are disaggregated or deaveraged within a study area that is used for purposes of jurisdictional separations, except as otherwise provided in this chapter.

17. Amend § 69.4 by revising paragraph (g) and adding paragraph (i), to read as follows:

§ 69.4 Charges to be filed.

* * * * *

(g) Local exchange carriers subject to price cap regulation, as that term is defined in Section 61.3(x) of this chapter, may establish appropriate rate elements for a new service, within the meaning of Section 61.3(t) of this chapter, in any tariff filing with a scheduled effective date after [insert date 30 days after publication in the Federal Register].

* * * * *

(i) Paragraphs (b) and (h) of this section are not applicable to a price cap local exchange carrier to the extent that it has been granted the pricing flexibility in Section 69.727(b)(1) of this part.

18. In § 69.110, revise paragraph (e) to read as follows:

§ 69.110 Entrance facilities.

* * * * *

(e) Except as provided in paragraphs (f), (g), and (h) of this section, and Subpart H of this chapter, telephone companies shall not offer entrance facilities based on term discounts or volume discounts for multiple DS3s or any other service with higher volume than DS3.

19. Amend § 69.123 by revising paragraphs (a), (b), (e)(2), and (f)(1), to read as follows:

§ 69.123 Density pricing zones.

(a)(1) Incumbent local exchange carriers not subject to price cap regulation may establish a reasonable number of density pricing zones within each study area that is used for purposes of jurisdictional separations, in which at least one interconnector has taken the subelement of

connection charges for expanded interconnection described in Section 69.121(a)(1) of this subpart.

(2) Such a system of pricing zones shall be designed to reasonably reflect cost-related characteristics, such as the density of total interstate traffic in central offices located in the respective zones.

(3) Non-price cap incumbent local exchange carriers may establish only one set of density pricing zones within each study area, to be used for the pricing of both special and switched access pursuant to paragraphs (c) and (d) of this section.

(b)(1) Incumbent local exchange carriers subject to price cap regulation may establish any number of density zones within a study area that is used for purposes of jurisdictional separations, provided that each zone, except the highest-cost zone, accounts for at least 15 percent of that carrier's trunking basket revenues within that study area, calculated pursuant to the methodology set forth in Section 69.725 of this part.

(2) Price cap incumbent local exchange carriers may establish only one set of density pricing zones within each study area, to be used for the pricing of all services within the trunking basket for which zone density pricing is permitted.

(3) An access service subelement for which zone density pricing is permitted shall be deemed to be offered in the zone that contains the telephone company location from which the service is provided.

(4) An access service subelement for which zone density pricing is permitted which is provided to a customer between telephone company locations shall be deemed to be offered in the highest priced zone that contains one of the locations between which the service is offered.

* * *

(e) * * *

(2) Notwithstanding Section 69.3(e)(7) of this part, incumbent local exchange carriers subject to price cap regulation may charge different rates for services in different zones pursuant to Section 61.47(f) of this chapter, provided that the charges for any such service are not deaveraged within any such zone.

(f)(1) An incumbent local exchange carrier that establishes density pricing zones under this section must reallocate additional amounts recovered under the interconnection charge prescribed in Section 69.124 of this subpart to facilities-based transport rates, to reflect the higher costs of serving lower density areas. Each incumbent local exchange carrier must reallocate costs

from the interexchange charge each time it increases the ratio between the prices in its lowest-cost zone and any other zone in that study area.

* * * * *

20. Revise Part 69 by adding Subpart H to read as follows:

Subpart H -- Pricing Flexibility

§ 69.701 Application of rules in this subpart.

The rules in this subpart apply to all incumbent LECs subject to price cap regulation, as defined in Section 61.3(x) of this chapter, seeking pricing flexibility on the basis of the development of competition in parts of its service area.

§ 69.703 Definitions.

For purposes of this subpart:

(a) *Channel terminations.*

(1) A channel termination between an IXC POP and a serving wire center is a dedicated channel connecting an IXC POP and a serving wire center, offered for purposes of carrying special access traffic.

(2) A channel termination between a LEC end office and a customer premises is a dedicated channel connecting a LEC end office and a customer premises, offered for purposes of carrying special access traffic.

(b) *Metropolitan Statistical Area (MSA).* This term shall have the definition provided in Section 22.909(a) of this chapter.

(c) *Interexchange Carrier Point of Presence (IXC POP).* The point of interconnection between an interexchange carrier's network and a local exchange carrier's network.

(d) *Wire center.* For purposes of this subpart, the term "wire center" shall refer to any location at which an incumbent LEC is required to provide expanded interconnection for special access pursuant to Section 64.1401(a) of this chapter, and any location at which an incumbent LEC is required to provide expanded interconnection for switched transport pursuant to Section 64.1401(b)(1) of this chapter.

(e) *Study area.* A common carrier's entire service area within a state.

§ 69.705 Procedure.

Price cap LECs filing petitions for pricing flexibility shall follow the procedures set forth in Section 1.774 of this chapter.

§ 69.707 Geographic scope of petition.

(a) *MSA.*

(1) A price cap LEC filing a petition for pricing flexibility in an MSA shall include data sufficient to support its petition, as set forth in this subpart, disaggregated by MSA.

(2) A price cap LEC may request pricing flexibility for two or more MSAs in a single petition, provided that it submits supporting data disaggregated by MSA.

(b) *Non-MSA.*

(1) A price cap LEC will receive pricing flexibility with respect to those parts of a study area that fall outside of any MSA, provided that it provides data sufficient to support a finding that competitors have collocated in a number of wire centers in that non-MSA region sufficient to satisfy the criteria for the pricing flexibility sought in the petition, as set forth in this subpart, if the region at issue were an MSA.

(2) The petitioner may aggregate data for all the non-MSA regions in a single study area for which it requests pricing flexibility in its petition.

(3) A petitioner may request pricing flexibility in the non-MSA regions of two or more of its study areas, provided that it submits supporting data disaggregated by study area.

§ 69.709 Dedicated transport and special access services other than channel terminations between LEC end offices and customer premises.

(a) *Scope.* This paragraph governs requests for pricing flexibility with respect to the following services:

(1) Entrance facilities, as described in Section 69.110 of this part.

(2) Transport of traffic over dedicated transport facilities between the serving wire center and the tandem switching office, as described in Section 69.111(a)(2)(iii) of this part.

(3) Direct-trunked transport, as described in Section 69.112 of this part.

(4) Special access services, as described in Section 69.114 of this part, other than channel terminations as defined in Section 69.703(a)(2) of this subpart.

(b) *Phase I Triggers.* To obtain Phase I pricing flexibility, as specified in Section 69.727(a) of this subpart, for the services described in paragraph (a) of this section, a price cap LEC must show that, in the relevant area as described in Section 69.707 of this subpart, competitors unaffiliated with the price cap LEC have collocated:

(1) in fifteen percent of the petitioner's wire centers, and that at least one such collocator in each wire center is using transport facilities owned by a transport provider other than the price cap LEC to transport traffic from that wire center; or

(2) in wire centers accounting for 30 percent of the petitioner's revenues from dedicated transport and special access services other than channel terminations between LEC end offices and customer premises, determined as specified in Section 69.725 of this subpart, and that at least one such collocator in each wire center is using transport facilities owned by a transport provider other than the price cap LEC to transport traffic from that wire center.

(c) *Phase II Triggers.* To obtain Phase II pricing flexibility, as specified in Section 69.727(b) of this subpart, for the services described in paragraph (a) of this section, a price cap LEC must show that, in the relevant area as described in Section 69.707 of this subpart, competitors unaffiliated with the price cap LEC have collocated:

(1) in 50 percent of the petitioner's wire centers, and that at least one such collocator in each wire center is using transport facilities owned by a transport provider other than the price cap LEC to transport traffic from that wire center; or

(2) in wire centers accounting for 65 percent of the petitioner's revenues from dedicated transport and special access services other than channel terminations between LEC end offices and customer premises, determined as specified in Section 69.725 of this subpart, and that at least one such collocator in each wire center is using transport facilities owned by a transport provider other than the price cap LEC to transport traffic from that wire center.

§ 69.711 Channel terminations between LEC end offices and customer premises.

(a) *Scope.* This paragraph governs requests for pricing flexibility with respect to channel terminations between LEC end offices and customer premises.

(b) *Phase I Triggers.* To obtain Phase I pricing flexibility, as specified in Section 69.727(a) of this subpart, for channel terminations between LEC end offices and customer premises, a price cap LEC must show that, in the relevant area as described in Section 69.707 of this subpart, competitors unaffiliated with the price cap LEC have collocated:

(1) in 50 percent of the petitioner's wire centers, and that at least one such collocator in each wire center is using transport facilities owned by a transport provider other than the price cap LEC to transport traffic from that wire center; or

(2) in wire centers accounting for 65 percent of the petitioner's revenues from channel terminations between LEC end offices and customer premises, determined as specified in Section 69.725 of this subpart, and that at least one such collocator in each wire center is using transport facilities owned by a transport provider other than the price cap LEC to transport traffic from that wire center.

(c) *Phase II Triggers.* To obtain Phase II pricing flexibility, as specified in Section 69.727(b) of this subpart, for channel terminations between LEC end offices and customer premises, a price cap LEC must show that, in the relevant area as described in Section 69.707 of this subpart, competitors unaffiliated with the price cap LEC have collocated:

(1) in 65 percent of the petitioner's wire centers, and that at least one such collocator in each wire center is using transport facilities owned by a transport provider other than the price cap LEC to transport traffic from that wire center; or

(2) in wire centers accounting for 85 percent of the petitioner's revenues from channel terminations between LEC end offices and customer premises, determined as specified in Section 69.725 of this subpart, and that at least one such collocator in each wire center is using transport facilities owned by a transport provider other than the price cap LEC to transport traffic from that wire center.

§ 69.713 Common line, traffic-sensitive, and tandem-switched transport services.

(a) *Scope.* This paragraph governs requests for pricing flexibility with respect to the following services:

(1) Common line services, as described in Sections 69.152, 69.153, and 69.154 of this part.

(2) Services in the traffic-sensitive basket, as described in Section 61.42(d)(2) of this chapter.

(3) The traffic-sensitive components of tandem-switched transport services, as described in Sections 69.111(a)(2)(i) and (ii) of this part.

(b) *Phase I Triggers.*

(1) To obtain Phase I pricing flexibility, as specified in Section 69.727(a) of this subpart, for the services identified in paragraph (a) of this section, a price cap LEC must provide convincing evidence that, in the relevant area as described in Section 69.707 of this subpart, its unaffiliated competitors, in aggregate, offer service to at least 15 percent of the price cap LEC's customer locations.

(2) For purposes of the showing required by paragraph (b)(1), the price cap LEC may not rely on service the competitors provide solely by reselling the price cap LEC's services, or provide through unbundled network elements as defined in Section 51.5 of this chapter, except that the price cap LEC may rely on service the competitors provide through the use of the price cap LEC's unbundled loops.

(c) [Reserved.]

§§ 69.714-69.724 [Reserved.]

§ 69.725 Attribution of revenues to particular wire centers.

If a price cap LEC elects to show, in accordance with Sections 69.709 or 69.711 of this subpart, that competitors have collocated in wire centers accounting for a certain percentage of revenues from the services at issue, the LEC must make the following revenue allocations:

(a) For entrance facilities and channel terminations between an IXC POP and a serving wire center, the petitioner shall attribute all the revenue to the serving wire center.

(b) For channel terminations between a LEC end office and a customer premises, the petitioner shall attribute all the revenue to the LEC end office.

(c) For any dedicated service routed through multiple wire centers, the petitioner shall attribute 50 percent of the revenue to the wire center at each end of the transmission path, unless the petitioner can make a convincing case in its petition that some other allocation would be more representative of the extent of competitive entry in the MSA or the non-MSA parts of the study area at issue.

§ 69.727 Regulatory relief.

(a) *Phase I Relief.* Upon satisfaction of the Phase I triggers specified in Sections 69.709(b), 69.711(b), or 69.713(b) of this subpart for an MSA or the non-MSA parts of a study area, a price cap LEC will be granted the following regulatory relief in that area for the services specified in Sections 69.709(a), 69.711(a), or 69.713(a) of this subpart, respectively:

- (1) Volume and term discounts;
- (2) Contract tariff authority, provided that
 - (i) Contract tariff services are made generally available to all similarly situated customers; and
 - (ii) The price cap LEC excludes all contract tariff offerings from price cap regulation pursuant to Section 61.42(f)(1) of this chapter.
 - (iii) Before the price cap LEC provides a contract tariffed service, under Sections 69.727(a) of this subpart, to one of its long-distance affiliates, as described in Section 272 of the Communications Act of 1934, as amended, or Section 64.1903 of this chapter, the price cap LEC certifies to the Commission that it provides service pursuant to that contract tariff to an unaffiliated customer.

(b) *Phase II Relief.* Upon satisfaction of the Phase II triggers specified in Sections 69.709(c) or 69.711(c) of this subpart for an MSA or the non-MSA parts of a study area, a price cap LEC will be granted the following regulatory relief in that area for the services specified in Sections 69.709(a) or 69.711(a) of this subpart, respectively:

- (1) Elimination of the rate structure requirements in Part 69, Subpart B, of this chapter;
- (2) Elimination of price cap regulation; and
- (3) Filing of tariff revisions on one day's notice, notwithstanding the notice requirements for tariff filings specified in Section 61.58 of this chapter.

§ 69.729 New services.

(a) Except for new services subject to paragraph (b) of this section, a price cap LEC may obtain pricing flexibility for a new service that has not been incorporated into a price cap basket by demonstrating in its pricing flexibility petition that the new service would be properly

incorporated into one of the price cap baskets and service bands for which the price cap LEC seeks pricing flexibility.

(b) Notwithstanding paragraph (a) of this section, a price cap LEC must demonstrate satisfaction of the triggers in Section 69.711(b) of this subpart to be granted pricing flexibility for any new service that falls within the definition of a "channel termination between a LEC end office and a customer premises" as specified in Section 69.703(a)(2) of this subpart.

§ 69.731 Low-end adjustment mechanism.

(a) Any price cap LEC obtaining Phase I or Phase II pricing flexibility for any service in any MSA in its service region, or for the non-MSA portion of any study area in its service region, shall be prohibited from making any low-end adjustment pursuant to Section 61.45(d)(1)(vii) of this chapter in all or part of its service region.

(b) Any affiliate of any price cap LEC obtaining Phase I or Phase II pricing flexibility for any service in any MSA in its service region shall be prohibited from making any low-end adjustment pursuant to Section 61.45(d)(1)(vii) of this chapter in all or part of its service region.

**Separate Statement
of
Commissioner Susan Ness**

Re: Access Charge Reform (CC Docket No. 96-262); Price Cap Performance Review for Local Exchange Carriers (CC Docket No. 94-1).

During the past decade, exchange access competition has increased significantly. I am optimistic that the investment and infrastructure deployment that has occurred demonstrates a strong and irreversible trend toward a multiplicity of carriers in the marketplace. We must ensure that our regulations do not impede this progress.

Part of the calculus is to determine not just when to regulate, but when to deregulate. Today we take a measured step forward. By first providing incumbents with some downward pricing flexibility for high-capacity services, we allow them to respond to the new competitive marketplace for these services. Consumers should also benefit from lower prices. And, by using the presence of collocation in a market as the trigger for regulatory relief, incumbents should have additional incentives to work more cooperatively with new entrants - ironing out collocation wrinkles that should have disappeared long ago.

Although I am enthusiastic about this step forward, I cast my vote with guarded optimism. I intend to watch marketplace reactions very carefully. I prefer to act incrementally, so that we can ensure that no harm to competition occurs. If the framework we set out today is successful, I expect to take more steps in this direction as we continue down a path toward deregulation.

**SEPARATE STATEMENT OF
COMMISSIONER HAROLD FURCHTGOTT-ROTH
APPROVING IN PART, CONCURRING IN PART,
AND DISSENTING IN PART**

Re: Access Charge Reform, CC Docket No. 96-262, Price Cap Performance Review for Local Exchange Carriers, CC Docket No. 94-1, Interexchange Carrier Purchases of Switched Access Services Offered by Competitive Local Exchange Carriers, CCB/CPD File No. 98-63, Petition of U S West Communications, Inc. for Forbearance from Regulation as a Dominant Carrier in the Phoenix, Arizona MSA, CC Docket No. 98-157.

It is very difficult to rationalize any occasion where the government stands between consumers and lower prices. Thus I support much of the regulatory relief contemplated in this item. As a result of the relief made possible by today's Order, the Commission will begin to release its regulatory hold on certain carriers operating in competitive markets. I respectfully dissent from portions of this item posing the mere suggestion of regulating competitive carriers in these same markets.

I fully support the immediate regulatory relief granted in this item. In my view, any reduction of unnecessary regulatory burdens is beneficial. The Commission should streamline its procedures wherever possible to lessen the administrative burden imposed by regulation.

Today's Order establishes triggering mechanisms that will open the door to a degree of regulatory relief that will, in turn, provide lower prices to consumers. While I support the relief made possible by these triggering mechanisms, I remain concerned that these tests may be more cumbersome than necessary. Although the goal of identifying competitive conditions in order to provide regulatory relief is commendable, I would have preferred a simpler approach. I am particularly concerned that the "trigger" for providing relief to providers of switched access services could prove extraordinarily cumbersome in its execution. Notwithstanding these concerns, however, I wholeheartedly support the idea of letting prices fall as a result of competitive forces, and accordingly, I concur with this section of the Order to the extent it makes this regulatory relief possible.

Although the Notice of Proposed Rulemaking details additional *deregulatory* proposals that I can support, I object to the mere suggestion of adopting *new* regulatory approaches to CLEC terminating access. On numerous occasions, I have made clear my opposition to any suggestion that the Commission may return, despite the presence of competition, to old habits of regulating carriers.¹ Any such proposal has a chilling effect on industry participants. Moreover, the mere suggestion of regulating a competitive market is antithetical to the Telecommunications Act of 1996. I also note that I am troubled by the suggestion to deaverage the Subscriber Line Charge and the Presubscribed Interexchange Carrier Charge based on geographic zones within a state, as I am not sure that it is appropriate for the federal government to set different rate elements for similar customers within a state.

¹ See, e.g., Dissenting Statement of Commissioner Harold Furchtgott-Roth, Low-Volume Long-Distance Users, CC Docket 99-249.