

### C. Incentives for Anticompetitive Pricing

Throughout the transition and for an indefinite time beyond, the Commission will continue to confront the problem of regulating the NECs and LECs in such a way as to bring the benefits of workable competition (and thus regulatory forbearance) into as many markets and services as possible. In this context, the issue of potential anticompetitive behavior on the part of such firms remains a serious concern. The majority of such anticompetitive behavior is price related, including the pricing of competitive services at unreasonably low levels (competitive underpricing), the use of revenues from less competitive services to financially support, or cross-subsidize, more competitive services, and the overpricing of bottleneck services, including those used by competitors.

When dealing with the subject of costs apportioned between a utility's noncompetitive (monopoly) and competitive operations, a cross-subsidy is said to exist within the firm if the revenue from one of its noncompetitive services is used to offset the cost of one of its competitive services, thereby allowing the firm to price the latter service below cost.

More generally, a problem exists whenever a firm operating in both monopoly and competitive markets takes advantage of opportunities which may exist to shift costs from the former to the latter category, to overprice its less competitive services, and/or to underprice its more competitive services. A generic term for these practices, including those which fall within the strict definition of "cross-subsidization" and those which do not, is "anticompetitive pricing." Essentially, this term indicates that an integrated firm is strategically pricing its services in order to take advantage of the market power it enjoys in the less competitive markets. The goal of this strategic pricing behavior may include deterring entry, gaining a competitive advantage, or maintaining a dominant share of markets which potentially could become more competitive, absent the pricing strategy.

Integrated carriers have an incentive to maximize costs charged to competitors for services and facilities that are necessary inputs to the competitors' services. These "bottleneck" facilities are typically associated with local services under the monopoly control of the incumbent LEC. As such, they

generally cannot be duplicated by the competitors, who thus cannot avoid paying other charges in addition to the causal costs relating to these inputs.

As long as these LECs remain vertically integrated and consist of a mix of competitive and monopoly operations, they will have incentives to engage in anticompetitive pricing. Similarly, opportunities for cross-subsidization and competitive underpricing will continue to exist wherever an integrated firm provides both monopoly and competitive services using joint or common resources. However, if it is appropriately implemented, a competitive regulatory framework may significantly reduce the opportunities to engage in anticompetitive pricing.