

1       **Q.     The Telecommunications Act of 1996 requires BA-PA to make all its services**  
2       **and UNEs available for resale at discounts or cost-based rates. Are these**  
3       **provisions sufficient to eliminate all economic barriers to entry facing carriers**  
4       **that do not install their own cable facilities?**

5       A.     No. For the customer, switching IXCs is simple and easy, and carriers are usually  
6       willing to pay the customer's transaction costs in order to acquire the customer's  
7       business. Switching one's long distance carrier is nearly as easy and inexpensive as  
8       switching one's supplier of breakfast cereal the next time one goes to the grocery store.  
9       (In fact, the ease of changing carriers helps explain why "slamming" occurs so  
10      frequently).

11            But switching local exchange carriers is a different matter, involving physical  
12      connections to the customer's home or place of business which cannot be instantly  
13      modified. As the FCC has pointed out, "because an incumbent LEC currently serves  
14      virtually all subscribers in its local serving area, an incumbent LEC has little economic  
15      incentive to assist new entrants in their efforts to secure a greater share of that market."  
16      *Local Competition Order*, ¶10. Thus one cannot expect BA-PA to be very interested  
17      in promoting the resale of its services or UNEs while it continues to hold a monopoly or  
18      near monopoly of access lines.

19            It is not being condemnatory of BA-PA to recognize that the Company's  
20      perceived self-interest lies in keeping as much retail market share as possible. Although  
21      the Baby Bells were among the chief proponents of the 1996 Act (or large parts of it),  
22      their advocacy position is more antiregulatory than truly pro-competitive in nature.  
23      Free market rhetoric notwithstanding, I doubt that there is a large-scale business in this  
24      country that doesn't consider an ideal position to be that of an unregulated monopolist.  
25      It would therefore be unrealistic to expect BA-PA not to defend its control of the local

1 exchange market. One source of such control is the barriers to entry created by the  
2 various transaction costs which arise when a customer changes local service carriers.

3  
4 **Q. Would you please explain further about these transaction costs?**

5 A. Most of these costs closely relate to the process by which customers obtain or change  
6 their telephone service. While such costs are incurred by any customer that moves to a  
7 new location, or adds additional phone lines, they will fall most heavily on customers  
8 that change carriers or try another carrier's service offerings. In economic terms, these  
9 "move and change costs" are classified as *transaction costs*, like brokerage fees and  
10 credit card processing fees. It is well established that high transaction costs reduce the  
11 efficiency of markets and make it more difficult to achieve effective competition. In  
12 general, high transaction costs discourage transactions, inhibit the exercise of consumer  
13 choice, and create market friction (i.e., slow down or halt competitive pressures by  
14 inhibiting customers from shopping around or slowing the movement of price signals).  
15 An important characteristic of purely competitive markets is that transaction costs are  
16 very low, relative to the value of the goods and services being purchased. Where  
17 transaction costs are high, effective competition is less likely.

18 These general economic characteristics are particularly applicable in the current  
19 context. High nonrecurring costs tend to discourage new carriers from entering the  
20 market. If the entrants try to pass the costs on to their customers, they will also tend to  
21 discourage customers from changing from one carrier to another. Currently, BA-PA  
22 directly serves most of the retail market. To the extent relatively high levels of costs are  
23 incurred and imposed when customers change from BA-PA to a CLEC, this becomes  
24 an economic barrier to entry, which discourages carriers from signing up new  
25 customers, and discourages customers from experimenting with a new carrier.

1                   If transaction costs were close to zero, it would be easier for CLECs to enter  
2                   the market, and it would be relatively costless for customers to change carriers, in order  
3                   to “try out” a competing carrier’s service, or to respond to a small price difference.  
4                   With high transaction costs, movement between carriers are discouraged, and minor  
5                   differences in prices and quality aren’t sufficient to motivate such changes. In general, a  
6                   high level of transaction costs will tend to result in a market that is relatively rigid and  
7                   inefficient. Customers will be discouraged from changing carriers, and the transition  
8                   away from monopoly conditions may be greatly slowed, or precluded entirely.  
9                   Accordingly, from a public interest perspective, it is preferable to keep transaction  
10                  costs as low as possible. While the nonrecurring charges imposed by BA-PA are not  
11                  enormous, they certainly exceed those imposed when a customer changes toll carriers.  
12                  Furthermore, the CLEC incurs internal transaction costs in addition to those imposed  
13                  by BA-PA. Thus, one cannot simply look to BA-PA’s nonrecurring charges to gain an  
14                  appreciation for the level of transaction costs which currently exist, and are most likely  
15                  slowing the transition to a more competitive market.

16  
17       **Q.     Is there reason to believe transaction costs will decline over time?**

18       A     Yes. While the Company has been operating in a quasi-monopolistic retail environment  
19              for most of this century, it has been operating in an unbundled element/wholesale  
20              environment for a very brief period. BA-PA employees and the entire industry are at  
21              the very beginning of what is likely to be a long and very steep learning curve. As  
22              individual employees and the industry gains experience with the unbundled  
23              element/multi-carrier environment, activities which currently seem very difficult and time  
24              consuming may become highly routinized and simplified. There is every reason to  
25              anticipate that the time required to perform the various functions involved in changing

1 local carriers will significantly diminish as experience is gained, and the most efficient,  
2 cost-effective methods are learned. Thus the barrier to entry represented by such costs  
3 can be expected to decline over time.

4 .  
5 **Q. Not all customers are deterred by the transaction costs and hassles associated**  
6 **with changing carriers. According to Company witness Harry M. Shooshan, a**  
7 **number of companies his firm interviewed were considering “switching all or a**  
8 **part of their telecommunications to a [BA-PA] competitor.” BA-PA Statement**  
9 **No. 3, at 7. Isn’t this indicative of “rapidly developing supply conditions [that]**  
10 **support BA-PA’s petition”?**

11 A. No. First, all but one of the surveys Mr. Shooshan cites were commissioned by the  
12 Company itself, and cannot be expected to present balanced, objective assessments of  
13 market conditions. The one exception dates from 1990-91. BA-PA Response to OCA  
14 IR III-6.

15 Second, many large businesses like to diversify the suppliers, especially with  
16 regard to services which are vitally important to their business. Thus, the fact that many  
17 large businesses intend to switch to another vendor for “part” of their  
18 telecommunications services says very little about the extent to which these other  
19 vendors provide a viable competitive threat to BA-PA.

20 Third, the large businesses that comprise the interview samples are obvious  
21 candidates for facilities bypass and “Hi-cap” services (which have already been  
22 classified as competitive) as well as for consolidation of their interexchange business.  
23 Thus, the referenced responses may indicate more about competitive conditions in the  
24 long distance and special access markets than they do about the local exchange market.  
25 An effective response to competitive threats in the long distance and special access

1           markets does not require or justify BA-PA's proposed reclassification of its local  
2           business services as competitive. As AT&T has noted,

3                     ... for a number of services, such as "Hi-cap" services, Bell actually  
4                     possesses greater pricing flexibility than the new entrants seeking to  
5                     compete with it.

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7           AT&T Brief in Opposition to the Petition of Bell Atlantic - Pennsylvania, Inc. for  
8           Commission Review and Answer to a Material Question, at 8. I would also point out  
9           that BA-PA's inability to offer complete "one-stop shopping" is entirely unrelated to the  
10          competitive status of local service. The Company can offer the full range of  
11          interexchange and local service in a package as soon as it satisfies the requirements of  
12          section 271 of the 1996 Telecom Act.