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

In the Matter of

Rye Telephone Communications, Inc. and
US West Communications, Inc.,

Joint Petition for Waiver of the Definition of "Study Area" Contained in the Part 36 Appendix-Glossary of the Commission's Rules — AAD 95-130

and

Rye Telephone Communications, Inc.

Petition for Waiver of Section 61.41(c)(2) of the Commission Rules

MEMORANDUM OPINION AND ORDER

Adopted: February 1, 1996; Released: February 1, 1996

By the Chief, Accounting and Audits Division:

I. INTRODUCTION

1. On September 12, 1995, Rye Telephone Communications, Inc. ("Rye") and US West Communications, Inc. ("US West") (collectively, "Petitioners"), filed a joint petition for waiver ("Joint Petition") of two Commission rules. Rye and US West seek a waiver of the definition of "Study Area" contained in the Part 36 Appendix-Glossary of the Commission's rules. That definition constitutes a rule freezing all study area boundaries. The requested study area waivers would allow Rye and US West to alter the boundaries of their Colorado study area when transferring one telephone exchange from US West to Rye.[1] In addition, Rye seeks a waiver of the Commission's price cap rule contained in Section 61.41(c)(2). That rule requires non-price cap companies--and the telephone companies with which they are affiliated--to become subject to price cap regulation after acquiring a price cap company or any part thereof. The requested waivers would permit Rye to operate under rate-of-return regulation after acquiring the one exchange which is currently under price cap regulation. And finally, by separate petition filed concurrently, Rye and US West seek waiver and a full refund of the filing fee they paid as permitted by Section 1.1116(a) of the Commission's rules.[2] This rule states that a filing fee may be waived where good cause is shown, and where waiver would promote the public interest.

2. On September 20, 1995, the Common Carrier Bureau ("Bureau") released a public notice soliciting comments on the Joint Petition.[3] On October 20, 1995, the Bureau received comments supporting the Joint Petition from two parties: the National Exchange Carrier Association, Inc. ("NECA"), and the National Telephone Cooperative Association ("NTCA"). In this Order, we find that the public interest would be served by allowing Rye and US West to alter their study area boundaries and allowing Rye to continue operating under rate-of-return regulation after acquiring the exchange. We therefore grant the Joint Petition, as explained more fully below. With respect to the waiver of the filing fee, Section 1.1116(c) of the Commission's rules requires that a specified form be filed with the Office of the Managing Director. To expedite resolution of this waiver request, we have forwarded a copy of this petition to the Office of the Managing Director.[4]

II. STUDY AREA WAIVERS

3. *Background.* 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. Study area boundaries are important primarily because carriers perform jurisdictional separations at the study area level.[5] For jurisdictional separations purposes, the Commission froze all study area boundaries effective November 15, 1984.[6] The Commission took that action primarily to ensure that local exchange carriers ("LECs") do not set up high-cost exchanges within their existing service territories as separate study areas to maximize high-cost payments.[7] The study area freeze also prevents LECs from transferring exchanges among existing study areas for the purpose of increasing interstate revenue requirements and compensation. A LEC must apply to the Commission for a waiver of the frozen study area rule if the LEC wishes to sell an exchange to another carrier and if that transaction would have the effect of changing the study area boundaries of either carrier.[8]

[1] For ease of presentation, we refer to the transferred properties as "one exchange" although Rye actually proposes to acquire one small portion of an exchange.

[2] *See* 47 C.F.R. § 1.1116(a).

[3] Public Notice, 10 FCC Rcd 12260 (Com. Car. Bur. 1995).

[4] *See* 47 C.F.R. § 1.1116(c).

[5] The phrase "jurisdictional separations," or "separations," refers to the process of dividing costs and revenues between a carrier's state and interstate operations. *See generally* 47 C.F.R. §§ 36.1 - 36.741.

[6] 47 C.F.R., Part 36, Appendix-Glossary, definition of "Study Area" (1993). *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) (*1984 Joint Board Recommended Decision*), adopted by the Commission, 50 Fed. Reg. 939 (Jan. 8, 1985) (*1985 Order Adopting Recommendation*). *See also* Amendment of Part 36 of the Commission's Rules and Establishment of a Joint Board, CC Docket No. 80-286, Notice of Proposed Rulemaking, 5 FCC Rcd 5974 (1990) (*Study Area Notice*).

[7] *See 1985 Order Adopting Recommendation*, 50 Fed. Reg. 939, 940. *Also see 1984 Joint Board Recommended Decision*, 49 Fed. Reg. 48325, 48337.

[8] 47 C.F.R. Part 36, Appendix-Glossary. *See also* 47 C.F.R. § 1.3.

4. Waiver of Commission rules is appropriate only if special circumstances warrant deviation from the general rule[9] and such a deviation will serve the public interest.[10] In evaluating petitions seeking a waiver of the rule freezing study area boundaries, the Commission employs a three-prong standard:[11] first, that the change in study area boundaries does not adversely affect the Universal Service Fund ("USF") support program;[12] second, that the state commission(s) having regulatory authority over the exchange(s) to be transferred does not object to the change; and third, that the public interest supports such a change. In evaluating whether the change would adversely affect the USF, the Commission applies a "one percent" guideline to study area waiver requests filed after January 5, 1995.[13] This guideline does apply in the instant case because Petitioners filed after that date.

5. *Petition.* US West seeks a waiver of the rule freezing study area boundaries to enable it to remove one exchange serving approximately 19 access lines, from its Colorado study area. Rye seeks a similar waiver to enable it to add the one exchange to its existing Colorado study area serving approximately 1,561 access lines. Petitioners also request that the Federal Communications Commission ("Commission") expeditiously grant this request without requiring the submission of the detailed information that the Commission has required when considering larger Part 36 study area waivers requests.[14] Petitioners state that as this small exchange area consists of only approximately 19 access lines, it does not warrant the extensive public interest review by the Commission accorded much larger exchange transfers.[15] In addition, the petitioners state that the cost of preparation of detailed information by Rye and US West and the subsequent review by the Commission far outweighs any value that could be attributed to requiring the filing of additional information concerning this small study area boundary change.[16]

6. Petitioners state that this exchange transfer has been previously approved by the Colorado Public Utilities Commission ("CPUC") and found to be in the public interest.[17] The Petitioners state that the CPUC found that the proposed transactions were beneficial to the public interest and welfare of the subscribers--toll calls to areas of community of interest will become local calls, upgrades to single-party lines will be done more quickly with the transfer than without; and rates for basic local exchange service for these customers will be reduced.[18] In addition, petitioners state that Rye is entirely devoted to the provision of service to rural areas and customers. The petitioners also state that the 19 access lines are adjacent to Rye's existing Colorado City exchange which is currently served by an AT&T 5ESS digital switch.[19] Finally, the petitioners state that the change in the study area boundary with regard to these 19 access lines will have a *de minimis* impact on the USF.[20]

7. *Discussion.* Petitioners' proposals demonstrate that current and potential customers in the affected exchange will likely be better served by Rye than US West. Petitioners state that the CPUC has approved the transaction; the CPUC has found the proposed transaction beneficial to the public interest and welfare of the subscribers; and the impact on the USF will be *de minimis.* We therefore find, on the basis of the record before us, that the petitioners have shown good cause for granting the requested waiver. Accordingly, the petition for waiver is granted to permit US West to remove the one exchange from its existing Colorado study area and allow Rye to add the one exchange into its Colorado existing study area.[21] Further, we

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9 *Northeast Cellular Telephone Company v. FCC,* 897 F.2d 1164, 1166 (D.C. Cir. 1990).

10 *WAIT Radio v. FCC,* 418 F.2d 1153, 1159 (D.C. Cir. 1969).

11 *See* US West Communications, Inc., and Eagle Telecommunications, Inc., Joint Petition for Waiver of the Definition of "Study Area" Contained in Part 36, Appendix-Glossary of the Commission's Rules, Memorandum Opinion and Order, 10 FCC Rcd 1771 (1995) (*US West-Eagle Study Area Order)* at ¶ 5.

12 *See 1984 Joint Board Recommended Decision,* 49 Fed. Reg. at 48337, ¶ 66. The Commission created the USF to preserve and promote universal service. *See* Amendment of Part 67 of the Commission's Rules and Establishment of a Joint Board, 96 FCC 2d 781 (1984). The USF allows LECs with high local loop plant costs to allocate a portion of those costs to the interstate jurisdiction, thus enabling the states to establish lower local exchange rates in study areas receiving such assistance. To determine which LEC study areas are eligible for USF support, the USF rules prescribe an eligibility threshold set at 115 percent of the national average unseparated loop cost per working loop. When loop cost in a particular study area exceeds that threshold, the study area is eligible for support equal to a certain percentage of the loop cost in excess of that threshold. The study area becomes eligible for higher levels of support as its loop cost rises above additional thresholds set farther above the national average unseparated loop cost. Because USF assistance is targeted primarily at small study areas, the level of support provided at each threshold generally is greater if the study area has 200,000 or fewer working loops. *See* 47 C.F.R. § 36.631.

13 The Commission stated that no waiver of the rule freezing study area boundaries should result in an annual aggregate shift in USF assistance in an amount equal to or greater than one percent of the total USF, unless the parties can demonstrate extraordinary public interest benefit. The USF effect for the year must be computed on an annualized basis. To prevent carriers from evading this limitation by disaggregating a single large sale of exchanges into a series of smaller transactions that in the aggregate have the same effect on the USF, the Commission further requires that the "one percent" guideline be applied to all study area waivers granted to either carrier, as a purchaser or seller, pending completion of the current review of the USF program. In this context, the Commission defines the term "carrier" to include all affiliated carriers *(i.e.,* those carriers that are in common control, as the term "control" is defined in Section 32.9000 of the Commission's rules, 47 C.F.R. § 32.9000). *See US West-Eagle Study Area Order* at ¶ ¶ 14-17.

14 *Public Notice,* Common Carrier Bureau Established Expedited Processing Procedures For Petitioners Seeking Part 36 Study Area Waivers, DA 95-1344 (rel. June 21, 1995).

15 Petition at 2.

16 *Id.*

17 *See In the Matter of the Joint Application of US West Communications, Inc. and Rye Telephone Company, Inc. to Transfer Service Territory, Decision and Order Granting Joint application to Transfer Authority,* Docket No. 94-A-585T (adopted Jan. 25, 1995)*(CPUC Approval Order).*

18 Joint Petition at 5. *See CPUC Approval Order* at 7-8.

19 *Id.* at 5.

20 *Id.* at 2. *See* Letter from Margaret Nyland, Kraskin & Lesse, to Office of the Secretary, FCC, dated Jan. 29, 1996.

21 These study area waivers also are subject to the condition that, if the selling LEC is a price cap carrier selling a high-cost portion of its operations, it shall make a downward exogenous adjustment to its Price Cap Index to reflect the change in its study area boundaries. See Price Cap Performance Review for Local Exchange Carriers, First Report and Order, 10 FCC Rcd 8962 (1995) ("LEC Price Cap Review Order"), at ¶ ¶ 328 and 330. Under that requirement, US West must reduce the Price

find that the three-prong standard that is applied in evaluating petitions to change study area boundaries has been met. Namely, that the boundary change does not adversely affect the USF support program; that the state commission having regulatory authority does not object to the change; and finally, that the change is in the public interest.

8. Rye and US West also requests a waiver and a full refund of the filing fee filed by a separate petition. Petitioners state that the petition for waiver of the filing fee, if imposed, would equate to approximately $280 per access line; and the 19 lines at issue are to be transferred from US West to Rye for $1.00.[22] Petitioners state that a waiver of the filing fee is in the public interest as the fee is significantly disproportionate to the number of access lines involved and the overall transaction price.[23] Finally, the petitioners state that the imposition of the filing fee would significantly raise the overall cost of this *de minimis* access line transfer and would be burdensome to the parties, particularly to Rye, a small independent rural telephone company.[24] Pursuant to Section 1.1116(a) of the Commission's Rules filing fees may be waived where good cause is shown and where waiver of the filing fee would promote the public interest.[25] Section 1.1116(c) of the Commission's rules requires that petitions for fee waivers be acted upon by the Managing Director after FCC Form 155 has been completed. Therefore, pursuant to Section 1.1116(c) of the Commission's rules, the request for filing fee waiver must be submitted in accordance with that rule. *See, generally,* 47 C.F.R. § 1.1116(c). To facilitate this aspect of the Petitioner's request, we have forwarded a copy of the petition for waiver of the filing fee and will forward a copy of this order top the Managing Director.

III. PRICE CAP WAIVERS

9. *Background.* Section 61.41(c)(2) of the Commission's rules provides that, when a non-price cap company acquires a price cap company, the acquiring company--and any LEC with which it is affiliated--shall become subject to price cap regulation within a year of the transaction.[26] The Commission stated that this "all-or-nothing" rule applies not only to the acquisition of an entire LEC but also to the acquisition of part of a study area.[27] Hence, under this rule, Rye's acquisition of US West's one exchange obligates it to exit the NECA pools and become subject to price cap regulation instead of rate-of-return regulation.

10. The Commission explained that the all-or-nothing rule is intended to address two concerns it has regarding mergers and acquisitions involving price cap LECs. The first concern is that, in the absence of the rule, a company might attempt to shift costs from its price cap affiliate to its non-price cap affiliate, allowing the non-price cap affiliate to earn more--due to its increased revenue requirement--without affecting the earnings of the price cap affiliate, *i.e.*, without triggering the sharing mechanism. The second concern is that, absent the rule, a LEC may attempt to "game the system" by switching back and forth between rate-of-return regulation and price cap regulation. The Commission cited, as an example, the incentive a LEC may have to raise rates by building up a large rate base under rate-of-return regulation and, then, after opting for price caps again, to increase earnings by cutting costs back to an efficient level. It would disserve the public interest, the Commission stated, to allow a LEC to alternately "fatten up" under rate-of-return regulation and "slim down" under price caps regulation, because rates would not fall in the manner intended under price cap regulation.[28]

11. The Commission nonetheless recognized that a narrow waiver of the all-or-nothing rule might be justified if efficiencies created by the purchase and sale of a few exchanges were to outweigh the threat that the system may be subject to gaming.[29] Such a waiver would not be granted unconditionally, however. Rather, similar to certain study area waivers,[30] waivers of the all-or-nothing rule would be granted subject to the condition that the selling price cap LEC shall make a downward exogenous adjustment to its Price Cap I ndex to reflect the change in its study area. That adjustment is needed to remove the effects of the transferred exchanges from price-capped rates that have been based, in whole or in part, upon the inclusion of those exchanges in the price-capped study areas.[31]

12. *Petition.* Rye seeks waiver of Section 61.41(c)(2) so it may operate as a rate-of-return LEC, rather than a price cap LEC, after acquiring the one exchange that is currently under price cap regulation. Petitioners argue that the rule's application in this instance is contrary to the public interest and does not serve the purposes for which the rule was adopted. Petitioners further argue that the Commission's two concerns, the threat of cost shifting between affiliates and gaming of the system, are not at issue in this case.[32]

13. *Discussion.* We agree with Petitioners that the Commission's first concern underlying the all-or-nothing rule is not applicable in this case. Rye has no incentive to shift costs between price cap and rate-of-return affiliates, because Rye is not seeking to maintain separate affiliates under different systems of regulation. As to the Commission's second concern, we find it implausible that US West could game the system by moving the one exchange back and

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Cap Index for its Colorado study area if the change in study area boundaries reduces the cost basis for that index. The Price Cap Index, which is the cost index on which price-capped rates are based, is calculated pursuant to a formula specified in the Commission's rules for price cap LECs. See 47 C.F.R. § 61.45.

22 Joint Petition at 3.

23 *Id.*

24 *Id.*

25 *See* n.2, *supra.*

26 47 C.F.R. § 61.41(c). *See* Second Report and Order, 5 FCC Rcd 6786, 6821 (1990) and Erratum, 5 FCC Rcd 7664 (1990) (*LEC Price Cap Order*), *modified on recon.* 6 FCC Rcd 2637 (1991) (*LEC Price Cap Reconsideration Order*), *petitions for further recon. dismissed,* 6 FCC Rcd 7482 (1991), *aff'd, National Rural Telecom Assoc. v. FCC,* 988 F.2d 174 (D.C. Cir. 1993), *further modification on recon.*, 6 FCC Rcd 4524 (1991)(*ONA Part 69 Order*), *second further recon.*, 7 FCC Rcd 5235 (1992).

27 The Commission explained that, if these two types of acquisitions were not treated the same under the all-or-nothing rule, a LEC could avoid the rule by selling all but one of its exchanges. *See LEC Price Cap Reconsideration Order,* 6 FCC Rcd 2637, 2706.

28 *LEC Price Cap Reconsideration Order,* 6 FCC Rcd 2637, 2706.

29 *Id.*

30 *See supra* at note 21.

31 *See LEC Price Cap Review Order* at ¶ 330.

32 Joint Petition at 10. We note that, although US West signed the Joint Petition, US West does not seek a waiver of the all-or-nothing rule.

forth between price cap and rate-of-return regulation, because US West is selling this exchange and a reacquisition would require a second study area waiver. Moreover, US West cannot transfer the one exchange without removing the rate-effects of that exchange from the price-capped rates that have been based, in part, upon the inclusion of that exchange in its Colorado study area.[33]

14. We therefore find there is good cause to grant Rye waivers of the all-or-nothing rule to permit it to remain under rate-of-return regulation after acquiring the one exchange which is currently under price cap regulation. For the present, we will continue to regulate Rye as a rate-of-return carrier. Because we are waiving Section 61.41(c)(2), Rye needs not withdraw from the NECA pools. We note that, as with any other rate-of-return carrier, Rye may elect price cap regulation in the future if it decides to withdraw from the NECA pools.

IV. ORDERING CLAUSE

15. Accordingly, IT IS ORDERED, pursuant to Sections 4(i) and 5(c) of the Communications Act of 1934, as amended, 47 U.S.C. §§ 154(i) and 155(c) and Sections 0.91 and 0.291 of the Commission's Rules, 47 C.F.R. §§ 0.91, 0.291, that the Joint Petition of Rye Telephone Company, Inc., and US West communications, Inc. for waiver of Part 36, Appendix-Glossary, and for waiver of Section 61.41(c)(2) of the Commission's Rules, 47 C.F.R. § 61.41(c)(2) IS GRANTED.

FEDERAL COMMUNICATIONS COMMISSION

Kenneth P. Moran
Chief, Accounting and Audits Division
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[33] *See supra* at ¶ 11.