

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

In the Matter of	)	
	)	
Access Charge Reform	)	CC Docket No. 96-262
	)	
Price Cap Performance Review for Local Exchange Carriers	)	CC Docket No. 94-1
	)	
Low-Volume Long Distance Users	)	CC Docket No. 99-249
	)	
Federal-State Joint Board On Universal Service	)	CC Docket No. 96-45
	)	
	)	
	)	

**SIXTH REPORT AND ORDER IN CC DOCKET NOS. 96-262 AND 94-1  
REPORT AND ORDER IN CC DOCKET NO. 99-249  
ELEVENTH REPORT AND ORDER IN CC DOCKET NO. 96-45**

**Adopted:** May 31, 2000

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

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**I. INTRODUCTION**

1. In this Order, we adopt an integrated interstate access reform and universal service proposal put forth by the members of the Coalition for Affordable Local and Long Distance Service (CALLS).<sup>1</sup> This action provides many benefits. It will bring lower rates and less confusion to consumers; and create a more rational interstate rate structure. This, in turn, will support more efficient competition, more certainty for the industry, and permit more rational investment decisions.

2. This Order resolves historically vexing issues, some going back nearly two decades, in a manner that benefits consumers. Consumers that make no or few long distance calls and consumers that make many long distance calls will both enjoy meaningful savings. The savings from the elimination of the Presubscribed Interexchange Carrier Charge (PICC) and the long distance companies' pass-through of that charge exceed the modest increases to the Subscriber Line Charge (SLC) that this plan allows. In addition, the commitments by AT&T and Sprint to offer reasonably priced long-distance plans without any Minimum Usage Charge (MUC) ensures that low-volume users will enjoy substantially lower overall rates. At the same time, significant and immediate reductions to per-minute carrier access charges will bring those rates closer to cost and translate into lower per-minute long-distance rates, benefiting high-volume consumers.

3. By simultaneously removing implicit subsidies from the interstate access charge system and replacing them with a new interstate access universal service support mechanism that supplies portable support to competitors, this Order allows us to provide more equal footing for

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<sup>1</sup> CALLS consists of the following members: AT&T, Bell Atlantic, BellSouth, GTE, SBC, and Sprint. They represent four of the five largest local exchange companies and two of the three largest long distance companies in the nation. These local and long distance companies have historically been adversaries in our access reform and universal service proceedings. CALLS first submitted its proposal on July 29, 1999 (Letter from John T. Nakahata, Counsel to CALLS, to Magalie Roman Salas, Secretary, FCC, July 29, 1999; resubmitted with edits on August 20, 1999 (Original Proposal)). CALLS submitted a modified proposal on March 8, 2000 (Letter from John T. Nakahata, Counsel to CALLS, to Magalie Roman Salas, Secretary, FCC, March 8, 2000 (Modified Proposal)). CALLS has made some refinements to its proposal since that date. See Appendix E. Unless otherwise indicated, the terms "CALLS Proposal" and "proposal" refer to the Modified Proposal, as revised by CALLS in its subsequent filings.

In reviewing the CALLS Proposal, the Commission has twice requested and received comment. Access Charge Reform, CC Docket 96-262, Notice of Proposed Rulemaking, 14 FCC Rcd 16872 (1999) (*CALLS NPRM*); Coalition for Affordable Local and Long Distance Services (CALLS) Modified Proposal, CC Docket No. 96-262, Public Notice, DA-00-533 (Comm. Carr. Bur., rel. Mar. 8, 2000). A comment or reply comment to the *CALLS NPRM* is identified as Comment or Reply, respectively. A comment or reply comment to the supplemental request for comment in the Public Notice is identified as Supp. Comment or Supp. Reply, respectively. Appendix A includes a list of parties filing comments on the CALLS Proposal and Low-Volume Long-Distance Users, CC Docket No. 99-249, Notice of Inquiry, 15 FCC Rcd 6298 (1999) (*Low-Volume Long-Distance Users NOI*).

competitors in both the local and long-distance markets, while still keeping rates in higher cost areas affordable and reasonably comparable with those in lower cost areas.

## II. BACKGROUND

4. In passing the Telecommunications Act of 1996 (1996 Act),<sup>2</sup> Congress sought to establish “a pro-competitive, deregulatory national policy framework” for the United States telecommunications industry. In the 1996 Act, Congress also directed that universal service support “should be explicit and sufficient to achieve the purposes” of section 254,<sup>3</sup> which include the purpose that all Americans should have access to telecommunications services at affordable and reasonably comparable rates. Therefore, with this Order, we take action designed to further accelerate the development of competition in the local and long-distance telecommunications markets, and to establish an explicit interstate access universal service support mechanism that will be sustainable in an increasingly competitive marketplace.

### A. Access Charges

5. For much of this century, most telephone subscribers obtained both local and long-distance services from the same company, the pre-divestiture Bell System, owned and operated by AT&T. Its provision of local and intrastate long-distance services through its wholly-owned operating companies, the Bell Operating Companies (BOCs), was regulated by state commissions. The Commission regulated AT&T's provision of interstate long-distance service. Much of the telephone plant that is used to provide local telephone service, such as the local loop,<sup>4</sup> is also needed to originate and terminate interstate long-distance calls. Consequently, a portion of the costs of this common plant historically was assigned to the interstate jurisdiction and recovered through the rates that AT&T charged for interstate long-distance calls. The balance of the costs of the common plant was assigned to the intrastate jurisdiction and recovered through the charges for intrastate services regulated by the state commissions. The system of allocating costs between the interstate and intrastate jurisdictions is known as the separations process. The difficulties inherent in allocating the costs of facilities that are used for multiple services between the two jurisdictions are discussed below.

6. At first, there was no formal system of tariffed charges to determine how the BOCs and the hundreds of unaffiliated, independent local exchange carriers (LECs) would recover the costs allocated to the interstate jurisdiction by the separations rules. Instead, AT&T remitted to these companies the amounts necessary to recover their allocated interstate costs, including a return on allocated capital investment.

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<sup>2</sup> Telecommunications Act of 1996, Pub. L. No. 104-104, 110 Stat. 56 (1996) (1996 Act). The 1996 Act amended the Communications Act of 1934. 47 U.S.C. §§ 151 *et seq.*

<sup>3</sup> 47 U.S.C. § 254(e).

<sup>4</sup> A local loop is the connection between the telephone company's central office building and the customer's premises.

7. In the 1970s, MCI and other interexchange carriers (IXCs) began to provide switched long-distance service in competition with AT&T. AT&T, however, still maintained monopolies in the local markets served by its local subsidiaries, the BOCs. The BOCs owned and operated the telephone wires that connected the customers in their local markets. Other independent (non-Bell) LECs held similar monopoly franchises in their local service areas. MCI and the other IXCs were dependent on the BOCs and the independent LECs to complete the long-distance calls to the end user.

8. For much of the 1970s, MCI and AT&T fought over the fees -- the access charges -- that MCI should pay the BOCs for originating and terminating interstate calls placed by or to end users on the BOCs' local networks. That battle took place before federal regulators, as well as in the federal courts. In December 1978, under Commission supervision, AT&T, MCI, and the other long-distance competitors entered into a comprehensive interim agreement, known as Exchange Network Facilities for Interstate Access (ENFIA), that set rates that AT&T would charge long-distance competitors for originating and terminating interstate traffic over the facilities of its local exchange affiliates.<sup>5</sup> Several years afterwards, AT&T's divestiture was completed, separating the local exchange operations of the BOCs from the rest of AT&T's operations, including AT&T's long distance business. The BOCs maintained monopoly franchises in their local market, but by splitting them off from AT&T's long-distance business, the federal courts removed an incentive for the BOCs to favor AT&T's long distance business over its competitors. Now AT&T competed directly with MCI and the other competitors to provide interstate service, and all of the competitors, including AT&T, paid the BOCs for the service of providing the necessary access to end users.

9. In 1978, the Commission commenced a wide-ranging review of the system by which LECs were compensated for originating and terminating interstate traffic. In 1983, following the decision to break-up AT&T, the Commission adopted uniform access charge rules in lieu of earlier agreements.<sup>6</sup> These rules governed the provision of interstate access services by all incumbent LECs, BOCs as well as independents. The access charge rules provide for the recovery of the incumbent LECs' costs assigned to the interstate jurisdiction by the separations rules.

10. The Commission uses a multi-step process to identify the cost of providing access service. First, the rules require an incumbent LEC to record all of its expenses, investments, and revenues in accordance with accounting rules set forth in our regulations.<sup>7</sup> Second, the rules divide these costs between those associated with regulated telecommunications services and those

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<sup>5</sup> For additional background on the ENFIA agreement, *see, e.g.*, Investigation of Access and Divestiture-Related Tariffs, CC Docket No. 83-1145, Phase I and Phase II, Part 1, FCC 85-100, 57 Rad.Reg.2d 1229, 1241 (rel. March 8, 1985).

<sup>6</sup> MTS and WATS Market Structure, CC Docket No. 78-72, Third Report and Order, Phase 1, 93 FCC 2d 241, *recon.*, 97 FCC 2d 682 (1983), *second recon.*, 97 FCC 2d 834 (1984).

<sup>7</sup> These rules are referred to as the Uniform System of Accounts and are contained in Part 32 of the Commission's Rules. *See* 47 C.F.R. §§ 32.1-.9000.

associated with nonregulated activities.<sup>8</sup> Third, the separations rules determine the fraction of the incumbent LEC's regulated expenses and investment that should be allocated to the interstate jurisdiction.<sup>9</sup> After the total amount of interstate cost is identified, the access charge rules translate these interstate costs into charges for the specific interstate access services and rate elements. Part 69 of our rules specifies in detail the rate structure for recovering those costs.<sup>10</sup> That is, the rules tell the incumbent LECs the precise manner in which they may assess charges on interexchange carriers and end users.

11. Determining the costs that an incumbent LEC incurs to provide interstate access services and that, consequently, should be recovered from those services, is relatively straightforward in some cases and problematic in others. Some facilities, such as private lines, can be used exclusively for interstate services and, in such cases, the entire cost of those facilities is assigned to the interstate jurisdiction by the separations rules. Most facilities, however, are used for both intrastate and interstate services. The costs of some of these facilities vary depending on the amount of telecommunications traffic that they handle. The separations rules typically assign these traffic-sensitive costs on the basis of the relative interstate and intrastate usage of the facilities, as measured, for example, by the relative minutes of interstate and intrastate traffic carried by such facilities. By contrast, the costs of other facilities used for both interstate and intrastate traffic do not vary with the amount of traffic carried over the facilities, *i.e.*, the costs are non-traffic-sensitive. These costs pose particularly difficult problems for the separations process: the costs of such facilities cannot be allocated on the basis of cost-causation principles because all of the facilities would be required even if they were used only to provide local service or only to provide interstate access services. A significant illustration of this problem is allocating the cost of the local loop, which is needed both to provide local telephone service as well as to originate and terminate long-distance calls. The current separations rules allocate 25 percent of the cost of the local loop to the interstate jurisdiction for recovery through interstate charges.<sup>11</sup>

12. In promulgating its access charge rules, the Commission has recognized that, to the extent possible, costs of interstate access should be recovered in the same way that they are incurred. This approach is consistent with principles of cost-causation and promotes economic efficiency. Thus, non-traffic-sensitive costs should be recovered through fixed, flat-rated fees. Similarly, traffic-sensitive costs should be recovered through corresponding per-minute access rates. The Commission's rules, however, are not fully consistent with this goal. In particular, because the Commission has taken a cautious approach in addressing affordability concerns, it has taken measured steps toward this goal by limiting the amount of the allocated interstate cost of a

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<sup>8</sup> This is governed by sections 64.901-.904 of our Rules. *See* 47 C.F.R. §§ 64.901-.904.

<sup>9</sup> This step is governed by Part 36 of the Rules. *See* 47 C.F.R. §§ 36.1-.741.

<sup>10</sup> 47 C.F.R. §§ 69.1-69.731.

<sup>11</sup> The general process of separating these costs between the interstate and intrastate jurisdictions is discussed by the Supreme Court in *Smith v. Illinois Bell Tel. Co.*, 282 U.S. 133 (1930).

local loop that is assessed directly on residential and business customers as a flat monthly charge.<sup>12</sup>

13. Through the end of 1990, access revenues were governed by "rate-of-return" regulation. Under rate-of-return regulation, incumbent LECs calculate the specific access charge rates using projected costs and projected demand for access services.<sup>13</sup> An incumbent LEC is limited to recovering its costs plus a prescribed return on investment, and is potentially obligated to provide refunds if its interstate rate of return exceeds the authorized level. Regulatory structures that base a firm's allowable rates directly on the reported costs of the individual firm can create perverse incentives, because reimbursing the firm's costs removes the incentive to reduce costs and improve productive efficiency.

14. Consequently, in 1991 we implemented a system of price cap regulation that altered the manner in which the largest incumbent LECs establish their interstate access charges. While most rural and small LECs remained subject to rate-of-return rules, generally the largest incumbent LECs<sup>14</sup> are now subject to price cap regulations. The Commission's price cap plan for LECs was intended to avoid the perverse incentives of rate-of-return regulation in part by divorcing the annual rate adjustments from the performance of each individual LEC, and in part by adjusting the cap based on actual experience, only with a considerable lag.

15. Briefly stated, rate-of-return regulation is designed to limit the profits an incumbent LEC may earn from interstate access service, whereas price cap regulation focuses primarily on the prices that an incumbent LEC may charge and the revenues it may generate from interstate access services. Under the Part 69 cost-of-service rules, revenue requirements are based on embedded or accounting costs allocated to individual services. Incumbent LECs are limited to earning a prescribed return on investment and are potentially obligated to provide refunds if their interstate rate of return exceeds the authorized level.

16. By contrast, although the access charges of price cap LECs originally were set at the levels that existed at the time they entered price caps, their prices have been limited ever since by price indices that have been adjusted annually pursuant to formulae set forth in our Part 61 rules. Price cap carriers whose interstate access charges are set by these pricing rules are permitted to earn returns significantly higher, or potentially lower, than the prescribed rate of

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<sup>12</sup> See, e.g., Access Charge Reform, CC Docket No. 96-262, First Report and Order, 12 FCC Rcd 15982, 16010-11 (1997) (*Access Charge Reform Order*), *aff'd sub. nom.*, *Southwestern Bell V. FCC*, 153 F.3d 523 (8<sup>th</sup> Cir. 1998).

<sup>13</sup> Since 1981, the Commission has allowed certain smaller incumbent LECs to base their access rates on historic, rather than projected, cost and demand. See 47 C.F.R. § 61.39.

<sup>14</sup> The Commission required price cap regulation for the BOCs and GTE, and permitted other LECs to elect price cap regulation voluntarily, provided that all their affiliates also convert to price cap regulation and that they withdraw from the pools administered by the National Exchange Carrier Association (NECA). Policy and Rules Concerning Rates for Dominant Carriers, CC Docket No. 87-313, Second Report and Order, 5 FCC Rcd 6786, 6818-20 (1990) (*LEC Price Cap Order*).

return that incumbent LECs are allowed to earn under rate-of-return rules. Price cap regulation encourages incumbent LECs to improve their efficiency by harnessing profit-making incentives to reduce costs, invest efficiently in new plant and facilities, and develop and deploy innovative service offerings, while setting price ceilings at reasonable levels.<sup>15</sup> Individual companies retain an incentive to cut costs and to produce efficiently, because in the short run their behavior has no effect on the prices they are permitted to charge, and they are able to keep any additional profits resulting from reduced costs. In this way, price caps act as a transitional regulatory scheme until the advent of actual competition makes price cap regulation unnecessary.<sup>16</sup>

17. Although price cap regulation eliminates the direct link between changes in allocated accounting costs and change in prices, it does not sever the connection between accounting costs and prices entirely. The overall interstate revenue levels still generally reflect the accounting and cost allocation rules used to develop access rates to which the price cap formulae were originally applied. Price cap indices are adjusted upwards if a price cap carrier earns returns below a specified level in a given year. Moreover, a price cap LEC may petition the Commission to set its rates above the levels permitted by the price cap indices based on a showing that the authorized rate levels will produce earnings that are so low as to be confiscatory. In the past, all or some price cap LECs were required to "share," or return to ratepayers, earnings above specified levels. This sharing requirement was eliminated in 1997.<sup>17</sup>

18. With the passage of the 1996 Act, the Commission determined that it was necessary to make substantial revisions to access charges. In the *Access Charge Reform Order*, the Commission instituted reforms that changed the manner in which price cap LECs recover access costs by aligning the rate structure more closely with the manner in which costs are

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<sup>15</sup> The price cap regulations also give incumbent LECs greater flexibility in determining the amount of revenues that may be recovered from a given access service. The price cap rules group services together into different baskets, service categories, and service subcategories. The rules then identify the total permitted revenues for each basket or category of services. Within these baskets or categories, incumbent LECs are given some discretion to determine the portion of revenue that may be recovered from specific services. Subject to certain restrictions, this flexibility allows incumbent LECs to alter the access charge rate level associated with a given service. For example, within the category of switching services, an incumbent LEC may choose to recover a greater portion of its switching revenues through access charges assessed to one kind of switching service rather than through charges assessed to another switching service. Although the LEC must still observe the switched-access rate structure that is set forth in Part 69 of our rules (which determines what services may be offered and whether charges may be imposed on a per-minute or flat-rated basis), the rate level of the access charge will vary depending on the amount of revenues that the LEC chooses to recover from a given service.

<sup>16</sup> Price Cap Performance Review for Local Exchange Carriers, Second Further Notice of Proposed Rulemaking in CC Docket No. 94-1, Further Notice of Proposed Rulemaking in CC Docket No. 93-124, and Second Further Notice of Proposed Rulemaking in CC Docket No. 93-197, 11 FCC Rcd 858, 862 (1995) (*Price Cap Second FNPRM*).

<sup>17</sup> Price Cap Performance Review for Local Exchange Carriers, Fourth Report and Order in CC Docket No. 94-1 and Second Report and Order in CC Docket No. 96-262, 12 FCC Rcd 16642, 16700 (1997) (*1997 Price Cap Review Order*), *aff'd in part, rev'd in part, USTA v. FCC*, 188 F.3d 521 (D.C. Cir. 1999).

incurred.<sup>18</sup> Prior to such reform, some costs that did not vary with usage, in particular the local loop, were not wholly recovered through flat charges. The SLC, which is a flat charge that recovers the interstate portion of local loop costs from an end user, is subject to a cap that, particularly for residential customers, is often below the level that would enable the LEC to recover the entire interstate cost of the local loop. Prior to the *Access Charge Reform Order*, a price cap LEC recovered the shortfall created by the SLC caps wholly through the carrier common line (CCL) charge, which is a per-minute charge assessed on the end user's IXC whenever the end user placed an interstate long-distance call. The IXC, in turn, passed this charge on to its customers in the form of higher rates. By making the end-user rate for long distance calls more expensive, the CCL charge artificially suppresses demand for interstate long distance services.

19. The *Access Charge Reform Order* also created the PICC, a flat per-line charge imposed by a price cap LEC on an end user's IXC, in order to phase out CCL charges. The Commission sought to establish economically efficient rate structures to encourage the development of efficient competition, thereby enhancing consumer welfare. PICCs have markedly reduced the per-minute recovery of local loop costs and raised flat recovery of non-traffic sensitive costs. Unfortunately, the advent of PICCs has also created market inefficiencies. Because IXCs have recovered the residential PICCs on a per-account basis, residential customers with only one line pay the same as those with two or more lines, and so pay more than the costs IXCs have incurred for providing them service. In addition, because PICCs are not assessed directly on consumers, but instead are subjected to averaging and mark-ups by the IXCs, consumers are prevented from making head-to-head comparisons among local service providers.

20. In the *Access Charge Reform Order*, the Commission also stated that its primary method for bringing about cost-based access charges was by letting competition establish efficient rates.<sup>19</sup> The Commission anticipated creating, in a later stage of access reform, a mechanism whereby rate regulation of services would be lessened, and eventually eliminated, as competition developed.<sup>20</sup> To the extent that competition did not fully achieve the goal of moving access rates toward costs, the Commission reserved the right to adjust rates in the future to bring them into line with forward-looking costs.<sup>21</sup> To assist in that effort, the Commission said it would require price cap LECs to start forward-looking cost studies by no later than February 8, 2001 for all services then remaining under price caps.<sup>22</sup>

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<sup>18</sup> *Access Charge Reform Order*, 12 FCC Rcd at 16007-33.

<sup>19</sup> *Access Charge Reform Order*, 12 FCC Rcd at 16001-02.

<sup>20</sup> *Access Charge Reform Order*, 12 FCC Rcd at 16003.

<sup>21</sup> *Access Charge Reform Order*, 12 FCC Rcd at 16002-03.

<sup>22</sup> *Access Charge Reform Order*, 12 FCC Rcd at 16003.

## B. Universal Service

21. One of the primary purposes of universal service support is to allow LECs and other eligible telecommunications carriers to provide certain basic services to customers in high-cost areas without having to charge these customers unaffordable rates.<sup>23</sup> Historically, in the interest of meeting the goal of universal service, LEC services have been subsidized or “supported” to enable high-cost consumers to be served at rates that are reasonably comparable to those in lower cost areas. This universal service support has been both explicit and implicit.

22. *Explicit Support.* Several federal programs have provided explicit universal service support in the form of direct monetary payments to carriers. This support has been provided for both intrastate and interstate services. For example, the Commission’s high-cost support mechanism provides support for the costs of the intrastate portion of the local loop that significantly exceed the national average. By providing this federal support for intrastate costs, the Commission assists the states in ensuring that rates for intrastate rates remain affordable and reasonably comparable. Several state universal service programs also provide carriers with explicit support for their intrastate rates so that those carriers can serve customers in high-cost areas without having to charge prohibitively high rates. Carriers have also received explicit federal support for their interstate costs. For example, the Commission’s Long Term Support (LTS) mechanism provides certain small carriers with support for the interstate portion of the local loop. This support allows such carriers to reduce the amount of the interstate costs that they would otherwise recover through access charges.

23. *Implicit Support.* In addition to receiving explicit universal service support, LECs also received implicit universal service support from a variety of sources. Some state rate structures have permitted LECs to charge rates for certain services that significantly exceeded the costs of providing those services, thereby enabling those LECs to charge below-cost rates for other services. For example, by charging above-cost rates for vertical services (*e.g.*, caller identification, call waiting), carriers can support the rates for basic local service. The Commission’s interstate access charge structure also provided LECs with implicit universal service support. For example, LECs charge business customers interstate access rates that generally exceed those charged to residential customers, even though the costs of providing access to these groups of customers does not differ significantly. In particular, the multi-line business PICC creates a subsidy running from multi-line business subscribers to residential and single-line business subscribers to help LECs recover revenues that they would not otherwise recover from residential and single-line business subscribers due to the lower SLC caps on those

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<sup>23</sup> The “designated” or “core” services a carrier must provide in order to be eligible to receive universal service support include: single-party voice service; voice grade access to the public switched network; DTMF signaling or its functional equivalent; access to emergency services; access to operator services; access to interexchange service; access to directory assistance; and toll limitation services for qualifying low-income consumers. See Federal-State Joint Board on Universal Service, CC Docket No. 96-45, Report and Order, 12 FCC Rcd 8776, 8809 (1997) (*Universal Service First Report and Order*), as corrected by Federal-State Joint Board on Universal Service, CC Docket No. 96-45, Errata, FCC 97-157 (rel. June 4, 1997), *aff’d in part, rev’d in part, and remanded in part, Texas Office of Public Utility Counsel v. FCC*, 183 F.3d 393 (5<sup>th</sup> Cir. 1999) (affirming in relevant part the Commission’s decisions regarding implementation of the high-cost universal service support mechanism).

lines.<sup>24</sup> In addition, by allowing LECs to recover non-traffic-sensitive (flat) costs through traffic sensitive (per minute) rates, high-volume users bear a greater share of the non-traffic-sensitive costs than low-volume users, thus creating an implicit support flow from high-volume users to low-volume users. Furthermore, the practice of averaging rates over large geographic areas, for both intrastate and interstate services, results in subscribers in low-cost areas subsidizing the rates of subscribers in higher cost areas.

24. *Universal Service in a Competitive Environment.* This “patchwork quilt” of implicit support helped keep rates largely affordable in a monopoly environment where incumbent LECs could be guaranteed an opportunity to earn returns from certain services and customers that are sufficient to support the high cost of providing other services to other customers. The new competitive environment envisioned by the 1996 Act, however, threatens to undermine this implicit support structure over the long run. The 1996 Act removed barriers to entry in the local market, generating competitive pressures that may make it difficult for incumbent LECs to maintain access charges above economic cost. Thus, where existing rules require an incumbent LEC to set access charges above cost for a high-volume user, a competing provider of local service can lease unbundled network elements at cost, or construct new facilities, thereby undercutting the incumbent’s access charges. As competition develops, incumbent LECs may be forced to lower their access charges or lose market share, in either case jeopardizing the source of revenue that, in the past, has permitted the incumbent LEC to offer service to other customers, particularly those in high-cost areas, at below-cost prices.<sup>25</sup> Incumbent LECs have been claiming that this process has already made more than trivial inroads on their high-volume customer base.<sup>26</sup>

25. Recognizing the disruptive effects that competition would have on universal service support mechanisms developed in a monopoly environment, Congress instructed the Commission, after consultation with the Federal-State Joint Board on Universal Service (Joint Board), to establish specific, predictable, and sufficient mechanisms to preserve and advance universal service.<sup>27</sup> Congress concluded that the support provided by these mechanisms “should be explicit and sufficient to achieve the purposes” of section 254, which include the purpose that all Americans should have access to telecommunications services at affordable and reasonably

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<sup>24</sup> See *Access Charge Reform Order*, 12 FCC Rcd at 16022-26.

<sup>25</sup> See, e.g., H. REP. NO. 204, 104th Cong., 1st Sess. 68 (1995) (The bill “would make such internal subsidies much less viable because deregulation would remove the near-guaranteed returns allowed in a regulated market, and with them the ability of the regulated firm to subsidize high-cost customers.”)

<sup>26</sup> See, e.g., 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); and Ameritech Forbearance Petition, CC Docket No. 99-65 (filed Feb. 5, 1999).

<sup>27</sup> 47 U.S.C. § 254(a), (d). See also Federal-State Joint Board on Universal Service, CC Docket No. 96-45, Notice of Proposed Rulemaking and Order Establishing Joint Board, 11 FCC Rcd 18092 (1996) (*Universal Service NPRM*).

comparable rates.<sup>28</sup> In response to this directive, the Commission has taken several actions to put in place universal service support mechanisms that will be sustainable in an increasingly competitive marketplace. These actions fall into three general categories: (1) reforming our existing universal service support mechanisms;<sup>29</sup> (2) reforming our interstate access charge regime to identify implicit universal service support and to remove such implicit support from our interstate access charges,<sup>30</sup> and (3) establishing new universal service mechanisms.<sup>31</sup> In this Order, we focus our efforts in these last two categories.

### C. The Current Situation

26. Undoing the Gordian knot of determining the appropriate level of interstate access charges and converting implicit subsidies in interstate access charges into explicit, portable, and sufficient universal service support cannot be accomplished with one stroke of the sword. Determining the cost of providing service in every area of the country is a difficult, time-consuming task that regulators cannot perform with exactitude. The particular method that should be used for determining the cost of providing service is itself a contentious issue as are the results achieved from various proposed methods. The incumbent LECs have traditionally argued that they must maintain their current revenue streams to support universal service, while IXCs and consumer groups have argued that access charges should be reduced by amounts in excess of the amount that is converted into explicit universal service support. The subsidies implicit in geographic averaging must be reduced if competition is to develop outside of urban areas; but these subsidies can never be entirely eliminated, without pricing service on a line-by-line-by-line basis. Affordability concerns deter us from allowing end-user charges in higher cost areas to increase to the point where they recover the cost of providing service in those areas, whether cost is determined on a forward-looking or historic basis. These disputes and concerns have dragged on for years and could do so indefinitely.

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<sup>28</sup> 47 U.S.C. § 254(b), (e). According to the Joint Explanatory Statement, the purpose of the 1996 Act is "to provide for a pro-competitive, de-regulatory national policy framework designed to accelerate rapidly private sector deployment of advanced telecommunications and information technologies and services to all Americans by opening all telecommunications markets to competition . . . ." Joint Explanatory Statement of the Committee of Conference, H.R. Conf. Rep. No. 458, 104th Cong., 2d Sess. at 113 (Joint Explanatory Statement).

<sup>29</sup> Federal-State Joint Board on Universal Service, Seventh Report and Order and Thirteenth Order on Reconsideration in CC Docket No. 96-45, and Fourth Report and Order in CC Docket No. 96-262 and Further Notice of Proposed Rulemaking, 14 FCC Rcd 8078 (1999), petition for review filed *sub. nom. Vermont Department of Public Service v. FCC*, No. 99-60530 (5<sup>th</sup> Cir., filed June 23, 1999) (*Universal Service Seventh Report and Order*); Federal-State Joint Board on Universal Service, CC Docket No. 96-45, Ninth Report and Order and Eighteenth Order on Reconsideration, 14 FCC Rcd 20432 (1999) (*Universal Service Ninth Report and Order*).

<sup>30</sup> *Universal Service First Report and Order*, 12 FCC Rcd at 9162; *Access Charge Reform Order*, 12 FCC Rcd at 16144-50 .

<sup>31</sup> See, e.g., *Universal Service First Report and Order*, 12 FCC Rcd at 9007.

27. As we devise a transition to a more economically rational approach to access charges and universal service, we need to balance various and sometimes conflicting interests – including promotion of competition, deregulation, maintaining affordability for all, and avoiding rate shock to consumers. It is important, however, that the Commission not permit itself to be gridlocked into inactivity by endeavoring to find precise solutions to each component of this complex set of problems. It is preferable and more reasonable to take several steps in the right direction, even if incomplete, than to remain frozen with indecision because a perfect, ultimate solution remains outside our grasp.

28. Against this background, certain segments of the industry have developed a comprehensive consensus approach to resolve outstanding issues concerning access charges and universal service. The Order we adopt today will result in lower rates for both low-volume and high-volume long-distance consumers, more competition, fewer line items on consumers' phone bills, greater flexibility for price cap LECs to meet competition, and an explicit, portable interstate access universal support mechanism. It is this comprehensive solution of historically contentious issues that allows us to take these actions while ensuring that consumers in high-cost areas will continue to have affordable service.

### III. EXECUTIVE SUMMARY

29. CALLS has presented us with an integrated and cohesive proposal that aims to resolve major outstanding issues concerning access charges: the pending NPRM to address implicit universal service support in access charges,<sup>32</sup> the X-factor remand,<sup>33</sup> the Low-Volume Long-Distance Users NOI,<sup>34</sup> the pending NPRM on geographically deaveraging SLCs<sup>35</sup> and the next scheduled price cap performance review.<sup>36</sup> In addressing these issues, the CALLS Proposal reduces, and in most instances eliminates, implicit subsidies among end-user classes; makes implicit universal service funding in access charges explicit and portable; provides significant benefits to consumers who make few or no long distance calls; and sets carrier charges at reasonable levels. Because we find that the CALLS Proposal resolves these issues in a way that benefits consumers and is pro-competitive and economically efficient, we adopt certain parts of the plan, largely rate structure components, as mandatory for all price cap LECs for the full five-years of the plan. As discussed in more detail below, for certain rate-level components of the plan, we adopt it as mandatory on an interim basis. Price cap LECs will be able to choose

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<sup>32</sup> *Universal Service Seventh Report and Order*, 14 FCC Rcd at 8078.

<sup>33</sup> Price Cap Performance Review For Local Exchange Carriers, CC Docket No. 94-1, Notice of Proposed Rulemaking, 14 FCC Rcd 19717 (1999) (*1999 Price Cap FNPRM*).

<sup>34</sup> *Low-Volume Long-Distance Users NOI*, 15 FCC Rcd 6298.

<sup>35</sup> Access Charge Reform, CC Docket No. 96-262, Fifth Report and Order and Further Notice of Proposed Rulemaking, 14 FCC Rcd 14221, 14320-23 (1999) (*Pricing Flexibility Order*).

<sup>36</sup> *1997 Price Cap Review Order*, 12 FCC Rcd at 16707.

between having these interim rate-level components apply for the full five years or having their rates reinitialized based on forward-looking economic cost.

30. The proposal provides for the following:
- 1) Elimination of the residential PICC;
  - 2) Increases to the primary residential and single-line business SLC caps, beginning at \$4.35 on July 1, 2000, and gradually increasing to \$6.50 on July 1, 2003, provided that LECs can justify any increase beyond \$5.00;
  - 3) A review of the SLC rates prior to the increase scheduled for July 1, 2002, including evaluation of forward looking cost information;
  - 4) Targeting of an X-factor<sup>37</sup> for switched access to switching and switched transport elements;
  - 5) Creation of a separate X-factor for special access services;
  - 6) \$2.1 billion in reductions to switched access usage rates effective July 1, 2000;
  - 7) Reduction of the switched access X-factor to the Gross Domestic Product-Price Index (GDP-PI) once specific target rate levels are achieved;
  - 8) Removal of \$650 million in implicit universal service support from access charges, and the creation of an explicit, portable interstate access universal service support mechanism at the same level;
  - 9) Recovery of LEC universal service contributions directly from end users;
  - 10) Elimination of MUCs by participating long-distance carriers;
  - 11) A commitment by participating long distance carriers to flow through reductions in access rates to residential and business customers over the life of the plan; and
  - 12) Adjustment of the Lifeline Assistance universal service support mechanism to shield low-income customers from increases in the residential SLC.

31. As an initial point, the CALLS Proposal reduces, and in many cases eliminates, implicit subsidies among customer classes through two means. First, by permitting a greater proportion of the local loop costs of primary residential and single line business customers to be recovered through the SLC, rather than through the CCL charge and the multi-line business PICC, the CALLS Proposal reduces, and in most instances removes, the subsidies associated with both of the latter charges. Second, by permitting participating LECs to deaverage their SLCs

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<sup>37</sup> The X-factor is a mechanism used to reduce access rates. See Section IV.B. *infra* for a full discussion.

once the CCL charge and multi-line business PICCs are eliminated, the CALLS Proposal reduces the subsidy that subscribers in low-cost areas provide those in higher cost areas.

32. The CALLS Proposal reduces these subsidies, and keeps rates affordable in high-cost areas, by replacing the subsidies with explicit interstate access universal service support. In section 254(e), Congress stated that federal universal service support should be made explicit.<sup>38</sup> The CALLS Proposal identifies and removes \$650 million of implicit universal service support in interstate access charges, creates an explicit interstate access universal service support mechanism in this amount to replace the implicit support, and makes interstate access universal service support fully portable among eligible telecommunications carriers.<sup>39</sup> The CALLS Proposal conforms with our tentative conclusion in the *Universal Service Seventh Report and Order* that price cap LECs should reduce their interstate access rates to reflect any increase in explicit high-cost support.<sup>40</sup> In addition, we conclude that this interstate access universal support mechanism is specific, predictable and sufficient. Moreover, by making universal service support explicit and portable, the interstate access universal support mechanism should also encourage competitive entry into high-cost areas.

33. We note that even as the CALLS Proposal phases out these subsidies, it maintains several safeguards that ensure that the rates consumers pay for the SLC remain well within a zone of reasonableness. The CALLS Proposal maintains an overall cap on the SLC assessed on primary residential and single-line business lines at \$6.50, and could set the cap even lower if price cap LECs cannot justify higher increases. Thus, as explained below, CALLS ensures that basic telephone service does not become too expensive. The CALLS Proposal also asks the Commission to examine the appropriateness of setting the SLC caps for primary residential and single-line business lines above \$5.00 before doing so.<sup>41</sup> In addition, the CALLS Proposal provides for additional Lifeline support so that low-income subscribers will not be hurt by increases to the primary residential SLC cap. LEC signatories to the CALLS Proposal have also agreed not to assess universal service charges on Lifeline customers.<sup>42</sup>

34. Low-volume long-distance users also benefit from the CALLS proposal. First, AT&T and Sprint both commit to having no monthly minimum charge on their Basic Schedule for at least three years. Second, both carriers agree to eliminate their PICC pass-through charges for residential and single-line business subscribers in light of the elimination of the PICCs for those

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<sup>38</sup> 47 U.S.C. § 254(e).

<sup>39</sup> The interstate access universal service support is distinct from the intrastate high-cost support already in place for local rates. See, e.g., *Universal Service Ninth Report and Order*, 14 FCC Rcd at 20436.

<sup>40</sup> *Universal Service Seventh Report and Order*, 14 FCC Rcd at 8139.

<sup>41</sup> As revised, the CALLS Proposal acknowledges that at the time of the cost proceeding, parties can argue that certain revenues, rather than be incorporated into the SLC, should be disallowed. See *Wallman March 30 Letter* at 2.

<sup>42</sup> *Wallman March 30 Letter* at 3.

customers. Third, in a move that benefits all subscribers, both carriers have agreed to flow through to residential and business customers the savings they realize from the CALLS-related reductions in access charges. We find that these commitments are in the public interest and adopt them as requirements of this Order.

35. Today, we adopt the CALLS Proposal because it accomplishes many objectives that the Commission to date has been unable to achieve in the absence of an industry consensus plan, while providing significant consumer benefits that we would not otherwise be able to ensure on such a wide-scale basis and in such a timely manner. We therefore find the CALLS Proposal to be in the public interest. Certainly there is no guarantee that, at the end of the CALLS Proposal's five-year term, competition will exist to such a degree that deregulation of access charges for price cap LECs is the next logical step. Nevertheless, the CALLS Proposal provides stability during its term and addresses several issues that have served as major obstacles to access charge reform and universal service. We also find the CALLS Proposal to be consistent with our market-based approach to regulation.

#### IV. DISCUSSION

36. We approve and adopt the CALLS Proposal because it resolves in a manner consistent with the public interest a number of complex, contentious and interrelated issues that stand as a roadblock to a competitive marketplace.<sup>43</sup> The CALLS Proposal is a reasonable approach for moving toward the Commission's goals of using competition to bring about cost-based rates, and removing implicit subsidies without jeopardizing universal service. The CALLS proposal is not designed as a permanent solution to all of the issues it addresses; instead, it is a transitional plan that moves the marketplace closer to economically rational competition, and it will enable us, once such competition develops, to adjust our rules in light of relevant market developments.<sup>44</sup> Consequently, as the term of the CALLS Proposal nears its end, we envision that the Commission will conduct a proceeding to determine whether and to what degree it can deregulate price cap LECs to reflect the existence of competition.<sup>45</sup> At that time, the Commission can also examine whether the interstate access universal service support mechanism remains sufficient.

37. The CALLS Proposal provides relative certainty in the marketplace during its five-year term. All parties will have a much clearer blueprint for developing their business plans and attracting capital than they would in the absence of CALLS. As the Massachusetts Department

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<sup>43</sup> Indeed, in a similar context, the D.C. Circuit has admonished the Commission that "[t]he best must not become the enemy of the good, as it does when the FCC delays making any determination while pursuing the perfect tariff." *MCI v. FCC*, 627 F.2d 322, 341-42 (D.C. Cir. 1980).

<sup>44</sup> As explained below, price cap LECs that do not elect the rate level components of the CALLS Proposal will be subject to a forward-looking costs proceeding for those rates.

<sup>45</sup> We note that the Commission has the authority to modify the rules we adopt today before the end of the five-year term of the CALLS Proposal. This Order addresses a marketplace that is dynamic and evolving, and the Commission may exercise its authority should the need arise.

observes, “Resolving so many contentious issues . . . as the CALLS plan does, reduces this uncertainty to the point that it should not be a significant factor in capital investment.”<sup>46</sup>

38. The level of access rates, the amount of universal service support in access rates, and the appropriate X-factor have all been subject to contentious proceedings that heretofore have not been resolved despite years devoted to their resolution. For many years, IXCs and consumer groups have argued that access rates are significantly above cost and contain monopoly profits, the amount of which was itself subject to serious debate.<sup>47</sup> Incumbent LECs, on the other hand, have contended that reducing access charges threatened universal service support. This dispute cannot be resolved with exactitude, as setting access charges is at best an imprecise process whose success can be measured only by using a zone of reasonableness. With adoption of the CALLS Proposal, we believe that we have achieved a reasonable and appropriate up front reduction to access rates that addresses the positions of both sides.

39. The 1996 Act stated that the Commission should create explicit universal service mechanisms that would be secure in a competitive environment.<sup>48</sup> The interstate access universal service support mechanism we create today to replace the implicit universal service support removed from access charges has been subject to heated debate as to the appropriateness of its size and distribution methodology. During the course of the proceeding, some parties have argued that the amount of implicit universal service support in access charges is as high as \$3.9 billion, while others have argued that the figure is only \$250 million.<sup>49</sup> As explained below, determining the amount of implicit universal service support is an imprecise exercise at best. Consequently, it is only today, more than four years after the passage of the 1996 Act, that we issue a decision on this matter.

40. Similarly, the size of the X-factor has been subject to debate ever since the first time it was set with the creation of price caps. More recently, the current X-factor of 6.5 percent, which was set in 1997,<sup>50</sup> is currently on remand with the Commission. By adopting the reasonable approach set forth in the CALLS Proposal, which treats the X-factor not as a productivity estimate but as a method to reduce rates to certain levels, we expect to end the debate over the appropriate size of the X-factor now and for the next five years for participating price cap LECs.

41. The rates proposed by CALLS are reasonable. We have compared LEC revenues over the five-year period under the modified CALLS Proposal with what their revenues would be

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<sup>46</sup> Mass. DTE Comments at 8.

<sup>47</sup> See, e.g., *Access Charge Reform Order*, 12 FCC Rcd at 16249-51.

<sup>48</sup> See 47 U.S.C. § 254.

<sup>49</sup> See Section IV.C.3.b *infra*.

<sup>50</sup> See *1997 Price Cap Review Order*.

under the status quo, and conclude that they are roughly the same.<sup>51</sup> Overall LEC revenues are roughly \$700 million lower than they would have been for the first year of the plan, but gradually increase in the later years so that projected revenue is higher than the status quo at the end of the plan. We note, however, that these estimates make no adjustment to account for voluntary reductions participating LECs might make in response to the development of competition in the marketplace, something that is much more likely to occur in the later years of the plan, in part due to the reduction of implicit subsidies by the CALLS Proposal.<sup>52</sup>

42. We find that the CALLS Proposal provides a number of consumer benefits that are in the public interest. By eliminating the residential PICC, the CALLS Proposal provides immediate reductions to consumers' overall rates, even after taking the increase to the primary residential SLC into account. By having IXCs provide calling plans with no monthly minimum charges, CALLS also provides additional benefits to low-volume long-distance customers. In addition, by recovering a greater proportion of loop costs directly from the end user and by creating an explicit and portable interstate access universal service mechanism, the CALLS Proposal also promotes the development of greater facilities-based residential competition.

43. We reject the last-minute alternative proposed by ALTS and Time Warner.<sup>53</sup> Their proposal would not be as beneficial a plan as that submitted by CALLS because, among other considerations, the smaller annual reductions to per-minute rates would result in a delay to more economically efficient rates. We note that the ALTS and Time Warner plan contains several of the same elements as does CALLS. For example, it eliminates the residential and single-line business PICCs, and increases the primary residential and single-line business SLCs to \$4.35 on July 1, 2000. Nevertheless, for the reasons discussed below, we find that their plan is not well developed. To do what is necessary to flesh out their plan, including seeking comment on it and resolving internal inconsistencies, would require many more months of proceedings, thereby resulting in significant delay in implementation.<sup>54</sup>

44. We reject the contention by ALTS and Time Warner that by adopting the CALLS Proposal we are abandoning the Commission's commitment to using competition to drive down access charges.<sup>55</sup> By adopting the CALLS Proposal, we require price cap LECs to make a larger

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<sup>51</sup> See Appendix C, Graphs 1 and 2. These calculations assume that the X-factor remains at 6.5 percent, but that inflation remains relatively low, at 1.95%. If inflation is higher, the CALLS Proposal produces lower overall rates relative to the status quo. Our estimates are based on applying our current rules and the CALLS Proposal's proposed rules to publicly available data, so we are puzzled by MCI's insistence that CALLS should have released its own estimates. See MCI Supp. Comments at 3-5; see also New Jersey Div. Supp. Comments at 4-5; Ad Hoc Supp. Reply at 5-6.

<sup>52</sup> See also CALLS Supp. Reply at 39-41.

<sup>53</sup> ALTS and Time Warner Supp. Comments, Exhibit.

<sup>54</sup> The Original Proposal was, despite its shortcomings, exceptionally well developed. Nevertheless, it is only now being adopted, after 10 months and significant modification.

<sup>55</sup> ALTS and Time Warner Supp. Comments at 8.

rate reduction than they otherwise would have on July 1, 2000. For carriers that elect CALLS, however, we defer the rate prescription scheduled to take place next year that the Commission established as a “backstop” to the market-based approach in the event competition was slow to develop.<sup>56</sup> We thereby allow four additional years for competition to develop sufficiently to begin to control access rates.

45. In addition, we find that the ALTS/Time Warner plan is poorly defined. For example, ALTS and Time Warner fail to explain how a SLC cap of \$4.35, together with a \$300 million interstate access universal service mechanism, would be appropriate to ensure adequate recovery of interstate loop costs in rural and high cost areas. ALTS and Time Warner also fail to explain how SLCs could be deaveraged when the SLC caps are set at that level. The ALTS/Time Warner plan also lacks an overall rationale. For example, ALTS and Time Warner criticize the up front reductions in the CALLS Proposal as unjustified,<sup>57</sup> yet they propose an undefended reduction, albeit a smaller one, “as a compromise.”<sup>58</sup> ALTS and Time Warner also criticize the X-factor targeting employed by CALLS,<sup>59</sup> even though they propose an unsupported targeting of the X-factor different from the status quo.<sup>60</sup> In addition, unlike the CALLS Proposal, ALTS and Time Warner have no support from parties other than competitive LECs.

46. We conclude that adopting the ALTS and Time Warner proposal would not serve the public interest. Although they object to the initial reduction in per-minute rates, at no point do they assert that the reductions proposed by CALLS will result in below-cost access rates. We believe that despite the criticisms by ALTS and Time Warner, the CALLS Proposal creates significant business opportunities for Time Warner and the members of ALTS. By reducing and removing the subsidies that currently keep the primary residential SLC rates below the level of loop costs currently allocated to interstate service, as accomplished through the CALLS Proposal, we are encouraging facilities-based carriers such as Time Warner and the members of ALTS to compete for residential subscribers.<sup>61</sup>

47. With one exception that we discuss below, we decline to make any significant modifications<sup>62</sup> to the CALLS Proposal as some parties advocate,<sup>63</sup> and instead agree with the

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<sup>56</sup> *Access Charge Reform Order*, 12 FCC Rcd at 16097.

<sup>57</sup> ALTS and Time Warner Supp. Comments at 3, 11-12.

<sup>58</sup> ALTS and Time Warner Supp. Comments at 4, 16.

<sup>59</sup> ALTS Supp. Comments at 8-10.

<sup>60</sup> ALTS Supp. Comments at 4, 16.

<sup>61</sup> *See* CALLS Supp. Reply at 43.

<sup>62</sup> We do in fact make some minor and technical changes to the CALLS Proposal. *See* Section IV.B.2.c. *infra* (changing the inflation measurement used to calculate the price cap indices). *But see e.g.*, Letter from John T. Nakahata, Counsel to CALLS, to Magalie Roman Salas, Secretary, FCC, April 24, 2000 (asserting that CALLS considers this change in the CALLS Proposal to be a material one).

CALLS signatories that we should assess the proposal as a whole. In so doing, we note that the Original Proposal, made by a group of price cap LECs and IXC's but without comment from consumer groups, did not address the interests of consumers as adequately as the Modified Proposal. In response to the various critiques of the Original Proposal, CALLS made several pro-consumer changes that resulted in a substantially more equitable proposal. These changes include lowering the primary residential and single-line business SLC caps from the Original Proposal, both at the start of the plan and throughout its term; proposing a cost review to examine the appropriateness of raising the SLC caps above \$5.00; eliminating minimum usage charges for basic long distance service by CALLS long-distance signatories; and removing a significant amount of revenues from access charges altogether, rather than shifting those permitted revenues to the common line basket.

48. We acknowledge that CALLS signatories have made compromises, both among themselves and to accommodate other interests. Having two groups representing historically opposing positions, *i.e.*, LECs (sellers of access services) and IXC's (buyers), reach an agreement removes much of the rhetoric that has stood as an obstacle to comprehensive action. Thus, the CALLS Proposal allows us to move forward more quickly by removing certain issues from consideration that would have delayed reaching a comprehensive solution. The fact that the resolution of these issues was achieved through a joint proposal among a cross-section of LECs and IXC's provides us with some indication that the proposal is within a zone of reasonableness.<sup>64</sup> We believe the parties have negotiated with each other in good faith and fashioned a reasonable compromise that both addresses their competing interests and serves the broader public interest. We also believe that the proposal, particularly after taking its modifications into account, fairly balances the interests of all parties, including those who are not part of the coalition. We are supported in this belief by the support the plan has received from other interested parties, including certain consumer groups,<sup>65</sup> some state regulators,<sup>66</sup> and competitors.<sup>67</sup>

49. At the same time, we must exercise our own independent judgment to ensure that any proposal we adopt in this area -- even a proposal that reflects a substantial degree of

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<sup>63</sup> See, *e.g.*, Ad Hoc Supp. Comments at 3; Allegiance Supp. Comments at 4; Cincinnati Bell Supp. Comments at 1-2.

<sup>64</sup> We note that courts allow for pragmatic adjustments in the rate setting context. *FPC v. National Gas Pipeline Co.*, 315 U.S. 575, 586 (1942). Indeed, in reviewing rate setting decisions, the courts focus on the "net effect," allowing that "[e]rrors to the detriment of one party may well be canceled out by countervailing errors or allowances in another part of the proceeding." *Duquesne Light Co. v. Barasch*, 488 U.S. 299, 314 (1989).

<sup>65</sup> See APT Supp. Comments at 8; Rainbow/PUSH Supp. Comments at 2; NHCA Supp. Reply at 1; United Seniors Supp. Reply at 1; Letter from Martin A. Corry, Director, Federal Affairs, AARP, to William Kennard, Chairman, FCC, April 13, 2000. *But see* Joint Consumer Commenters

<sup>66</sup> See Mass. DTE Comments at 9; Maine Joint Commenters Supp. Reply at 2. *But see*, Maryland Commission Supp. Reply Comments at 4; Florida Commission Comments at 1.

<sup>67</sup> See Qwest Supp. Comments at 3; CompTel Supp. Reply at 2 (generally supporting CALLS Proposal). *But see* ALTS Supp. Reply at 4; Joint Consumer Commenters at 2.

consensus among historically adverse parties -- is reasonable and in the public interest. We have exercised that judgment here, and we find that CALLS falls easily within the range of reasonable solutions to the problems it addresses. CALLS is most appropriately judged as a single, cohesive proposal, because the underlying issues it addresses are themselves interrelated. We therefore focus our inquiry on the reasonableness of the proposal taken as a whole, although we also find that its essential constituent parts individually fall within the range of reasonableness. There is no one "right answer" to many of the disputes that the CALLS proposal resolves. There are instead ranges of reasonable solutions, and the ultimate question is whether CALLS is a sensible transitional plan for accommodating the Act's universal service goals with the development of fuller, more rational competition. Moreover, while we of course have the legal authority to make substantive changes to the CALLS Proposal and impose them on the industry, we generally decline to do so. Although we might ourselves, after further delay, independently devise a different set of reasonable solutions to the problems addressed by the current proposal, the preferable course is to adopt the proposal itself, because it is reasonable in its own right, because it is ready to be implemented, and because it already commands a commendable degree of industry consensus.

50. Although we find the CALLS proposal is reasonable for CALLS signatories and is likely to be reasonable for non-signatory price cap LECs, we recognize that it was developed with the idea that it would be voluntary for price cap LECs. At the same time, however, the benefits of the CALLS Proposal could not be fully realized if all price cap LECs did not participate. Because the CALLS Proposal is a cohesive proposal, failure to implement it fully would frustrate the consumer benefits we find appropriate for its adoption. Moreover, failure to implement CALLS completely will impede advancement toward the 1996 Act's competition and universal service goals.

51. Section 254(g) of the Act requires IXCs to average their rates.<sup>68</sup> Accordingly, AT&T and Sprint cannot honor their commitments to eliminate residential PICCs and single-line business PICCs for customers of participating price cap LECs without eliminating these charges for customers of all carriers. AT&T and Sprint committed to eliminate their PICC pass-through charges for residential and single-line business customers on the condition that they would no longer be assessed PICCs for those customers. If some price cap LECs continued under the status quo, they would continue to charge PICCs on residential and single-line business lines, and one would expect that IXCs would seek to recover these costs through a flat charge.

52. If IXCs assessed a PICC pass-through charge on all residential and single-line business customers to recover the PICCs assessed on them by non-participating price cap LECs, residential and single-line business customers of participating LECs would end up paying higher overall rates than would residential and single-line business customers of non-participating LECs.

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<sup>68</sup> 47 U.S.C. § 254(g) ("[R]ates 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 telecommunications 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.")

The primary residential and single-line business customers of non-participating LECs would have their SLCs capped at \$3.50, and would have PICCs assessed on their lines to recover additional local loop costs, which would be averaged by IXC among all customers. Customers of participating LECs would then pay a higher SLC, yet still be paying a PICC pass-through charge that reflects the IXCs' cost of paying PICCs to any non-participating price cap LECs. This would reduce some of the significant consumer benefits of the CALLS Proposal. It would also create a new subsidy running from customers of participating LECs to those of non-participating LECs, thereby frustrating the goal of removing implicit subsidies.

53. In addition, AT&T's commitments are predicated on there being a \$2.1 billion aggregate reduction to access charge usage rates.<sup>69</sup> Because each CALLS LEC signatory has only committed to a proportional share of this sum based on an assumption of full participation,<sup>70</sup> full participation by price cap LECs is necessary to reach the overall access charge usage rate reduction. Therefore, in the absence of full participation, neither AT&T nor Sprint<sup>71</sup> would be obligated to fulfill their commitments, including those commitments regarding elimination of minimum usage charges, the flow-through of access charge reductions to residential and business customers, and consumer education efforts.

54. We also note that for price cap LECs that would not participate in CALLS, the implicit universal service subsidies contained in those LECs' access charges would remain. We would thus be required to conduct a proceeding to determine the size of that implicit universal service support, thereby delaying the creation of an explicit and portable interstate access universal service support mechanism for those areas. Until we completed that proceeding, competitive LECs in those price cap LECs' service areas would be unable to receive interstate access universal service support.

55. Similarly, without full participation by price cap LECs, the averaging requirements imposed on IXCs under section 254(g) of the Act could place IXCs at a competitive disadvantage if Bell Operating Company (BOC) long-distance affiliates only offer service to their in-region customers as they enter the long distance market. A long-distance affiliate of a BOC participating in CALLS would be able to offer lower per-minute rates than would an IXC having to average its access charges across all regions, including those serving non-participating price cap LEC customers.<sup>72</sup> Non-participating LECs would receive a windfall from CALLS, because the IXCs'

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<sup>69</sup> *AT&T March 30 Letter* at 1.

<sup>70</sup> Modified Proposal at § 3.2.4.

<sup>71</sup> *Sprint February 25 Letter* at 1 ("Sprint will not impose a minimum usage charge ("MUC") on at least one basic rate plan for the duration of the CALLS plan, provided that if any other interexchange carrier that is now or hereafter a party to the CALLS plan reserves the right to impose a MUC on its basic rate plan prior to the termination of the CALLS plan, Sprint reserves the right to do so as well under similar terms and circumstances.").

<sup>72</sup> We note that the national rate averaging requirement of section 254(g) already places nationwide IXCs at a competitive disadvantage because they must average rates for all areas, including regions served by rate-of-return (continued....)

averaged rates, which would be significantly lower due to the effects of the CALLS Proposal, would stimulate demand for interstate access in the LECs' regions, even though those LECs would not have significantly reduced their in-region per-minute rates.

56. Nevertheless, we recognize that not all price cap LECs could agree on all aspects of the CALLS Proposal.<sup>73</sup> CALLS members worked among themselves to develop the mechanisms under which price cap LECs contribute toward reducing switched access usage charges by \$2.1 billion, as well as the rules that determine the size and distribution of the \$650 million interstate access universal service support mechanism. These decisions necessarily pit each price cap LEC's interest against the interests of all other price cap LECs. Consequently, price cap LECs that did not agree to the CALLS Proposal might not receive the same benefits or carry the same burdens as the CALLS LEC signatories.

57. Accordingly, out of an abundance of caution, we provide an opportunity for price cap LECs to choose between two options for certain rate-level, as opposed to rate structure, components of the CALLS proposal. Specifically, price cap LECs may elect CALLS for the full five-year period. Alternatively, price cap LECs may elect to submit a cost study based on forward-looking economic cost that will be the basis for reinitializing rates to the appropriate level. Because a cost study proceeding necessarily requires data specific to the price cap LEC to be submitted and analyzed, we find it necessary to mandate the CALLS rate-level components on an interim basis, subject to true-up, in order to provide sufficient time to complete a cost study. A price cap LEC that elects the second option will be subject to the following rate-level components of the CALLS Proposal until we have completed the forward-looking economic cost review: the size of the up-front reduction; the size of the carrier's interstate access universal service support; the X-factor; and the switching target levels. Adopting these components on an interim basis will permit realization of the full consumer benefits of the CALLS proposal and preserve the \$2.1 billion reduction in switched access usage charges for the first year.

58. At the same time, we adopt the rate structure components of the CALLS Proposal as mandatory for all price cap LECs, for the five-year period envisioned by the CALLS proposal. The rate structure components are the new SLC caps, elimination of the residential PICC, the multi-line business PICC caps, the creation of a separate basket for special access, elimination of the marketing basket and the recovery of the revenues it recovered as part of CMT revenues, recovery of universal service contributions directly from end users, SLC deaveraging, portability of the interstate access universal service mechanism, and increased Lifeline support to cover the new SLC caps. For the reasons discussed elsewhere in this order, the changes made in these components are reasonable and in the public interest and consistent with our policy of requiring, to the extent possible, that non-traffic sensitive costs be recovered through fixed rates or flat charges. In addition, these changes do not affect carriers' overall recovery of their costs and thus do not raise the same issues as the rate-level components.

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LECs. Permitting large carriers such as U S West to maintain rates significantly above the CALLS target levels would exacerbate this competitive disadvantage.

<sup>73</sup> See Letter from John Kure, Executive Director, Federal Regulatory, U S West, to Magalie Roman Salas, Secretary, FCC, April 28, 2000.

59. For the rate level components, each price cap LEC will, at the holding-company level, choose between two options. The first alternative is to subscribe to the CALLS Proposal for its full five-year term. The second alternative is to submit a cost study based on forward-looking economic costs, resulting in the LEC's rates being reinitialized to the appropriate level indicated by the study and then made subject to a price cap plan and X-factor that we would determine.

60. This cost-study proceeding is consistent with what we outlined in the *Access Charge Reform Order*.<sup>74</sup> In the *Access Charge Reform Order*, the Commission stated that its goal was for interstate access charges to reflect the forward-looking economic costs of providing interstate access services.<sup>75</sup> The Commission adopted a two-phased approach to reach that goal. It adopted a market-based approach that relied on competitive pressures to bring prices toward forward-looking economic cost, with incumbent LECs receiving additional pricing flexibility where competition has developed. The second phase provided, however, that the Commission would require forward-looking cost studies by no later than February 8, 2001 for access services that were not subject to competition and “eventually prescribe rates for those services at forward-looking economic cost levels.”<sup>76</sup> For those carriers that accept the CALLS Proposal, we are extending for five years the period during which we will allow the market-based approach to bring interstate access prices toward forward-looking economic cost. Those carriers that reject the CALLS Proposal will operate under the framework the Commission set forth in the *Access Charge Reform Order* to address services that are not subject to substantial competition.<sup>77</sup>

61. Each price cap LEC will have 60 days from the release of this Order to make its election between the two options. This election will be binding for the five-year term of CALLS. Price cap LECs that elect to proceed with a cost study will be subject to the rules we adopt today until the completion of our cost study proceeding. We make this election binding because we believe the CALLS proposal, coupled with a true-up mechanism discussed below, will ensure reasonable rate levels for all price cap LECs, while ensuring that the Commission does not waste its limited resources in cost proceedings performed solely for the purpose of having LECs determine under which approach they would be better off.

62. For a price cap LEC electing the cost study option, we also adopt a true-up mechanism to be applied to such price cap LEC's rates. This will enable the LEC and its customers to be treated as it would have been, had we completed the cost study in time to avoid the need for imposing the CALLS Proposal for an interim period. Should any price cap LEC elect to participate in the cost-study proceeding, the Commission will consider the sufficiency of the interstate access universal service support mechanism, including both the size and distribution

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<sup>74</sup> *Access Charge Reform Order*, 12 FCC Rcd at 16096-97.

<sup>75</sup> *Access Charge Reform Order*, 12 FCC Rcd at 16092-99.

<sup>76</sup> *Access Charge Reform Order*, 12 FCC Rcd at 16099.

<sup>77</sup> These carriers may still obtain pricing flexibility for those services that are subject to competition pursuant to the *Pricing Flexibility Order*.

of support, concurrently with the industry-wide review of the increase to the primary residential SLC cap after July 2001, to avoid duplication of effort. We reject arguments offered by parties asking that we make the CALLS Proposal wholly mandatory.<sup>78</sup> CompTel's contention that we have not previously implemented opt-in regulation for incumbent LECs is wrong.<sup>79</sup> Other than the BOCs and GTE, all incumbent LECs have had the choice of whether to elect rate-of-return or price cap regulation.<sup>80</sup> In addition, for several years all price cap LECs were permitted to elect the level of sharing and the X-factor to which they would be bound.

63. Below, we discuss each portion of the CALLS proposal in detail. In Section A., we address the impact of the CALLS proposal on services in the common line and marketing baskets. In Section B., we set forth the impact of the proposal on the local switching and trunking baskets, including the modifications to the X-factor and the creation of a separate basket for special access. In Section C., we discuss the universal service components of the CALLS proposal. In Section D., we conclude that the CALLS Proposal addresses the concerns raised in the *Low-Volume Long-Distance NOI*.

## A. Common Line Charges

### 1. Background

64. In the *1983 Access Charge Order*, the Commission established a comprehensive mechanism for LECs to recover their costs of providing access service to complete interstate and foreign telecommunications.<sup>81</sup> This mechanism distinguished between traffic sensitive costs and non-traffic sensitive (NTS) costs incurred by a LEC to provide interstate access service. The Commission emphasized in the *1983 Access Charge Order* that its long range goal was for LECs to recover a large share of their NTS common line costs on a flat-rated basis from end users instead of from carriers.<sup>82</sup> The rules adopted in 1983 apportioned charges for common line costs between a monthly flat-rated SLC assessed on end users and a per-minute CCL charge assessed on the IXCs, which ultimately was recovered from end users through long distance charges.<sup>83</sup>

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<sup>78</sup> See, e.g., CompTel Comments at 7-8; CPI Reply at 4, 9; Iowa Utilities Board Supp. Comments at 6.

<sup>79</sup> CompTel Comments at 8.

<sup>80</sup> *LEC Price Cap Order*, 5 FCC Rcd at 6787.

<sup>81</sup> *1983 Access Charge Order*, 93 F.C.C.2d at 241. Although we had not moved to a price cap regulatory regime at that time, LECs who later became price cap LECs were subject to the access charge system.

<sup>82</sup> *1983 Access Charge Order*, 93 F.C.C.2d at 264-65. The Commission found that a subscriber who does not use the subscriber line to place or receive interstate calls imposes the same NTS costs as a subscriber who does use the line. Thus, simply by requesting telephone service, the subscriber causes local loop costs whether she uses the service for intrastate or interstate calls. *1983 Access Charge Order*, 93 F.C.C.2d at 278.

<sup>83</sup> Thus, LEC common line revenues = end-user SLC "plus" (CCL charge "times" usage), when access charges were first adopted.

65. In the *Access Charge Reform Order*, in order to align the rate structure more closely with the manner in which costs are incurred, the Commission changed the manner in which price cap LECs recover their permitted common-line revenues.<sup>84</sup> Consistent with the goal enunciated in the *1983 Access Charge Order*, because the costs of using the price cap LEC's common line (or "local loop") do not increase with usage, the Commission decided that these costs should be recoverable entirely through flat, non-traffic-sensitive fees.<sup>85</sup> Out of an abundance of caution for affordability and universal service concerns at that time, however, the Commission did not raise the SLC cap for primary residential and single-line business lines above the \$3.50 level in effect at the time to permit the full recovery of common line revenues.<sup>86</sup> Rather, to the extent that common line revenues are not recovered through the end-user's SLC, the Commission permitted LECs to recover these revenues through the PICC, a flat, per-line charge assessed on the IXC to whom the access line is presubscribed.<sup>87</sup>

66. Affordability concerns were not as significant for non-primary lines and multi-line business customers.<sup>88</sup> As a result, the Commission permitted increases in their SLC caps from \$3.50 to \$5.00 plus future increases for non-primary lines, and from \$6.00 to \$9.00 plus increases for inflation for multi-line business customers to permit recovery of the price cap LECs' average per-line common line revenues.<sup>89</sup> The Commission also established flat-rated PICCs on non-primary residential and multi-line businesses to recover common line revenues that cannot be recovered from residential and single-line business customers due to the caps on SLCs and primary residential PICCs.<sup>90</sup>

67. The PICC was designed to be phased in over a several year period. The PICC for primary residential and single-line business lines was capped at \$0.53 in the first year with annual adjustments thereafter for inflation plus \$0.50 until the sum of the SLC plus the PICC equals the price cap LEC's permitted common line revenues per line. Under current rules, the caps on non-primary and multi-line business PICCs also increase over time. As the primary residential and single-line business PICCs increase, however, the resulting increase in recovery of common line costs through flat charges on primary residential and single-line business lines will eliminate the subsidization of subscribers' rates for those lines by non-primary residential and multi-line

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<sup>84</sup> *Access Charge Reform Order*, 12 FCC Rcd at 16007-33. Incumbent LECs that are subject to rate of return regulation remain under the original 1983 common line rate structure rules.

<sup>85</sup> *Access Charge Reform Order*, 12 FCC Rcd at 16004.

<sup>86</sup> *Access Charge Reform Order*, 12 FCC Rcd at 16010-11.

<sup>87</sup> 47 C.F.R. § 69.153; *Access Charge Reform Order*, 12 FCC Rcd at 16019-20. Thus, after access reform, price cap LEC common line revenues = end-user SLC "plus" IXC PICC "plus" (CCL charge "times" usage).

<sup>88</sup> *Access Charge Reform Order*, 12 FCC Rcd at 16005.

<sup>89</sup> *Access Charge Reform Order*, 12 FCC Rcd at 16005.

<sup>90</sup> *Access Charge Reform Order*, 12 FCC Rcd at 16022.

business lines.<sup>91</sup> At this point, non-primary residential and multi-line business lines will no longer be assessed PICCs. Some price cap LECs already have reached this point; others would not reach this point for a number of years.

68. To the extent that the caps on SLCs and PICCs do not allow recovery through flat charges of all common line revenues, LECs are still permitted to impose a per-minute CCL charge assessed on originating minutes.<sup>92</sup> As the PCCC caps for non-primary residential and multi-line business lines increase, and as flat-rated revenues received from primary residential and single-line businesses increase, the per-minute CCL charge will be eliminated. At present, among the price cap LECs, only BellSouth, Citizens, and certain study areas of GTE, Frontier, and Sprint continue to collect CCL charges.<sup>93</sup>

69. In the Further Notice of Proposed Rulemaking adopted in August, 1999, the Commission sought comment on whether to permit price cap LECs to geographically deaverage common line access and traffic sensitive elements without a competitive showing and whether to condition such authority on certain regulatory developments.<sup>94</sup> The Commission also sought comment on whether it should grant pricing flexibility for switched access and common line services.<sup>95</sup> That proceeding remains pending.

## 2. CALLS Proposal

70. The CALLS signatories propose reforming and simplifying common line charges by combining the SLC, PCCC and CCL charges into a single end-user charge that can be deaveraged under limited circumstances. Under the CALLS Proposal, the PCCC for residential and single-line businesses would be eliminated beginning July 1, 2000.<sup>96</sup> The SLC for primary residential and single-line business lines would be capped at \$4.35 upon implementation of the proposal beginning July 1, 2000, \$5.00 as of July 1, 2001, \$6.00 as of July 1, 2002, and \$6.50 as of July 1, 2003.<sup>97</sup> The proposal also calls for the Commission to initiate a proceeding after the SLC cap reaches \$5.00 to examine whether increases to the SLC cap for residential and single-line businesses above \$5.00 are appropriate, and reflect the costs in the UNE zone or zones where

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<sup>91</sup> *Access Charge Reform Order*, 12 FCC Rcd at 15999-00, 16005.

<sup>92</sup> *Access Charge Reform Order*, 12 FCC Rcd at 16005.

<sup>93</sup> The CCL charge already has been eliminated for Ameritech, Bell Atlantic, PacTel, Southwestern Bell Telephone, U S WEST, Aliant, SNET and Cincinnati Bell.

<sup>94</sup> *Pricing Flexibility Order*, 14 FCC Rcd at 14320-24.

<sup>95</sup> *Pricing Flexibility Order*, 14 FCC Rcd at 14324-26.

<sup>96</sup> Modified Proposal at § 2.1.2.1.

<sup>97</sup> Modified Proposal at § 2.1.2.2.1. See Appendix C, Chart 1 for a comparison of the SLC and PCCC caps under our current rules and as proposed by CALLS.

they would apply.<sup>98</sup> The maximum primary residential and single-line business SLC in any zone would be the average price cap common line, marketing and transport interconnection charge revenue (Price Cap CMT Revenue) per line for the highest cost unbundled network element (UNE) zone<sup>99</sup> in a study area up to the nominal cap.<sup>100</sup> Price Cap CMT Revenue is defined as the total revenue a filing entity is permitted to receive for SLCs, PICCs and CCL charges.<sup>101</sup> Price Cap CMT Revenue also includes marketing expenses pursuant to section 69.156(a) of the Commission's current rules, and residual interconnection charge revenues collected through PICCs.<sup>102</sup>

71. In addition to eliminating the PICC for non-primary residential lines, the CALLS Proposal would cap the maximum SLC for these lines at the lower of \$7.00 or the greater of the current rate or average Price Cap CMT Revenue per line for the highest average revenue per line UNE zone in a study area.<sup>103</sup> Once charges for primary and non-primary residential lines are equal within a zone or study area, a price cap LEC could eliminate the distinction between primary and non-primary lines within that zone or study area.<sup>104</sup> Although the distinction between primary and non-primary residential lines could be eliminated in most circumstances under the proposal, it would remain for those subscribers where the average Price Cap CMT Revenue exceeds the maximum primary residential SLC cap.

72. For multi-line business customers, the SLC and PICC would not be combined.<sup>105</sup> The multi-line business PICC would continue to be charged to the IXCs with a cap of \$4.31 per line.<sup>106</sup> It would be reduced as the residential SLCs increase until it is phased out.<sup>107</sup> The SLC

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<sup>98</sup> Although the CALLS Proposal describes this cost review proceeding to be limited to primary residential and single-line business lines, CALLS subsequently clarified its submission to include all residential lines as part of the proposed cost review proceeding. *See Wallman March 30 Letter* at 2.

<sup>99</sup> A UNE Zone is a state created zone pursuant to Section 51.507(f) of the Commission rules, which requires states to establish different rates for unbundled network elements in at least three defined geographic areas within the state to reflect geographic cost differences. 47 C.F.R. § 51.507(f).

<sup>100</sup> Modified Proposal at §§ 2.1.1.1, 2.1.2.2.1.

<sup>101</sup> Under the CALLS Proposal, the price cap LEC common line revenues for residential and single-line businesses = end-user SLC "plus" (CCL charge "times" usage).

<sup>102</sup> Modified Proposal at § 2.1.1.1.

<sup>103</sup> Modified Proposal at §§ 2.1.3.1, 2.1.3.2.1.

<sup>104</sup> Modified Proposal at § 2.1.3.2.3.

<sup>105</sup> Under the CALLS Proposal, the price cap LEC common line revenues for multi-line businesses = end-user SLC "plus" IXC PICC "plus" (CCL charge "times" usage).

<sup>106</sup> Modified Proposal at § 2.1.4.1.

<sup>107</sup> Modified Proposal at §§ 2.1.4.1, 2.1.6.

would be the lesser of \$9.20 or the greater of (1) the rate as of December 31, 1999, less certain amounts of SLC reductions or (2) Average Price Cap CMT Revenue Per Line where SLCs have not been deaveraged.<sup>108</sup> Multi-line business SLCs would be frozen until the carrier's multi-line business PICC and CCL charges are eliminated – except where a carrier chooses to reduce the SLC through voluntary reductions.<sup>109</sup>

73. SLCs could be deaveraged subject to certain limitations.<sup>110</sup> Price cap LECs could only geographically deaverage their SLCs after a state commission establishes deaveraged UNE rates by zone and PICCs and CCL charges are eliminated. Deaveraged SLCs by customer class within each UNE zone also could not generate more revenue than that generated by geographically averaged SLCs.<sup>111</sup> A price cap LEC, however, could take a voluntary reduction at any time. Price cap LECs may have up to four SLC zones, absent Commission review and approval, and price cap LECs can determine which zones to consolidate if they have more than four UNE zones.<sup>112</sup> A carrier need not eliminate CCL charges and PICCs prior to deaveraging by voluntary reductions. A price cap LEC also could not reduce multi-line business SLCs below non-primary residential SLCs or non-primary residential SLCs below primary residential and single-line business SLCs in a given UNE pricing zone.<sup>113</sup> SLCs of a given customer class, such as multi-line business, could not have a lower price in higher cost zones than any line in a lower cost zone.<sup>114</sup> Finally, except with respect to voluntary reductions, the proposal would establish a minimum charge within the lowest cost zone, which allows consumers outside the lowest cost zone to share the benefits of SLC deaveraging.<sup>115</sup>

74. Each CALLS LEC signatory also commits to reduce “switched access usage charges” by its proportional share of \$2.1 billion on July 1, 2000.<sup>116</sup> Most LECs would achieve these reductions solely through rate decreases. Under the proposal, however, two mutually

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<sup>108</sup> Modified Proposal at § 2.1.4.2.1.

<sup>109</sup> Modified Proposal at § 2.1.4.2.1. “Voluntary Reduction” is one in which the price cap LEC reduces prices other than through offset. Modified Proposal at § 2.1.5.6.3.

<sup>110</sup> Modified Proposal at § 2.1.5.

<sup>111</sup> Modified Proposal at §§ 2.1.5.1, 2.1.5.5, 2.1.5.6.1.

<sup>112</sup> Modified Proposal at §§ 2.1.5.2, 2.1.5.6.1.

<sup>113</sup> Modified Proposal at § 2.1.5.3.

<sup>114</sup> Modified Proposal at § 2.1.5.4.

<sup>115</sup> Modified Proposal at § 2.1.5.6.2.

<sup>116</sup> Modified Proposal at § 3.2.4.

exclusive alternatives are proposed to permit certain carriers to move some of these permitted revenues to the common line basket.<sup>117</sup>

### 3. Discussion

75. We adopt the common line rate structure aspects of the CALLS Proposal because it is pro-competitive and provides immediate significant consumer benefits through reduced consumer rates. Furthermore, consistent with the 1996 Act, including section 254(k), it simplifies the current rate structure and long distance bills, reduces consumer confusion, and furthers the Commission's efforts over the past two decades to eliminate per-minute recovery of common line costs.<sup>118</sup> Although support for the CALLS Proposal was not unanimous, the proposal is a major step forward from the Commission's current access charge regime, and preferable in moving access charges to cost-based levels than the current process.<sup>119</sup>

#### a. Residential and Single Line Business SLCs and PICCs

76. In this Order, we eliminate residential and single-line business PICCs. We also increase the related SLC caps as proposed and modify our rules accordingly. As explained below, we find that this action is within the Commission's statutory authority to order proper recovery of the portion of common line costs that has been allocated to the interstate jurisdiction through charges imposed on telephone subscribers, and that doing so does not violate the Communications Act of 1934, as amended.<sup>120</sup>

77. Our actions today are in furtherance of our goal of having price cap LECs recover a large share of their NTS common line costs from end users who cause them instead of carriers, and to recover these costs on a flat-rated, rather than a usage-sensitive, basis.<sup>121</sup> As explained below, we find that modifying these charges in the proposed manner will simplify the current rate structure and consequently consumers' bills by eliminating some of the complexity involved with

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<sup>117</sup> Modified Proposal at §§ 3.2.4.1, 3.2.4.2; *see* Section IV. B. *infra* for discussion of this portion of the CALLS Proposal.

<sup>118</sup> 47 U.S.C. § 254(k).

<sup>119</sup> Cable & Wireless Comments at 1-3; CompTel Comments at 2, 10; Western Wireless Reply at 2; Cincinnati Bell Comments at 2; Cincinnati Bell Supp. Comments at 6; Global Crossing Supp. Comments at 1; Qwest Supp. Comments at 2-3.

<sup>120</sup> 47 U.S.C. §§ 4(i), 201-205; *see National Association of Regulatory Utility Commissioners v. Federal Communications Commission*, 737 F.2d 1095, 1114 (D.C. Cir. 1984) (*NARUC v. FCC*) (Commission may properly order recovery, through charges imposed on telephone subscribers, of the portion of loop costs placed in the interstate jurisdiction); *see also Smith v. Illinois Bell*, 282 U.S. at 148-49 (portion of the costs of local subscriber plant relating to interstate services may be recovered only under the authority of a body with interstate regulatory powers).

<sup>121</sup> *See 1983 Access Charge Order*, 93 F.C.C.2d at 264-65, 278; *see also Access Charge Reform Order*, 12 FCC Rcd at 16007.

these charges and the billing practices that gave rise to the *Truth-in-Billing Order* and *Low-Volume Long-Distance Users NOI*.<sup>122</sup>

78. By eliminating the residential and single-line business PICCs, the CALLS Proposal establishes a straightforward, economically rational pricing structure which enables consumers to make a choice among competing providers through head-to-head comparisons and better promotes competition by sending potential entrants economically correct entry incentives.<sup>123</sup> Furthermore, because of the PICC billing practices of many IXCs, the new SLC caps ultimately will result in a further reduction of the overall amount many consumers currently pay for their individual SLCs and PICCs. Most IXCs currently recover PICCs from their customers through a blended PICC pass-through charge<sup>124</sup> on a per-account basis. This practice results in consumers with only one line paying more than they otherwise would had the LECs simply passed onto them directly the \$1.04 worth of permitted revenues that the LEC recovers through the single-line PICC.<sup>125</sup> We estimate that IXCs are recovering additional amounts per account in “transaction costs” to recover their Lifeline costs, universal service contributions and bad debt associated with non-paying subscribers. Specifically, while we estimate that the average IXC blended PICC pass-through rate absent any additional amounts recovered by IXCs currently is approximately \$1.23,<sup>126</sup> AT&T, MCI WorldCom and Sprint currently charge their residential customers \$1.51, \$1.46 and \$1.50, respectively, as a blended PICC pass-through charge on a per-account basis. Eliminating the PICC, therefore, will make common line billing more efficient and more closely aligned with costs.<sup>127</sup>

79. Under the CALLS Proposal, the primary residential and single-line business SLC cap will be less than the combined SLC and PICC would be beginning July 1, 2000 under our existing rules. Under our existing rules, the primary residential and single-line business SLC currently is capped at \$3.50 per line. The primary residential and single-line business PICC cap

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<sup>122</sup> Truth-in-Billing and Billing Format, CC Docket No. 98-170, First Report and Order, 14 FCC Rcd 7492 (1999) (*Truth-in-Billing Order*); *Low-Volume Long-Distance Users NOI*; see also CALLS Comments at 9.

<sup>123</sup> See CALLS Comments at 9-10.

<sup>124</sup> The “blended PICC pass-through charge” is the flat, averaged, monthly IXC charge to end users designed to recover the PICC that the long-distance carriers were paying regulated local carriers for primary and secondary lines.

<sup>125</sup> Indeed, under our existing rules, we have permitted LECs to bill the PICC directly to end users who do not presubscribe to an IXC. The PICC charged in these situations has generally been less than those charged by IXCs. See *Access Charge Reform Order*, 12 FCC Rcd at 15999; see also American Petroleum Comments at 4.

<sup>126</sup> This estimate is based upon a weighted average of the primary residential PICC and the non-primary residential PICC as of January 1, 2000. This figure is estimated to increase under our current rules to \$1.46 on July 1, 2000.

<sup>127</sup> This assumes that long distance carriers eliminate PICC pass-through charges for residential customers, consistent with the commitment letters from AT&T and Sprint. See *AT&T March 30 Letter* at 2; *Sprint February 25 Letter* at 1.

currently is \$1.04 per line, and it is scheduled to increase on July 1, 2000 by \$0.50 per line, plus an amount for inflation.<sup>128</sup> The total amount of the SLC and PICC caps beginning July 1, 2000 under existing rules therefore, would be approximately \$5.06. Under the CALLS Proposal, the primary residential and single-line business SLC is capped at \$4.35 per line beginning July 1, 2000. Consequently, most subscribers with only one line could save more than \$0.70 per line under the CALLS Proposal compared to amounts they otherwise might have paid had these caps gone into effect beginning July 1, 2000. This estimate does not reflect the additional savings that result from the elimination of the blended PICC pass-through. Given that the new SLC cap will be less than the SLC and PICC caps would be under our current rules, we have a sufficient basis to find that the rates charged primary residential and single-line business customers will not be excessive and therefore unreasonable. Furthermore, because per-line CMT revenues are below the proposed caps in some areas, the average primary residential and single-line business SLC will not be as high as the cap particularly if the caps are raised in 2002 and 2003. We estimate the average primary residential SLC will be \$4.93 in July 2001, \$5.63 in July 2002, \$5.82 in July 2003, and \$5.83 after full implementation and transition of the proposal in July 2004 if the caps are fully implemented not counting voluntary reductions due to competition or any modifications to the proposed caps which might occur as a result of the cost review proceeding prior to the SLC increasing to \$5.00.<sup>129</sup> It is difficult to compare these rates with the estimated primary residential SLC and PICC rates in 2004 under our current rules because of variables beyond our control. For example, the SLC under the CALLS Proposal's proposed rules is largely unaffected by inflation, whereas the projected SLCs and PICCs under our current rules would vary widely depending on what happens with inflation over the time period. In addition, further into the future, it is more difficult to estimate what IXCs would charge as a PICC pass-through to end users, and what the X-Factor would be.

80. Similarly, the SLC cap for non-primary residential lines will be lower than the SLC cap that would otherwise apply beginning July 1, 2000. The non-primary residential SLC cap currently is \$6.07 per line and is scheduled under our current rules to increase on July 1, 2000 by \$1.00 per line, plus an amount for inflation. Additional increases to this SLC cap of \$1.00 per line plus an amount for inflation also are scheduled in subsequent years.<sup>130</sup> Under the CALLS Proposal, the non-primary residential SLC cap will be \$7.00 beginning July 1, 2000, and remain unchanged for the five-year term of the proposal.<sup>131</sup> Because the actual charges assessed on many

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<sup>128</sup> The inflation rate adjustment would result in an additional increase of approximately 2.8 per cent based upon the inflation rate during the time period specified under the Commission rules. *See* 47 C.F.R. § 69.152(k)(2).

<sup>129</sup> Our estimate is based upon publicly available data filed by the price cap LECs with their tariffs and the CALLS Proposal's projections of the sum of the primary line SLC (charged to end users) and the primary line PICC charge (charged to carriers) over the five year term of the proposal. In addition, GTE estimates that the primary residential SLC at the end of the plan will be approximately \$5.80 which is only \$0.30 more than the combined flat-rate amount that consumers could expect to pay for the SLC under existing rules beginning July 1, 2000, plus the IXC blended PICC pass-through charge IXCs could be expected to charge at that time. GTE Supp. Reply at 24.

<sup>130</sup> 47 U.S.C. § 69.152(e)(2)(ii).

<sup>131</sup> Modified Proposal at § 2.1.3.2.1.

non-primary residential lines will be below the SLC cap under either approach, these subscribers will not see additional benefits. However, the remaining subscribers will immediately benefit by saving approximately \$0.24, and on average will enjoy considerable savings in subsequent years.<sup>132</sup>

81. We find that this rate restructuring and rate decrease is in the public interest because it simplifies the current rate structure, moves towards cost-based rates, reduces consumers' overall rates, and simplifies long distance bills, thereby resulting in less consumer confusion. Similarly, simplifying the current rate structure benefits price cap LECs and IXC's by eliminating some of the complexities involved in the administration of current Commission rules and providing greater opportunities for pricing flexibility. These are all goals we have sought to achieve through our access charge reform, truth-in-billing and low-volume long distance user proceedings.<sup>133</sup>

82. We recognize that although consumers will experience considerable immediate savings, they also will see an additional line item charge on their bill when price cap LECs begin recovering Universal Service Fund contributions through an end-user charge. This charge could have been assessed regardless of the CALLS Proposal as a result of the Fifth Circuit's decision in *Texas Office of Public Utility Counsel v. FCC*.<sup>134</sup> Although the removal of the implicit subsidies from access charges to an explicit universal service support mechanism will be part of this line item charge, the increase attributed to interstate access universal service support mechanism should be offset by the decreases in other rates and charges resulting from the implementation of the CALLS Proposal.

83. As set forth in the CALLS Proposal, we shall review any increases to residential and single-line business SLC caps above \$5.00 to verify that any such increases are appropriate and reflect higher costs where they are to be applied.<sup>135</sup> We will initiate and complete a cost

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<sup>132</sup> We estimate that the non-primary residential SLC cap on July 1, 2000 under current Commission rules will be approximately \$7.24 based upon a GDP-PI of 2.8% for the 18 month period ending March 31, 2000. Because the PICC pass-through charge is currently assessed by IXC's on a per-account basis, most consumers do not pay an additional PICC for non-primary lines. For this reason, we do not take the elimination of the non-primary PICC into consideration when considering the difference between the status quo and the CALLS Proposal.

<sup>133</sup> See 1999 Price Cap FNPRM; Low-Volume Long-Distance Users NOI; Truth-in-Billing Order.

<sup>134</sup> *Texas Office of Public Utility Counsel v. FCC*, 183 F.3d 393 (5<sup>th</sup> Cir. 1999) (affirming in part the Commission's decisions regarding implementation of the high-cost universal service support system, and reversed in part the Commission's decision that incumbent LECs could recover their universal service contributions from access charges). See Section IV. C. *infra* for a discussion of the interstate access universal service support mechanism portion of the CALLS Proposal.

<sup>135</sup> We note that in other proceedings, we are considering allowing price cap LECs to adjust their depreciation rates to amortize the difference between their regulatory books and financial books through a five-year above-the-line amortization. See 1998 Biennial Review – Review of Depreciation Requirements for Incumbent Local Exchange Carriers, CC Docket 98-137, Further Notice of Proposed Rulemaking, FCC 00-119 (rel. Apr. 3, 2000) (*Depreciation Relief NPRM*). We emphasize here that any decision to permit above-the-line amortization in that docket will have no effect on the Commission's cost proceeding.

review proceeding prior to any scheduled increases above this cap taking effect to determine the appropriate SLC cap. For this proceeding, the price cap LECs have agreed to provide, and we will examine, forward-looking cost information associated with the provision of retail voice grade access to the public switched telephone network. We will address in that proceeding whether an increase in the SLC cap above \$5.00 is warranted and, if not, whether a decrease in common line charges is warranted.<sup>136</sup>

84. We disagree with CALLS opponents who argue that this cost study should occur prior to the adoption of the proposal. This proposal is good for all end users because it reduces the overall rates paid by them. Initiating and completing a cost study would take a considerable amount of time, which would delay the immediate savings end users would realize from the implementation of the proposal on July 1, 2000.<sup>137</sup> Scheduling the cost study prior to the SLC cap increasing above \$5.00 in July 2002, will enable end users to reap the immediate benefits of this proposal without the delay that would otherwise result from conducting the study beforehand. We further disagree with CALLS opponents who want the Commission today to specifically define the scope of the cost review study as well as the specific information to be examined in it. We believe that these issues are more appropriately addressed when we initiate the cost study.

85. We are not persuaded by arguments that increasing the SLC cap would violate the principle set forth in section 254(b) that consumers in all regions of the nation should have affordable access to telecommunications and information services at rates that are reasonably comparable to those services provided in urban areas.<sup>138</sup> The SLC cap was set over a decade ago and was determined to be generally affordable.<sup>139</sup> It has never been adjusted for inflation. Our rate restructuring today will result in lower overall charges than consumers experience with the current SLC and PICC, and a more efficient recovery of common line revenues through flat charges.<sup>140</sup> Furthermore, the data indicate that if the SLC cap for primary residential lines had

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<sup>136</sup> See *Wallman March 30 Letter* at 1.

<sup>137</sup> Wyoming Commission Supp. Comments at 3-4; NASUCA Supp. Comments at 5, 20; New Jersey Div. Supp. Comments at 5; Joint Consumer Commenters Supp. Comments at 15-18.

<sup>138</sup> The universal service policies of 47 U.S.C. § 254(b), among others, provide that

Consumers in all regions of the Nation, including low-income consumers and those in rural, insular, and high cost areas, should have access to telecommunications and information services, including interexchange services and advanced telecommunications and information services, that are reasonably comparable to those services provided in urban areas and that are available at rates that are reasonably comparable to rates charged for similar services in urban areas.

47 U.S.C. § 254(b)(3).

<sup>139</sup> See *Access Charge Reform Order*, 12 FCC Rcd at 16008-09.

<sup>140</sup> Carrier common line charges would have decreased more rapidly than they have to date had the SLC caps been adjusted over time for inflation. This would have resulted in a more efficient recovery of non-traffic sensitive per-line common line costs through flat charges than what has occurred to date.

been adjusted annually for inflation since it became effective in 1984, by July 2000, the \$3.50 primary residential and single-line business SLC cap that was in place in 1989 and retained in the *Access Charge Reform Order* would have increased to \$4.94 per line.<sup>141</sup> Thus, for residential customers, the primary residential SLC cap we adopt today is more affordable now than what it otherwise would have been had the \$3.50 cap we previously deemed affordable been adjusted for inflation annually.

86. Increasing the SLC cap and eliminating the PICC as proposed will, in most areas, enable the full recovery of common line revenues for residential and single-line business lines through a single charge. Although, in the past, the Commission was reluctant to increase the SLC cap, the CALLS Proposal mitigates our reluctance.<sup>142</sup> Indeed, although we established the PICC as a charge that LECs assess IXC instead of an end-user charge in order to minimize any impact on end users potentially resulting from a higher SLC, the reality in the marketplace is that IXCs have marked-up and passed-through the PICC to end users, thereby imposing higher flat charges for the majority of residential customers than would have occurred had we increased the SLC cap by the amount of the PICC caps. Even an end user who does not presubscribe to an IXC, and who pays the PICC directly to the LEC, could have been paying more in SLC and PICC on July 1, 2000, than the proposed SLC in the CALLS Proposal. Furthermore, subscribership has not been negatively impacted by these charges. Since the introduction of these charges, subscribership rates have remained relatively stable.<sup>143</sup> We are unpersuaded by the arguments therefore, that revising the rate structure as proposed will negatively impact subscribership.<sup>144</sup> Thus, in light of all of the benefits associated with the proposed restructuring of common line billing, such as the savings shown above, reductions in switched access usage rates and the interstate access universal service support mechanism of the CALLS Proposal, our prior concerns about whether increasing the SLC cap above \$3.50 would render telephone service unaffordable are sufficiently mitigated to allow an increase in the SLC.

87. We acknowledge that states are concerned about the impact the CALLS Proposal may have on intrastate access charges, due to the fact that many states require that intrastate access fees mirror interstate access charges.<sup>145</sup> We agree with the Joint Board in the *Second Recommended Decision*, that “[t]he Commission’s efforts to remove implicit universal service

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<sup>141</sup> See *Access Charge Reform Order*, 12 FCC Rcd at 16015-16. As in our *Access Charge Reform Order*, adjustments for inflation are based upon the Consumer Price Index (CPI) rather than Gross Domestic Product Price Index (GDP-PI), for comparison purposes because consumer affordability issues relate more to the CPI than to the GDP-PI.

<sup>142</sup> See *Access Charge Reform Order*, 12 FCC Rcd at 16010-11.

<sup>143</sup> See Telephone Subscribership in the United States, FCC Common Carrier Bureau, Industry Analysis Division (released January 2000).

<sup>144</sup> Joint Board Supp. Comments at 12.

<sup>145</sup> Joint Board Supp. Comments at 11.

support from interstate access charges will not affect intrastate rates directly.<sup>146</sup> We believe that the states' concern over an indirect consequence of our action today is outweighed by our efforts, consistent with the 1996 Act, to remove implicit supports from access charges. For this reason, and because the 1996 Act directs that states should take action to preserve and advance universal service,<sup>147</sup> we leave it to the individual states to adjust their rates as they deem necessary in response to this Order.

88. In addition, the CALLS Proposal will provide rate benefits for rural customers including those not served by price cap LECs.<sup>148</sup> Most IXCs currently assess a flat-rated charge to recover the PICC on all of their subscribers, including those subscribers served by rate-of-return LECs. By eliminating the PICC, we eliminate these charges from the bills of these subscribers as well. This benefit is in addition to the savings they otherwise will experience from the reductions in long distance charges resulting from the pass through by the long distance signatories of the proposed lower access charges.<sup>149</sup> Because long distance providers must offer their geographically-averaged rates to all of their customers, including those served by rate-of-return carriers,<sup>150</sup> rural customers also will benefit from reductions in per-minute rates. We also anticipate addressing access reform and universal service reform for rural carriers in the near future.<sup>151</sup>

89. Some of the proposal's critics suggest that the more appropriate competitive route to access reform is to eliminate the SLC rather than the PICC.<sup>152</sup> These parties believe that, because the long distance market is currently more competitive than the local exchange market, these charges are more likely to be competed away if assessed on IXCs. We disagree with this proposition. Because PICCs are an external cost to the IXCs that they cannot reduce by managing it better or being more efficient, PICCs are unlikely to be competed away.<sup>153</sup> Indeed, we are now into the third year of its introduction, and there is no sign that the PICC is being

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<sup>146</sup> Federal-State Joint Board on Universal Service, CC Docket No. 96-45, Second Recommended Decision, 13 FCC Rcd 24744, 24755 (1998) (*Second Recommended Decision*).

<sup>147</sup> 47 U.S.C. § 254(f); Policy and Rules Concerning the Interstate, Interexchange Marketplace, CC Docket 96-61, Report and Order, 11 FCC Rcd 9564 (1996).

<sup>148</sup> NADO Reply at 5.

<sup>149</sup> See *AT&T March 30 Letter* at 2; *Sprint February 25 Letter* at 2.

<sup>150</sup> 47 U.S.C. § 254(g).

<sup>151</sup> The Rural Task Force is scheduled to make recommendations to the Joint Board in early Fall 2000. See also Letter from David B. Cohen, Vice President – Small Company Affairs, United States Telecom Association, to Magalie Roman Salas, Secretary, FCC, March 17, 2000, CC Docket 98-77 (submitting Multi-Association Group Plan for Rate-of-Return Regulated Services).

<sup>152</sup> New Jersey Div. Comments at 11; NASUCA Comments at 33; New Jersey Div. Supp. Comments at 7-8; NASUCA Supp. Comments at 8-9, 17-18.

<sup>153</sup> GTE Supp. Reply Attachment B at 2.

competed away. Rather, we believe that one of the major benefits of recovering common line costs through the SLC alone is to encourage efficient competitive entry, particularly in providing competing alternatives for loop service.<sup>154</sup> The only way an IXC can reduce its PICC charges is by discouraging presubscription by customers that it would prefer not to serve, such as those who make few long distance calls. This type of behavior could raise issues regarding unjust, unreasonable and discriminatory practices under sections 201<sup>155</sup> and 202<sup>156</sup> of the 1996 Act. This is not a result that we would like to encourage. If common line costs are recovered in the SLC, a LEC can reduce its costs through efficiency gains and will have the incentive to avoid costs and reduce prices as it faces increased competition from competing local exchange carriers.<sup>157</sup> Further, we find that the proposed cost recovery structure will be more apparent to the end user, whereas PICCs currently are at least partially buffered against direct comparison because of the manner in which they are processed from the LEC through the IXC to the end user. Proceeding in this manner will provide greater economic incentives to stimulate alternative sources for the loop through facilities-based competition, and thus subject loop prices to competitive pressure.

90. Opponents also argue that the CALLS Proposal violates section 254(k) of the 1996 Act<sup>158</sup> for two reasons: (1) it fails to recover costs from all services that use the loop and

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<sup>154</sup> See CALLS Reply at 29.

<sup>155</sup> 47 USC § 201(b) states

All charges, practices, classifications, and regulations for and in connection with such communication service, shall be just and reasonable, any such charge, practice, classification, or regulation that is unjust or unreasonable is hereby declared to be unlawful.

47 U.S.C. § 201(b).

<sup>156</sup> 47 USC § 202(a) states

It shall be unlawful for any common carrier to make any unjust or unreasonable discrimination in charges, practices, classifications, regulations, facilities, or services for or in connection with like communication service, directly or indirectly, by any means or device, or to make or give any undue or unreasonable preference or advantage to any particular person, class of person, or locality, or to subject any particular person, class of persons, or locality to any undue or unreasonable prejudice or disadvantage.

47 U.S.C. § 202(a).

<sup>157</sup> See CALLS Supp. Reply at 17-18.

<sup>158</sup> 47 U.S.C. § 254(k) states

A telecommunications carrier may not use services that are not competitive to subsidize services that are subject to competition. The Commission, with respect to interstate services, and the States, with respect to intrastate services, shall establish any necessary cost allocations rules, accounting safeguards, and guidelines to ensure that services included in the definition of universal service bear no more than a reasonable share of the joint and common costs of facilities used to provide those services.

47 U.S.C. § 254(k).

permits the uncompensated use of the loop by IXCs; and (2) it causes services included in the definition of universal service to bear more than a reasonable share of the joint and common costs of facilities used to provide those services.<sup>159</sup>

91. We find that section 254(k) is not implicated by our action today. Section 254(k) is directed at the allocation of costs between competitive and non-competitive services, both regulated and non-regulated, and prohibits subsidization of competitive services by non-competitive services.<sup>160</sup> The SLC is a method of recovering loop costs; not an allocation of those costs between supported and unsupported services.<sup>161</sup> Contrary to the opponents' arguments, nothing in section 254(k) precludes the Commission from permitting recovery of common line charges properly apportioned to interstate access from subscribers on a flat-rated basis. Under current rules, no PICC or CCL charges are paid by IXCs with respect to non-primary residential and multi-line business lines after the phase-in specified in the *Access Charge Reform Order* is completed. Similarly, for primary residential lines that are not presubscribed to an IXC, there is no common line recovery from IXCs in those places where the CCL charge has been phased out.

92. Moreover, section 254(k) addresses the concern that price cap LECs may attempt to gain an unfair market advantage in competitive markets by allocating to their less competitive services, for which subscribers have no available alternative, an excessive portion of the costs incurred by their competitive operations.<sup>162</sup> Whether a LEC allocates all of its interstate loop costs to the end user or to the IXC, the LEC's competitive position as compared to other suppliers of local exchange facilities remains the same. Section 254(k) was not designed to regulate the apportionment of loop costs between end users and IXCs because this allocation does not involve improperly shifting costs from a competitive to non-competitive service.<sup>163</sup>

93. Consequently, we agree with the CALLS proponents that there is no legal impediment to a federal recovery mechanism that simply requires all telephone subscribers to pay, on a per-line basis, for that portion of their *necessarily-incurred local telephone plant costs* that is assigned to the interstate jurisdiction.<sup>164</sup> Section 254(k) does not apply to the question of

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<sup>159</sup> *E.g.*, Smithville Comments at 5; NASUCA Comments at 20-22; Washington Commission Comments at 9-10; California Commission Comments at 11; Joint Consumer Commenters Reply at 3-5; New Jersey Div. Comments at 7-8; Michigan Commission Supp. Comments at 3; Montana Commission Supp. Comments at 3; Wisconsin Commission Supp. Comments at 5-7; Joint Board Supp. Comments at 9-10; Joint Consumer Commenters Supp. Comments at 4, 26, 37-38; NASUCA Supp. Comments at 6, 21-22.

<sup>160</sup> 47 U.S.C. § 254(k); *see* Implementation of Section 254(k) of the Communications Act of 1934, as Amended, 12 FCC Rcd 6415, 6419 (1997) (*Section 254(k) Order*).

<sup>161</sup> *See Southwestern Bell Telephone v. Federal Communications Commission*, 153 F.3d 523, 559 (8<sup>th</sup> Cir. 1998).

<sup>162</sup> *Section 254(k) Order*, 12 FCC Rcd at 6419-20.

<sup>163</sup> *See Southwestern Bell v. FCC*, 153 F.3d at 559.

<sup>164</sup> *See* CALLS Reply at 27; *see also* NARUC v. FCC, 737 F.2d at 1115.

whether prices should be set through SLCs alone or through a combination of SLCs and PICCs. Neither the PICC nor the CCL charge is legally compelled by section 254(k) or any other provision of law.

94. Indeed, these arguments have already been addressed and rejected by the United States Court of Appeals for the Eighth Circuit.<sup>165</sup> In *Southwestern Bell v. FCC*, the Texas Office of Public Utility Counsel argued, among other things, that the Commission's decision in the *Access Charge Reform Order* to increase the SLC cap for certain lines resulted in a "free ride by the IXCs on the common line facilities" and that loop costs were being shifted from competitive services to basic services, contrary to the intent of section 254(k) of the 1996 Act. Texas Counsel argued that as a result of section 254(k), the recovery of joint and common costs, such as NTS loop costs, must be borne mutually both by end users and by IXCs. Texas Counsel asserted that it was improper for the Commission to shift additional NTS loop cost recovery from the access rates LECs charge IXCs for interstate access onto the rates end users pay for certain telephone lines.<sup>166</sup> Texas Counsel contended that increasing the SLC cap imposed on end users allowed IXCs to evade their fair share of the common line costs.<sup>167</sup> Texas Counsel maintained that this approach violated section 254(k) "in that the existing proportion of NTS loop cost recovery by the IXCs through competitive services would be reduced through increases on end users for basic services."<sup>168</sup>

95. The Eighth Circuit upheld the Commission's increases to various LEC SLC caps, however, and found that "Texas Counsel's contention that increasing the SLC price ceiling violates the prohibition against using non-competitive services to subsidize competitive services [wa]s unpersuasive."<sup>169</sup> In doing so, the court reaffirmed the Commission's long standing view that the subscriber "causes" local loop costs, whether the subscriber uses the service for intrastate or interstate calls. These costs are, in any event, recovered from the end user, either through direct end-user charges or indirectly through higher rates or additional charges paid to IXCs. The court further affirmed the Commission's conclusion that it was appropriate and rational for the Commission to impose these costs on the end user. The court concluded as a result that increasing SLC caps on certain lines did not result in a windfall for IXCs.<sup>170</sup>

96. Similarly, the court in *Southwestern Bell* rejected the argument that increasing the SLC cap violates the second sentence of section 254(k) by causing services included in the definition of universal service to bear more than a reasonable share of the joint and common costs

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<sup>165</sup> See *Southwestern Bell v. FCC*, 153 F.3d at 559.

<sup>166</sup> See *Southwestern Bell v. FCC*, 153 F.3d at 559.

<sup>167</sup> See *Southwestern Bell v. FCC*, 153 F.3d at 559.

<sup>168</sup> See *Southwestern Bell v. FCC*, 153 F.3d at 558-59.

<sup>169</sup> See *Southwestern Bell v. FCC*, 153 F.3d at 559.

<sup>170</sup> See *Southwestern Bell v. FCC*, 153 F.3d at 558.

of facilities used to provide those services. The second provision of section 254(k) separates telecommunications services into those that are supported by universal service, and those that are not.<sup>171</sup> This provision empowers the Commission to establish rules to prevent LECs from overallocating to supported services the costs of facilities that are used to provide services in both categories. It places a continuing obligation on the Commission to ensure that the treatment of joint and common costs, such as corporate overheads, prescribed by our accounting, cost allocation, separations, and access charge rules will safeguard the availability of universal service.<sup>172</sup> Opponents argue that by eliminating the PICC and increasing the SLC cap, the Commission violates section 254(k) by allocating 100 per cent of the joint and common costs to the common line elements paid by the end user. The Commission, however, has complied with the requirements of section 254(k) by allocating joint and common costs to various interstate services, including those that are supported by universal service, such as common line and switching, and those that are not, such as special access services.<sup>173</sup> The Commission also has in place a comprehensive system of accounting and non-accounting safeguards designed to discourage carriers from misallocating the costs of non-regulated activities, and to ensure that ratepayers share in any efficiencies generated from joint use of the network by non-regulated activities.<sup>174</sup> None of the proposal's critics challenge these safeguards as insufficient or flawed, or our allocation as improper. Because the SLC is a method of recovering properly allocated loop costs, not an allocation of those costs between supported and unsupported services, section 254(k) is not implicated.<sup>175</sup>

97. Moreover, the SLC and PICC were established to recover loop costs for the same service – interexchange access. Interexchange access is a supported service as defined in the *Universal Service First Report and Order*.<sup>176</sup> Therefore, contrary to the arguments of opponents,

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<sup>171</sup> 47 U.S.C. § 254(k); see *Southwestern Bell v. FCC*, 153 F.3d at 559.

<sup>172</sup> *Section 254(k) Order*, 12 FCC Rcd at 6420.

<sup>173</sup> See, e.g., 47 C.F.R. §§ 69.401-414.

<sup>174</sup> See, e.g., Regulatory and Policy Problems Presented by the Interdependence of Computer and Communications Services and Facilities, Tentative Decision, 28 FCC 2d 291 (1970); Final Decision and Order, 28 FCC 2d 267 (1971), *aff'd sub. nom. GTE Services Corp. v. FCC*, 474 F.2d 724 (2d Cir. 1973); *decision on remand*, 40 FCC 2d 293 (1973); Amendment of Section 64.702 of the Commission's Rules and Regulations, 77 FCC 2d 384 (1980), *recon.* 84 FCC 2d 50 (1980), *further recon.* 88 FCC 2d 512 (1981), *aff'd sub nom. Computer and Communications Industry Ass'n v. FCC*, 693 F.2d 198 (D.C. Cir. 1982), *cert. denied*, 461 U.S. 938 (1983); Policy and Rules Concerning Rates for Competitive Carrier Services and Facilities Authorizations Thereof, CC Docket No. 79-252, Fifth Report and Order, 98 FCC 2d 1191 (1984); Separation of Costs of Regulated Telephone Service from Costs of Nonregulated Activities, Amendment of Part 31, the Uniform System of Accounts for Class A and Class B Telephone Companies, CC Docket No. 86-111, Report and Order, 2 FCC Rcd 1298 (1987) (*Joint Cost Order*), *recon.* 2 FCC Rcd 6283 (1987), *further recon.* 3 FCC Rcd 6701 (1988), *aff'd sub nom. Southwestern Bell Corp. v. FCC*, 896 F.2d 1378 (D.C. Cir. 1990).

<sup>175</sup> See *Southwestern Bell v. FCC*, 153 F.3d at 559.

<sup>176</sup> *Universal Service First Report and Order*, 12 FCC Rcd at 8807.

moving the recovery of loop costs associated with interexchange access service from the PICC to the SLC is not a change in the allocation between supported and unsupported service.

98. We also reject the argument that elimination of the PICC is inconsistent with the *Line Sharing Order*.<sup>177</sup> The *Line Sharing Order* concluded that states should not permit incumbent LECs to charge more to competitive LECs for access to shared local loops than the amount of loop costs the incumbent LEC allocated to ADSL services when it established its interstate retail rates for those services.<sup>178</sup> To date, we are not aware of any incumbent LECs that have allocated any loop costs to ADSL services.

99. Many of the proposal's critics also erroneously argue that the consolidation of the SLC and PICC violates the requirements for reasonable recovery of shared costs as interpreted by *Smith v. Illinois Bell*.<sup>179</sup> We find no requirement anywhere that we are required to prescribe the recovery of properly allocated common line costs from IXCs rather than in the cost causative manner that we follow. In making their arguments, the opponents misinterpret and confuse the issues in *Smith v. Illinois Bell*. Indeed, their arguments have already been addressed and rejected in *NARUC v. FCC*. Specifically, in *NARUC v. FCC*, the D.C. Circuit held that *Smith v. Illinois Bell* dealt with jurisdiction and that a portion of the costs of local subscriber plant may be recovered only under the authority of a body with interstate regulatory powers.<sup>180</sup> The D.C. Circuit further held that *Smith v. Illinois* did not address the manner in which the Commission was to perform this task.<sup>181</sup> The court specifically found that *Smith v. Illinois Bell* did not compel the Commission to use a particular formula to recover costs allocated to its jurisdiction.<sup>182</sup> Rather, the Commission may properly order recovery, through charges imposed on telephone subscribers, of the portion of the local loop costs, that, in accordance with *Smith v. Illinois*, have been placed in the interstate jurisdiction.<sup>183</sup> Contrary to the arguments of many opponents, therefore, *Smith v. Illinois Bell* does not preclude our action today as the common line costs in question have been properly allocated by the Commission.

100. In this Order, we also permit price cap LECs to eliminate over time the distinction between primary and non-primary residential lines. Under the revised proposal, this distinction

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<sup>177</sup> NASUCA Supp. Comments at 7; Deployment of Wireline Services Offering Advanced Telecommunications Capability, CC Docket 98-147, Third Report and Order, 14 FCC Rcd 20912 (1999) (*Line Sharing Order*).

<sup>178</sup> *Line Sharing Order*, 14 FCC Rcd at 20976.

<sup>179</sup> NASUCA Comments at 19-22; Joint Consumer Commenters Comments at 16-18; NRTA/NTCA Comments at 9-10; *see also Smith v. Illinois Bell*, 282 U.S. 133.

<sup>180</sup> *See NARUC v. FCC*, 737 F.3d at 1112.

<sup>181</sup> *See NARUC v. FCC*, 737 F.3d at 1112.

<sup>182</sup> *See NARUC v. FCC*, 737 F.3d at 1112; *see also Rural Telephone Coalition v. Federal Communications Commission*, 838 F.2d 1307, 1314 (D.C. Cir. 1988).

<sup>183</sup> *See NARUC v. FCC*, 737 F.3d at 1114.

can be eliminated in most circumstances, but will remain for those subscribers where the average CMT revenue exceeds the maximum proposed SLC cap for primary residential lines.<sup>184</sup> This will go a long way to eliminate the consumer confusion that now exists relating to this distinction. Although the primary/non-primary line distinction has served a role during the transitional regulatory process we established, we agree that eliminating this distinction to the extent that we can will further simplify the current rate structure and eliminate the costs associated with administering this distinction, which are ultimately borne by consumers.

101. We also eliminate the Marketing Basket in this Order. We established this basket in our *Access Charge Reform Order* to prevent price cap LECs from recovering retail marketing expenses from carrier access services, and to ensure that the recovery of these expenses was directed at multi-line users rather than primary residential and single-line business users. Under current Commission rules, the marketing expenses allocated to the Marketing Basket are recovered through common line charges.<sup>185</sup> Under the CALLS Proposal, these marketing expenses are included in the total revenue a price cap LEC is permitted to recover as Price Cap CMT Revenue.<sup>186</sup>

102. We adopt the CALLS Proposal with respect to its treatment of marketing expenses. In doing so, we expand the common line elements from which these expenses can be recovered to include the primary residential and single-line business SLC. In the *Access Charge Reform Order* we prevented the recovery of marketing expenses from primary residential and single-line business SLCs and PICCs because we believed that price cap LEC retail marketing may have focused more on the sale of optional vertical features such as call waiting and caller ID, and on features and services designed for business customers.<sup>187</sup> At the time, there was insufficient evidence in the record demonstrating that price cap LECs marketed to primary residential and single-line business subscribers. As a result, we determined that the most efficient and cost-causative method for recovering these expenses was from the end users to whom the price cap LECs' marketing was directed – multi-line business and non-primary residential line end users.<sup>188</sup> We therefore limited recovery of these expenses to the non-primary residential and multi-line business common line elements in the common line basket.<sup>189</sup> In addition, by proceeding in

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<sup>184</sup> We estimate that by July 2004, the distinction can be eliminated for approximately two-thirds of all non-primary lines.

<sup>185</sup> 47 C.F.R. § 69.156. Marketing expenses can be recovered from multi-line business and non-primary residential SLCs, then multi-line business and non-primary residential PICCs, then CCL charges.

<sup>186</sup> Modified Proposal at § 2.1.1.1.

<sup>187</sup> See *Access Charge Reform Order*, 12 FCC Rcd at 16121.

<sup>188</sup> See *Access Charge Reform Order*, 12 FCC Rcd at 16122.

<sup>189</sup> See *Access Charge Reform Order*, 12 FCC Rcd at 16122.

this manner, we avoided potential universal service concerns relating to increasing the primary residential SLC.<sup>190</sup>

103. Since the adoption of the *Access Charge Reform Order*, evidence has developed which demonstrates that price cap LECs incur marketing expenses relating to primary residential and single-line business services as well.<sup>191</sup> Consequently, consistent with the cost-causative approach we adhered to in the *Access Charge Reform Order*, we now permit the recovery of these expenses from all elements in the common line basket, including the primary residential and single-line business SLC.

104. This change will have little, if any, impact on subscribers, given the existence of the SLC caps, the elimination of the primary and non-primary residential PICCs, and the distribution of these expenses across a larger subscriber base. In light of the integrated nature of the CALLS Proposal and the considerable benefits resulting from the simplification of and overall rate reductions in the common line basket, the reductions to the switched access usage charges, and the implementation of the interstate access universal service support mechanism, our prior universal service concerns relating to increasing the primary residential and single-line business SLC cap above \$3.50 are allayed. The overall effect of the proposal is to lower costs for consumers. Eliminating this basket also promotes efficiency and streamlines the process by which a participating price cap LEC recovers its marketing expenses, while at the same time reducing the administrative costs associated with maintaining and managing this basket.

#### **b. Multi-line Business SLC and PICC**

105. We also cap the multi-line business PICC at \$4.31 and reduce it over time until it is eliminated as provided for in the CALLS Proposal. Under the CALLS Proposal, the multi-line business PICC in virtually all areas is eliminated over the next several years or can be eliminated through voluntary reductions in order to permit deaveraging. Several critics of this aspect of the proposal assert that the multi-line business PICC and SLC should be consolidated, eliminated or reduced further, and that it should be billed directly from the price cap LECs to subscribers to avoid any mark-up by IXC.<sup>192</sup> We believe for the following reasons, however, that the restructuring of the multi-line business PICC proposed in the CALLS Proposal is the better approach at this time.

106. The multi-line business PICC was established to recover revenue that would otherwise be recoverable through charges on residential and single-line business lines, and not to

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<sup>190</sup> See *Access Charge Reform Order*, 12 FCC Rcd at 16122.

<sup>191</sup> See Letter from Anthony M. Alessi, Director, Federal Relations, Ameritech, to William F. Caton, Acting Secretary, Federal Communications Commission, September 11, 1997, CC Docket No. 96-262; Letter from Frank G. Kennedy, Director, Legal and Regulatory Affairs, United States Telephone Association, to William F. Caton, Acting Secretary, Federal Communications Commission, September 29, 1997, CC Docket No. 96-262.

<sup>192</sup> GSA Comments at 7-9; Pathfinder Comments at 5; Ad Hoc Supp. Comments at 8-10; U S WEST Supp. Comments at 5, 10-12; TRA Supp. Comments at 2, 4-7; MCI Supp. Comments at 29.

recover the cost of serving multi-line business lines. For most price cap LECs, a SLC of \$9.00 or less fully recovers average per line permitted revenues, and the multi-line business PICC represents a subsidy running from business long-distance users to residential users. Under current rules, this subsidy is to be phased out over time pursuant to the *Access Charge Reform Order* as price cap LECs are eventually able to recover their full per-line common line revenues from each line through the SLC and PICC. Under the CALLS Proposal, this subsidy also is to be phased out over time although not as quickly as it would be under our current rules. Because of rate averaging by IXCs, the overall effect of this subsidy mechanism is spread out over a large number of multi-line business subscribers which permits this subsidy to remain sustainable until we are able to reevaluate this rate structure at the end of the five year period covered by the CALLS Proposal. At the time the multi-line business PICC was established, the Commission determined that it was a reasonable measure to avoid an adverse impact on universal service and residential customers. Maintaining this transitional mechanism continues to be a reasonable measure to avoid an adverse impact on universal service and residential customers, and is the better approach in establishing a more efficient interstate access charge rate structure consistent with our long-term universal service goals in a competitive local exchange environment.

107. We reject the opponents' arguments that the multi-line business PICC should be consolidated with the multi-line business SLC or recovered differently,<sup>193</sup> because doing so would exaggerate the difference between business end-user charges in high cost and low cost areas and impact rate comparability between urban and rural areas. In addition, combining the multi-line business SLC and multi-line business PICC would place price cap LECs at a competitive disadvantage with competitive LECs. The multi-line business SLC is intended to recover a price cap LEC's interstate portion of local loop costs for multi-line business services, while the multi-line business PICC is intended to subsidize the price cap LEC's interstate portion of local loop costs for residential service. Competitive LECs are not regulated by the Commission and are not restricted in the same manner as price cap LECs in how they recover their costs. A combined SLC and PICC, therefore, could exceed a competitive LEC's rate that recovers its loop costs, even where the SLC alone would be less than a competitive LEC's loop cost recovery mechanism. Because the multi-line business PICC is a subsidy, this could encourage inefficient entry by competitors.

108. We also recognize, however, allegations that IXCs mark-up the multi-line business PICC well above the average rate. These commenters argue that merging the multi-line business SLC and PICC would make it subject to competitive pressures, forcing price cap LECs to lower their multi-line PICC charges to stay competitive with competitive LECs.<sup>194</sup> We are troubled by these mark-up allegations and remind carriers of our statutory authority to investigate any charges that appear unreasonable or unlawful.<sup>195</sup> We will not hesitate to take action on a case-by-case

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<sup>193</sup> Ad Hoc Supp. Comments at 8-9; TRA Supp. Comments at 8.

<sup>194</sup> Ad Hoc Supp. Comments at 8-10.

<sup>195</sup> See 47 U.S.C. §§ 204-205. See also *Interexchange Carrier End-User Charges to Recover Universal Service Contributions*, CC Docket No. 99-324, Suspension Order, 14 FCC Rcd 20032.

basis against carriers that impose unjust or unreasonable line item charges.<sup>196</sup> We are hopeful, however, that the mandatory detariffing of IXC charges that recently took effect will increase the competitive pressure on IXCs to bring their multi-line business PICC pass-through closer to the average multi-line business PICC.

109. Although we will not merge the multi-line business SLC and PICC at this juncture, we will revisit this issue during the cost review proceeding scheduled to occur before the residential and single-line business SLC cap increases above \$5.00. At that time, we will be better able to evaluate the long-term impact of the multi-line business PICC and competition in the IXC market.

110. In addition, the timeframe for eliminating the multi-line business PICC for most subscribers under the CALLS Proposal generally is consistent with the current timeframe under which the multi-line business PICC would be eliminated for most subscribers. For example, we estimate that by July 2004, the multi-line business PICC will be eliminated under current rules for all RBOCs whereas it will be eliminated under the proposal for all RBOCs except for BellSouth, which would have a multi-line business PICC at that time of approximately \$0.20 per line.<sup>197</sup> We also estimate that the multi-line business PICC for GTE, Sprint and some other price cap LECs will remain in some areas where it might otherwise have been eliminated under existing rules. Multi-line business PICCs also can be immediately eliminated through voluntary reductions in order to deaverage SLCs as described below. Consequently, we reject the suggestion that the proposal should be modified to accelerate the elimination of the multi-line business PICC.<sup>198</sup>

111. We recognize that the continued existence of the multi-line business PICC in some areas may constitute an implicit non-portable subsidy.<sup>199</sup> As the Eighth Circuit held in reviewing our *Access Charge Reform Order*, however, this does not violate section 254.<sup>200</sup> In our *Access Charge Reform Order*, we created the multi-line business PICC as an interim mechanism for price cap LECs to recover permitted common line revenues they were otherwise unable to recover because of the SLC and PICC caps on primary residential and single-line business lines.<sup>201</sup> Although our action today affects the cap at which the multi-line business PICC can be assessed, it does not alter the interim nature of this mechanism nor the underlying reason why we established it. The Eighth Circuit upheld this rate structure as a reasonable solution to the “implicit tension between the [Commission’s] goals of moving toward cost-based rates and

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<sup>196</sup> See 47 U.S.C. § 201(b). See also *Truth-in-Billing Order*.

<sup>197</sup> Our estimates are based upon applying our current rules and the CALLS Proposal’s proposed rules to publicly available data.

<sup>198</sup> MCI Supp. Comments at 29.

<sup>199</sup> See, e.g., Ad Hoc Supp. Reply at 5.

<sup>200</sup> See *Southwestern Bell v. FCC*, 153 F.3d at 537-38.

<sup>201</sup> See *Access Charge Reform Order*, 12 FCC Rcd at 16022.

protecting universal service.”<sup>202</sup> More importantly, the CALLS Proposal phases out the multi-line business PICC for most customers until it is eliminated.<sup>203</sup> At the end of the five year term, we will examine to what extent competition and voluntary reductions have further eliminated it, and to the extent that they have not we will consider additional measures to address those areas. Although this proposal does not eliminate transitional higher rates for business users, it generally maintains the rate structure we established in our *Access Charge Reform Order* for the reasons stated therein, of redistributing recovery from a very few high-volume users to business users in general.<sup>204</sup> The CALLS Proposal will continue to permit the charges to be sustainable during our transition to a more economically rational approach to access charges and universal service.<sup>205</sup> We find that this aspect of the proposal is a reasonable measure in moving toward cost-based rates and protecting universal service.

112. We agree that freezing and eventually reducing the current combined level of multi-line business PICCs and SLCs further reduces the distortions in the current rate structure. This in turn reduces the likelihood that competitive LECs and incumbent LECs will target their investments towards urban business customers due to artificial regulatory incentives, and to a greater extent than would be required by economic efficiency. Consequently, we expect a greater proportion of competitive LEC investment in rural and residential urban areas as a result of these actions.<sup>206</sup>

### c. SLC Deaveraging

113. We also modify our rules today to permit deaveraging of the SLC in the limited manner outlined in the CALLS Proposal. Granting price cap LECs more flexibility to deaverage these rates enhances the efficiency of the local telephone market by allowing prices to be tailored more easily and accurately to reflect costs and, therefore, promotes competition in both urban and rural areas. In addition, deaveraging SLCs will have the effect of reducing implicit subsidies that otherwise exist under the current rate structure.

114. Geographic deaveraging refers to charging different rates in different zones to reflect the relative costs of providing service in each zone. Since 1992, the Commission has permitted incumbent 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 subscribers

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<sup>202</sup> See *Southwestern Bell v. FCC*, 153 F.3d at 538.

<sup>203</sup> See Modified Proposal at § 2.1.6.

<sup>204</sup> See *Access Charge Reform Order*, 12 FCC Rcd at 16023-24.

<sup>205</sup> See *Access Charge Reform Order*, 12 FCC Rcd at 16023-24.

<sup>206</sup> See Robert W. Crandall and Jeffrey H. Rohlfs, *The Economic Case for the CALLS Proposal*, December 3, 1999.

of the benefits of more vigorous competition.<sup>207</sup> We also have ordered the deaveraging of the rates for interconnection and unbundled elements,<sup>208</sup> and permitted deaveraging of rates for trunking services as well.<sup>209</sup> In doing so, we found that deaveraging reduces implicit support inherent in some rates and helps promote competition in both low-cost and high-cost areas whereas averaging across large geographic areas may distort 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 services.<sup>210</sup> We found that deaveraged rates more closely reflect the actual cost of providing service, which promotes competition and efficiency by allowing a LEC to compete for subscribers when it is the lowest cost service provider, and by removing support flows to the LEC's higher-cost services.<sup>211</sup> 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.<sup>212</sup> 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.<sup>213</sup> These findings and conclusions clearly support the proposed limited deaveraging of SLCs.

115. We agree with the CALLS proponents that permitting deaveraging of the SLC under the proposed limited conditions and safeguards substantially reduces the implicit support of rural rates by urban ratepayers, and is a critical step in the development of increased competition in rural areas and the preservation of universal service.<sup>214</sup> Integrating SLC deaveraging with

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<sup>207</sup> 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 (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); 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*).

<sup>208</sup> Interconnection Between Local Exchange Carriers and Commercial Mobile Radio Service Providers, 11 FCC Rcd 15499 (1996); *Iowa Utilities Board v. FCC*, 96 F. 3d 1116 (8<sup>th</sup> Cir. 1996) (*per curiam*); *see also Iowa Utilities Board v. FCC*, 109 F.3d 418 (8<sup>th</sup> Cir. 1996); *Iowa Utilities Board v. FCC*, 120 F.3d 753 (8<sup>th</sup> Cir. 1997), *rev'd in part and aff'd in part*, *AT&T v. Iowa Utilities Board*, 119 S.Ct. 721 (1999), *on remand* Implementation of the Local Competition Provisions of the Telecommunications Act of 1996, 14 FCC Rcd 8300 (1999).

<sup>209</sup> *Pricing Flexibility Order*, 14 FCC Rcd at 14249-51.

<sup>210</sup> *Access Charge Reform Order*, 11 FCC Rcd at 21434; *Pricing Flexibility Order*, 14 FCC Rcd at 14253-54.

<sup>211</sup> *Special Access Expanded Interconnection Order*, 7 FCC Rcd at 7454.

<sup>212</sup> *Access Charge Reform Order*, 11 FCC Rcd at 21434; *Pricing Flexibility Order*, 14 FCC Rcd at 14253-54.

<sup>213</sup> *Access Charge Reform Order*, 11 FCC Rcd at 21434; *Pricing Flexibility Order*, 14 FCC Rcd at 14253-54.

<sup>214</sup> *CALLS NPRM*, 14 FCC Rcd at 16969-70; *see also, e.g.,* ALTS Comments at 7-8; USTA Comments at 2; Western Wireless Comments at 5; Time-Warner Comments at 2; Intermedia Reply at 4-5; GTE Reply at 16; U S WEST Comments at 2-6 (safeguards should be simplified); USTA Supp. Comments at 5; Global Crossing Supp. Comments at 3-4..

explicit universal service support and deaveraged UNE loop rates strengthens both rural and urban competition, and ensures affordable rates.<sup>215</sup> We are satisfied that by capping SLCs at affordable levels and limiting SLC deaveraging to a maximum of four zones as proposed,<sup>216</sup> we satisfy the statutory principle that rates in rural, insular, and high cost areas remain “reasonably comparable” to those in urban areas.<sup>217</sup> Indeed, this action is consistent with our prior findings that three zones are presumptively sufficient to reflect geographic cost differences in setting rates for interconnection and unbundled elements.<sup>218</sup> We also are satisfied that the interstate access universal service support mechanism established under CALLS is designed to ensure that subscribers in all areas of the country pay rates that are affordable and reasonably comparable.

116. Opponents of deaveraging SLCs contend that doing so complicates the administration of the SLC and potentially violates the section 254(b) principle that rates should be affordable and reasonably comparable between rural and urban areas.<sup>219</sup> Opponents also argue that deaveraging makes it difficult for long-distance companies to maintain geographically averaged rates as required by section 254(g). They argue that section 254(g) is intended to incorporate the policies of geographic rate averaging and rate integration of interexchange services in order to ensure that all subscribers in rural and high cost areas are able to continue to receive both intrastate and interstate interexchange services at rates no higher than those paid by urban subscribers.<sup>220</sup> In their view, permitting SLC deaveraging evades the 1996 Act’s geographic averaging mandate by shifting the interstate loop costs out of the IXCs’ long-distance rates and into deaveraged SLCs to be collected from the price cap LEC’s customers, rather than as averaged PICC pass-through charges imposed on the IXCs’ presubscribed customers.<sup>221</sup>

117. Opponents further argue that section 254(g) does not provide any exception for interstate interexchange access service provided to end users on a flat-rated basis. In their view, once the SLC is deaveraged, no rural end user in price cap LECs’ service areas will be able to receive interstate interexchange services without paying more than an urban user because of the

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<sup>215</sup> *CALLS NPRM*, 14 FCC Rcd at 16969-70.

<sup>216</sup> *CALLS NPRM*, 14 FCC Rcd at 16972.

<sup>217</sup> 47 U.S.C. § 254(b)(3).

<sup>218</sup> Implementation of the Local Competition Provisions in the Telecommunications Act of 1996, CC Docket No. 96-98, First Report and Order, 11 FCC Rcd 15499, 15882 (1996) (*Local Competition Order*). States could establish more than three zones where cost differences in geographic regions are such that it finds that additional zones are needed to adequately reflect the costs of providing service. *Local Competition Order*, 11 FCC Rcd at 15882.

<sup>219</sup> Joint Consumer Commenters Supp. Comments at 40; NRTA/NTCA Supp. Reply at 9; Joint Board Supp. Comments at 12. In response to the *Pricing Flexibility Order* FNPRM, many commenters also argue that common line costs should not be deaveraged prior to certain prerequisites having been met in a study area.

<sup>220</sup> NRTA/NTCA Comments at 5; Joint Board Supp. Comments at 13.

<sup>221</sup> NRTA/NTCA Comments at 9.

higher access costs in rural areas.<sup>222</sup> In support of their position, they point out that the Commission previously recognized in the *Access Charge Reform Order* that letting the IXCs pass the PICCs through to their customers on a deaveraged basis might conflict with section 254(g) and “create a substantial risk that many subscribers in rural and high-cost areas may be charged significantly more than subscribers in other areas.”<sup>223</sup> They argue that the Commission’s same analysis should prevail over any effort to achieve the deaveraging indirectly by manipulation of the cost recovery responsibility, the name of the charge, or the identity of who must pay for it.<sup>224</sup>

118. We are unpersuaded by the arguments that section 254(g) applies to SLCs charged by incumbent LECs. Moreover, we disagree with the arguments that (1) the SLC, as set forth under the CALLS Proposal, represents a “rate” charged by an interexchange service provider within the meaning of section 254(g) because IXCs benefit from the SLC payment,<sup>225</sup> and (2) the SLC is a “rate” of a subscriber’s LEC which remains a charge for interstate interexchange service because it facilitates access to the service.<sup>226</sup> The statutory rate integration requirement applies on its face only to rates charged by providers of “interexchange telecommunications services to subscribers,” not to providers of interexchange access service.<sup>227</sup> SLCs, which are charged by LECs, do not fall within the statutory standard.<sup>228</sup> As described above, the SLC is a LEC charge designed to recover the cost of the interstate portion of facilities that subscribers use jointly to connect to the telephone network for the purpose of making and receiving both local and interexchange calls. Therefore, the SLC is not a “rate” charged by IXCs to subscribers within the meaning of Section 254(g).

119. Moreover, we believe that interpreting this provision in the manner suggested by these commenters goes beyond what Congress intended when it incorporated geographic rate averaging and integration policies into section 254(g). These policies apply only to interexchange service, not to exchange access whether paid by the carrier or the end user.<sup>229</sup> SLCs, which are charged by LECs, do not fall within the statutory standard.<sup>230</sup> Indeed, our view is consistent with the current system wherein multi-line business SLCs vary from one price cap LEC to another and, even within a single LEC or LEC holding company, from study area to study area, with a low of

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<sup>222</sup> NRTA/NTCA Comments at 6.

<sup>223</sup> NRTA/NCTA Comments at 6-7; *see also Access Charge Reform Order*, 12 FCC Rcd at 16022.

<sup>224</sup> NRTA/NTCA Comments at 6-7; New Jersey Div. Comments at 16-18.

<sup>225</sup> Vermont Dept. Reply at 16-17.

<sup>226</sup> Vermont Dept. Reply at 17.

<sup>227</sup> 47 U.S.C. 254(g); *see* CALLS Reply at 28; NADO Reply at 5.

<sup>228</sup> NADO Reply at 5.

<sup>229</sup> CALLS Reply at 28; NADO Reply at 5.

<sup>230</sup> NADO Reply at 5.

\$3.77 to a high of \$9.20.<sup>231</sup> More specifically, Bell Atlantic has for many years assessed a residential SLC in the District of Columbia that is lower than the residential SLCs it charges in some other states because of the lower average cost in the District of Columbia. These SLCs varied before the enactment of the 1996 Act and the adoption of the *Access Charge Reform Order*.<sup>232</sup> Despite this occurrence, Congress did not suggest that section 254(g) was applicable to SLCs, nor has there ever been any suggestion that this variation in price cap LEC SLC rates from high cost areas to low cost areas violated section 254(g), or that Section 254(g) was intended to address that situation.

120. In addition, the CALLS Proposal, contrary to some arguments, does not shift IXC costs to LEC customers. Allowing the recovery of common line costs through a single end-user charge billed directly from a price cap LEC to an end user does not “evade” section 254(g) by shifting the interstate loop costs out of IXCs’ long distance rates and into deaveraged SLCs. As we have maintained, loop costs are incurred by LECs, not IXCs. The District of Columbia Circuit in *NARUC v. FCC* upheld our finding that “[l]ocal telephone plant costs are real; they are necessarily incurred for each subscriber by virtue of that subscriber’s interconnection into the local network, and they must be recovered regardless of how many or how few interstate calls (or local calls for that matter) a subscriber makes.”<sup>233</sup> Therefore, requiring price cap LECs to bill their own customers for a cost they are in fact required by law to incur - because use of the loop is a mandatory component of universal service - is not an end-run around the statute. The proposal does not shift IXC costs to price cap LEC customers. The fact that CCL charges and the recently created PICC have resulted in some of these costs being passed on to IXCs (and subsequently recovered through end-user pass-through charges) does not forever transform loop costs into an IXC cost.<sup>234</sup> These costs are, in fact, LEC costs, regardless whether they are recovered directly from end users or recovered indirectly through IXC payments that are then passed onto end users.

121. In addition, we are unpersuaded by the arguments that our previous decision not to forbear from applying section 254(g) to the recovery of IXC costs through the PICC pass-through charges precludes us from permitting the deaveraging of SLCs by LECs.<sup>235</sup> Our decision at that time was in response to some IXCs’ requests for the Commission to forbear from applying section 254(g) to the recovery of their PICC costs through charges to end users.<sup>236</sup> At that time, the IXCs offered nothing in support of their request other than that the action was necessary in response to LECs’ recovery of NTS common line costs through deaveraged rates assessed on

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<sup>231</sup> See, e.g., Bell Atlantic Tariff No. 1, Section 4.1.7 and Bell Atlantic Tariff No. 11, Section 31.4.1.

<sup>232</sup> Under the prior system, these SLCs were capped at \$6.00.

<sup>233</sup> See *NARUC v. FCC*, 737 F.2d at 1113-14.

<sup>234</sup> See CALLS Reply at 28-29.

<sup>235</sup> NRTA/NCTA Comments at 6-7; New Jersey Div. Comments at 16-18; see also *Access Charge Reform Order*, 12 FCC Rcd at 16022.

<sup>236</sup> See *Access Charge Reform Order*, 12 FCC Rcd at 16021-22.

IXCs.<sup>237</sup> We concluded that they failed to demonstrate in the record that they met the forbearance test set forth in Section 10(a) of the 1996 Act, and denied their request.<sup>238</sup> That finding is irrelevant to a determination that a charge not covered by section 254(g) should be allowed to be deaveraged.

122. We also find no basis in this record to conclude that interexchange rates under the CALLS Proposal would be higher for rural than urban customers. Indeed, we believe that eliminating the geographic disparity of the PICC will make IXC costs more uniform, and thus make complying with section 254(g) less difficult for IXCs.<sup>239</sup> For example, price cap LEC PICC assessments range from \$0 to \$4.31, resulting in geographic disparity for IXCs which recover the PICC through charges to end users on an averaged basis, even in areas where PICCs are not assessed on them.

123. We also are unpersuaded by the arguments of some opponents that the SLC deaveraging provisions of the CALLS Proposal conflict with the reasonable rate comparability principle of section 254(b)(3) of the 1996 Act.<sup>240</sup> On the contrary, the CALLS Proposal's SLC deaveraging provisions are consistent with our interpretation of section 254(b)(3). As we concluded in the *Universal Service Seventh Report and Order*, the "reasonably comparable" rate provisions of section 254(b)(3) were intended as a national, as opposed to a state-by-state, comparison.<sup>241</sup> This standard refers to "a fair range of urban/rural rates both within a state's

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<sup>237</sup> See *Access Charge Reform Order*, 12 FCC Rcd at 16022.

<sup>238</sup> 47 USC § 10(a) states

[T]he Commission shall forbear from applying any regulation or any provision of this Act to a telecommunications carrier or telecommunications services, in any or some of its or their geographic markets, if the Commission determines that –

(1) enforcement of such regulation or provision is not necessary to ensure that the charges, practices, classifications, or regulations by, for, or in connection with that telecommunications carrier or telecommunications service are just and reasonable and are not unjustly or unreasonably discriminatory;

(2) enforcement of such regulation or provision is not necessary for the protection of consumers; and

(3) forbearance from applying such provision or regulation is consistent with the public interest.

47 U.S.C. § 10 (a). The Commission concluded that the information in the record at the time did not demonstrate that it was required by section 10(a) of the 1996 Act to forbear from applying section 254(g) as it relates to the manner in which IXCs recover their costs. See *Access Charge Reform Order*, 12 FCC Rcd at 16022.

<sup>239</sup> CALLS Reply at 29; Smithfield Comments at 2.

<sup>240</sup> NRTA/NTCA Comments at 11; Florida Commission Comments at 6-8; Vermont Dept. Reply at 14-15.

<sup>241</sup> *Universal Service Seventh Report and Order*, 14 FCC Rcd at 8094.

borders, and among states nationwide.”<sup>242</sup> This does not mean that rate levels in all states, or in every area of every state, must be the same.<sup>243</sup> As the local exchange market becomes more competitive, we believe that it would be unreasonable to expect rate levels not to vary to reflect the varying costs of serving different areas.<sup>244</sup> Therefore, the goal of maintaining a “fair range” of rates means that support levels must be sufficient to prevent pressure from high costs in certain areas and the development of competition from causing unreasonable increases in rates in the high cost areas above affordable levels.<sup>245</sup>

124. Section 254(b)(3) permits the use of federal support to enable reasonable rate comparability among states. The approach for enabling rate comparability which we previously adopted relies not on a national urban rate, but rather on a methodology that ensures that no state will face per-line costs that substantially exceed the costs faced by other states, taking into account the individual state’s ability to support its own universal service needs. In this way, we seek to ensure that every state has at its disposal the means to achieve reasonable comparability of rates in that state.<sup>246</sup>

125. The CALLS Proposal is consistent with our interpretation of section 254(b)(3) and satisfies the requirements of the statute. It protects high-cost subscribers by providing that no SLC, whether averaged or deaveraged, may exceed the overall proposed SLC caps. Although prices will begin to reflect geographic variations in the forward-looking cost of providing service, newly explicit universal service support will protect rural subscribers against substantial rate increases. This approach is consistent with prior actions we have taken in furtherance of our universal service goals. For example, we previously capped SLC adjustments as a means of preventing end users in high-cost areas from paying SLCs that are significantly higher than in other parts of the country in order to ensure that all subscribers receive affordable rates that are comparable in different parts of the nation.<sup>247</sup> The CALLS Proposal’s SLC cap is consistent with this approach, and ensures that end users in high-cost areas do not pay SLCs that are significantly higher than in low-cost areas.

126. We also believe that the Lifeline and Universal Service Fund aspects of the CALLS Proposal address to some extent concerns about potential rate increases to high-cost customers as a result of the geographic deaveraging aspects of the proposal.<sup>248</sup> Under the CALLS Proposal, Lifeline support will be increased so that all of the increased SLC is waived for Lifeline

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<sup>242</sup> *Universal Service Seventh Report and Order*, 14 FCC Rcd at 8092.

<sup>243</sup> *Universal Service Seventh Report and Order*, 14 FCC Rcd at 8092.

<sup>244</sup> *Universal Service Seventh Report and Order*, 14 FCC Rcd at 8092.

<sup>245</sup> *Universal Service Seventh Report and Order*, 14 FCC Rcd at 8092.

<sup>246</sup> *Universal Service Seventh Report and Order*, 14 FCC Rcd at 8094.

<sup>247</sup> *Access Charge Reform Order*, 12 FCC Rcd at 16013.

<sup>248</sup> See Section IV. C. *infra*.

customers, with carriers reimbursed from the Universal Service Fund. Although Lifeline customers today pay no SLC, they must pay IXC-billed PICC charges, unless the IXC voluntarily waives that fee. The CALLS Proposal therefore benefits Lifeline customers by eliminating the PICCs and by ensuring that their fixed monthly charges do not increase in the future.

127. We disagree with the argument that deaveraged UNEs should be the sole trigger for deaveraging, and that the remaining proposed safeguards should be eliminated.<sup>249</sup> As in the case of the trunking basket and the deaveraging provisions in our *Pricing Flexibility Order*, the proposed safeguards generally reflect minimum revenue requirements for pricing zones and limits on price increases that are simple and easily verified. These limitations also generally are consistent with the comments filed by some CALLS opponents on this issue in response to the Further Notice of Proposed Rulemaking in the *Pricing Flexibility Order*.<sup>250</sup> We find therefore, that the public interest benefits associated with maintaining the proposed safeguards outweigh the benefits that might accrue from deaveraging occurring sooner than what might otherwise occur without these simple and easily verified safeguards. The proposal provides an incentive to LECs to deaverage voluntarily other than through offset free from the limitations of the proposed safeguards. The proposed safeguards ensure that the deaveraging of SLCs maintains affordable rural rates while developing competition and preserving universal service. Not permitting deaveraging unless a state has created geographically deaveraged UNE rates for loops ensures that deaveraging will not inadvertently hamper UNE-based entry or LEC competitive response.<sup>251</sup>

128. There is no cost causative way to deaverage multi-line business PICCs and CCL charges because they are subsidies. Requiring multi-line business PICCs and CCL charges to be eliminated before permitting SLC deaveraging helps ensure that the burdens of implicit support are spread evenly. To the extent that implicit support is included in the multi-line business SLC rates above what results from geographic averaging, allowing geographic deaveraging of the multi-line business SLC before the multi-line business PICC and CCL charges are eliminated would allow carriers to deaverage that implicit support and impose a greater burden on those multi-line business customers with fewer competitive options. By the time the multi-line business PICC and CCL charges are eliminated, however, implicit subsidies in the multi-line business SLC other than those resulting from geographic averaging should be reduced, and geographic deaveraging of the multi-line business SLC to reduce the subsidies resulting from averaging is appropriate. Also, by requiring that the multi-line business SLC not be lower than the non-primary residential SLC, or the non-primary residential SLC not be lower than the primary residential and single-line business SLC, the CALLS Proposal ensures that all consumers in low cost areas share the benefits of SLC deaveraging.<sup>252</sup>

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<sup>249</sup> U S WEST Supp. Comments at 12-13.

<sup>250</sup> See U S West Comments, CC Docket No. 96-262 at 3-5 (Oct. 29, 1999).

<sup>251</sup> CALLS NPRM, 14 FCC Rcd at 16971.

<sup>252</sup> CALLS NPRM, 14 FCC Rcd at 16971.

## B. Local Switching, Trunking, and Special Access Baskets

### 1. Background

#### a. Rate Structure

129. 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.<sup>253</sup> For example, a rate structure that recovers non-traffic sensitive costs through traffic sensitive access rates increases the per-minute rates paid by IXC's 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 serving them. Meanwhile, low-volume customers pay rates that are less than the cost of the dedicated equipment.<sup>254</sup>

130. To recover the costs of providing interstate access services, incumbent LECs charge IXC's and end users for access services in accordance with our Part 69 access charge rules.<sup>255</sup> Part 69 establishes two basic categories of access services: special access services and switched access services. Special access services generally employ dedicated facilities that run directly between the end user and the IXC's point of presence (POP), or between a LEC's switch and an IXC's POP.<sup>256</sup> 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 for special access services in Part 69.<sup>257</sup> For switched access, Part 69 establishes specific elements and a mandatory rate structure for each element.<sup>258</sup>

131. 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 (the serving wire center (SWC))

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<sup>253</sup> *Access Charge Reform Order*, 12 FCC Rcd at 15995-96, 15998; Investigation of Interstate Access Tariff Non-Recurring Charges, CC Docket No. 85-166, Memorandum Opinion and Order, 2 FCC Rcd 3498, 3501-02 (1987).

<sup>254</sup> See *Access Charge Reform Order*, 12 FCC Rcd at 15996, 16008.

<sup>255</sup> 47 C.F.R. Part 69.

<sup>256</sup> A POP is the physical point where an IXC connects its network with the LEC network.

<sup>257</sup> *Access Charge Reform*, CC Docket No. 96-262, Notice of Proposed Rulemaking, 11 FCC Rcd 21354, 21367 (1996) (*Access Charge Reform NPRM*).

<sup>258</sup> *Access Charge Reform NPRM*, 11 FCC Rcd at 21367.

are known as entrance facilities.<sup>259</sup> 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.<sup>260</sup> 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.<sup>261</sup> 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.

132. 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.<sup>262</sup> In the *Second Transport Order*, the Commission removed transport services from the traffic sensitive basket and combined these services with special access services in the newly created trunking basket.<sup>263</sup> 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.<sup>264</sup> The PCI is adjusted annually by a measure of inflation minus a "productivity factor," or "X-factor."<sup>265</sup> A separate adjustment is

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<sup>259</sup> See 47 C.F.R. § 69.110 (requiring LECs to impose flat-rated charges on IXCs to recover the costs of entrance facilities).

<sup>260</sup> 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).

<sup>261</sup> 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 SWC 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).

<sup>262</sup> *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.*

<sup>263</sup> Transport Rate Structure and Pricing, CC Docket No. 91-213, Second Report and Order, 9 FCC Rcd 615, 622 (1994) (*Second Transport Order*). Additionally, in the *Access Charge Reform Order*, the Commission determined that, "consistent with principles of cost-causation and economic efficiency, [non-traffic sensitive] NTS costs associated with local switching should be recovered on a flat-rated, rather than usage sensitive, basis. Accordingly, for price-cap LECs, [the Commission] reassign[ed] all line side port costs from the Local Switching rate element to the Common Line rate elements." *Access Charge Reform Order*, 12 FCC Rcd at 16035. See also Section IV.A.1 *supra*.

<sup>264</sup> *LEC Price Cap Order*, 5 FCC Rcd at 6788.

<sup>265</sup> *Price Cap Second FNPRM*, 11 FCC Rcd at 863. For a complete discussion of the "X-Factor," see Price Cap Performance Review for Local Exchange Carriers, CC Docket No. 94-1, First Report and Order, 10 FCC Rcd (continued....)

made to the PCI for “exogenous” cost changes, which are changes outside the carrier’s control not otherwise reflected in the price cap formula.<sup>266</sup>

133. In the *First Transport Order*, the Commission restructured interstate transport rates for incumbent LECs.<sup>267</sup> The restructuring created facility-based rates for dedicated transport services based on comparable special access rates as of September 1, 1991, derived per-minute tandem-switched transport transmission rates from those dedicated transport rates, established a tandem switching rate, and established a transport interconnection charge (TIC) that initially recovered the difference between the revenues from the new facility-based rates and the revenues that would have been realized under the preexisting “equal charge rule.”<sup>268</sup> The TIC was intended as a transitional measure that initially made the transport rate restructure revenue neutral for incumbent LECs and reduced any harmful interim effects on small IXCs caused by the restructuring of transport rates.<sup>269</sup> The Commission, however, subsequently determined that as a per-minute charge assessed on all switched access minutes, the TIC adversely affected the development of competition in the interstate access market.<sup>270</sup> Therefore, the Commission reassigned several costs included in the TIC and established a mechanism that virtually eliminated the remaining per-minute TIC over a short, but reasonable period, primarily by targeting X-factor reductions to the per-minute TIC.<sup>271</sup>

134. In the *Access Charge Reform Order*, the Commission instituted reforms so that access costs are recovered in a manner that more accurately reflects how they are incurred. Recognizing that a significant portion of local switching costs, (i.e., the costs associated with line

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8961, 9005-06 (1995) (*1995 Price Cap Review Order*); see also *1997 Price Cap Review Order*, 12 FCC Rcd at 16642.

<sup>266</sup> *LEC Price Cap Order*, 5 FCC Rcd at 6792, 6807. Exogenous costs are those triggered by administrative, legislative, or judicial action beyond the carriers’ control. These costs are created by such events as: the expiration of amortizations; changes in the Uniform System of Accounts; separations changes; changes in universal service fund obligations; the reallocation of regulated and nonregulated costs; tax law changes; retargeting the PCI for price cap carriers taking advantage of the low-end adjustment mechanism; inside wire amortizations; and the completion of amortization of equal access expenses. 47 C.F.R. § 61.45(d)(1).

<sup>267</sup> *Transport Rate Structure and Pricing*, CC Docket No. 91-213, Report and Order, 7 FCC Rcd 7006 (1992) (*First Transport Order*).

<sup>268</sup> *First Transport Order*, 7 FCC Rcd at 7009-10, 7029. Under the equal charge rule, which arose from the AT&T divestiture of the BOCs, the BOCs were required to charge a per-minute, distance sensitive rate for their transport offerings, regardless of how the underlying costs were incurred.

<sup>269</sup> *First Transport Order*, 7 FCC Rcd at 7038-42.

<sup>270</sup> *Access Charge Reform Order*, 12 FCC Rcd at 16073.

<sup>271</sup> *Access Charge Reform Order*, 12 FCC Rcd at 16073-86. At present only GTE still retains a per-minute TIC.

cards and trunk ports)<sup>272</sup> do not vary with usage, the Commission required that such non-traffic sensitive costs be recovered on a flat-rated, rather than usage sensitive basis.<sup>273</sup> Because the record was not adequate, however, to determine whether and to what extent the remaining switching costs were traffic sensitive or non-traffic sensitive, LECs continue to recover these costs through traffic sensitive charges. As part of the *Pricing Flexibility Order*, the Commission invited comment on whether and to what extent it should modify further its price cap rules for the traffic sensitive and trunking baskets to reflect capacity-based local switching and tandem switching rate structures.<sup>274</sup> Also in the *Pricing Flexibility Order*, the Commission proposed adding a “q” factor to the formulas used to adjust annually the PCIs for the baskets that contain the charges for local switching and tandem switching.<sup>275</sup> The q factor would reduce switching charges based on growth in demand.<sup>276</sup> As proposed, the PCIs of the affected baskets would be reduced annually by both the X-factor and the q factor.

**b. The X-Factor**

**(i) Prior Commission Decisions and Pending Proposals**

135. The Commission’s LEC price cap scheme allows prices to increase by a measure of inflation minus a productivity offset, or X-factor.<sup>277</sup> In the Commission’s LEC price cap formula, the X-factor represents the amount by which LECs can be expected to outperform economy-wide productivity gains.<sup>278</sup> The X-factor adopted in the *LEC Price Cap Order* initiating price cap regulation for the largest LECs consisted of a component based on historical LEC productivity, and an additional productivity obligation of 0.5 percent as a consumer productivity dividend (CPD) to assign the first productivity gains to customers in the form of lower rates.<sup>279</sup>

136. Initially, price cap LECs were required to share a portion of their earnings in excess of specified rates of return with their access customers by temporarily reducing the price

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<sup>272</sup> Line cards connect subscriber lines to the switch, and trunk ports connect interoffice trunks to the switch. *Access Charge Reform Order*, 12 FCC Rcd at 16034.

<sup>273</sup> *Access Charge Reform Order*, 12 FCC Rcd at 16034.

<sup>274</sup> *Pricing Flexibility Order*, 14 FCC Rcd at 14327-33.

<sup>275</sup> *Pricing Flexibility Order*, 14 FCC Rcd at 14330-31, 14333.

<sup>276</sup> The q factor would operate as a mechanism to allocate revenue between price cap LECs and IXC, similar to the g factor present in the common line PCI formula. See *Pricing Flexibility Order*, 14 FCC Rcd at 14330-31. The g factor is used to share with IXCs the benefits of demand growth that LECs receive from per-minute growth per access line. *LEC Price Cap Order*, 5 FCC Rcd at 6794.

<sup>277</sup> Rules governing price cap LECs are set forth in Part 61 of our rules. 47 C.F.R. Part 61.

<sup>278</sup> *LEC Price Cap Order*, 5 FCC Rcd at 6796.

<sup>279</sup> *LEC Price Cap Order*, 5 FCC Rcd at 6796.

cap ceiling in a subsequent period.<sup>280</sup> In 1990, the Commission prescribed two X-factors: a minimum 3.3 percent X-factor, and an optional 4.3 percent X-factor.<sup>281</sup> Price cap LECs that opted to use the higher X-factor were allowed to retain larger shares of their earnings. Additionally, the Commission adopted a low-end adjustment mechanism for LECs with earnings below a specified threshold.<sup>282</sup> The *LEC Price Cap Order* required that the Commission periodically review the performance of the price cap regime.<sup>283</sup> The order in the first performance review was released in 1995, at which time the Commission increased the minimum X-factor from 3.3 percent to 4.0 percent, and provided two optional X-factors of 4.7 and 5.3 percent.<sup>284</sup> In the next performance review order, released in 1997, the Commission further revised the price cap plan by eliminating all sharing requirements and prescribing a new X-factor of 6.5 percent.<sup>285</sup> This X-factor prescription relied primarily on a staff study (1997 Staff TFP Study) of the historical rate of growth in LEC total factor productivity (TFP).<sup>286</sup> The Commission also retained the low-end adjustment mechanism for incumbent LECs with earnings below a specified threshold in the *1997 Price Cap Review Order*.<sup>287</sup>

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<sup>280</sup> The price cap sharing requirement established three sharing zones determined by specified rate of return levels. In the first “no-sharing zone,” price cap LECs were allowed to keep all of their earnings up to the first rate of return ceiling. Above that ceiling, in the “50-50 sharing zone,” price cap LECs were entitled to retain 50 percent of their earnings and were required to return 50 percent of their earnings to ratepayers up to the second ceiling. Price cap LECs were required to return 100 percent of any earnings above the “50-50 sharing zone” ceiling to ratepayers. *LEC Price Cap Order*, 5 FCC Rcd at 6801.

<sup>281</sup> *LEC Price Cap Order*, 5 FCC Rcd at 6787. These amounts included the CPD.

<sup>282</sup> The low-end adjustment mechanism 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 allow them to earn 10.25 percent. *LEC Price Cap Order*, 5 FCC Rcd at 6804; *1997 Price Cap Review Order*, 12 FCC Rcd at 16691. In the *Pricing Flexibility Order*, the Commission eliminated the low-end adjustment for price cap LECs that qualify for and elect to exercise either Phase I or Phase II pricing flexibility. *Pricing Flexibility Order*, 14 FCC Rcd at 14304.

<sup>283</sup> *LEC Price Cap Order*, 5 FCC Rcd at 6789.

<sup>284</sup> *1995 Price Cap Review Order*, 10 FCC Rcd at 9055-56. These amounts included a 0.5 percent CPD. No sharing obligations were imposed on LECs that chose the 5.3 percent option.

<sup>285</sup> *1997 Price Cap Review Order*, 12 FCC Rcd at 16645.

<sup>286</sup> *1997 Price Cap Review Order*, 12 FCC Rcd at 16645. TFP measurement is a methodology commonly used to measure productivity and productivity growth in the economy as a whole. Productivity is measured as the ratio of an index of the outputs of a firm (or industry, or nation) to an index of its inputs. Productivity growth is measured by changes in this ratio over time. The 1997 Staff TFP Study calculated the historical difference in productivity growth between LECs and the economy nationwide for the period 1986 through 1995. Specifically, it calculated the difference between LEC TFP change and economy-wide TFP change. The study then calculated an input price differential reflecting the difference in the rate of change of LEC input prices as compared with the economy as a whole. These two factors were then added together for each year.

<sup>287</sup> *1997 Price Cap Review Order*, 12 FCC Rcd at 16649.

137. In the *Pricing Flexibility Order*, the Commission tentatively concluded that it should measure inflation in the PCI formula with a chain-weighted GDP-PI, which bases weights for the current year's index on the prior year.<sup>288</sup> The Commission reasoned that it should change from the "Fixed Weight Price Index for Gross Domestic Product, 1987 Weights" to a chain-weighted GDP-PI to be consistent with the U.S. Department of Commerce's Bureau of Economic Analysis (BEA) inflation measure and with that used in setting the X-factor.<sup>289</sup> The Commission sought comment on its tentative conclusion.<sup>290</sup>

## (ii) Court Decision

138. Several entities filed petitions for review of the *1997 Price Cap Review Order* with the U.S. Court of Appeals for the District of Columbia Circuit (D.C. Circuit). In its decision on appeal, the court reversed and remanded for further explanation the Commission's decision to select an X-factor of 6.5 percent, although it affirmed the order against petitioners' remaining challenges.<sup>291</sup> The court rejected the Commission's stated rationales for selecting 6.0 percent as the historical component of the X-factor. In particular, the court rejected the Commission's reasons for placing less weight on the lowest averages of productivity growth used to establish the range of reasonableness of 5.2 to 6.3 percent.<sup>292</sup> The court also found that the Commission failed to explain adequately its reliance on an apparent upward trend in productivity growth for the period 1992-1995 in choosing 6.0 percent from this range, as well as its reliance on AT&T's productivity estimates to extend the range of reasonableness upward.<sup>293</sup> In addition, the court remanded for explanation the Commission's choice of 0.5 percent as a CPD component of the X-factor.<sup>294</sup> The court withheld issuance of its mandate, pending the Commission's reconsideration of the X-factor, through June 30, 2000.<sup>295</sup>

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<sup>288</sup> *Pricing Flexibility Order*, 14 FCC Rcd at 14338.

<sup>289</sup> Although the *Pricing Flexibility Order* states that the Bureau of Labor Statistics (BLS) measures inflation with a chain-weighted GDP-PI, the inflationary measure is actually created by the BEA. *Pricing Flexibility Order*, 14 FCC Rcd at 14338.

<sup>290</sup> *Pricing Flexibility Order*, 14 FCC Rcd at 14338.

<sup>291</sup> *USTA v. FCC*, 188 F.3d at 521, 530 (D.C. Cir. 1999).

<sup>292</sup> *Id.* at 525-26.

<sup>293</sup> *Id.* at 526.

<sup>294</sup> *Id.* at 527.

<sup>295</sup> See *USTA v. FCC*, Order, No. 97-1469 *et al.* (June 21, 1999); *USTA v. FCC*, Order, No. 97-1469 *et al.* (Apr. 13, 2000).

**(iii) Resulting Commission Price Cap FNPRM**

139. Following the Court's decision in *USTA v. FCC*, the Commission commenced a rulemaking seeking comment on alternative bases for prescribing the X-factor.<sup>296</sup> The *1999 Price Cap FNPRM* was released after CALLS filed its Original Proposal. In the *1999 Price Cap FNPRM*, the Commission noted that adoption of the CALLS Proposal would eliminate the need to adjust the X-factor retrospectively in response to the court's remand, or prescribe an X-factor on a going-forward basis.<sup>297</sup> In response to the *1999 Price Cap FNPRM*, commenters proposed X-factor amounts ranging from 3.71 percent<sup>298</sup> to 11.2 percent.<sup>299</sup>

**c. The CALLS Proposal**

140. The X-factor would serve a different function under the CALLS Proposal than in the original price cap plan. Instead of representing an estimate of expected annual productivity gains, the X-factor under the CALLS Proposal would be used to reduce local switching and switched transport rates to specified target rate levels, and to reduce special access rates over a set period of time.<sup>300</sup> The proposal thus transforms the X-factor from a productivity factor into a transitional mechanism that operates to reduce rates at a certain pace, and it would not be linked to a specific measure of productivity.

141. Under the original price cap regime, the X-factor would continue indefinitely, subject to periodic performance reviews. X-factor reductions were applied to each price cap basket on a pro rata basis, except for the period of time during which those reductions were targeted to eliminate the per-minute TIC. The CALLS Proposal would alter both of these principles. First, the CALLS Proposal includes two X-factors: one for switched access services, and a separate X-factor for special access services. After predetermined rates are reached, the switched access X-factor would be adjusted to GDP-PI. The special access X-factor would also eventually be adjusted to GDP-PI on July 1, 2004. Because the price cap formula is adjusted by GDP-PI minus the X-factor, setting the X-factor at GDP-PI would effectively freeze the price caps for the remainder of the term of the CALLS Proposal. Second, under the CALLS Proposal, the switched access X-factor reductions would be targeted to the trunking and traffic-sensitive baskets. This means that total switched access revenues would be used to calculate the size of the X-factor reduction, but the actual reductions would only be made to revenues in the trunking and traffic-sensitive baskets. This would cause rates in the targeted baskets to decrease more rapidly

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<sup>296</sup> *1999 Price Cap FNPRM*, 14 FCC Rcd at 19718.

<sup>297</sup> *1999 Price Cap FNPRM*, 14 FCC Rcd at 19718.

<sup>298</sup> See USTA Reply, CC Docket No. 94-1 at 13 (Jan. 24, 2000).

<sup>299</sup> See AT&T Comments, CC Docket No. 94-1 at 12-15, 20 (Jan. 7, 2000) (arguing that the historical component of the X-factor should have been 10.1 percent during the period 1997-2000, and the CPD should have been 1.1 percent during the period 1997-2000 and going forward).

<sup>300</sup> *CALLS NPRM*, 14 FCC Rcd at 16984-85; Modified Proposal at §§ 3.2.2 and 3.2.7; Appendix B § 61.45(b)(1).

and significantly, while rates in the untargeted baskets to which the X-factor would not be applied would remain largely unchanged.

142. CALLS proposes to target a 6.5 percent X-factor for switched access services to the following rates in this sequence: first to the residual per-minute TIC until that rate is \$0.00; then to the information surcharge until that rate is \$0.00;<sup>301</sup> and finally to the local switching charge and switched transport charges until the carrier's interstate average traffic sensitive charge equals a specified target rate.<sup>302</sup> CALLS proposes a multi-tier target rate system for interstate average traffic sensitive charges, with a target rate of 0.55 cents for the BOCs and GTE, and a target rate of 0.65 cents for other price cap LECs.<sup>303</sup> A further modification of the CALLS Proposal submitted by CALLS and VALOR Telecommunications Company proposes a third target rate of 0.95 cents for entirely rural price cap LECs.<sup>304</sup>

143. CALLS proposes that where a price cap LEC sells a filing entity or portion of a filing entity to another price cap LEC during the term of the CALLS Proposal, the sold filing entity would retain its pre-existing target rate. Two exceptions to this rule exist. First, if a filing entity sold during the term of the CALLS Proposal is merged with a filing entity with a different target rate, the target rate for the merged filing entity would be a weighted average of the combined target rates. Second, if a binding and executed contract existed for the sale of a filing entity on April 1, 2000, the target rate for the filing entity would be the greater of the applicable target rate of the acquiring company, or the target rate under the previous owner.<sup>305</sup> CALLS proposes that price cap LECs account for the differing target rates of filing entities under contract of sale in their tariff review plans (TRPs). Selling price cap LECs would file TRPs on June 16,

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<sup>301</sup> The "information surcharge" is a rate element by which carriers recover the costs of white pages directory expenses. It applies to all interstate access switched minutes of use. *See* Petitions for Waiver Concerning 1985 Annual Access Tariff Filings, Memorandum Opinion and Order, Mimeo No. 5007 (Com. Car. Bur., June 7, 1985).

<sup>302</sup> Modified Proposal at § 3.2.2; *CALLS NPRM*, 14 FCC Rcd at 16989-90; Appendix B § 61.45(i)(2). The "average traffic sensitive charge" is the sum of the local switching component and the transport component. The local switching component will be calculated by dividing the proposed local switching revenues (end office switch, local switching trunk ports, information surcharge, and STP port) by the base period local switching minutes of use. The transport component will be calculated by dividing the proposed transport revenues (switched direct trunk transport, signaling for switched direct trunk transport, entrance facilities for switched access traffic, tandem switched transport, signaling for tandem switching and TIC) by incumbent LEC-only base period transport minutes of use (including meet-point billing arrangements for jointly-provided interstate access by an incumbent LEC and any other LEC). Appendix B § 61.3(e).

<sup>303</sup> Modified Proposal at §§ 3.1.2 and 3.1.3; *CALLS NPRM*, 14 FCC Rcd at 16985; Appendix B § 61.3(qq).

<sup>304</sup> *See VALOR April 14 Letter*. The 0.95-cent target rate would be available to price cap LECs with a holding company average of less than 19 End User Common Line charge lines per square mile served. Appendix B § 61.3(qq)(2).

<sup>305</sup> *VALOR April 14 Letter*; Appendix B § 61.48(o).

2000 that reflected the target rates of the filing entities after they are acquired by the purchasing price cap LEC.<sup>306</sup>

144. For switching and switched transport services, CALLS proposes to apply an X-factor of 6.5 percent until the interstate average traffic sensitive charge target rate is reached. After carriers with target rates of 0.55 cents or 0.65 cents reach these targets, the annual X-factor for baskets except special access would equal GDP-PI. Setting the X-factor at GDP-PI would effectively freeze the price caps for the services comprising switched access services.<sup>307</sup> For primarily rural carriers electing the 0.95-cent target rate, the 6.5 percent X-factor would continue to apply after the target rate is reached and would be applied to the common line basket to reduce CCL charges.<sup>308</sup> Upon the earlier of the elimination of the CCL charges or June 30, 2004, the X-factor for the primarily rural carriers would equal inflation.<sup>309</sup> The CALLS Proposal offered contingencies in the case that GDP-PI is greater than 6.5 percent or less than zero after an entity has eliminated its CCL and multi-line business PICC charges. If the GDP-PI is greater than 6.5 percent, the X-factor for common line would equal 6.5 percent and all SLC rates and nominal caps on SLC rates would be increased by the difference between GDP-PI and the X-factor. If GDP-PI is less than zero, the X-factor for common line would be zero.<sup>310</sup>

145. Under the CALLS Proposal, price cap LECs would agree to waive the low-end adjustment to interstate access rates for rates charged during the tariff year beginning on July 1, 2000, but not for subsequent years.<sup>311</sup> CALLS members also would agree not to initiate legal or regulatory action to adjust price cap determined rates for interstate access charges billed for access minutes prior to July 1, 2000.<sup>312</sup>

146. CALLS also proposes that price cap LECs would reduce switched access usage charges by an aggregate amount of \$2.1 billion on July 1, 2000.<sup>313</sup> The switched access usage charges to be reduced would include average traffic sensitive charges and CCL charges, but would exclude SLCs and PICCs.<sup>314</sup> The switched access usage charge reductions would be

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<sup>306</sup> Letter from John T. Nakahata, Counsel to CALLS, to Magalie R. Salas, Secretary, FCC, May 25, 2000.

<sup>307</sup> Modified Proposal at § 3.2; *CALLS NPRM*, 14 FCC Rcd at 16988; Appendix B § 61.45(b)(1)(ii).

<sup>308</sup> *VALOR April 14 Letter*; Appendix B § 61.45(i)(4).

<sup>309</sup> *VALOR April 14 Letter*; Appendix B § 61.45(b)(1)(iii)(B).

<sup>310</sup> Modified Proposal at § 3.2.3; Appendix B § 61.45(b)(1)(iii)(A).

<sup>311</sup> Modified Proposal at § 4.4; Appendix B § 61.45(d)(1)(vii).

<sup>312</sup> However, payees may accept, and payors may not resist any refunds ordered by the Commission. Modified Proposal at § 4.3; *CALLS April 28 Letter*.

<sup>313</sup> Modified Proposal at § 3.2.4. The reductions necessary to achieve this amount are calculated under Appendix B § 61.48(l).

<sup>314</sup> Modified Proposal at § 3.2.4; Appendix B § 61.48(l).

accomplished through: 1) the targeting of the 6.5 percent X-factor to switching and switched transport services until the applicable average traffic sensitive charge rates are reached;<sup>315</sup> 2) reductions in CCL charges through application of \$650 million of explicit interstate access universal service support;<sup>316</sup> 3) reductions in CCL charges through application of increased SLCs;<sup>317</sup> and 4) reductions in CCL charges from application of a 6.5 percent X-factor to the common line basket for primarily rural carriers after they reach the average traffic sensitive charge rate of 0.95 cents.<sup>318</sup> If these reductions do not total \$2.1 billion, price cap LECs will make additional reductions to switched access usage charges to make up the difference. These additional reductions would be calculated as a percentage of the local switching element of the price cap LECs, who could take these reductions against any of the average traffic sensitive charge rate elements.<sup>319</sup> Most price cap LECs would not offset these additional reductions by increasing other rate elements. Two mutually exclusive alternatives, however, are proposed to permit certain carriers to move some of these permitted revenues to the common line basket.<sup>320</sup>

147. The first alternative is available to price cap carriers other than the BOCs and GTE that have at least 20 percent of total holding company lines operated by rural telephone companies. These carriers may elect to redistribute to the common line basket the additional reductions to average traffic sensitive charge rates necessary to yield their proportionate share of the total reduction in switched access usage rates.<sup>321</sup> Eligibility for this option is determined at the holding company level, and the amounts to be shifted to the common line basket are determined at the filing entity level. Specifically, eligible companies' non-rural filing entities may shift the amount of additional reductions that exceed 25 percent of local switching element revenues.<sup>322</sup> The predominantly rural filing entities of the eligible price cap LECs may shift the entire proportionate amount of the additional reductions attributable to those filing entities.<sup>323</sup> To the

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<sup>315</sup> Modified Proposal at § 3.2; *VALOR April 14 Letter*; Appendix B § 61.48(l)(17)(ii)(A).

<sup>316</sup> Modified Proposal at §§ 2.1.6; Appendix B § 61.48(l)(17)(i)(A) and (B).

<sup>317</sup> Modified Proposal at § 2.1.6; Appendix B § 61.48(l)(17)(i)(C).

<sup>318</sup> *VALOR April 14 Letter*; Appendix B § 61.45(b)(1)(iii)(B).

<sup>319</sup> Modified Proposal at § 3.2.4; Appendix B § 61.48(l)(18).

<sup>320</sup> Modified Proposal at §§ 3.2.4.1 and 3.2.4.2; Appendix B § 61.48(m).

<sup>321</sup> Modified Proposal at § 3.2.4.1; Appendix B § 61.48(m)(1)(ii).

<sup>322</sup> Non-rural filing entities are those within which more than 50 percent of all lines are operated by telephone companies other than those that as of December 31, 1999 were certified by the holding company as rural. *See Universal Service First Report and Order*, 12 FCC Rcd at 8943-44; Self-Certification as a Rural Telephone Company, Public Notice, 12 FCC Rcd 12093 (1997) (*Rural Certification Public Notice*). Modified Proposal at § 3.2.4.1(i); Letter from John T. Nakahata, Counsel to CALLS, to Jack Zinman, Legal Counsel, FCC, May 25, 2000 at 3; Appendix B § 61.48(m)(1)(ii)(A).

<sup>323</sup> Predominantly rural filing entities are those with greater than 50 percent of lines operated by telephone companies that as of December 31, 1999 were certified by the holding company as rural. *See Universal Service* (continued....)

extent the eligible carrier cannot recover all of these revenues within the filing entity, it may recover these amounts from multi-line business PICC and multi-line business SLC charges of other filing entities within the same holding company, provided that they do not exceed the established caps for these charges.<sup>324</sup> This alternative affects only those rate reductions above and beyond the reductions that result from the operation of the existing price cap rules. Price cap LECs qualifying for this alternative still will make their normal price cap rate reductions. These carriers also will implement the additional switched access rate reductions called for by the CALLS Proposal. This mechanism will be evaluated in the proposed cost review proceeding to determine whether retaining it is warranted.

148. The second option is available to any price cap company that would have July 1, 2000 price cap reductions at the holding company level greater than the industry-wide total July 1, 2000 price cap reductions.<sup>325</sup> These price cap carriers may elect temporarily to shift to the common line basket the amount of the additional reductions above 25 percent of the local switching element revenues necessary to yield their proportionate share of the total reduction in switched access usage rates on July 1, 2000. These carriers may then recover the amounts as additional components of a multi-line business SLC or PICC within the same filing entity. A 6.5 percent X-factor will be applied to the shifted amounts, even after the carriers reach their interstate average traffic sensitive target rates, until the shifted amounts are eliminated.<sup>326</sup>

149. CALLS also would create a separate special access basket.<sup>327</sup> Under the CALLS Proposal the revenues in the special access basket would not be included in the targeting of the X-factor reductions to the switched access usage charges. Instead, the services in the special access basket would be subject to their own X-factor. The special access X-factor would be set at 3.0 percent in 2000, and would be set at 6.5 percent for each of the next three years. After 2003, there essentially would be a freeze on special access PCIs, as the X-factor would equal GDP-PI.<sup>328</sup>

## 2. Discussion

150. As discussed above, we are adopting the CALLS Proposal on an interim mandatory basis. Price cap LECs that choose not to be regulated under the CALLS Proposal will  
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*First Report and Order*, 12 FCC Rcd at 8943-44; *Rural Certification Public Notice*. Modified Proposal at § 3.2.4.1(ii); Letter from John T. Nakahata, Counsel to CALLS, to Jack Zinman, Legal Counsel, FCC, May 25, 2000 at 3; Appendix B § 61.48(m)(1)(ii)(B).

<sup>324</sup> Modified Proposal at § 3.2.4.1; *CALLS April 14 Letter*, Appendix B § 61.48(m)(2)(vii). The redistributed switching revenue will not be included in calculations to determine eligibility for interstate access universal service support. *CALLS April 14 Letter*, Appendix B § 61.48(m)(2)(i).

<sup>325</sup> For purposes of this option, July 1, 2000 price cap reductions are as a percentage of base period price cap revenues. Appendix B § 61.48(m)(1)(i).

<sup>326</sup> Modified Proposal at § 3.2.4.2; *CALLS April 14 Letter*, Appendix B §§ 61.48(m)(1)(i) and 61.48(m)(2)(vi).

<sup>327</sup> Modified Proposal at § 3.2.7; Appendix B §§ 61.42(d)(5), 61.42(e)(3), and 61.48(n).

<sup>328</sup> Modified Proposal at § 3.2.7; Appendix B § 61.45(b)(1)(iv).

have their PCIs set at forward-looking economic costs after the completion of a proceeding to determine those costs. Until the cost proceeding is concluded for those price cap LECs that elect it, the CALLS Proposal price cap rules, as described below, will apply to all price cap LECs.

**a. Reductions in Switched Access Usage Charges**

151. We adopt the CALLS Proposal as it relates to local switching, trunking, and special access. We believe the proposal is in the public interest because it provides an immediate reduction in switched access rates that will result in lower long-distance charges for consumers, while also simplifying the current price cap access charge regime. Adoption of the CALLS Proposal will result in an immediate \$2.1 billion reduction in switched access usage charges. All price cap LECs will make the CALLS Proposal's switched access usage charge reductions on July 1, 2000. Upon completion of the required cost proceeding, price cap LECs that choose not to be regulated under the CALLS Proposal will be subject to a true-up of their rates under the CALLS Proposal and of those based on forward-looking economic cost.

152. The CALLS IXCs have committed to pass the reduction to switched access usage charges on to residential and business long-distance consumers,<sup>329</sup> and, except in very limited circumstances, price cap LECs will not recover any of these reductions through non-traffic sensitive flat-rated end-user fees. This means that, contrary to CALLS opponents' concerns,<sup>330</sup> LECs generally will not subsidize the rates they charge high-volume users with revenue they receive from an end-user fee applied to everyone, including low-volume users.

153. Although most price cap LECs would achieve the switched access usage charge reduction solely through rate decreases, CALLS proposed two mutually exclusive alternatives to permit certain carriers to shift some of these charges to limited elements of the common line basket as described below. We adopt these limited exceptions for smaller rural carriers, and for carriers that would have initial reductions above the average of all price cap carriers.

154. Under the first alternative established by these rules, price cap carriers other than the BOCs and GTE that have at least 20 percent of total holding company lines operated by rural telephone companies may elect to shift to the common line basket the switched access usage charges necessary to yield those filing entities' proportionate share of the total reduction in switched access usage rates.<sup>331</sup> As noted above, this mechanism will be evaluated in the proposed cost review proceeding to determine whether retaining this exception or transferring the additional switched access reduction amounts to the common line basket is warranted.

155. Citizens and Global Crossing comment that this option is not an effective solution for smaller rural price cap LECs because the shifted amounts would be recovered from multi-line

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<sup>329</sup> See *AT&T March 30 Letter*; *Sprint February 25 Letter*.

<sup>330</sup> Intermedia Comments at 7-8; Time Warner Comments at 2; ALTS Reply at 5; Joint Consumer Commenters Reply at 15.

<sup>331</sup> Modified Proposal at § 3.2.4.1; Appendix B § 61.48(m)(1)(ii).

business SLCs and PICCs, thereby increasing rates in their most competitive markets.<sup>332</sup> We note that the shifting mechanism is not mandatory; smaller rural price cap LECs can choose not to recover their additional switched access usage charge reductions from multi-line business SLCs and PICCs. We believe, however, it is in the public interest to allow these carriers some ability to recover the switched access usage charge reductions. As discussed below, we are adopting a higher interstate average traffic sensitive access charge target rate of 0.95 cents for smaller rural carriers. We believe that adoption of the limited revenue shifting exception, with the availability of the higher target rate, will address sufficiently any concerns raised by the immediate switched access usage charge reduction to small rural price cap LECs.

156. We also permit any price cap company with reductions per line at the holding company level greater than the industry average to elect temporarily to shift to the common line basket a portion of the amount of the additional reductions to switched access usage charges necessary to yield that carrier's proportionate share of the total reduction in switched access usage rates on July 1, 2000.<sup>333</sup> These shifted amounts will be eliminated through the application of a 6.5 percent X-factor.

157. This transitional exception is reasonable because it permits carriers with above average reductions per line in the first year to spread those reductions more equitably over time while maintaining the \$2.1 billion reduction in switched access charges to IXCs on July 1, 2000. Carriers that elect this option can shift a portion of their initial-year reductions to the common line basket and recover these amounts as additional components of a multi-line business SLC or PICC.<sup>334</sup> Although the recovery of the shifted amounts temporarily creates an implicit subsidy, the shifted revenue added to the multi-line business SLC or PICC will eventually be eliminated through application of an X-factor of 6.5 percent beyond the date on which the average traffic sensitive access rates reach the applicable targets.<sup>335</sup>

158. Subject to these two narrowly defined alternatives, price cap LECs will be making significant reductions to switched access usage charges on July 1, 2000 without recovering these reductions through flat-rated end-user charges. We find that these reductions in switched access usage charges have several significant, direct benefits for consumers. First, the IXCs' commitment to eliminate their minimum usage charges in return for this reduction will especially benefit low-volume and moderate long-distance users.<sup>336</sup> Because low-volume and moderate

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<sup>332</sup> Citizens Supp. Comments at 9-10; Global Crossing Supp. Comments at 7-8.

<sup>333</sup> The shifted amounts are restricted to reduction amounts that exceed 25 percent of local switching element revenues necessary to yield the carrier's proportionate share of a total \$2.1 billion reduction of switched access usage rates on July 1, 2000. Modified Proposal at § 3.2.4.2; *CALLS April 14 Letter*, Appendix B § 61.48(m)(1)(i).

<sup>334</sup> *CALLS April 14 Letter*, Appendix B § 61.48(m)(2)(vi).

<sup>335</sup> *CALLS April 14 Letter*, Appendix B § 61.48(m)(1)(i).

<sup>336</sup> See *AT&T March 30 Letter*; *Sprint February 25 Letter*; *CALLS Supp. Comments* at 2-4; *USTA Supp. Comments* at 2. For a full discussion of the IXC commitments, see Section IV.D.3 *infra*.

long-distance users make so few calls, such fees have impacted them disproportionately.<sup>337</sup> Second, the reduction in switching charges, when taken with the IXC pass-through commitment, also will result in lower per-minute long-distance rates for all consumers.<sup>338</sup> Finally, the reduction in switched access usage charges will promote competition in the long-distance market between BOC affiliates entering this market and IXCs. To the extent switched access usage charges paid by IXCs are significantly above cost, BOC affiliates would have a competitive advantage because they would obtain switching services from the BOCs at cost. By driving switched access usage charges closer to their actual costs more quickly than would occur under the existing price cap regime, the CALLS Proposal will minimize the competitive advantages BOC affiliates would have over IXCs in offering long-distance services while switched access rates were significantly above cost.<sup>339</sup>

159. Some commenters request that we modify the CALLS Proposal to require that a proportionate share of the additional switched access usage charge reductions agreed upon to reach \$2.1 billion in reductions by July 1, 2000 come from tandem-switched rates.<sup>340</sup> Specifically, commenters argue that absent such a requirement, price cap LECs are more likely to decrease rates for direct-trunked transport than tandem-switched transport, thereby competitively disadvantaging smaller IXCs that rely heavily on tandem-switching.<sup>341</sup> We decline to require that a proportionate share of the switched access usage charge reductions come from tandem-switched rates. Our current price cap plan allows price cap LECs flexibility to determine how X-factor reductions should be applied among tandem-switched rates and direct-trunked transport rates. Price cap LECs are free to make that determination on the basis of the relative costs of providing the services and market considerations. The CALLS Proposal does not change that situation and we see no reason to do so. We have previously determined that rules to protect smaller IXCs in competition with large IXCs are unnecessary because the long-distance market is competitive.<sup>342</sup> Therefore, we will not alter our rules to require price cap LECs to take a proportionate share of the \$2.1 billion reduction from tandem-switched rates. If price cap LECs do not make any reductions to tandem-switched rates, but target the required additional reductions only to direct-trunked transport, the significant reductions to these rates should make either the purchase of direct-trunked transport or the leasing of transport from larger IXCs an affordable alternative for smaller IXCs.

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<sup>337</sup> *Low-Volume Long-Distance Users NOI*, 15 FCC Rcd at 6301.

<sup>338</sup> See Global Crossing Supp. Comments at 12.

<sup>339</sup> See MCI Comments at 6; Sprint Supp. Reply Comments at 6.

<sup>340</sup> Cincinnati Bell Supp. Comments at 5-6; Global Crossing Supp. Comments at 11-12; CompTel Supp. Reply at 1-3.

<sup>341</sup> Global Crossing Supp. Comments at 11-12.

<sup>342</sup> See *Pricing Flexibility Order*, 14 FCC Rcd at 14329; *Access Charge Reform Order*, 12 FCC Rcd at 16060.

**b. X-Factor**

160. During the five-year term of the CALLS Proposal, the X-factor as adopted herein will not be a productivity factor as it has been in past price cap formulas. Instead, the X-factor is now a transitional mechanism to lower access charges to target rates for switched access, and to lower rates for a specified time period for special access. Although the X-factor under the CALLS Proposal will not be tied to price cap LEC productivity, it will lower access charges over the term of the proposal. As noted by CALLS, the prescriptions of prior productivity factors in the price cap formula have been the subject of extensive regulatory proceedings and litigation, and the Commission's decision to select 6.5 percent as the most recent X-factor has been reversed and remanded by the court.<sup>343</sup> The compromise advocated by CALLS will provide a solution to the contentious X-factor prescription proceeding for the term of the CALLS Proposal for those price cap LECs that do not elect to set rates based on a cost study proceeding.<sup>344</sup>

161. We adopt the CALLS Proposal regarding the targeting of X-factor reductions to switching and switched transport services. Specifically, we will apply the reductions from imposing an X-factor of 6.5 percent to all price cap baskets except special access as indicated above: first to the residual per-minute TIC until that rate is eliminated; then to the information surcharge until that rate is eliminated;<sup>345</sup> and finally to the local switching charge and switched transport charges until the carrier's average traffic sensitive interstate access charge equals a specified target rate. At the current time, only one filing entity in GTE currently retains the TIC, therefore we find that targeting X-factor reductions first to eliminate the minimal remaining TIC serves the public interest.<sup>346</sup> We also find that the elimination of the information surcharge is consistent with the Commission's policy that non-traffic sensitive costs be recovered by a non-traffic sensitive charge.

162. We also adopt target rates of 0.55 cents for the BOC price cap LECs and GTE, 0.95 cents for primarily rural price cap LECs, and 0.65 cents for other price cap LECs.<sup>347</sup> For purposes of applying the 0.95-cent target rate, a primarily rural price cap LEC is one with a holding company average of less than 19 End User Common Line charge lines per square mile served. Target rates for filing entities that are purchased by price cap LECs during the term of the CALLS Proposal will retain the target rate of the selling price cap LEC, subject to the exceptions

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<sup>343</sup> See *CALLS NPRM*, 14 FCC Rcd at 16983-84; Section IV.B.1.b *supra*.

<sup>344</sup> If a price cap LEC elects to set rates based upon a cost study, the X-factor would be based on LEC productivity.

<sup>345</sup> The information surcharge permits LECs, upon receipt of a waiver from the Commission, to recover costs presently assigned to the information rate element that are intrastate in nature and do not relate to the provision of interstate directory assistance. 47 C.F.R. § 69.109(b). Carriers calculate these costs on a traffic sensitive basis, per minute of access use.

<sup>346</sup> As noted above in Section IV.B.1.A, we established a mechanism to eliminate the TIC in the *Access Charge Reform Order*.

<sup>347</sup> Modified Proposal at §§ 3.1.2 and 3.1.3; *VALOR April 14 Letter*; Appendix B §§ 61.3(qq).

described above.<sup>348</sup> Rates for price cap LECs that elect to participate in the cost study proceeding in lieu of the CALLS Proposal will be set at forward-looking costs.

163. Once a price cap LEC reaches the applicable target rate level, the X-factor for all baskets except special access will equal GDP-PI. For primarily rural carriers electing the 0.95-cent target rate, X-factor reductions after the target level is reached will be targeted to the removal of CCL charges in the common line basket.<sup>349</sup> Upon the earlier of the elimination of the CCL charges, or June 30, 2004, the X-factor for primarily rural carriers will equal GDP-PI.

164. CALLS proposes to include revenues and demand from contract tariff services and from UNEs used to provide switched access services in calculating whether the target rates have been reached.<sup>350</sup> We decline to include these amounts in the target rate calculations. In granting price cap LECs flexibility to offer contract-based tariffs, we required the removal of contract tariff offerings from price cap regulation. This removal was to ensure that the individually-tailored contract tariffs do not adversely impact the prices made available to the majority of price cap LEC customers.<sup>351</sup> Including revenue from contract tariffs in the calculation of average traffic sensitive target rates as proposed by CALLS would thwart this goal. Furthermore, we noted in the *Pricing Flexibility Order* that it would be difficult to allocate properly demand for contract tariff offerings that include a package of two or more access services, and declined to adopt a method to do so.<sup>352</sup> Including contract tariff revenues and demand in calculating the CALLS Proposal target rates would require implementing such an allocation method, which we have recently rejected. We have distinguished between UNEs and interstate access charges and have treated them separately under our rules.<sup>353</sup> UNEs are not included in the LEC PCIs. UNEs are irrelevant to carriers using switched access services because UNEs are only a substitute for access services in the special circumstance where the carrier is also providing local service to the end-user customer.<sup>354</sup>

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<sup>348</sup> Specifically, target rates for properties that are merged into a filing entity with a different target rate will be a weighted average of the prior and new target rates. The 0.95-cent target rate will be available for all filing entities which were, as of April 1, 2000, under a binding and executed contract for purchase by a primarily rural price cap LEC. See para. 143 *supra*; *VALOR April 14 Letter*; Appendix B §§ 61.3(qq)(2) and 61.48(o).

<sup>349</sup> *VALOR April 14 Letter*; Appendix B § 61.45(b)(1)(B).

<sup>350</sup> Modified Proposal at § 3.1.1; Letter from John T. Nakahata, Counsel to CALLS, to Magalie R. Salas, Secretary, FCC, May 17, 2000.

<sup>351</sup> *Pricing Flexibility Order*, 14 FCC Rcd at 14287-88; 47 C.F.R. § 69.727(a)(2)(ii).

<sup>352</sup> *Pricing Flexibility Order*, 14 FCC Rcd at 14305-06.

<sup>353</sup> See *Access Charge Reform Order*, 12 FCC Rcd at 16129.

<sup>354</sup> See Implementation of the Local Competition Provisions in the Telecommunications Act of 1996, CC Docket Nos. 96-98, 95-185, Third Order on Reconsideration and Further Notice of Proposed Rulemaking, 12 FCC Rcd 12460, 12483-84 (1997). The Commission is examining the issue of using shared transport for switched access where a competitive LEC is not providing local service in a Further Notice of Proposed Rulemaking. Implementation of the Local Competition Provisions of the Telecommunications Act of 1996, CC Docket No. 96-98, Third Report and Order and Fourth Further Notice of Proposed Rulemaking, 15 FCC Rcd 3696, 3914-15 (1999) (*UNE Remand Order*).

Furthermore, even in this circumstance, UNEs and access charges are subject to different pricing standards. The purpose of establishing a target rate is to guarantee a particular rate level for switched access services. Including UNEs may drive access charges above or below the intended target rate, depending upon whether the total element long-run incremental cost (TELRIC) of UNEs is below or above the target rate.

165. Opponents of the CALLS Proposal contend that the proposal eviscerates price cap regulation by eliminating the X-factor adjustment after target rates are reached.<sup>355</sup> According to its opponents, the CALLS Proposal wrongfully assumes that LECs' costs are changing at the rate of inflation and are not affected by productivity gains.<sup>356</sup> As such, the opponents assert, LECs will be allowed to avoid about \$1 billion in access reductions in the later years of the proposal.<sup>357</sup> Some opponents suggest that the X-factor should continue to apply to all baskets, even after the target rate is achieved.<sup>358</sup> Under this approach, end-user rates would decline over time through the application of the X-factor and switched access rates would continue to fall even after the target rate was achieved.

166. We reject these contentions in the overall context of the CALLS Proposal. First, switched access usage charges will be reduced immediately by \$2.1 billion on July 1, 2000. The reductions in or elimination of some charges, such as the residential PICC, and the increases in other charges, such as the SLC, are approximately equal. Thus, there is a net reduction in overall access and universal service charges of approximately \$2.1 billion, an amount \$700 million greater than the reduction that would have been achieved through application of the X-factor under our current price cap scheme.<sup>359</sup> Second, we believe that increased competition will serve to constrain access rates in the later years of the CALLS Proposal as X-factor reductions are phased out. We believe that market forces, instead of regulatory prescription, should be used to constrain prices whenever possible.<sup>360</sup> As competitors utilizing a range of technologies, including cable, cellular, MMDS and LMDS, continue to enter the local exchange market, we expect that rates will continue to decrease.<sup>361</sup> We also believe that adoption of the CALLS Proposal will encourage competition by removing implicit subsidies in access charges and recovering costs from those

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<sup>355</sup> CPI Comments at 2, 5; MCI Comments at 17; ALTS Reply at 6-7; NASUCA Reply at 16-17; Focal Supp. Comments at 13.

<sup>356</sup> CPI Comments at 5.

<sup>357</sup> MCI Comments at 9.

<sup>358</sup> MCI Comments at 17; Focal Supp. Comments at 10-11; NASUCA Supp. Comments at 19.

<sup>359</sup> See Appendix C, Graph 2.

<sup>360</sup> See *UNE Remand Order*, 15 FCC Rcd at 3906 (“[T]he market price should prevail, as opposed to a regulated rate which, at best, is designed to reflect the pricing of a competitive market.”); *Pricing Flexibility Order*, 14 FCC Rcd at 14233 (The Commission eliminated limitations in the density zone pricing plan after concluding that “market forces, as opposed to regulation, are more likely to compel LECs to establish efficient prices.”)

<sup>361</sup> See CALLS Reply at 55.

services that cause them. Therefore, the significant up-front reductions coupled with increased competition ultimately should result in access charges that are comparable to those that would be achieved under our current price cap system over the five-year term of the CALLS Proposal. Furthermore, after the five-year term we can re-examine the issue to determine whether competition has emerged to constrain rates effectively.

167. We further disagree with commenters who oppose targeting and argue that the X-factor should continue to apply to all baskets equally.<sup>362</sup> The Commission has targeted reductions to certain baskets since it first adopted price caps. Even though the same productivity factor was applied to all service baskets, the Commission specifically targeted certain reductions to the common line basket by including a “g factor” reduction, representing per-minute growth per access line, in the common line PCI formula.<sup>363</sup> We also targeted X-factor reductions to eliminate the per-minute TIC.<sup>364</sup> In addition, similar to the targeting in the CALLS Proposal, we recently sought comment on a proposal to target reductions to the traffic sensitive and trunking PCI formulas. We proposed introducing a q factor, similar to the g factor in the common line PCI, that would share the benefits of growth in local switching and tandem switching demand with IXCs, because IXCs may be responsible in part for the increase in demand, and the increased demand may not lead to a measurable increase in switching costs to the LECs.<sup>365</sup> We find it reasonable and consistent with past Commission practice to target the X-factor reductions to specific baskets. We note that under the CALLS Proposal, an X-factor equal to the GDP-PI, up to 6.5 percent, will be applied to all the baskets once the target rate for average traffic sensitive access charges is reached, and to the special access basket after 2003.<sup>366</sup> Targeting the X-factor reductions to switching and switched transport services will more quickly reduce charges for these services toward cost-based levels than would be possible under the existing price cap methodology.<sup>367</sup>

168. Focal characterizes the CALLS Proposal’s targeting mechanism as an “attempt to escape the price cap rules,” arguing that CALLS failed to seek a waiver of the Commission’s rules.<sup>368</sup> The CALLS Proposal seeks to *amend* the price cap rules, not to *waive* them; because we issued a notice of proposed rulemaking to amend our price cap rules as proposed by CALLS, there is no need for any waiver of these rules.

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<sup>362</sup> ALTS and Time Warner Supp. Comments at 8-11; Focal Supp. Comments at 6-15.

<sup>363</sup> *LEC Price Cap Order*, 5 FCC Rcd at 6787, 6794-95; 47 C.F.R. § 61.45(c).

<sup>364</sup> *See Access Charge Reform Order*, 12 FCC Rcd at 16081; Section IV.B.1.a *supra*.

<sup>365</sup> *Pricing Flexibility Order*, 14 FCC Rcd at 14331, 14333.

<sup>366</sup> *See Modified Proposal* at §§ 3.2, 3.2.3, and 3.2.7; Appendix B §§ 61.45(b)(1)(ii), 61.45(b)(1)(iii)(A), and 61.45(b)(1)(iv).

<sup>367</sup> *See GTE Supp. Reply* at 30-31.

<sup>368</sup> Letter from Richard J. Metzger, Vice President Regulatory and Public Policy, Focal Communications, to Magalie R. Salas, Secretary, FCC, May 8, 2000 at 2 (*Focal May 8 Letter*).

169. Some commenters argue that the CALLS Proposal's X-factor targeting approach would reduce facilities-based local exchange competition.<sup>369</sup> Specifically, these commenters object to the targeting of reductions to traffic-sensitive rates, which are subject to competition, while rate levels in the less-competitive common line basket are maintained.<sup>370</sup> In response, Sprint contends that the competitive market has not controlled prices in the exchange access market, and that competitive LECs are charging access rates that are significantly higher than the above-cost rates currently charged by incumbent LECs.<sup>371</sup>

170. In addition, we observe that the target rates are not predatory.<sup>372</sup> To engage in predatory practices, a price cap LEC would have to charge rates below its incremental costs to drive out its competitors, and then raise prices to monopoly levels after the competitors have left the market.<sup>373</sup> As evidence that the target rates are not below price cap LECs' incremental costs, we note that interconnection agreements reached through negotiations in the marketplace contain access rates that are below the target rates.<sup>374</sup> In addition, the CALLS signatory LECs have agreed to charge these rates for a sustained period of time, which they would not do if the rates were predatory. Price cap LECs will not be able to increase these prices to monopoly prices; the rates will remain at the target rates until July 1, 2005, at which time the Commission will re-examine them. We find that targeting is appropriate to drive average traffic sensitive charges closer to the cost of providing these services, and that it will not harm efficient competition.

171. Furthermore, we find it reasonable not to target reductions to the common line basket at this time. When price caps were first implemented, initial rates were targeted to produce the same return across all baskets.<sup>375</sup> Currently, however, price cap LECs' basket earnings are significantly higher for traffic-sensitive services than for common line services.<sup>376</sup>

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<sup>369</sup> ALTS and Time Warner Supp. Comments at 10; CPI Supp. Comments at 9-10; Allegiance Supp. Reply at 3; Focal Supp. Reply at 2-3.

<sup>370</sup> CPI Supp. Comments at 10; Allegiance Supp. Reply at 3; ALTS and Time Warner Supp. Reply at 7; Focal Supp. Reply at 2.

<sup>371</sup> Sprint Supp. Reply at 7.

<sup>372</sup> Although no commenter alleges that the target rates are predatory, Focal argues that adoption of the CALLS Proposal would permit predation by circumventing the PCI and the upper pricing bands. *Focal May 8 Letter* at 2-3. We are not eliminating either the PCI or the upper pricing bands in this Order. PCIs will continue to apply to each price cap basket, and upper pricing bands will continue to apply to service categories and subcategories within the price cap baskets. See Appendix B §§ 61.45, and 61.47(e).

<sup>373</sup> See *Price Cap Second FNPRM*, 11 FCC Rcd at 870; Telephone Company-Cable Television Cross-Ownership Rules, Sections 63.54 - 63.58, CC Docket No. 87-266, Memorandum Opinion and Order on Reconsideration and Third Further Notice of Proposed Rulemaking, 10 FCC Rcd 244, 343 (1994).

<sup>374</sup> See *Cable & Wireless Comments* at 4.

<sup>375</sup> See *LEC Price Cap Order*, 5 FCC Rcd at 6814-17.

<sup>376</sup> Based on 1999 ARMIS data, Commission staff calculated approximate rates of return of 85 percent for the traffic-sensitive basket, 20 percent for the trunking basket, and 15 percent for the common line basket. AT&T (continued....)

This is consistent with our observation that the current traffic-sensitive rate structure provides price cap LECs with more revenue when demand increases, regardless of whether costs have increased, resulting in higher earnings.<sup>377</sup> Therefore we find it reasonable to target reductions to traffic-sensitive services rather than to common line services.

172. We also adopt the creation of a special access basket with a separate X-factor as proposed by CALLS. The creation of a separate special access basket, with its own X-factor, benefits dedicated or high-volume users through the reduction of special access rates. Separating special access into its own basket, in conjunction with the IXC commitments, also will benefit residential and small business end users. Under our current rules, special access is recovered through the trunking basket. If it were to remain in that basket, price cap LECs could reduce special access rates while increasing rates for the other rate elements in that basket so that the average rate for that basket remains at the target rate. The creation of a separate price cap basket for special access will preclude price cap LECs from funding reductions in special access charges by increasing the rates for switched transport services in other baskets once the target rates are reached.

173. Cincinnati Bell and Global Crossing argue that a separate, smaller X-factor should be applied to them and other mid-size price cap LECs under the CALLS Proposal because these carriers are not able to achieve the same levels of productivity growth as larger price cap LECs.<sup>378</sup> As noted above, however, the X-factor adopted under the CALLS Proposal is not a productivity offset as past X-factors have been, but is instead merely a ramp-down method to reduce traffic sensitive charges to the stated target levels.<sup>379</sup> Therefore, the asserted inability of smaller price cap LECs to match the productivity growth of larger price cap LECs is irrelevant in this proceeding and we decline to adopt a separate X-factor for smaller price cap LECs. In addition, the price cap low-end adjustment remains available as a backstop mechanism for LECs that have earnings below a specified threshold.<sup>380</sup> Finally, we note that the CALLS Proposal recognizes and addresses the disparity in subscriber bases and resources by providing higher target rates for mid-size and rural price cap LECs. We believe the differences of smaller price cap LECs are

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has also provided estimates based on 1997 data that show rates of return of 45 percent for the switching basket, 15 percent for the trunking basket, and 9 percent for the common line basket. See Letter from Bruce K. Cox, Government Affairs Vice President, AT&T, to Magalie R. Salas, Secretary, FCC, CC Docket No. 96-262, Feb. 19, 1999 at 6. See also Letter from Pete Sywenki, Director, Sprint, to Magalie R. Salas, Secretary, FCC, May 12, 2000 at 6.

<sup>377</sup> *Pricing Flexibility Order*, 14 FCC Rcd at 14332 (seeking comment on whether to require a one-time downward adjustment to price cap LECs' traffic-sensitive PCIs to correct for the earnings imbalance).

<sup>378</sup> Cincinnati Bell Supp. Comments at 2-4; Global Crossing Supp. Comments at 8-10; Letter from John S. Morabito, Vice President Federal Legislative and Regulatory Affairs, Global Crossing, to Magalie R. Salas, Secretary, FCC, May 11, 2000.

<sup>379</sup> Modified Proposal at § 3.2; Appendix B § 61.45(b)(1).

<sup>380</sup> The low-end adjustment permits incumbent LECs with rates of return less than 10.25 percent to increase their PCIs to a level that would enable them to earn 10.25 percent.

reasonably accommodated under the CALLS Proposal, therefore we decline to adopt a separate X-factor for smaller price cap LECs.

174. As observed by some commenters, the controversy regarding the current status of the X-factor and the concurrent uncertainty over the resolution of the controversy disrupts business expectations and future investment decisions of both LECs and new entrants.<sup>381</sup> As referenced above, we recently issued a Notice of Proposed Rulemaking regarding the prescription of the X-factor.<sup>382</sup> Currently, the Commission has before it comments on whether it should prescribe two X-factors to address separately the period July 1, 1997 to June 30, 2000 and the period from July 1, 2000 forward, or a single X-factor to cover the combined periods. The CALLS Proposal resolves the uncertainty of whether to prescribe one or two X-factors and the uncertainty concerning the appropriate level of the X-factor for those price cap LECs that will be regulated under the CALLS Proposal. CALLS signatories have agreed not to initiate legal or regulatory action to adjust price cap determined rates billed for access minutes prior to July 1, 2000, including the period covered by the D.C. Circuit's stay of the mandate in *USTA v. FCC*.<sup>383</sup> Therefore, those entities that have signed on to the CALLS Proposal have agreed to waive any right to recoupment that they might be entitled to seek if we were unable to justify the 6.5 percent X-factor remanded by the court.

175. We note that not all affected price cap LECs had voluntarily agreed to this term of the CALLS Proposal. The issue of whether recoupment may be warranted for the period covered by the D.C. Circuit's stay of the *USTA v. FCC* mandate is not obviated with respect to price cap LECs that have not voluntarily signed on to the CALLS Proposal. The issue of fashioning remedies, however, is well within our discretion.<sup>384</sup> Available data show that non-signatory price cap LECs have experienced earnings above the prescribed rate of return for interstate access during this period, and thus non-signatory price cap LECs have not been subjected to unreasonably low rates.<sup>385</sup> Because available data do not suggest that specific recoupment is warranted, we do not generally provide for it here. Any non-signatory price cap LEC may, however, seek to show that its access charge rates under the 6.5 percent X-factor were confiscatory, and therefore may seek recoupment of amounts it undercharged during the period of the court's remand.

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<sup>381</sup> GTE Reply at 37-38; Global Crossing Supp. Comments at 5.

<sup>382</sup> *1999 Price Cap FNPRM*, 14 FCC Rcd at 19717.

<sup>383</sup> See Modified Proposal § 4.3; *CALLS April 28 Letter*.

<sup>384</sup> See *Public Utilities Comm'n of the State of California v. FERC*, 988 F.2d 154, 163 (D.C. Cir. 1993) (“agency discretion ‘is often at its “zenith” when the challenged action relates to the fashioning of remedies.”); *Natural Gas Clearinghouse v. FERC*, 965 F.2d 1066, 1073 (D.C. Cir. 1992).

<sup>385</sup> See Interstate Rate of Return Summary for 1999 Based on Initial Reports Filed by Price-Cap Carriers (Apr. 4, 2000). This report showed that the weighted arithmetic mean for all price cap LECs' interstate rate of return was 18.52 percent, up from 16.52 percent for 1998.

176. With respect to the interstate average traffic sensitive charge target levels proposed by CALLS, we conclude that the target rates will significantly reduce per-minute access rates, from today's average rate of 1.1 cents per access minute to the target rates of 0.55 cents for the BOC LECs and GTE; 0.95 cents for primarily rural price cap LECs; and 0.65 cents for all other price cap LECs, thereby lowering long-distance bills.<sup>386</sup> We find further that these target rates are just and reasonable. The target rates are within the range of estimated economic costs of switched access that have been presented to the Commission.<sup>387</sup> In addition, the fact that both purchasers and suppliers of access services, including non-CALLS members, supported the target rates further indicates that they are a reasonable temporary estimate of prices that might be set in a competitive market. In support of the 0.55-cent target rate, MCI commented that adoption of the target rates during the five-year term of the CALLS Proposal will provide an immediate reduction in switched access rates without requiring the completion of a time-consuming review of cost studies.<sup>388</sup>

177. We further conclude that the multi-tier target rate system addresses the reality of a diverse LEC population. We find that the lower target rate of 0.55 cents is reasonable for the larger BOC LECs and GTE due to their economies of scale and broad subscriber bases. We find that a slightly higher target rate of 0.65 cents is reasonable for other LECs that by definition do not have the subscriber bases and resources of the larger BOCs. In addition, we find that a target rate of 0.95 cents for primarily rural price cap LECs is reasonable. Due to the nature of their service areas, primarily rural price cap LECs experience costs that are significantly higher than other price cap LECs of their size, and are unable to spread those costs over a large subscriber base.<sup>389</sup> Therefore, we agree that the higher level is appropriate for primarily rural price cap LECs.

178. Some commenters have argued that the target rates should be lower because, according to state approved interconnection rates, access costs are actually below one half of one cent per minute.<sup>390</sup> The commenters contend that the Commission should reduce access rates to

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<sup>386</sup> See *CALLS NPRM*, 14 FCC Rcd at 16984; APT Comments at 7.

<sup>387</sup> See Bell Atlantic/NYNEX Comments, CC Docket No. 96-262 at 22 (Jan. 29, 1997) (cost study supporting traffic sensitive switching costs of approximately one cent a minute); Letter from Joel E. Lubin, Vice President, Federal Government Affairs, AT&T, to Magalie R. Salas, Secretary, FCC, CC Docket No. 96-262 (Feb. 25, 1999) (estimating the economic cost of a switched access minute at \$0.00255 for RBOCs and \$0.00373 to \$0.00544 as a potential proxy for interstate switched access costs); GTE Comments, CC Docket Nos. 96-262, 94-1, 97-250 at 7 (Oct. 26, 1998) (estimating universal service support using a switched access rate of \$0.008/minute).

<sup>388</sup> MCI Comments at 4-5.

<sup>389</sup> For example, because VALOR and Citizens have fewer lines per square mile of service area than non-rural price cap LECs, their lines must run farther, and the cost of exchanges is distributed among fewer end users. See VALOR Supp. Comments at 3, 7. See also Citizens Supp. Comments at 5.

<sup>390</sup> Cable & Wireless Comments at 4; Level 3 Comments at 7; Illinois Commission Reply at 7; NASUCA Reply at 10.

forward-looking costs, like the unbundled network element rates for local transport and termination.<sup>391</sup> The Commission has recognized that, as a legal matter, transport and termination of local traffic are different services than access service for long-distance telecommunications and therefore are regulated differently.<sup>392</sup> As a policy matter, we have determined that a market-based approach, instead of a prescriptive approach in which we set access charge rates at economic cost levels, better serves the public interest.<sup>393</sup> We believe that the target rates we are adopting are a reasonable transitional estimate of rates that might be set through competition. Not only are the target rates supported by both price cap LECs and IXCs, but competitive LECs have also proposed reducing access charges to the same target rates.<sup>394</sup> Reducing the rates to access costs, as the commenters suggest, would necessitate a lengthy and complex proceeding.<sup>395</sup> We believe the public interest is better served by the immediate reduction in access rates brought about by our adoption of the CALLS Proposal target rates. After the five-year term of the CALLS Proposal, we can re-examine the issue to determine whether competition has emerged to effectively constrain rates.

179. Time Warner has argued that the access charge reductions under the CALLS Proposal occur too quickly. Instead, Time Warner urges the Commission to phase-in access charge reform rather than adopting a flash-cut approach.<sup>396</sup> In response, we note that we are adopting a phased-in approach of reducing access charges. Price cap LECs will not reduce access charges to forward-looking cost levels on July 1, 2000, or even by the end of the five-year period, unless they choose to do so by electing not to be regulated under the CALLS Proposal. Instead, we are implementing transitional rates to reduce access charges closer to cost-based rates. We disagree with Time Warner's contention that the access charge reductions made in response to this Order are too steep.<sup>397</sup> Instead we believe that they are a reasonable transitional measure until competition develops sufficiently to enable market forces to determine access charges.

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<sup>391</sup> Level 3 Comments at 4-10.

<sup>392</sup> See *Local Competition Order*, 11 FCC Rcd at 16012-13.

<sup>393</sup> See *Access Charge Reform Order*, 12 FCC Rcd at 16001, 16107 ("Regulation cannot replicate the complex and dynamic ways in which competition will affect the prices, service offerings, and investment decisions of both incumbent LECs and their competitors. A market-based approach to rate regulation should produce, for consumers of telecommunications services, a better combination of prices, choices, and innovation than can be achieved through rate prescription.").

<sup>394</sup> See ALTS and Time Warner Supp. Comments at 18; ALTS and Time Warner Supp. Reply at 7. ALTS and Time Warner submitted an alternate plan to the CALLS Proposal that would reduce access charges to the target rates more slowly.

<sup>395</sup> See MCI Comments at 4.

<sup>396</sup> Letter from Donald F. Shephard, Vice President Federal Regulatory Affairs & Policy, Time Warner Telecom, to Magalie R. Salas, Secretary, FCC (May 8, 2000) (*Time Warner May 8 Letter*).

<sup>397</sup> *Time Warner May 8 Letter* at 1.

180. As noted above, CALLS has proposed a method for addressing the target rates for filing entities that are being transferred wholly or in part among price cap LECs.<sup>398</sup> We find that this approach avoids rate churn and customer confusion. We also believe addressing these transfers in the June 16, 2000 TRP filings is the most administratively simple way to handle the sale of filing entities with different target rates. Therefore, we find that the public interest is served by adopting these requirements.

181. Finally, we adopt the CALLS Proposal's treatment of the low-end adjustment. Price cap LECs cannot claim this adjustment for rates charged during the tariff year beginning July 1, 2000, but will be able to claim this adjustment during the remaining years in which the CALLS Proposal adopted today is effective.<sup>399</sup> Allowing price cap LECs to claim a low-end adjustment in 2000 would complicate the calculation of the \$2.1 billion immediate reduction in switched access usage charges called for in the CALLS Proposal. Therefore we are precluding price cap LECs from taking the adjustment in that year. We note, however, that even without the availability of the low-end adjustment mechanism in the first year, price cap LECs are protected by the takings clause of the Constitution from making rate reductions that would be confiscatory. To the extent that price cap LECs can demonstrate that rate reductions under the CALLS Proposal are confiscatory, they may seek recoupment of the confiscatory amounts.

182. We disagree with commenters who argue that the low-end adjustment should not be available to price cap LECs in the remaining years of the CALLS Proposal.<sup>400</sup> We have included the low-end adjustment in our system of LEC price cap regulation to protect LECs from events beyond their control that would affect earnings to an extraordinary degree.<sup>401</sup> Moreover, as noted by commenters, the low-end adjustment is not likely to have a significant practical effect because it has been rarely invoked in the past, and price cap LECs must agree to waive it before taking advantage of pricing flexibility under our rules.<sup>402</sup> We find it reasonable to continue to include this adjustment, to the extent applicable under the CALLS Proposal.

### c. Measure of Inflation

183. In implementing the CALLS Proposal, we use GDP-PI as the measure of inflation to which the X-factor will be set once the target levels are reached for switching and switched transport rates, and after 2003 for special access. We take this opportunity to adopt our tentative conclusion in the *Pricing Flexibility Order* to use the BEA chain-weighted GDP-PI to measure

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<sup>398</sup> See para. 143 *supra*; Letter from John T. Nakahata, Counsel to CALLS, to Magalie R. Salas, Secretary, FCC, May 25, 2000.

<sup>399</sup> Modified Proposal at § 4.4; Appendix B § 61.45(d)(1)(vii).

<sup>400</sup> California Commission Supp. Comments at 8-9; MCI Supp. Comments at 23-27; Ad Hoc Supp. Reply at 14-15.

<sup>401</sup> *LEC Price Cap Order*, 5 FCC Rcd at 6804.

<sup>402</sup> Bell Atlantic Supp. Reply at 9; Sprint Supp. Reply at 8-9; *Pricing Flexibility Order*, 14 FCC Rcd at 14304-07.

inflation in the PCI formula. The BEA changed its measurement of GDP-PI from fixed-weighted indexes, on which our current measure of GDP-PI in the LEC price cap rules is based, to chain-weighted indexes because it found that the chain-weighted indexes are significantly more accurate.<sup>403</sup> CALLS member AT&T agrees, noting in the *Pricing Flexibility Order* proceeding that chain indexes provide the only significant economic comparisons for medium and longer term periods, while fixed-weight indexes become unrepresentative after only a few years of economic change.<sup>404</sup> Use of the BEA chain-weighted GDP-PI will not affect the aggregate switched access usage charge reductions to be taken on July 1, 2000; however it will make the average traffic sensitive charges reach the target rates slightly faster. The BEA chain-weighted GDP-PI will also result in slightly greater special access charge reductions.

184. Although the change in the measure of GDP-PI was not proposed in the CALLS Proposal, we believe it is in the public interest for the reasons stated above and adopt it in this Order. CALLS has informed us that its proposal was based on the GDP-PI fixed-weight index and changing to a chain-weighted GDP-PI index would materially affect its proposal.<sup>405</sup> We believe instead that this change is merely a technical one that reflects an independent agency's refinement of one of its measurements. As stated above, the chain-weighted index has been found to be more accurate than the fixed-weight index, and is therefore BEA's featured measure of GDP-PI.

## C. Universal Service

### 1. Introduction

185. In the preceding sections of this Order, we have restructured and significantly reduced the interstate access charges imposed by price cap LECs. In this section, based on the CALLS Proposal, we identify a specific amount of access charges as implicit support for universal service, and we establish an explicit interstate access universal service support mechanism to replace such implicit support. In contrast to the Commission's existing high-cost support mechanisms for rural and non-rural carriers, which provide support to enable states to ensure reasonably affordable and comparable *intrastate* rates, the purpose of this federal mechanism is to provide explicit support to replace the implicit universal service support in *interstate* access charges.

186. As explained below, consistent with the principles of the 1996 Act, this interstate access universal service support mechanism proposed by CALLS will provide explicit support that is specific, predictable, and sufficient to ensure that consumers in all regions of the nation have access to telecommunications services at affordable and reasonably comparable rates.

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<sup>403</sup> See J. Steven Landefeld and Robert P. Parker, *BEA's Chain Indexes, Time Series, and Measures of Long-Term Economic Growth*, 77 *Surv. of Current Bus.* 58 (May 1997).

<sup>404</sup> AT&T Reply, CC Docket No. 96-262 at 25 (Nov. 29, 1999), citing F.G. Forsyth and R.F. Fowler, *The Theory and Practice of Chain Price Index Numbers*, 144 *J. Stat. Soc'y Am.* 224 (1981).

<sup>405</sup> *CALLS April 24 Letter*.

Moreover, this support mechanism will provide support that is portable among competing carriers -- if a competitor serves a supported customer, the competitor will receive the interstate access support for that customer. Thus, by adopting the interstate access universal service support mechanism proposed by CALLS, we are able to serve the 1996 Act's dual goals of promoting competition in the telecommunications marketplace and simultaneously preserving and advancing universal service. Specifically, the interstate access universal service support mechanism that we establish today has the following features:

- Support is fixed at an annual amount of \$650 million.
- Support is explicit, rather than implicit.
- Support is targeted to the density zones that have the greatest need for it.
- Support is provided on a portable, per-line basis.
- Support is available on a competitively neutral basis to any eligible telecommunications carrier serving a supported customer, regardless of the technology used by that carrier.
- Support under the Commission's universal service Lifeline Assistance program for low-income consumers is increased to cover the increase in the residential SLC.

187. In the remainder of this section, we first provide background on universal service principles and Commission actions concerning universal service, followed by an overview of the interstate access universal service support mechanism proposed by CALLS. We then discuss the size of the support mechanism, the distribution of interstate access support, including a discussion of the portability of interstate access support, the changes to our existing Lifeline program, the recovery of universal service contributions by incumbent LECs, and implementation issues for the support mechanism. Finally, we provide a brief summary of our consultations with the Federal-State Joint Board on Universal Service (Joint Board) regarding the issues discussed in this section.

## 2. Background

188. As previously noted, historically, one of the goals of universal service has been to support the provision of telecommunications service in areas where the cost of providing such service would otherwise be significantly higher than the average cost of providing service in the United States as a whole.<sup>406</sup> This goal has been accomplished by providing support to carriers for both interstate and intrastate services to enable them to serve high-cost consumers at below-cost rates. There are generally three sources of universal service support: (1) state support for basic telephone service;<sup>407</sup> (2) federal support for intrastate costs of local telephone service that

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<sup>406</sup> See, e.g., *Universal Service Ninth Report and Order*, 14 FCC Rcd at 20439.

<sup>407</sup> Some state rate designs have provided implicit high-cost support flowing from (1) urban areas to rural areas; (2) business customers to residential customers; (3) vertical services to basic service; and/or (4) intrastate long distance service to local service. First, many states have adopted the practice of setting uniform local rates throughout the territory that a given company serves within the state, thereby enabling incumbent LECs to charge above-cost rates in urban (low-cost) areas to support the below-cost rates they charge in rural (high-cost) areas. Second, some state regulators have allowed incumbent LECs to charge business customers higher rates than residential customers even though the costs of serving business and residential customers in the same area are roughly the same, thereby creating a business-to-residential support flow. Third, through rate regulation in (continued...)

significantly exceed the national average;<sup>408</sup> and (3) federal support for the interstate portion of the local loop and port.<sup>409</sup> In the *Universal Service Ninth Report and Order* and *Universal Service Tenth Report and Order*, we reformed our high-cost support mechanism for non-rural carriers, which provides federal support for *intrastate* costs. In this Order, we reform federal support for the *interstate* portion of the local loop and port.

189. Universal service support has been both explicit and implicit. For example, various federal support mechanisms provide explicit monetary support payments to LECs.<sup>410</sup> LECs have also received implicit support from the Commission's interstate access charge regime, which permitted LECs to recover the interstate cost of the local loop and port in a manner different from the way that cost was incurred. For example, instead of allowing LECs to recover the entire non-traffic-sensitive cost of the local loop and port through a flat-rated charge to the customer, the Commission capped the amount of that charge because of concerns that customers would disconnect their telephone service if the charge were too high.<sup>411</sup> LECs recovered the non-traffic-sensitive costs that exceeded the cap on flat-rated charges through traffic-sensitive (per-minute) charges to IXCs, thus creating an implicit support flow from the IXCs to the LECs' customers. In addition, the LECs' flat-rated charges for business customers were higher than the flat-rated charges for residential customers, even though the costs of serving these different customer classes did not significantly differ. This rate differential created an implicit support flow from business customers to residential customers. Finally, LECs were permitted to average their flat-rated charges over large geographic areas. This geographic averaging created an implicit support flow from low-cost customers to high-cost customers.

190. *Universal Service Principles.* In the 1996 Act, Congress codified the Commission's historical policy of promoting universal service to ensure that consumers in all regions of the nation have access to telecommunications services.<sup>412</sup> Specifically, in section 254 of

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some states, incumbent LECs are able to charge above-cost rates for vertical services (e.g., touch tone, conference calling, speed dialing, call waiting, caller identification, etc.) in order to support the rates for basic local service. Fourth, incumbent LECs in some states have been able to charge relatively high intrastate access charges to interexchange carriers to cover costs not recovered through local rates. IXCs pass these access charges on to their long distance customers in the form of higher usage charges for intrastate long distance service, thus creating implicit support from long distance service to local service. In addition, some states provide explicit universal service support through direct monetary payments to carriers.

<sup>408</sup> See, e.g., *Universal Service Ninth Report and Order*, 14 FCC Rcd at 20453.

<sup>409</sup> See, e.g., *Universal Service Ninth Report and Order*, 14 FCC Rcd at 20451-52 (deferring the issue of identification and removal of implicit support in the interstate access charge system).

<sup>410</sup> See, e.g., 47 C.F.R. §§ 54.301 (Local Switching Support), 54.303 (Long Term Support) and 54.309 (Forward-looking high-cost support for non-rural carriers).

<sup>411</sup> *Access Charge Reform Order*, 12 FCC Rcd at 15992-93.

<sup>412</sup> According to the Joint Explanatory Statement, the purpose of the 1996 Act is "to provide for a pro-competitive, de-regulatory national policy framework designed to accelerate rapidly private sector deployment of advanced telecommunications and information technologies and services to all Americans by opening all (continued....)

the Act, Congress instructed the Commission, after consultation with the Joint Board, to establish specific, predictable, and sufficient mechanisms to preserve and advance universal service.<sup>413</sup> Moreover, recognizing the vulnerability of implicit support to competition, Congress directed the Commission and the states to take the necessary steps to create universal service mechanisms that would be sustainable in a competitive environment.<sup>414</sup> To achieve this end, Congress directed that universal service support “should be explicit and sufficient to achieve the purposes of [section 254].”<sup>415</sup>

191. The 1996 Act further establishes as a principle, on which we must base our universal service policies, that quality services should be available across the nation at affordable and reasonably comparable rates.<sup>416</sup> Support mechanisms should also require all providers of telecommunications services to make an equitable and nondiscriminatory contribution to the preservation and advancement of universal service.<sup>417</sup> Support mechanisms should neither unfairly advantage nor disadvantage one provider over another, and neither unfairly favor nor disfavor one technology over another.<sup>418</sup> Thus, any telecommunications carrier, using any technology, including wireless technology, is eligible to receive universal service support if it meets the criteria for “eligible telecommunications carrier” status under section 214(e)(1).<sup>419</sup>

192. In conducting universal service reform pursuant to the principles of the Act, the Commission has “broad discretion” to balance the dual goals of providing explicit and sufficient universal service support while promoting local competition.<sup>420</sup> Moreover, as long as the Commission’s universal service methodology provides sufficient support for universal service, the

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telecommunications markets to competition . . . .” Joint Explanatory Statement of the Committee of Conference, H.R. Conf. Rep. No. 458, 104th Cong., 2d Sess. at 113 (Joint Explanatory Statement).

<sup>413</sup> 47 U.S.C. § 254(a), (d); *see also Universal Service NPRM*, 11 FCC Rcd 18092.

<sup>414</sup> *See* 47 U.S.C. § 254; *see also* H. Rep. No. 204, 104<sup>th</sup> Cong., 1<sup>st</sup> Sess. 80 (1995).

<sup>415</sup> 47 U.S.C. § 254(e).

<sup>416</sup> *See* 47 U.S.C. § 254(b)(1) and (3).

<sup>417</sup> 47 U.S.C. § 254(b)(4).

<sup>418</sup> *Universal Service First Report and Order*, 12 FCC Rcd at 8802. Besides the universal service principles specified in the 1996 Act, Congress directed that the Joint Board and the Commission be guided by such other principles they determine to be consistent with the Act, and necessary and appropriate for the protection of the public interest, convenience, and necessity. 47 U.S.C. § 254(b)(7). At the recommendation of the Joint Board, the Commission adopted competitive neutrality as an additional principle for universal service. *Universal Service First Report and Order*, 12 FCC Rcd at 8801-03.

<sup>419</sup> *Universal Service First Report and Order*, 12 FCC Rcd at 8858-59.

<sup>420</sup> *Alenco v. FCC*, 201 F.3d 608, 620 (5<sup>th</sup> Cir. 2000); *Texas Office of Public Utility Counsel v. FCC*, 183 F. 3d at 412.

Commission is free to adopt a methodology that serves its other goal of encouraging local competition.<sup>421</sup>

193. *Initial Efforts to Convert Implicit Support to Explicit Support.* In the *Universal Service First Report and Order* and the *Access Charge Reform Order*, the Commission began the process of identifying and converting implicit interstate universal service support to explicit support.<sup>422</sup> The Commission determined that implicit support for universal service should be identified and removed from interstate access charges, and should be provided instead through explicit support mechanisms.<sup>423</sup> For example, as an initial step toward achieving this task, the Commission reformed the mechanism for Long Term Support (LTS).<sup>424</sup> Historically, the Commission's rules required non-pooling LECs (generally, large price cap carriers) to make contributions to the LTS mechanism, which then made explicit monetary payments to the members of the NECA pool. These non-pooling LECs recovered their contributions through increased interstate access charges. Thus, while LTS was being provided explicitly through direct monetary payments, it was being recovered implicitly through inflated interstate access charges. In order to eliminate this implicit recovery, the Commission directed that LTS be derived from an explicit federal support mechanism funded by all interstate carriers, and that non-pooling LECs reduce their interstate access charges to reflect the elimination of their obligation to contribute directly to the NECA pool.<sup>425</sup>

194. As described below, the CALLS Proposal also seeks to remove implicit universal service support from our interstate access charge regime. Unlike LTS, where there was an existing mechanism providing explicit support but allowing implicit recovery, the CALLS Proposal begins by identifying implicit universal service support still in interstate access charges, removes that support, and then creates a mechanism that allows for the explicit provision and recovery of interstate access universal service support.

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<sup>421</sup> *Texas Office of Public Utility Counsel v. FCC*, 183 F. 3d at 412.

<sup>422</sup> *Universal Service First Report and Order*, 12 FCC Rcd at 8782; *see generally Access Charge Reform Order*, 12 FCC Rcd 15982.

<sup>423</sup> *Universal Service First Report and Order*, 12 FCC Rcd at 8786, 9163-66; *Access Charge Reform Order*, 12 FCC Rcd at 15986-87.

<sup>424</sup> The LTS mechanism supports carriers with higher-than-average loop costs by providing LECs that are members of the NECA pool (generally, small non-price cap carriers) with enough support to enable them to charge a nationwide average CCL interstate access rate element. *Universal Service First Report and Order*, 12 FCC Rcd at 8893.

<sup>425</sup> *Universal Service First Report and Order*, 12 FCC Rcd at 9169.

### 3. The Calls Proposal: Interstate Access Universal Service Support

#### a. Overview

195. CALLS proposes the establishment of an explicit interstate universal service support mechanism that will provide support to replace \$650 million of annual implicit support currently collected through interstate access charges, which is being phased out as part of the CALLS Proposal's common line restructuring.<sup>426</sup> In contrast to the Commission's existing high-cost support mechanisms for rural and non-rural carriers, which provide support to enable states to ensure reasonable comparability of *intrastate* rates, the purpose of the new federal interstate access universal service support mechanism is to provide explicit support to replace the implicit universal service support in *interstate* access charges. As explained below, the new mechanism provides support to carriers serving lines in areas where they are unable to recover their permitted revenues from the newly revised SLCs.

196. Under the CALLS Proposal, in any geographically deaveraged UNE zone where the average common line revenue per line for that zone would exceed a benchmark of \$7.00 per line for residential and single-line business lines and a benchmark of \$9.20 per line for multi-line business lines, the interstate access support mechanism would provide support for a portion of the difference between permitted common line revenue and the benchmarks.<sup>427</sup> Although the aggregate difference between permitted common line revenue per line and the benchmarks exceeds \$650 million, CALLS employs a series of formulas to pro rate the amount of interstate access support so that it does not exceed \$650 million per year.<sup>428</sup> The amount of interstate access support provided in each study area is also adjusted on a phased-in basis so that by July 1, 2003, CCL charges and multi-line business PICCs will be eliminated for most customers served by price cap LECs.<sup>429</sup> This interstate access support will be portable to competing eligible telecommunications carriers and targeted to areas with the greatest differential between permitted common line revenue and the benchmarks. In addition, the CALLS Proposal would increase the maximum amount of federal Lifeline support provided under our existing rules in order to match the increase in the new residential SLC, thus shielding low-income consumers from the cost of the increased residential SLC.<sup>430</sup>

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<sup>426</sup> Modified Proposal at § 2.0.

<sup>427</sup> Modified Proposal at § 2.0. The SLC cap on non-primary residential lines and single-line business lines is set at \$7.00, and the SLC cap on multi-line business lines is set at \$9.20. Although the maximum residential SLC cap changed from \$7.00 in the Original CALLS Proposal to \$6.50 in Modified Proposal, the CALLS members continue to use \$7.00 for purposes of allocating interstate access support to each price cap LEC's service area to maintain consistency of benchmarks between primary and non-primary residential lines. See CALLS *ex parte* statement of April 14, 2000.

<sup>428</sup> Modified Proposal at § 2.0.

<sup>429</sup> Modified Proposal at § 2.0.

<sup>430</sup> Modified Proposal at § 2.1.2.3. Additional Lifeline support is estimated to be \$60 million for the first year of the plan.

197. As discussed in Section IV above, in this Order, we provide price cap LECs the opportunity to choose between the rate levels that are part of the CALLS Proposal, including the \$650 million interstate access universal service support mechanism, or to elect to submit to a cost study based on forward-looking economic cost that would be the basis for reinitializing rates to the appropriate level. In addition, as discussed in Section IV above, we plan to review any increases to residential and single-line business SLC caps above \$5.00 to verify that any such increases are appropriate and reflect higher costs where they are to be applied. Given the relationship between access charges and the interstate access universal service support mechanism, in the event that a price cap LEC elects to participate in the cost-study proceeding, we will consider the sufficiency of the support mechanism, including both the size and distribution of support, concurrently with the SLC cap proceeding. Any adjustments to the support mechanism shall be consistent with the principles that support should be explicit, portable and competitively neutral.

**b. Size of the Interstate Access Universal Service Support Mechanism**

**(i) Background**

198. CALLS proposes that the interstate access universal service support mechanism be sized at \$650 million.<sup>431</sup> This amount is fixed under the CALLS Proposal for five years.<sup>432</sup> According to the proponents of the CALLS Proposal, the size of the proposed interstate access universal service support mechanism is the product of negotiation between parties with adverse interests, *i.e.*, large IXC's, who are the biggest contributors to universal service, and certain large LECs, such as GTE and BellSouth, who are the biggest recipients of universal service support.<sup>433</sup> CALLS points out that a support mechanism sized at \$650 million is well within the estimates of existing implicit support in interstate access charges that have been filed with the Commission.

199. For example, the United States Telecom Association ("USTA"), estimated that based on embedded costs, current interstate common line rates contained \$3.9 billion in implicit universal service support.<sup>434</sup> In another estimate based on embedded costs, William Rogerson, the Commission's Chief Economist at the time, and Senior Economist Evan Kwerel estimated that interstate access charges contained \$1.9 billion in implicit universal service support, assuming that

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<sup>431</sup> See Modified Proposal at § 2.2.1. This amount does not include administrative expenses recovered pursuant to 47 C.F.R. 54.709. See Section IV.C.3.f *infra*.

<sup>432</sup> Modified Proposal at § 2.2.1.

<sup>433</sup> See CALLS Supp. Reply at 25; GTE Supp. Comments at 11-12.

<sup>434</sup> USTA Comments, CC Docket Nos. 96-45 and 96-262 (filed July 23, 1999). The level of implicit support estimated using USTA's methodology, however, would be lower using the SLC rates that are described in the Modified Proposal.

residential SLCs were capped at \$ 6.50 per month.<sup>435</sup> On the other hand, the HAI model, relying on forward-looking costs, has been used to estimate implicit support in interstate common line elements of approximately \$250 million.<sup>436</sup>

200. Moreover, according to CALLS, a support mechanism sized at \$650 million is consistent with AT&T's estimate of implicit support based on forward-looking costs.<sup>437</sup> Using the Commission's synthesis model<sup>438</sup> with the Commission's common inputs as of June 2, 1999, AT&T concluded that \$650 million is a reasonable estimate of the interstate portion of forward-looking loop and port costs exceeding a maximum residential and single-line business SLC of \$7.00 and multi-line business SLC of \$9.20.<sup>439</sup>

## (ii) Discussion

201. We find that the \$650 million interstate access universal service support mechanism proposed by CALLS satisfies section 254's goals that universal service support be

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<sup>435</sup> Rogerson and Kwerel also estimated implicit support to be \$3.2 billion at a residential SLC cap of \$4.50 per month. *See A Proposal for Universal Service and Access Reform*, Rogerson and Kwerel, CC Docket Nos. 96-45 and 96-262 (filed May 27, 1999).

<sup>436</sup> This estimate was provided by AT&T using the HAI Model Version 5.0a. *See CALLS Reply* at 11 n. 20 (citing HAI Model Version 5.0a, Docket No. 96-45, using SLC caps of \$7.00 for residential and single line business lines and \$9.20 for multi-line business lines and FCC Common Inputs as of March 10, 1999). The HAI model uses a series of algorithms designed to estimate the cost of building a telephone network. *See Universal Service Tenth Report and Order*, 14 FCC Rcd at 20162.

<sup>437</sup> *See Declaration of Joel E. Lubin, Modified Proposal, Appendix D.*

<sup>438</sup> The Commission's synthesis model is a series of algorithms that allow the user to estimate the cost of building a telephone network. *See generally* Federal State Joint Board on Universal Service, and Forward-Looking Mechanism for High-Cost Support for Non-Rural LECs, Fifth Report and Order, CC Docket No. 96-45, Fifth Report and Order, 13 FCC Rcd 21323 (1998) (*Universal Service Fifth Report and Order*); *Universal Service Tenth Report and Order*, 14 FCC Rcd at 20162-64.

<sup>439</sup> According to CALLS, AT&T used the following methodology to arrive at the \$650 million estimate:

AT&T aggregated the serving wire centers in each price cap LEC study area into three cost zones: low, medium and high, such that the number of lines in each cost zone were roughly equal. Then, AT&T used the FCC's Synthesis Model with FCC inputs as of June 2, 1999, to calculate the unseparated forward-looking costs of the loop and ports in all zones. AT&T then applied a 25% separations factor against the unseparated forward-looking costs of the loop and port, and compared 25% of the average forward-looking cost within each cost zone against a maximum affordable SLC of \$7 per residence and single line business line, and \$9.20 per multi-line business. To the extent that the forward-looking costs in a high-cost zone exceeded the SLC cap, the difference between 25% of the projected loop and port cost and the applicable SLC cap represents the amount to be funded by the Interstate Access-Related High-cost Fund. When summed across all zones in all price cap LEC study areas, the total forward-looking cost-based estimate of implicit support to be funded through the Interstate-Access-related USF is \$613 million. On the basis of this analysis, [AT&T] concluded that \$650 million would be a reasonably conservative estimate.

*See CALLS NPRM, Appendix C, 14 FCC Rcd at 16977.*

explicit as well as specific, predictable, and sufficient. By fixing the amount of support at \$650 million per year for five years, the CALLS Proposal provides a specific and predictable amount of explicit support.<sup>440</sup> In addition, we believe that this amount is sufficient to keep rates affordable and reasonably comparable. As the Fifth Circuit observed, section 254(e) is ambiguous as to what constitutes “sufficient” support, and thus the Commission must use its expertise and informed judgment to make a reasonable determination concerning the sufficiency of explicit universal service support.<sup>441</sup> The record in this proceeding, as well as our experience, reveals that identifying an amount of implicit support in our interstate access charge system to make explicit is an imprecise exercise. The various implicit support flows (*e.g.*, business to residential, high-volume to low-volume, and geographic rate averaging) are not easily severable and quantifiable. Moreover, the competitive pricing pressures present during this transitional period between monopoly and competition present additional complexities in identifying a specific amount of implicit support. Thus, we recognize that different estimates of this amount each may be considered reasonable.

202. We are persuaded, however, that at this time \$650 million is a reasonable estimate of the amount of universal service support that currently is in our interstate access charge regime. This estimate falls within the range of estimates that have been submitted in the universal service proceeding.<sup>442</sup> We also agree with the CALLS proponents who argue that the negotiated nature of the \$650 million estimate provides strong evidence that \$650 million will be sufficient, though not excessive, to ensure affordable and reasonably comparable rates.<sup>443</sup> CALLS includes companies such as AT&T and Sprint who, with MCI and other IXCs, pay the lion’s share of universal service contributions, as well as companies such as Bell Atlantic and SBC who provide local service in areas that tend to be lower cost to serve on average and who therefore are net payers of universal service contributions. As net payers, these carriers have incentives to minimize the size of universal service support mechanisms. Companies such as BellSouth, GTE, and Sprint Local, on the other hand, provide service in areas that generally have higher costs and therefore are usually net recipients of universal service support. As net recipients of universal service support, these LECs have incentives to maximize the size of the universal service support mechanisms. Because of the divergent interests of these parties, we believe that \$650 million represents a sufficient amount of explicit universal service support to replace the implicit support that has been removed from access charges, and should ensure affordable and reasonably comparable rates.

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<sup>440</sup> See 47 U.S.C § 254(e).

<sup>441</sup> *TOPUC v. FCC*, 183 F.3d at 425-26.

<sup>442</sup> The record in our universal service proceeding illustrates that there can be substantial variations in model-produced estimates of forward-looking costs, and therefore estimates of the amount of universal service support that is implicit in our interstate access regime. This largely is due to variations in model inputs. Estimates vary due to the cost of capital, depreciation rates, the number of entities sharing telephone poles, and the actual location of customers. See *Universal Service Fifth Report and Order*, 13 FCC Rcd 21323.

<sup>443</sup> CALLS Reply Comments at 11.

203. Consistent with our obligations under section 254, we emphasize that reforming access charges and creating an interstate access universal service support mechanism sized at \$650 million is a necessary first step on the path to a more competitive telecommunications marketplace. As discussed above, we will revisit the size and operation of this mechanism before the end of the five-year plan as part of any changes we make to access charges as a result of a price cap LEC cost study. Otherwise, we agree with commenters who suggest that this estimate should be reevaluated at the end of the five-year plan to determine the sufficiency of the fund based on the development of competition and market-based pricing.<sup>444</sup> At that time, we will make any adjustment to the fund that is necessary to ensure that such funding is sufficient, yet not excessive, to keep rates in high-cost areas affordable and reasonably comparable to rates in areas with greater population density.<sup>445</sup> Because we plan to reevaluate the size of the interstate access universal service mechanism, and because creation of this mechanism is a necessary first step to remove implicit support from our interstate access charge regime, we decline commenters' suggestions that we delay implementation of the mechanism pending further evaluation.<sup>446</sup>

204. Some commenters argue that the size of the interstate access universal service mechanism is too large.<sup>447</sup> Other commenters argue that the size of the interstate access universal service support mechanism is too small.<sup>448</sup> Still other commenters argue that the \$650 million estimate is not based on a reasonable measure of price cap LECs' forward-looking costs.<sup>449</sup> These commenters also argue that not all CMT revenues arise due to the provision of universal service, and thus the FCC must undertake a detailed examination of price cap LECs' rates and costs to determine the proper amount of implicit universal service support that should be recovered through the interstate access universal service support mechanism.<sup>450</sup> The estimates from parties commenting on the CALLS Proposal range from \$300 million<sup>451</sup> to \$1.2 billion.<sup>452</sup> For example,

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<sup>444</sup> See, e.g., MCI Comments at 4.

<sup>445</sup> See *Alenco v. FCC*, 201 F.3d at 620 (observing that “excessive funding may itself violate the sufficiency requirements of the Act. . . . Because universal service is funded by a general pool subsidized by all telecommunications providers—and thus indirectly by the customers—excess subsidization in some cases may detract from universal service by causing rates unnecessarily to rise, thereby pricing some consumers out of the market.”)

<sup>446</sup> See e.g., Joint Board Supp. Comments at 6; California Commission Supp. Comments at 6.

<sup>447</sup> ALTS and Time Warner Supp. Comments at 17 (arguing for a \$300 million interstate access mechanism); California Commission Supp. Comments at 6.

<sup>448</sup> Montana Commission Supp. Comments at 2; Wyoming Commission Supp. Comments at 2-3; U S West Supp. Reply at 1 (advocating a \$1.2 billion interstate access universal service support mechanism).

<sup>449</sup> California Commission Supp. Comments at 6; MCI Comments at 4; Ohio Commission Comments at 21; Joint Consumer Commenters Supp. Comments at 17; Washington Commission Comments at 6.

<sup>450</sup> California Commission Supp. Comments at 5-6;

<sup>451</sup> ALTS and Time Warner Supp. Comments at 17.

ALTS and Time Warner merely assert, without any empirical support, that the interstate access universal service support mechanism would be more appropriately sized at \$300 million.<sup>453</sup> U S West, on the other hand, estimates support at \$1.2 billion. U S West's effort to quantify interstate access universal service support illustrates the difficulty in calculating a precise amount of implicit universal service support that should be recovered through the interstate access universal service support mechanism. For example, U S West's estimate assumes a multi-line business SLC of \$6.50, rather than \$9.20.<sup>454</sup> Therefore, U S West's estimate fails to account for a significant amount of revenue that will be recovered through the multi-line business SLC, and thus does not need to be recovered through the interstate access universal service support mechanism. Although we do not believe these alternative estimates are more reliable than CALLS' \$650 million estimate, we find that the range of these estimates by parties with adverse interests supports the reasonableness of an interstate access universal service support mechanism sized at \$650 million per year.

205. We also reject suggestions by commenters<sup>455</sup> that the proposed \$650 million interstate access universal service support mechanism is excessive because it was designed to cover the "gap" between capped end user charges and LEC permitted revenues under price caps based on embedded costs. Under the universal service distribution formulas, as discussed below, the difference between price cap LEC permitted revenue and the SLC benchmarks exceeds the \$650 million cap on the interstate access universal service support mechanism. Nevertheless, price cap LECs, who are the largest net recipients of universal service support, have agreed that \$650 million provides adequate interstate access universal service support. Thus, we agree with CALLS and the Massachusetts Department of Telecommunications and Energy<sup>456</sup> that the \$650 million is a reasonable, yet not excessive, estimate of the amount necessary to provide sufficient universal service support to ensure affordable and reasonably comparable end-user rates.

### **c. Distribution of Interstate Access Support**

#### **(i) Background**

206. The methodology for distributing interstate access universal service support consists of a series of mathematical formulas that measure the difference between CMT revenue under price caps and benchmarks based on the new SLC caps.<sup>457</sup> These formulas compare price cap LEC CMT revenue per line to the SLC benchmarks at both the study area and UNE zone levels. These formulas target interstate access support to the study areas and UNE zones with the

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<sup>452</sup> U S West Supp. Comments at 7.

<sup>453</sup> ALTS and Time Warner Supp. Comments at 17.

<sup>454</sup> See U S West Supp. Comments at 8.

<sup>455</sup> See, e.g., Cable & Wireless Comments at 5.

<sup>456</sup> See Mass. DTE Comments at 5.

<sup>457</sup> See Modified Proposal at § 2.2.3-2.2.6; Appendix B §§ 54.800-54.807.

greatest difference between CMT revenue and the SLC benchmarks.<sup>458</sup> Because UNE zone prices, and the resulting CMT revenues, are based on costs, this methodology is designed to direct greater amounts of support to higher cost areas. Specifically, an amount up to the first \$75 million is allocated to study areas where the study area average revenue requirement per line is above the SLC benchmarks.<sup>459</sup> These study areas also receive priority for distribution of the remaining interstate access support. After distribution of up to the first \$75 million, the remaining interstate access support is distributed to carriers serving UNE zones where the UNE zone average CMT revenue per line is above the SLC benchmarks. To maintain the \$650 million cap, the distribution formulas also account for growth in the number of lines eligible to receive universal service support during the course of the year.<sup>460</sup>

207. To distribute the \$650 million of interstate access support among service areas served by price cap LECs, the CALLS Proposal derives a specific and separate amount of interstate access support for certain price cap LEC study areas and UNE zones on a per-line basis.<sup>461</sup> These per-line support amounts are known as Interstate Access Universal Service Support Per Line.<sup>462</sup> To calculate these amounts, the CALLS Proposal proposes the following seven steps.

- (1) *Study Area Average Price Cap CMT Revenue Per Line Per Month.* To calculate this amount, the CALLS Proposal starts with the prior year price cap CMT revenue per line,<sup>463</sup> adjusts it for exogenous costs, and multiplies it by the base period lines.<sup>464</sup> For

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<sup>458</sup> In this proceeding, the SLC “benchmarks” are used to quantify the relative differential between the maximum revenue recoverable through the SLC caps and a price cap LEC’s permitted CMT revenue. The CALLS Proposal targets support to areas with the greatest differential between these two measures. By contrast, in the high-cost proceeding for non-rural carriers, we adopted a support mechanism that compares the estimated state-wide average intrastate-allocated costs of providing universal service to a national benchmark set at 135 percent of the national average intrastate-allocated cost of providing universal service. *See Universal Service Ninth Report and Order*, 14 FCC Rcd at 20463-64. The non-rural high-cost support mechanism targets support to areas with the greatest costs relative to the national benchmark.

<sup>459</sup> This \$75 million is phased-in in the first two years of the plan. *See MAA Phase In Percentage*, Appendix B § 54.800 (e).

<sup>460</sup> Appendix B § 54.807. If reported line growth were to exceed projected line growth, the interstate access universal service support mechanism could slightly exceed \$650 million in a particular year. If reported line growth is less than projected line growth, the interstate access universal service support mechanism could be slightly below \$650 million in a particular year.

<sup>461</sup> Modified Proposal at §§ 2.2.2.-2.2.3; Appendix B §§ 54.800(m); 54.806(i) and (j); and 54.807.

<sup>462</sup> Appendix B § 54.807. The per line support amount is derived by dividing a price cap LEC’s study area universal service support (SAUSS), Appendix B § 54.800(m), by twelve months and all eligible telecommunications carriers’ base period lines in such study area. *See Appendix B § 54.807.*

<sup>463</sup> Price cap common line, marketing, and transport interconnection charge (TIC) revenue (collectively, CMT Revenue) is the total revenue a filing entity would be permitted to receive for SLCs, PICCs, and CCL charges, including marketing expenses presently collected pursuant to 47 C.F.R. § 69,156(a), and residual interconnection charge revenues collected through PICCs, but it does not include the current recovery of incumbent LEC (continued....)

price cap LECs that do not have study area specific common line rates (*i.e.*, SLC, PICC, and CCL charge that are study area specific), CMT revenue for the filing entity is allocated to study areas based on the base factor portion (BFP) costs for each study area.<sup>465</sup>

(2) *Preliminary Minimum Access Universal Service Support.* To determine this amount, the CALLS Proposal calculates the amount by which study area Average Price Cap CMT Revenue exceeds the revenue allowed under the \$7.00 and \$9.20 SLC benchmarks.<sup>466</sup>

(3) *Zone Average Revenue Per Line.* To calculate interstate access support levels on a geographically zoned basis, using UNE loop pricing zones where such zones exist,<sup>467</sup> deaveraged price cap common line revenue per line is calculated for each zone.<sup>468</sup>

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universal service contributions that are first removed from existing price cap baskets. See Modified Proposal at §2.1.1.1.

<sup>464</sup> See Appendix B § 54.800(a); 47 C.F.R. § 61.3(d). This is done prior to Tariff Review Plan (TRP) preparation.

<sup>465</sup> See Appendix B § 54.800(a).

<sup>466</sup> Modified Proposal at § 2.2.2. To derive this amount, the Administrator must perform the following calculations:

(a) If Average Price Cap CMT Revenue Per Line Per Month<sub>Study Area</sub> is greater than \$9.20 then: Preliminary Minimum Access USF<sub>study area</sub> = (Average Price Cap CMT Revenue Per Line Per Month<sub>study area</sub> x ILEC Base Period Lines x 12) - ((\$7.00 x ILEC Base Period Residential & Single Line Business Lines<sub>study area</sub> x 12) + (\$9.20 x ILEC Base Period Multi-line Business Lines<sub>study area</sub> x 12));

(b) If Average Price Cap CMT Revenue Per Line Per Month<sub>Study Area</sub> is greater than \$7.00 but less than \$9.20 then: Preliminary Minimum Access USF<sub>study area</sub> = (Average Price Cap CMT Revenue Per Line Per Month<sub>Study Area</sub> - \$7.00) x (ILEC Base Period Residential & Single Line Business Lines<sub>study area</sub> x 12); and,

(c) If Average Price Cap CMT Revenue Per Line Per Month<sub>Study Area</sub> is less than \$7.00 then the Preliminary Minimum Access USF<sub>study area</sub> is zero.

Appendix B § 54.804.

<sup>467</sup> Modified Proposal at § 2.2.3; Appendix B §§ 54.805. According to CALLS, where a state has not yet established geographically deaveraged UNE loop pricing zones, CALLS proposes the following:

the Universal Service Administrator would preliminarily calculate the potential universal service support for price cap LEC study areas within that state using a model or other appropriate tool, and roughly apportion lines by wire center into three zones with relatively equal numbers of lines. Those zones are used as a “placeholder” to size, but not actually distribute, the relative share of universal service support going to a given state.

See CALLS NPRM, Appendix C, 14 FCC Rcd at 16980 n. 65 (citing Original Proposal at 2.2.3.1.1(b)).

- (4) *Study Area Above Benchmark Revenues.* Zone Average Revenue Per Line is then compared to the \$7.00 residential and single-line business benchmark and the \$9.20 multi-line business benchmark to derive Zone Above Benchmark Revenue.<sup>469</sup> Zone Above Benchmark Revenue for each zone in a study area is then summed to arrive at Study Area Above Benchmark Revenue.<sup>470</sup>
- (5) *Study Area Access Universal Service Support (SAUSS).* To calculate SAUSS, the CALLS Proposal first provides for the calculation of Preliminary Study Area Universal Service Support (PSAUSS) and the Minimum Support Requirement (MSR).<sup>471</sup>
- (a) *PSAUSS.* To derive PSAUSS, the CALLS Proposal (1) sums Study Area Above Benchmark Revenue from each price cap LEC to derive Nationwide Total Above Benchmark Revenues, (2) divides \$650 million by the Nationwide Total Above Benchmark Revenues to get the Adjustment Factor, and (3) multiplies the Study Area Above Benchmark Revenues by the Adjustment Factor to derive PSAUSS.<sup>472</sup> These calculations are designed to limit interstate access universal service support to the \$650 million cap.
- (b) *MSR.* To derive MSR, the CALLS Proposal (1) compares Preliminary Minimum Access Universal Service Support to PSAUSS to derive the Minimum Delta, (2) sums the Minimum Delta amounts of each price cap LEC to derive Total National Minimum Delta, (3) calculates a Minimum Adjustment Amount (MAA),<sup>473</sup> and (4) adds the MAA to the PSAUSS to get the MSR for study areas with minimum support requirements.<sup>474</sup> The MSR is designed to target interstate access universal service support to study areas most in need of support. Finally,

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<sup>468</sup> Modified Proposal at § 2.1.1.3; Appendix B § 54.805. The relative price cap revenue per line in each zone reflects the relative UNE rates in that zone, and the level of revenue per line in each zone is such that the price cap LEC can recover total permitted price cap common line revenues. See Modified Proposal at 2.2.3.2; Appendix B § 54.800(q).

<sup>469</sup> Modified Proposal at § 2.2.3.1.1; Appendix B § 54.805.

<sup>470</sup> Modified Proposal at § 2.2.3.1.2; Appendix B § 54.805.

<sup>471</sup> Modified Proposal at § 2.2.3.2; Appendix B § 54.806.

<sup>472</sup> Modified Proposal at § 2.2.3.2; Appendix B § 54.806(c).

<sup>473</sup> The MAA is one of the following: (1) if the Total National Minimum Delta is greater than \$75 million, MAA equals the Minimum Delta multiplied by the current phase-in percentage; or (2) if the Total National Minimum Delta is less than \$75 million, MAA equals the Minimum Delta times the current phase-in percentage. See Appendix B § 54.806(f).

<sup>474</sup> See Appendix B § 54.806(g).

the PSAUSS for study areas that do not have an MSR must be adjusted to account for the distribution of the MSR.<sup>475</sup>

(6) *Interstate Access Universal Service Support Per Line.* To derive a per line support amount per month, SAUSS is allocated as follows:

(a) *Study Areas Without UNE Pricing.* In any study area within which the price cap LEC has not established state approved geographically deaveraged UNE loop rates, SAUSS is divided by twelve and by the total number of eligible telecommunications carriers' base period lines.<sup>476</sup>

(b) *Study Areas With UNE Pricing.* If UNE loop rates have been established, a per line support amount is calculated by allocating SAUSS to UNE zones first to the lines in the zones with the greatest differential between Zone Average Revenue Per Line<sup>477</sup> and the SLC benchmarks, "cascading" to lines in zones with lower differentials to the extent that funding remains available.<sup>478</sup>

(7) *Distribution of Interstate Access Universal Service Support Per Line.* Interstate Access Universal Service Support Per Line is distributed to all eligible telecommunications carriers based on their reported lines.<sup>479</sup>

## (ii) Discussion

208. Although there may be several methodologies by which the \$650 million of interstate access universal service support could be distributed, we conclude that the distribution methodology proposed by CALLS is reasonable and satisfies the universal service principles of

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<sup>475</sup> To adjust the PSAUSS, the CALLS Proposal (1) sums the MSR amounts to get Total National Minimum Support Requirements (Total National MSR) for areas with MSRs, (2) subtracts this amount from \$650 million to get funds available for study areas with no MSR, (3) sums PSAUSS amounts for study areas with no MSR, (4) divides the funds available from (2) by (3) to obtain the PSAUSS adjustment factor, and (5) multiplies PSAUSS by the PSAUSS adjustment factor to get SAUSS for study areas with no MSR. See Appendix B § 54.806(c).

<sup>476</sup> Modified Proposal at § 2.2.4.1; Appendix B §54.807(b). The base period lines for the relevant quarter are adjusted for growth.

<sup>477</sup> See Appendix B § 54.800(q).

<sup>478</sup> See Modified Proposal at § 2.2.4.1; Appendix B § 54.807(c). Because interstate access support is capped and does not allow each price cap LEC to recover all of its common line price cap revenue shortfall created by the new SLC caps and geographic rate deaveraging, the CALLS Proposal suggests this cascading distribution methodology to ensure that interstate access universal service support is made available first to eligible telecommunications carriers serving customers in the zones with the greatest differential between CMT revenue and the SLC benchmarks

<sup>479</sup> See Appendix B § 54.807.

the 1996 Act. Accordingly, for the reasons discussed below, we adopt the distribution methodology proposed by CALLS.

209. Through a series of mathematical formulas, the CALLS distribution methodology calculates a per-line support amount for a particular UNE zone. This per-line support amount is portable among competing eligible telecommunications carriers. In other words, if a competitor serves a customer in a supported study area or UNE zone, the competitor will receive the incumbent's support for that line. Moreover, as described below,<sup>480</sup> this per-line support amount will be published regularly by the Universal Service Administrative Company (USAC). Thus, both incumbents and competitors will know the per-line support amounts available for serving customers in a particular area, and can plan their business strategies accordingly.

210. Taken together, these features satisfy the concerns raised by the state members of the Joint Board that the interstate access universal service mechanism be consistent with the universal service principles of specificity, predictability, and competitive neutrality.<sup>481</sup> By calculating per-line support for lines served in a particular UNE zone, the CALLS methodology provides a specific amount of support for each line served by eligible telecommunications carriers in that zone. The CALLS methodology also provides predictable support because the total amount of interstate access universal service support is fixed at \$650 million for the five year life of the proposal<sup>482</sup> and the distribution of that support can be predetermined and published for a particular period based on the distribution formulas. Because the support provided under the CALLS proposal is portable among all eligible telecommunications carriers serving a supported customer, regardless of whether they are incumbents or competitors and regardless of the technology they use, the distribution methodology is competitively neutral.

211. Some commenters, however, criticize various aspects of the distribution methodology and suggest that we modify the methodology to address their concerns. U S West and the Washington Commission propose that universal service support be targeted to smaller geographic areas than UNE zones.<sup>483</sup> We recognize that targeting interstate access universal service support to levels more geographically deaveraged than the UNE zone level could, in theory, provide a more precise means of distributing universal service support than under the CALLS Proposal.<sup>484</sup> The distribution methodology in the interstate access support mechanism

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<sup>480</sup> See Section IV.C.3.f *infra*.

<sup>481</sup> See Joint Board Supp. Comments at 6.

<sup>482</sup> See Section IV *supra* discussing the optional forward-looking cost study.

<sup>483</sup> Washington Commission Comments at 4-5; U S West Supp. Comments at 5 (requesting distribution of universal service support targeted to density zones with less than five lines per square mile).

<sup>484</sup> Indeed, in reforming our high-cost universal service support mechanism for non-rural carriers, we chose to distribute support using a wire-center approach. See *Universal Service Ninth Report and Order*, 14 FCC Rcd at 20471. The support provided by that mechanism is designed to assist states in achieving reasonable comparability of *intrastate* rates within their borders by ensuring that no state faces costs significantly above the average among states nationwide. See *Universal Service Ninth Report and Order* 14 FCC Rcd at 20463. By contrast, the goal of the instant proceeding is to remove implicit universal service support from *interstate* access (continued....)

proposed by CALLS, however, cannot be viewed in isolation. Rather, it is but one piece of a larger effort at comprehensive reform for interstate access charges and universal service. The decision to deaverage interstate access universal service support to the UNE zone is directly linked to deaveraging SLCs to the UNE zone and the UNE-zone pricing requirements of the Commission's rules. Altering the interstate access universal service distribution methodology to accomplish a greater degree of geographic deaveraging would create dissonance between the universal service and access charge reforms achieved by the CALLS Proposal, which, taken as a whole, are reasonable.

212. U S West further argues that the distribution mechanism is not predictable because any change in UNE deaveraging will shift the allocation of universal service support among support recipients.<sup>485</sup> U S West maintains that such volatility in a universal service distribution methodology violates the 1996 Act's principle of predictability. We disagree. We do not believe that the statutory principle of predictability necessitates the level of certainty or permanence that U S West appears to be seeking. Support amounts provided under all of our universal service support mechanisms are intentionally subject to change to some degree, depending on the variables used to calculate support (*e.g.*, line counts, costs reported by carriers, UNE rates, etc.). This dynamic feature of our support mechanisms is necessary to ensure that support is provided in amounts commensurate with the recipient's needs. Although support amounts may change as the underlying variables change, the amounts are predictable because support can be precisely determined based on a given set of variables. Moreover, we do not expect that states will adjust their UNE zones so often and by such great magnitudes that the changes would render the interstate access universal service support mechanism unpredictable. Furthermore, U S West, and any other concerned carriers, can work with state commissions to address their concerns about fixing UNE zone rates.

213. MCI argues that the distribution formulas should be adjusted to target support in greater proportion to areas that have higher multi-line business SLCs, rather than to areas that have lower multi-line business PICCs.<sup>486</sup> While MCI's approach would lead to lower average multi-line business PICC rates sooner, multi-line business PICC rates will fall dramatically in any event under the CALLS Proposal.<sup>487</sup> Thus, we find no reason to adjust the distribution methodology based on MCI's claims.

(Continued from previous page) \_\_\_\_\_  
charges and replace it with explicit support. In achieving the different goals of these two proceedings, it does not necessarily follow that we must adopt support methodologies that mirror each other. So long as the support mechanisms that we adopt are consistent with the principles of the 1996 Act, we have the discretion to craft those mechanisms in the manner that best suits the needs of the particular proceeding before us. *See Alenco v. FCC*, 201 F.3d at 620

<sup>485</sup> U S West Supp. Comments at 9-10. For example, in the case of Colorado, U S West argues that a shift to more averaged UNE rates would dramatically reduce the amount of universal service funding allocated to that state from \$60 million to only \$12 million. U S West Supp. Comments at 10.

<sup>486</sup> MCI Supp. Comments at 29.

<sup>487</sup> *See* CALLS Supp. Reply at 28.

**d. Lifeline****(i) Background**

214. The Commission's Lifeline Assistance program provides federal universal service support to reduce the monthly service charges paid by qualifying low-income customers. There are three tiers of federal Lifeline support that provide up to a maximum of \$7.00 of support.<sup>488</sup> The first tier is the federal baseline Lifeline support amount of \$3.50 per qualifying low-income consumer,<sup>489</sup> which is designed to offset the SLC, currently capped at \$3.50. If the state commission in a particular state approves an additional reduction of \$1.75 in the amount paid by consumers, a second tier of federal Lifeline support in the amount of \$1.75 is made available to the carrier providing Lifeline service to that customer.<sup>490</sup> Finally, a third tier of up to \$1.75 in federal support is available to match 50 percent of any additional state support.<sup>491</sup>

215. The CALLS Proposal would increase Lifeline support for low-income consumers to offset the increase to the residential SLC cap. Under the CALLS Proposal, the first tier of Lifeline support equals the tariffed rate in effect for the primary residential end-user common line charge for qualifying low-income consumers.<sup>492</sup> Today, Lifeline consumers pay no SLC, but must pay IXC-billed PICC recovery charges, unless the IXC voluntarily waives that fee. Under the CALLS Proposal, the entire SLC is waived through a modification of first-tier Lifeline support, and the residential PICC is eliminated.<sup>493</sup> In addition, the LEC signatories to the CALLS Proposal have also agreed not to assess universal service charges on Lifeline customers.<sup>494</sup>

**(ii) Discussion**

216. We adopt the CALLS Proposal that any increase in the SLC be accompanied by a corresponding increase to the first tier of federal Lifeline support by the amount necessary to cover any increase in the SLC. Such an increase in support is consistent with the principles of the 1996 Act as outlined in our *Universal Service First Report and Order* because it will provide sufficient support to ensure that qualifying low-income consumers have access to telecommunications services at affordable and reasonably comparable rates.<sup>495</sup> Without such an

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<sup>488</sup> Appendix B § 54.403(a).

<sup>489</sup> Appendix B § 54.403(a).

<sup>490</sup> Appendix B § 54.403(a).

<sup>491</sup> See Appendix B § 54.403(a)(1).

<sup>492</sup> See Appendix B § 54.403(a)(1).

<sup>493</sup> Modified Proposal at § 2.1.2.3.

<sup>494</sup> *Wallman March 30 Letter* at 3.

<sup>495</sup> *Universal Service First Report and Order*, 12 FCC Rcd at 8954.

increase in Lifeline support, the CALLS Proposal would negatively and disproportionately affect low-income subscribers by increasing the cost of basic telephone service. Consistent with the Commission's decision in the *Universal Service First Report and Order*, this first-tier Lifeline support shall be available to any eligible telecommunications carrier serving a qualifying low-income consumer, regardless of whether the carrier charges a SLC or is a CALLS signatory.<sup>496</sup> As the Commission stated in the *Universal Service First Report and Order*, an incumbent LEC's SLC is a reasonable proxy for the interstate portion of other eligible telecommunications carriers' costs, and providing first-tier Lifeline support to all eligible telecommunications carriers is a competitively neutral way to encourage such carriers to serve qualifying low-income consumers.<sup>497</sup> We estimate that the increased Lifeline support associated with the CALLS Proposal will be approximately \$60 million in the first year of the plan and will gradually increase to approximately \$125 million in the fifth year of the plan.<sup>498</sup>

217. Some commenters question whether the increase in tier-one Lifeline support under the CALLS Proposal would be offset by changes to other tiers of Lifeline program. Other commenters question whether the increase in Lifeline support is included in the \$650 million interstate access universal service support mechanism, or whether the increase in Lifeline support is separate from and in addition to the \$650 million support mechanism. We clarify that tier-one Lifeline support proposed by CALLS does not affect the other tiers of Lifeline support and is not part of the \$650 million interstate access universal service support mechanism.<sup>499</sup> The additional Lifeline support required by CALLS will be collected and disbursed through the normal operation of the Commission's universal service contribution methodology, which, consistent with section 254 of the Act, assesses contributions on all interstate telecommunications carriers.

#### **e. LEC Recovery of Universal Service Contributions**

##### **(i) Background**

218. The CALLS Proposal provides that as of July 1, 2000, price cap LECs will establish a separate rate element (*e.g.*, line item) to recover all contributions to the universal service support mechanisms.<sup>500</sup> The CALLS Proposal allows a price cap LEC to assess this rate element on a per-line basis or as a percentage of interstate end-user revenues, and, at the option of the carrier, it may be combined for billing purposes with other end-user rate elements.<sup>501</sup> As

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<sup>496</sup> *Universal Service First Report and Order*, 12 FCC Rcd at 8970.

<sup>497</sup> *Universal Service First Report and Order*, 12 FCC Rcd at 8969-70.

<sup>498</sup> The estimate of \$125 million is based on a residential SLC cap of \$6.50 per line. As discussed in section IV.A. above, however, the Commission will initiate a cost proceeding to review whether the residential SLC should be increased above \$5.00.

<sup>499</sup> See Appendix B § 54.403(a)(1).

<sup>500</sup> Modified Proposal at § 1.

<sup>501</sup> Modified Proposal at § 1.2.

discussed above, the LEC members of CALLS have agreed not to assess universal service charges on Lifeline customers. Upon implementation of the interstate access universal service support mechanism, price cap LECs will make a corresponding exogenous adjustment to remove recovery of their universal service contributions from price cap baskets at the same percentage adjustment as they went into the price cap baskets.<sup>502</sup>

(ii) **Discussion**

219. We find that the CALLS method for LEC recovery of universal service contributions is reasonable and consistent with the Act, Commission precedent, and the Fifth Circuit decision in *TOPUC v. FCC*.<sup>503</sup> We reject the claim of commenters that the CALLS plan violates section 254(d) of the Act by eliminating price cap LECs' contributions to universal service insofar as the plan provides that incumbent LECs may recover universal service contributions through an end-user charge.<sup>504</sup> This argument misreads the Act, ignores the Fifth Circuit's decision in *TOPUC v. FCC*, and is contrary to our *Universal Service Eighth Report and Order*. Section 254(d) simply states that "[e]very telecommunications carrier that provides interstate telecommunications services shall contribute, on an equitable and nondiscriminatory basis, to the specific, predictable, and sufficient mechanisms established by the Commission to preserve and advance universal service." Nothing in section 254(d) prohibits any telecommunications carrier from recovering its universal service contributions from its customers.

220. In *TOPUC v. FCC*, the Fifth Circuit emphasized, based on section 254(e), that the Commission should not require incumbent LECs to recover their universal service contributions from access charges.<sup>505</sup> In response to the Fifth Circuit's decision, in the *Universal Service Eighth Report and Order*, the Commission permitted incumbent LECs to recover universal service contributions through an explicit line-item charge to end users.<sup>506</sup> Because the CALLS plan permits, but does not require, an incumbent LEC to recover contributions through an explicit line-item charge to end users, it is consistent with Commission precedent and the *TOPUC v. FCC*

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<sup>502</sup> Modified Proposal at § 1.3.

<sup>503</sup> Some commenters argue that recovery of interstate access universal service support from all interstate telecommunications carriers revenues negatively affects carriers, such as Commercial Mobile Radio Services Providers and rural LECs, who receive limited benefits from reductions in access charges. *See, e.g.*, Joint Board Supp. Comments at 8-9. The Commission fully addressed its decision to require all interstate telecommunications carriers to contribute to universal service mechanisms in the *Universal Service First Report and Order*, and the Fifth Circuit affirmed the Commission's decision on appeal. *Universal Service First Report and Order*, 12 FCC Rcd at 9171-88 (requiring all interstate telecommunications carriers to contribute to universal service funding with a few limited exceptions); *see also* *TOPUC v. FCC*, 183 F.3d at 429-30. Thus, we decline to revisit this issue here.

<sup>504</sup> *See, e.g.*, Joint Consumer Commenters Supp. Comments at 37.

<sup>505</sup> *Texas Office of Public Utility Counsel v. FCC*, 183 F. 3d at 425.

<sup>506</sup> *Universal Service Eighth Report and Order*, 15 FCC Rcd at 1693.

decision. We, therefore, reject the assertion that allowing price cap LECs to recover universal service contributions through end user charges violates section 254(d) of the Act.

221. Other commenters argue that we should require that price cap LECs recover their universal service contributions through a flat-rated per-line charge, rather than as a percentage charge applied to the interstate revenues derived from each customer.<sup>507</sup> According to these commenters, because price cap LECs still possess market power, the Commission cannot rely on market forces to discipline the price cap LECs' universal service contribution recovery practice.<sup>508</sup> Alternatively, these commenters argue that price cap LECs should only be permitted to recover universal service costs through a flat-rated charge because such costs are non-traffic sensitive.<sup>509</sup> In the *Universal Service Eighth Report and Order*, we decided to provide price cap LECs some flexibility to determine how they recover their contributions to the universal service support mechanisms from their customers, provided that they provide accurate and truthful information about the nature of the charge imposed and that they do not shift more than an equitable share of their contributions to any customer or group of customers.<sup>510</sup> We believe that permitting price cap LECs to recover their universal service contributions as either a flat-rated charge, or as a percentage of interstate revenues, is consistent with our earlier determination to allow price cap LECs some flexibility in how they recover their universal service contributions. We therefore reject suggestions that we should further restrict a price cap LEC's recovery of its universal service contributions. As we have cautioned previously, however, we will not hesitate to take action on a case-by-case basis against carriers that impose unjust or unreasonable line item charges.<sup>511</sup>

## **f. Implementation**

### **(i) Background**

222. Under our existing rules, the administrator of the universal service support mechanisms, USAC, submits estimated universal service support requirements to the Commission

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<sup>507</sup> See, e.g., Ad Hoc Supp. Comments at 10-11.

<sup>508</sup> See, e.g., Ad Hoc Supp. Comments at 10.

<sup>509</sup> See, e.g., Ad Hoc Supp. Comments at 10.

<sup>510</sup> See *Universal Service Eighth Report and Order*, 15 FCC Rcd at 1692-93; *Universal Service First Report and Order*, 12 FCC Rcd at 9211-12 (stating that "[i]f contributors [to universal service] choose to pass through part of their contributions and to specify that fact on customer's bills, contributors must be careful to convey information in a manner that does not mislead by omitting important information that indicates that the contributor has chosen to pass through the contribution or part of the contribution to its customers and that accurately describes the nature of the charge").

<sup>511</sup> See 47 U.S.C. § 201(b); In the Matter of Truth-in-Billing and Billing Format, CC Docket No. 98-170, First Report and Order and Further Notice of Proposed Rulemaking, 14 FCC Rcd 7492, 7528 (1999) (*Truth in Billing First Report and Order*).

approximately two months before the beginning of each quarter.<sup>512</sup> The Commission uses those estimated support requirements to establish a contribution factor, which it announces approximately one month before the beginning of each quarter.<sup>513</sup> USAC then uses the contribution factor to bill contributors and collect the appropriate amount of contributions to fund all of the universal service support mechanisms.<sup>514</sup>

223. The CALLS Proposal for an interstate access universal service support mechanism that we adopt today does not change the current universal service contribution methodology. Rather, it simply adds the new mechanism to the existing methodology. Thus, in addition to the support requirements of the existing support mechanisms for high-cost, low income, schools and libraries, and rural health care, USAC will submit estimated support requirements for the interstate access support mechanism, and the quarterly contribution factor will reflect those additional support requirements. The quarterly contribution factor also will reflect the increased Lifeline support required as a result of the increased SLC caps under the CALLS Proposal.

224. As discussed below, in order for USAC to calculate and distribute interstate access universal service support, eligible telecommunications carriers seeking support will be required to file certain line counts and other data on a regular basis. Additionally, because of the short time period before the July 1, 2000 implementation of the access charge and universal service reforms adopted in this Order, certain adjustments to the regular filing schedule will be necessary during the initial period of operation for the interstate access universal service support mechanism. In adopting these reporting requirements, we have attempted to minimize the reporting burdens on support recipients, while at the same time ensuring that we have sufficient information to enable the proper calculation and distribution of interstate access universal service support.

## (ii) Discussion

225. We agree with CALLS that the interstate access universal service support mechanism should be administered by USAC and collected in the same manner as the Commission's other universal service support mechanisms. No commenters objected to this aspect of the CALLS Proposal. We, therefore, make the following changes to our rules to facilitate implementation of the CALLS Proposal.

226. *Fund Administration.* We direct USAC to serve as the administrator for the interstate access universal service support mechanism.<sup>515</sup> The interstate access universal service support mechanism shall be administered by USAC's High Cost and Low Income Division under

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<sup>512</sup> 47 C.F.R. § 54.709(a).

<sup>513</sup> 47 C.F.R. § 54.709(a).

<sup>514</sup> 47 C.F.R. § 54.709(a). Pursuant to the 1996 Act, providers of interstate telecommunications services are required to contribute to the Commission's universal service support mechanisms. See 47 U.S.C. § 254(d); see also Appendix B § 54.706.

<sup>515</sup> See Appendix B § 54.702.

the direction of the High Cost and Low Income Committee of the USAC Board.<sup>516</sup> USAC shall keep separate accounts for the amounts of money collected and disbursed for interstate access universal service support,<sup>517</sup> and USAC shall account for and recover the administrative expenses that it incurs in connection with administering the interstate access universal service support mechanism.<sup>518</sup>

227. *Line Counts.* As specified in the rules listed in Appendix B, each eligible telecommunications carrier that is providing service within an area served by a price cap LEC in a particular study area and wishes to receive support must submit to USAC on the last business day of March, June, September, and December of each year data showing the number of lines it served in that study area as of the last business day of the previous quarter.<sup>519</sup> The line counts must be assigned to UNE Zones if UNE Zones have been established within that study area. This line count information must also show residential/single line business line counts separate from multi-line business line counts.<sup>520</sup> The residential/single line business lines reported include single and non-primary residential lines, single-line business lines, basic rate interface (BRI) integrated services digital network (ISDN) service, and other related residence class lines. Similarly, the multi-line business class lines reported include multi-line business, centrex, ISDN primary rate interface (PRI) and other related business class lines.<sup>521</sup>

228. *Other Data.* In addition to line count information, price cap LECs<sup>522</sup> must file on June 30, 2000, October 15, 2000, April 16, 2001 and annually after that, all information necessary for USAC to determine: (1) Average Price Cap CMT Revenue Per Line Per Month for each price cap LEC study area;<sup>523</sup> (2) the rates established for UNE Loops<sup>524</sup> and UNE Line Ports by UNE Zone in those study areas where UNE Zones have been established; and (3) the boundaries of each UNE Zone within each price cap study area.<sup>525</sup>

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<sup>516</sup> See Appendix B §§ 54.701(g) and § 54.705(c)(1).

<sup>517</sup> See Appendix B § 54.702(i).

<sup>518</sup> See Appendix B § 54.715(c).

<sup>519</sup> Appendix B § 54.802(a).

<sup>520</sup> Appendix B § 54.802(a).

<sup>521</sup> Such lines include all business class lines assessed the end user common line charge pursuant to 47 C.F.R. § 69.152.

<sup>522</sup> This reporting requirement does not apply to eligible telecommunications carriers other than price cap LECs.

<sup>523</sup> See Appendix B § 54.800(a).

<sup>524</sup> See Appendix B § 54.802(b)(2).

<sup>525</sup> Appendix B, § 54.802(b).

229. *First Year Implementation.* In order to implement interstate access support on July 1, 2000, certain adjustments must be made to the reporting schedule described above. First, we direct USAC to file with the Commission no later than June 5, 2000, a supplement to its third quarter 2000 filing, revising its estimate of the universal service support requirements in light of our action in this proceeding. This supplement should account for the additional support necessitated by the interstate access support mechanism as well as additional Lifeline support. To prevent fluctuations in the contribution factor and ensure a uniform collection of contributions, we direct USAC to estimate support requirements in its supplemental filing for the third quarter of 2000 as if all carriers potentially eligible for interstate access support will file to receive such support. In the event that not all eligible carriers ultimately seek such support, USAC shall apply any surplus contributions to reduce future collection requirements.

230. In early June, 2000, based on USAC's supplemental filing, we will release a Public Notice announcing the third quarter contribution factor.<sup>526</sup> On or before June 30, 2000, all eligible telecommunications carriers seeking interstate access universal service support shall file the applicable line counts and other data necessary to calculate interstate access support. On or around August 2, 2000, USAC shall file with the Commission estimated universal service support requirements for the fourth quarter. In early September 2000, we will release a Public Notice announcing the fourth quarter contribution factor. On or around September 29, 2000, USAC will disburse July and August interstate access support based on each eligible telecommunications carriers' June 30, 2000 line counts.<sup>527</sup> Thereafter, USAC will distribute interstate access support in accordance with its regular disbursement schedule, with one exception discussed below. Because a price cap LEC will not know precisely how much interstate access universal service support it will receive until September 2000, we shall allow such a carrier to make a good faith estimate of the amount of interstate access universal service support it likely will receive for purposes of our June 16, 2000 tariff filing. Carriers filing good faith estimates shall true-up their tariffs once the amount of their interstate access universal service support is known.

231. Because of the timing of this Order, we believe that it is in the public interest to provide eligible telecommunications carriers other than price cap LECs with additional time to gather third quarter line count information in order to take advantage of the portability of interstate access support. Therefore, in the event that such eligible telecommunications carriers cannot meet the June 30, 2000 line count reporting deadline, we shall allow these eligible telecommunications carriers to file their March 30, 2000 line counts on September 29, 2000, and receive interstate access support for the third quarter of 2000 retroactively.

232. *Section 254(e) Certification.* Section 254(e) provides that a carrier receiving universal service support must use that support "only for the provision, maintenance, and upgrading of facilities and service for which the support is intended."<sup>528</sup> In the *Universal Service*

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<sup>526</sup> See 47 C.F.R. § 54.709(a)(3).

<sup>527</sup> As stated below, however, eligible telecommunications carriers other than participating price cap LECs may file their March 30, 2000 line counts on September 29, 2000.

<sup>528</sup> 47 U.S.C. § 254(e).

*Ninth Report and Order*, we set forth rules requiring a state that wishes to receive federal universal service high-cost support for non-rural carriers within its territory to file a certification with the Commission stating that all federal high-cost funds flowing to non-rural carriers in such state will be used in a manner consistent with section 254(e).<sup>529</sup> Because the *Universal Service Ninth Report and Order* addressed federal universal service support for intrastate rates, we required states to file a certification of section 254(e) compliance with the Commission because states have jurisdiction over rates for intrastate services. In this Order, we address federal support for interstate rates, a matter over which the Commission has jurisdiction. Thus, to ensure that carriers receiving interstate access universal service support will use that support in a manner consistent with section 254(e), we shall require carriers seeking such support to file a certification with the Commission and USAC.<sup>530</sup> This certification is applicable to price cap LECs and eligible telecommunications carriers seeking support from our interstate access universal service mechanism. The certification shall be filed with the Commission and USAC at the same time a carrier files its first set of line count data with USAC.<sup>531</sup> Such certification shall be filed in CC Docket No. 96-45 annually thereafter on June 30<sup>th</sup>.<sup>532</sup> The certification may be filed in the form of a letter and must state that the carrier will use its interstate access universal service support only for the provision, maintenance, and upgrading of facilities and service for which the support is intended.<sup>533</sup> Carriers that fail to abide by this certification, or otherwise violate section 245(e), shall be subject to enforcement action by the Commission.

#### 4. Consultation with Joint Board

233. We wish to point out that our actions today are consistent with our obligation under the 1996 Act to consult with the Joint Board, and are based on the recommendations that we have received from the Joint Board throughout our universal service proceedings. In response to the Commission's latest request for input on access charge and universal service reform,<sup>534</sup> the state members of the Joint Board filed comments on the CALLS Proposal.<sup>535</sup> We value these suggestions and insights from our state colleagues, and we have responded to their comments in the appropriate sections of this Order.<sup>536</sup> We look forward to continued consultation and cooperation with the Joint Board in the future as we reform other aspects of our universal service

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<sup>529</sup> *Universal Service Ninth Report and Order*, 14 FCC Rcd at 20483.

<sup>530</sup> See Appendix B § 54.809; see also Joint Board Supp. Comments at 6 (raising the issue of certification pursuant to Section 254(e)).

<sup>531</sup> See Appendix B § 54.809(c).

<sup>532</sup> See Appendix B § 54.809.

<sup>533</sup> See Appendix B § 54.809(b).

<sup>534</sup> *CALLS Modified Proposal NPRM*.

<sup>535</sup> Joint Board Supp. Comments.

<sup>536</sup> See Sections IV.A.3.a and IV.A.3.c. *supra*.

support mechanisms in light of developments in the increasingly competitive telecommunications marketplace.

## **D. Low-Volume Long-Distance Proceeding**

### **1. Introduction**

234. We initiated an inquiry last summer to ensure that all Americans were benefiting from the Commission's pro-competitive reforms.<sup>537</sup> We were prompted to do so when a number of individuals and consumer groups questioned whether consumers who make few interstate long-distance calls were benefiting to the same degree as high-volume users from the Commission's access charge and universal service reforms. In that proceeding we sought comments from consumers and carriers alike.<sup>538</sup> Our primary focus concerned the impact of certain flat fees that interstate long-distance companies had begun charging consumers.

235. The CALLS proposal will, among other things, benefit low-volume long-distance callers by eliminating some of these flat fees, and making others avoidable. Although we decline to reach the question whether the flat charges at issue in the Notice of Inquiry are unreasonable, inequitable, or inconsistent with the Act, we conclude that the elimination or avoidability of these charges moots the factual premise that prompted us to begin the low-volume investigation. In light of our adoption today of the CALLS proposal, we are confident, for the reasons described below, that the needs of all consumers will be served by the industry, and that low-volume users will share in the benefits of the Commission's pro-competitive telecommunication reforms. Thus, we have resolved the issues raised by the low-volume long-distance inquiry, and bring that proceeding to a close.

### **2. Notice of Inquiry**

236. After we adopted our access charge and universal service reforms, interstate long-distance providers began assessing new flat fees on their end users. AT&T, for example, began charging a \$3.00 minimum usage fee that customers are required to pay even if they made no long-distance calls in a month.<sup>539</sup> Similarly, MCI charged its basic-rate customers either a \$5.00 or a \$3.00 minimum, depending upon when they had initiated their service with MCI.<sup>540</sup>

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<sup>537</sup> See *Low-Volume Long-Distance Users NOI*, 15 FCC Rcd 6298.

<sup>538</sup> Among those individuals who filed comments were: Mr. Eric Anderson, Mr. Richard A. Arsinow, Mr. Bob Beaudoin, Mr. and Mrs. James Besenger, Mr. Fred Bethke, Ms. Nancy T. Clark, Robert W. Cooper, Jr., Mr. Allan DeSmet, Ms. Sandra Farrell, D.D.S., Mr. Jonathan Freidin, Ms. Barbara N. Gibbons, Ms. Frances Gizerian, Mr. Frank A. Griffith, Mr. Donald G. Hyatt, Mr. Barry D. Johnson, Mr. T. David Krauser, Mr. Robert L. Lehr, Mr. Roger Merel, Ms. Ruth J. Pelt, Ms. Gwen Petitjean, Mr. Mark Plemmons, R. Rivera, Mr. Paul F. Schaeffer, Mr. Michael Schneider, Robert Sullivan, Mr. Richard Stallworthy, and Ms. Davena Swinford.

<sup>539</sup> AT&T Tariff FCC No. 27, 1st Rev. P. 4-7.3, at § 4.1.1.N (eff. June 15, 1999); 1st Rev. P. 24-57.39, at § 24.1.1.U.2 (eff. Sept. 5, 1998).

<sup>540</sup> MCI Tariff FCC No. 1, 140th Rev. P. 19.1, at § C.3.021211 (eff. Feb. 1, 1999); 3rd Rev. P. 19.183, at § C.3.421 (eff. Jan. 3, 1998).

According to these long-distance carriers, the charges were intended to recover the costs they incurred in maintaining separate account and billing records for their customers.<sup>541</sup>

237. AT&T, MCI, and Sprint also began charging their residential customers a flat, averaged, monthly charge designed to recover the PICC that the long-distance carriers were paying regulated local carriers. As of August 1, 1999, the charges AT&T, MCI, and Sprint were charging were \$1.51, \$1.46, and \$1.50, respectively.<sup>542</sup> These charges exceeded the \$1.04 the carriers actually were assessed for residential customers with just one line. In addition, AT&T began to recover some of its contributions to the high-cost universal service support mechanism,<sup>543</sup> as well as the contributions that regulated local carriers flowed-through to AT&T, through a flat charge of 93 cents per month.<sup>544</sup> AT&T did so even though carrier contributions to the universal service support mechanism are calculated based on a percentage of a carrier's interstate and international end-user revenues.<sup>545</sup> By November 2, 1999, AT&T had increased this fee to \$1.38.<sup>546</sup>

238. As a result of these flat charges, a number of individuals and consumer groups questioned whether end users who make few long-distance calls were benefiting to the same degree as high-volume users from the Commission's access charge and universal service reforms. Some argued that customers who make few long-distance calls have seen their bills go up, despite the reduction in per-minute charges. Consequently, on July 20, 1999, we commenced a proceeding seeking comments regarding the impact of flat charges on those consumers who make few or no long-distance calls.<sup>547</sup> We asked whether minimum usage fees and other flat charges imposed on consumers who make few long-distance calls are a reasonable result of competitive market dynamics and the removal of implicit subsidies, or whether they warrant regulatory intervention.<sup>548</sup>

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<sup>541</sup> *Low-Volume Long-Distance Users NOI*, 15 FCC Rcd at 6303-04.

<sup>542</sup> AT&T Tariff FCC No. 27, 3<sup>rd</sup> Rev. P. 24-555 at §24.1.18 C (eff. July 1, 1999); MCI Tariff FCC No. 1, 16<sup>th</sup> Rev. P. 16.3, §1.061111A. (eff. August 1, 1999); Sprint Tariff FCC No. 1, 6<sup>th</sup> Rev. P. 38.2, § 3.11.10 (eff. Aug. 1, 1999).

<sup>543</sup> As discussed in Section IV.C.2, in the *Universal Service Ninth Report and Order* we reformed our high-cost universal service support mechanism for non-rural carriers to enable states to maintain reasonably comparable intrastate rates.

<sup>544</sup> See AT&T Tariff FCC No. 27, 2<sup>nd</sup> Rev. P. 24-555 at §24.1.18 D (eff. July 1, 1998).

<sup>545</sup> See *Universal Service Ninth Report and Order*, 14 FCC Rcd at 20489.

<sup>546</sup> See AT&T Tariff FCC No. 27, 5<sup>th</sup> Rev. P. 24-555 at §24.1.18.D. (eff. Nov. 2, 1999).

<sup>547</sup> See *Low-Volume Long-Distance Users NOI*, 15 FCC Rcd 6298.

<sup>548</sup> *Id.*, 15 FCC Rcd at 6301-03.

239. We asked for comments on a number of possible courses of action. One proposal was to rely on competition--including that resulting from dial-around services<sup>549</sup> and entry into long-distance service by regulated local telephone companies<sup>550</sup>--to provide services suitable to the needs of low-volume residential customers.<sup>551</sup> This proposal was supported by both long-distance and regulated local telephone companies.<sup>552</sup>

240. Another proposal, supported mostly by consumer groups and local telephone companies, was to rely on direct regulatory intervention.<sup>553</sup> For instance, we asked whether the Commission should require regulated local carriers to bill end users directly, rather than long-distance carriers, or require carriers to combine into a single line item the charges associated with all of our pro-competitive reforms.<sup>554</sup> Another possibility was to require some or all long-distance carriers to maintain rate plans that do not include a minimum monthly charge.<sup>555</sup> Additionally, we asked whether the Commission should require all or some subset of long-distance carriers to pass through to their low-volume customers a specific portion of the cost savings they have received as a result of access charge reform.<sup>556</sup> Another option was to set a maximum percentage by which low-volume rates may exceed high-volume rates.<sup>557</sup> Several local telephone companies and consumer advocates also supported requiring long-distance carriers to recover the charges

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<sup>549</sup> Dial-around services are long-distance providers that are accessible on a per-call basis by dialing a 101-xxxx number.

<sup>550</sup> Until relatively recently, most regulated local telephone companies were absolutely prohibited from providing long-distance service in their immediate areas because of their market power. As of 1996, however, these carriers may ask the Commission to allow them to provide long-distance services once they open their local markets to competition. *See* 47 U.S.C. § 271.

<sup>551</sup> *See Low-Volume Long-Distance Users NOI*, 15 FCC Rcd at 6304.

<sup>552</sup> Ameritech Low-Volume Comments at 2; AT&T Low-Volume Comments at 2, 13, 24, and Declaration of Gregory L. Rosston at 3, 17; Bell Atlantic Low-Volume Comments at 1-3; BellSouth Low-Volume Comments at 3-4; SBC Low-Volume Reply at 2; CompTel Low-Volume Comments at 2-3, 6-7; MCI Low-Volume Comments at 1-2; Sprint Low-Volume Comments at 5-6; TRA Low-Volume Comments at 13; USTA Low-Volume Comments at 2, 5.

<sup>553</sup> *See Low-Volume Long-Distance Users NOI*, 15 FCC Rcd at 6303-05.

<sup>554</sup> *See id.*, 15 FCC Rcd at 6304-05, 6307. *See also* AARP Low-Volume Comments at 4-5; Ad Hoc Low-Volume Comments at 7; Bell Atlantic Low-Volume Comments at 1-2; BellSouth Low-Volume Comments at 7-8; GSA Low-Volume Comments at 8; TRA Low-Volume Reply at 5; TURN Low-Volume Comments at 2.

<sup>555</sup> *See Low-Volume Long-Distance Users NOI*, 15 FCC Rcd at 6305-06. *See also* AARP Low-Volume Comments at 3, 5; CFA Low-Volume Comments at v-vi, 26; CompTel Low-Volume Comments at 4, 6; TURN Low-Volume Comments at 2.

<sup>556</sup> *Low-Volume Long-Distance Users NOI*, 15 FCC Rcd at 6305-06. *See also* Ameritech Low-Volume Comments at 3; CFA Low-Volume Comments at 26; GSA Low-Volume Comments at 7; Rep. Hill Low-Volume Comments at 4; RTC Low-Volume Comments at 2, 4; USTA Low-Volume Comments at 4.

<sup>557</sup> *Low-Volume Long-Distance Users NOI*, 15 FCC Rcd at 6306. This option was supported by TURN. *See* TURN Low-Volume Comments at 7-8.

regulated local carriers assess on them as a percentage of the end user's bill, capped at a certain dollar level.<sup>558</sup>

241. We also requested comment on whether efforts by the Commission, states, carriers, and consumer groups to educate consumers regarding choices they can exercise in the marketplace could reduce or eliminate the need for additional regulation.<sup>559</sup> Finally, we asked whether there were any particular enforcement actions that the Commission should take.<sup>560</sup> Several commenters suggested that the Commission increase its enforcement efforts against carriers that recover more than their share of costs, or regulate the way in which carriers characterize their fees.<sup>561</sup>

### 3. Discussion

242. The CALLS proposal addresses most of the concerns raised by, and on behalf of, low-volume consumers, and may save customers who make no long-distance calls as much as \$4.00 to \$5.00 per month in flat fees. In view of our decision to adopt the CALLS proposal, we find that other regulatory intervention is not warranted at this time, and would not serve the public interest. The record before us indicates that the competitive marketplace the Commission is fostering is increasingly responsive to the needs of all consumers, including low-volume users. Consequently, we conclude that we have resolved the issues raised in the low-volume long-distance proceeding.

243. A number of carriers have agreed to offer long-distance plans with no monthly minimum charges. As part of the CALLS proposal, for example, AT&T has pledged to offer for at least three years--and possibly as long as five--a basic residential plan that has no monthly recurring charge and no minimum usage requirement.<sup>562</sup> Sprint has also committed to offering at least one basic rate plan without a minimum usage fee for the duration of the CALLS plan.<sup>563</sup> Now that we have approved Bell Atlantic's application to provide long-distance service in New York,<sup>564</sup> Bell Atlantic has also targeted two long-distance plans to residential, low-volume users

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<sup>558</sup> *Low-Volume Long-Distance Users NOI*, 15 FCC Rcd at 6305-07. *See also* Bell Atlantic Low-Volume Comments at 3; TURN Low-Volume Comments at 7-8.

<sup>559</sup> *Low-Volume Long-Distance Users NOI*, 15 FCC Rcd at 6304-06. *See also* GTE Low-Volume Comments at 10; TURN Low-Volume Comments at 2-3, 10-12; USTA Low-Volume Comments at 5; Qwest Low-Volume Comments at 16-17, and Sprint Low-Volume Comments at 7-8.

<sup>560</sup> *See Low-Volume Long-Distance Users NOI*, 15 FCC Rcd at 6305-06.

<sup>561</sup> *See* Ad Hoc Low-Volume Comments at 9-10; CompTel Low-Volume Comments at 9; GTE Low-Volume Comments at 16-17; TURN Low-Volume Reply at 5-6.

<sup>562</sup> *See AT&T March 30 Letter*.

<sup>563</sup> *See Sprint February 25 Letter*.

<sup>564</sup> Application of Bell Atlantic New York for Authorization under Section 271 of the Communications Act to Provide In-Region, Inter-Lata Service in the State of New York, CC Docket No. 99-295, Memorandum Opinion and Order, 15 FCC Rcd 75 (1999).

by eliminating minimum use charges.<sup>565</sup> As of May 1, 2000, MCI, which has not signed on to the CALLS proposal, also began a plan that has no monthly minimum charges.<sup>566</sup> Thus, more than eighty percent of long-distance users will have plans available to them with no monthly minimums.

244. The CALLS plan will also eventually combine the SLC and the PICC on the first line for residential end users, avoiding the concerns raised by the long-distance carriers' pass-through of the PICC.<sup>567</sup> In addition, both long-distance carriers and local service providers will bill their customers directly for their universal service costs, eliminating the similar flow-through problem. AT&T has also implemented changes to eliminate its flat 1.38 cent universal service charge. Instead, effective April 1, 2000, it is assessing a fee that is based on a percentage of the customer's long-distance bill.<sup>568</sup> AT&T made this change, in part, because of our investigation of its flat universal service fee.<sup>569</sup> MCI and Sprint were already assessing universal service fees on a percentage basis.<sup>570</sup>

245. Thus, under the CALLS plan, AT&T's Basic Schedule customers who make no long-distance calls will see their flat fees cut almost in half. Previously, such a customer would have paid a \$3.50 SLC, a \$1.51 PICC pass-through, a \$1.38 universal service charge, and a \$3.00 minimum use fee, for a total of \$9.39.<sup>571</sup> According to CALLS' estimates, that customer will now pay \$4.35 for the SLC and \$0.36 for universal service, for a total of \$4.71.<sup>572</sup> Perhaps more significantly, this means that customers who make no long-distance calls will pay nothing to their long-distance carriers. We conclude, therefore, that our adoption of CALLS, evidence that low-volume users are starting to benefit from the competition resulting from Commission reforms, and our existing regulatory authority eliminate the need to continue the Low-Volume, Long-Distance proceeding. We remind carriers, however, of our statutory authority to investigate any charges that appear unlawful.<sup>573</sup> As we have cautioned previously, we will not hesitate to take action on a

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<sup>565</sup> The "Timeless" plan would charge ten cents per minute at all times for calls that are dialed directly, with no monthly minimum. The "E-Values" plan, which also has no minimums, charges five cents per minute for weekend calls, and nine cents per minute weekdays for Internet customers who sign up via Bell Atlantic's web site.

<sup>566</sup> MCI FCC Tariff No. 1, 1<sup>st</sup> Rev. P. 364 §C.3.02.021 (eff. May 1, 2000).

<sup>567</sup> See *AT&T March 30 Letter*.

<sup>568</sup> AT&T Tariff FCC No. 13, 9<sup>th</sup> Rev. P. No. 38.6.3, §19.L.2; AT&T Tariff FCC No. 27, 6<sup>th</sup> Rev. P. 3-19.6, § 3.5.12.B. (eff. Feb. 19, 2000).

<sup>569</sup> See *Interexchange Carrier End-User Charges To Recover Universal Service Contributions*, CC Docket No. 99-324, Order, 14 FCC Rcd 20032 (Com. Car. Bur. Nov. 1, 1999) (*IXC Universal Service Suspension Order*).

<sup>570</sup> MCI Tariff FCC No. 1, 3<sup>rd</sup> Rev. P. No. 16.4, § C-1.061 (eff. Jan. 1, 1998); Sprint Tariff FCC No. 1, 2<sup>nd</sup> Rev. P. No. 38, §3.3.11.8 (eff. Jan. 1, 1998).

<sup>571</sup> CALLS Supp. Comments at 3.

<sup>572</sup> *Id.*

<sup>573</sup> See 47 U.S.C. §§ 204, 205. See also *IXC Universal Service Suspension Order*, 14 FCC Rcd 20032.

case-by-case basis against carriers that impose unjust or unreasonable line-item charges. We also will monitor the effect of the CALLS proposal on consumers.

246. Our decision to adopt the CALLS proposal, and to conclude the low-volume inquiry, is based in large part on the availability of interstate long-distance plans that meet the needs of low-volume users. Sprint and AT&T have committed to making such plans available in their support for the CALLS proposal. They each have said, for example, that they will eliminate their PICC pass-through charges for residential and single-line business customers, offer at least one basic rate plan that does not contain minimum usage charges, freeze the per-minute rates on certain plans, and flow through their access charge savings to residential and business customers.<sup>574</sup> We expect the IXCs will pass through these access charge reductions in a manner that benefits both residential and business customers. Sprint and AT&T have also committed to informing their residential customers of the various plans they offer for long-distance services.<sup>575</sup>

247. We find the commitments of Sprint and AT&T to be in the public interest because they will help ensure that low-volume users of long-distance service share in the benefits of the 1996 Telecommunications Act and the pro-competitive reforms that the Commission has adopted. Because we have made the rate structure components of the CALLS proposal mandatory for all price cap LECs, and the rate levels mandatory for at least an interim period, Sprint and AT&T will in fact receive the benefits provided by the CALLS proposal. Specifically, their switched access usage charges will be reduced by their proportionate share of \$2.1 billion, and the residential and single-line business PICCs will be eliminated. Consequently, we order Sprint and AT&T to comply with all the voluntary commitments they made in their respective February 25, 2000, and March 30, 2000, letters.<sup>576</sup> If they fail to do so, the carriers may be subject to any of the remedies available under the Act, including fines, forfeitures, or the rejection of any non-conforming rates.

248. In its revised submission to the Commission, the Coalition as a whole committed to working with the Commission's Consumer Information Bureau to develop a consumer education plan.<sup>577</sup> This plan must focus on educating consumers about important issues related to

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<sup>574</sup> See *Sprint February 25 Letter*; *AT&T March 30 Letter*. State members of the Federal-State Joint Board have expressed concern that Sprint and AT&T have not indicated when they will flow through these saving, or that low-volume consumers will benefit from such reductions. Joint Board Supp. Comments at 4. We note, however, that Sprint and AT&T have said that they will not increase the per-minute rates on their "no minimum use" plans for at least one year. *Sprint February 25 Letter*; *AT&T March 30 Letter*. Moreover, even if Sprint and AT&T do not flow the per-minute savings through to low-volume users, such users will have greatly benefited from the elimination of flat fees such as the minimum use charges.

<sup>575</sup> *Sprint February 25 Letter*; *AT&T March 30 Letter*.

<sup>576</sup> See *Sprint February 25 Letter*; *AT&T March 30 Letter*. Cf. Motion of AT&T Corp. to be Reclassified as a Non-Dominant Carrier, 11 FCC Rcd 3271, 3356 (1995) (*AT&T Non-dominance Order*) (ordering AT&T to comply with voluntary commitments from September 21 and October 5, 1995, *ex parte* letters it filed in a proceeding regarding its treatment as a non-dominant provider of interstate, domestic, interexchange service).

<sup>577</sup> Modified Proposal at § 7.

long-distance and local phone pricing and service. These markets are changing at an ever-accelerating rate; education by CALLS members will empower consumers to make better-informed decisions.

249. This education plan will entail informing consumers how they can best inventory their long-distance and local service needs, and choose the most appropriate calling plan. The education plan will promote available government programs that assist low-income consumers in obtaining telephone service. Finally, CALLS will create programs and materials to educate consumers on how to understand their phone bills.<sup>578</sup> Consumer education plan materials must be made available in alternative formats and languages, in order to reach the maximum number of consumers.

250. Not later than 90 days after the effective date of this order, CALLS members must submit to the Consumer Information Bureau a compliance statement detailing the actions taken to fulfill their consumer education plan, as well as further public education efforts they will take over the life of the CALLS plan.

## V. PROCEDURAL ISSUES

### A. Final Regulatory Flexibility Analysis

251. As required by the Regulatory Flexibility Act (RFA),<sup>579</sup> an Initial Regulatory Flexibility Analysis (IRFA) was incorporated in the CALLS NPRM,<sup>580</sup> and revised in the Public Notice requesting comment on the modified CALLS Proposal.<sup>581</sup> The Commission sought written public comment on the proposals in the CALLS NPRM and the CALLS Proposal, including comments on the IRFAs. This present Final Regulatory Flexibility Analysis (FRFA) conforms to the RFA, as amended.<sup>582</sup> To the extent that any statement 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.

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<sup>578</sup> We further note that our Truth in Billing Order and rules address the way carriers characterize their fees, as well as many of the problems that consumers have understanding charges. *See Truth In Billing First Report and Order*, 14 FCC Rcd at 7496. A carrier is required to list, item-by-item, each charge it bills to the consumer. *Id.*, 14 FCC Rcd at 7516. The language used must be clear to the average consumer, and the bill must include telephone numbers that consumers can call for further explanations of their telephone bills. *Id.*

<sup>579</sup> *See* 5 U.S.C. § 603. The RFA, 5 U.S.C. § 601 *et seq.*, has been amended by the Contract With America Advancement Act of 1996, Pub. L. No. 104-121, 110 Stat. 847 (1996) (CWAAA). Title II of the CWAAA is the Small Business Regulatory Enforcement Fairness Act of 1996 (SBREFA).

<sup>580</sup> *CALLS NPRM*, 14 FCC Rcd at 16875-76.

<sup>581</sup> Coalition for Affordable Local and Long Distance Services (CALLS) Modified Proposal, CC Docket No. 96-262, Public Notice, DA-00-533, at 1-3 (Comm. Carr. Bur., rel. Mar. 8, 2000).

<sup>582</sup> *See* 5 U.S.C. § 604.

## 1. Need for and Objectives of this Order

252. The CALLS members offer the proposal as a comprehensive solution to the members' access charge, universal service, and price cap concerns. The CALLS plan would revise the current system of common line charges by combining existing carrier and subscriber charges into one flat-rated subscriber line charge (SLC), and would provide for limited deaveraging of those charges under specific conditions. The CALLS plan also would establish an interstate access universal service support mechanism that provides explicit support to replace support currently implicit in interstate access charges. In addition, the CALLS plan calls for annual reductions in traffic-sensitive switching access rates until they reach a specified level.

253. As stated in Section I above, we believe that the CALLS Proposal is in the public interest, and so adopt it to the extent discussed in this Order. This Order agrees with the CALLS members that the CALLS Proposal is the result of certain segments of the telecommunications industry developing a comprehensive approach to resolve outstanding issues concerning access charges and universal service. By adopting the CALLS Proposal, this Order will result in lower rates for both low-volume and high-volume long distance consumers, more competition, greater flexibility for price cap LECs to meet competition, and an explicit, portable interstate access universal service support mechanism. It is the CALLS Proposal's comprehensive solution of historically contentious issues that allows the Commission to take these actions while ensuring that consumers in high-cost areas will continue to have affordable service.<sup>583</sup>

## 2. Summary of Significant Issues Raised by the Public Comments in Response to the IRFA

254. The Commission received no comments addressing the IRFA. We did, however, receive some general small-business-related comments. Some commenters request that the CALLS Proposal require a proportionate share of the agreed upon local switching rate reductions to come from tandem-switched rates. Other commenters argue that the CALLS Proposal should have a separate X-factor for mid-size price cap incumbent LECs. These comments are addressed in detail in this Order,<sup>584</sup> and are summarized in subsection 5 of the FRFA, *infra*.

## 3. Description and Estimate of the Number of Small Entities to Which the Rules Will Apply

255. 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.<sup>585</sup> The Regulatory Flexibility Act defines the term "small entity" as having the same meaning as the terms "small business," "small organization," and "small business concern" under section 3 of the

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<sup>583</sup> See Section II above.

<sup>584</sup> See Section IV.B.2 above.

<sup>585</sup> 5 U.S.C. § 603(b)(3).

Small Business Act.<sup>586</sup> 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 SBA.<sup>587</sup>

256. The SBA 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.<sup>588</sup>

Total Number of Telephone Companies Affected.

257. *Price Cap Local Exchange Carriers.* The Commission does 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 is 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 currently only 13 price cap LECs, four of which share common ownership.<sup>589</sup> Consequently, significantly fewer than 13 providers of local exchange service are estimated to be small entities or small price cap LECs that may be affected by these proposals. We have included small price cap 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."<sup>590</sup> The SBA's Office of Advocacy contends that, for RFA purposes, small price cap LECs are not dominant in their field of operation because any such dominance is not "national" in scope.<sup>591</sup> We have therefore included small price cap 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.

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<sup>586</sup> *Id.* § 601(3).

<sup>587</sup> *Id.* § 632.

<sup>588</sup> 13 C.F.R. § 121.201.

<sup>589</sup> Two carriers, VALOR and Iowa Telecom, are under contract to purchase exchanges from price cap LECs, and will be subject this Order. Both carriers are probably small entities.

<sup>590</sup> 5 U.S.C. § 601(3).

<sup>591</sup> 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. See, *e.g.*, 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).

258. *Competitive Local Exchange Carriers.* Neither the Commission nor the SBA has developed a definition of small providers of local exchange service. The closest applicable definition under SBA rules is for telephone telecommunications companies other than radiotelephone (wireless) companies.<sup>592</sup> The most reliable source of information regarding the number of competitive LECs nationwide of which the Commission is aware appears to be the data that the Commission collects annually in connection with the Telecommunications Relay Service (TRS). According to the Commission's 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.<sup>593</sup> The Commission does 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 is 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, the Commission estimates that fewer than 129 providers of local exchange service are small entities or small competitive LECs that may be affected by these proposals.

#### **4. Description of the Projected Reporting, Recordkeeping, and Other Compliance Requirements**

259. It is not clear whether, on balance, the CALLS Proposal will increase or decrease price cap incumbent local exchange carriers' administrative burdens. Some of the rate structure reforms in the CALLS Proposal will require additional filings. In particular, the CALLS Proposal requires price cap LECs to file with the Universal Service Administration Corporation (USAC) additional information pertaining to line counts by zone and customer class, revenue data, and information regarding zone boundaries. Competitive LECs would also have to file with USAC line counts by zone and customer class. The filings are on a quarterly basis. On the other hand, other reforms in the CALLS Proposal, such as the elimination of the PICC, should reduce administrative burdens for price cap LECs. Finally, some of the reforms in the CALLS Proposal may have a neutral affect on administrative burdens. For example, under the CALLS Proposal, implicit subsidies now collected by price cap LECs from IXCs through access charges will be collected as explicit subsidies from USAC. This reform should neither increase nor decrease the administrative burden for price cap LECs.

#### **5. Steps Taken to Minimize Significant Economic Impact on Small Entities, and Significant Alternatives Considered**

260. The proposals made by CALLS could have varying positive or negative impacts on price cap LECs, including any such small carriers. The alternative to consideration of adopting the CALLS proposal at this time would be to continue in effect the existing access charge and

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<sup>592</sup> Standard Industrial Classification (SIC) Code 4813.

<sup>593</sup> 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).

universal service fund rules. Neither this alternative, nor any other identified by the Commission, would lessen the significant economic impact on small entities while remaining consistent with this Order's objectives.

261. Several commenters, while not directly responding to our IRFA, did raise general small-business-related concerns. Commenters concerned about protecting smaller IXCs in competition with large IXCs request that the CALLS Proposal require a proportionate share of the agreed upon local switching rate reductions to come from tandem-switched rates.<sup>594</sup> This Order explains, however, that 1) competition in the long distance market eliminates the need for rules protecting smaller IXCs, and 2) even if price cap LECs target their access rate reductions only to direct-trunked transport, these reductions should make direct-trunked transport an affordable alternative for smaller IXCs.<sup>595</sup> Other commenters argue that the CALLS Proposal should have a separate X-factor for mid-size price cap incumbent LECs because these carriers are not able to achieve the same levels of productivity growth as larger LECs.<sup>596</sup> As this Order explains, however, the X-factor adopted under the CALLS proposal is not a productivity offset, but is merely a method to reduce traffic sensitive charges to the Proposal's target level.<sup>597</sup>

262. This Order makes two allowances for smaller price cap LECs. First, the Order allows a higher target access rate for smaller and rural price cap LECs. Whereas the target for the BOCs and GTE is set at 0.55 cents, the target is 0.95 cents for small rural price cap LECs and 0.65 cents for the other smaller price cap LECs.<sup>598</sup> Second, the Order allows mid-size price cap carriers with at least 20 percent of total holding company lines serving statutorily rural areas to pool their access charge reductions and to temporarily recover them from sources other than residential end users and per-minute charges.<sup>599</sup>

## 6. Report to Congress

263. The Commission will send a copy of this Order, including this FRFA, in a report to be sent to Congress pursuant to the Small Business Regulatory Enforcement Fairness Act of 1996.<sup>600</sup> In addition, the Commission will send a copy of this Order, including this FRFA, to the

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<sup>594</sup> See Section IV.B.2.a above.

<sup>595</sup> See Section IV.B.2.a above.

<sup>596</sup> See Section IV.B.2.b above.

<sup>597</sup> See Section IV.B.2.b above.

<sup>598</sup> See Appendix B § 61.3(nn).

<sup>599</sup> See Section IV.B.2.b above; *see also April 14 VALOR Letter.*

<sup>600</sup> See 5 U.S.C. § 801(a)(1)(A).

Chief Counsel for Advocacy of the Small Business Administration. A copy of this Order and FRFA (or summaries thereof) will also be published in the Federal Register.<sup>601</sup>

## B. Paperwork Reduction Act

264. The action contained herein has been analyzed with respect to the Paperwork Reduction Act of 1995 and found to impose new or modified reporting and recordkeeping requirements or burdens on the public. Implementation of these new or modified reporting and recordkeeping requirements will be subject to approval by the Office of Management and Budget (OMB) as prescribed by the Act, and will go into effect upon announcement in the Federal Register of OMB approval.

## VI. ORDERING CLAUSES

265. IT IS ORDERED, pursuant to sections 1, 4(i) and (j), 201-209, 218-222, 254, and 403 of the Communications Act, as amended, 47 U.S.C. §§ 151, 154 (i), 154(j), 201-209, 218-222, 254, and 403 that this Order IS HEREBY ADOPTED as described above.

266. We, therefore, ORDER that the Inquiry initiated in CC Docket 99-249 is hereby TERMINATED. This action is taken pursuant to authority contained in Sections 4(i) and 303 of the Communications Act of 1934, as amended, 47 U.S.C. §§ 4(i), 303.

267. IT IS FURTHER ORDERED that the Commission's Consumer Information Bureau, Reference Information Center, SHALL SEND a copy of this Order, including the Final Regulatory Flexibility Analysis, to the Chief Counsel for Advocacy of the Small Business Administration.

268. IT IS FURTHER ORDERED that the provisions in this Order SHALL BE EFFECTIVE immediately upon publication in the Federal Register. Pursuant to 5 U.S.C. § 553(d)(3), we find good cause exists to have the rules take effect immediately upon publication in the Federal Register. Local exchange carriers subject to price cap regulation must file access reform tariffs no later than June 16, 2000 in order for them to be effective by July 1, 2000, as required by Section 69.3 of the Commission's rules, 47 C.F.R. § 69.3. In addition, to ensure that the local exchange carriers subject to price cap regulation have actual notice of these rules immediately following their release, we are serving those entities by overnight mail. The collections of information contained within are contingent upon approval by the Office of Management and Budget.

## FEDERAL COMMUNICATIONS COMMISSION

Magalie Roman Salas  
Secretary

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<sup>601</sup> See 5 U.S.C. § 604(b).

**APPENDIX A**  
**Parties Filing Pleadings<sup>602</sup>**

**I. CALLS NPRM**

**A. Comments**

1. Ad Hoc Telecommunications Users Committee (Ad Hoc)
2. Alliance for Public Technology (APT)
3. American Association of Retired Persons (AARP)
4. American Petroleum Institute (API)
5. Association For Local Telecommunications Services (ALTS)
6. AT&T Corp. (AT&T)
7. Cable and Wireless USA, Inc. (Cable & Wireless)
8. California Public Utilities Commission (California Commission)
9. Cincinnati Telephone Company (Cincinnati Bell)
10. Coalition for Affordable Local and Long Distance Service (CALLS)
11. Competition Policy Institute (CPI)
12. Competitive Telecommunications Assoc. (CompTel)
13. Florida Public Service Commission (Florida Commission)
14. General Services Administration (GSA)
15. State of Hawaii (Hawaii)
16. Intermedia Communications Inc. (Intermedia)
17. Texas – Office of Public Utilities Counsel; Consumer Federation of America; and Consumer Union (Joint Consumer Commenters)
18. Level 3 Communications, LLC (Level 3)
19. Massachusetts Department of Telecommunications and Energy (Mass. DTE)
20. MCI WorldCom, Inc. (MCI)
21. National Association of Regulatory Utilities Commission (NARUC)
22. National Assoc. of State Utility Consumer Advocates (NASUCA)
23. National Rural Telecom Assoc. (NRTA) and National Telephone Cooperative Assoc. (NTCA) (NRTA/NTCA)
24. New Jersey Division of the Ratepayer Advocate (New Jersey Div.)
25. Oncor Communications, Inc. (Oncor)
26. One Call Communications, Inc. (One Call)
27. Pathfinder Communications, Inc. (Pathfinder)
28. Public Utilities Commission of Ohio (Ohio Commission)
29. Qwest Communications Corp. (Qwest)
30. SBC Communications, Inc. (SBC)
31. The Small Company Committee of Wisconsin State Telecommunications Assoc. (WSTA-SCC)

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<sup>602</sup> We note that, in addition to the listed commenters, the Commission has received in excess of 15,000 “form” postcards identical in their wording from individuals in opposition to CALLS.

32. Smithville Telephone Company, Inc. (Smithville)
33. Telecommunication Resellers Assoc. (TRA)
34. Time Warner Telecom (Time Warner)
35. United States Telecom Association (USTA)
36. Washington Utilities and Transportation Commission (Washington Commission)

## **B. Reply Comments**

1. Ad Hoc
2. ALTS
3. APT
4. Bell Atlantic Telephone Companies (Bell Atlantic)
5. BellSouth Corporation (BellSouth)
6. Frank Bowe
7. Cable & Wireless
8. Cincinnati Bell
9. CALLS
10. CPI
11. Florida Commission
12. GSA
13. GTE Service Corporation (GTE)
14. Harlem Consumer Education Council, Inc.
15. Illinois Commerce Commission (Illinois Commission)
16. Iowa Utilities Board (Iowa Board)
17. Joint Consumer Commenters
18. League of United Latin American Citizens
19. Level 3
20. Michigan Public Service Commission (Michigan Commission)
21. National Association for the Advancement of Colored People (Washington Bureau) (NAACP)
22. National Association of Development Organizations (NADO)
23. NASUCA
24. Oncor
25. One Call
26. Personal Communications Industry Assoc. (PCIA)
27. Sprint Corporation (Sprint)
28. Vermont Department of Public Service (Vermont Dept.)
29. Western Wireless Corporation (Western Wireless)

**II. CALLS Public Notice****A. Comments**

1. Ad Hoc
2. Allegiance Telecom, Inc.
3. ALTS and Time Warner
4. American Public Communications Council (APCC)
5. API
6. APT
7. California Commission
8. CALLS
9. Cincinnati Bell
10. Citizens Utility Company (Citizens)
11. CompTel
12. CPI
13. Enterprise Networking Technologies Users Association (ENTUA)
14. Florida Commission
15. Focal Communications Corporation (Focal)
16. Global Crossing North America, Inc. (Global Crossing)
17. Independent Telephone and Telecommunications Alliance (ITTA)
18. Iowa Board
19. Joint Consumer Commenters
20. Level 3
21. MCI
22. Michigan Public Service Commission (Michigan Commission)
23. Missouri Public Service Commission (Missouri Commission)
24. Montana Public Service Commission (Montana Commission)
25. NARUC
26. NASUCA
27. New Jersey Division of Ratepayer Advocate (New Jersey Div.)
28. NTCA/NRTA
29. Oncor
30. One Call
31. Public Utilities Commission of Texas (Texas Commission)
32. Public Service Commission of Wisconsin (Wisconsin Commission)
33. Qwest
34. Rainbow/PUSH Coalition and Citizenship Education Fund  
(Rainbow/PUSH)
35. Rural Independent Competitive Alliance (RICA)
36. Shonah P. Jefferson
37. State Members of the Federal-State Joint Board on Universal Service  
(Joint Board)
38. TRA
39. United States Hispanic Chamber of Congress
40. USTA

41. U S West Communications, Inc. (U S West)
42. Valor Telecommunications Southwest, LLC (VALOR)
43. Wyoming Public Services Commission (Wyoming Commission)

## **B. Reply Comments**

1. AARP
2. Ad Hoc
3. Allegiance
4. ALTS and Time Warner
5. APCC
6. AT&T
7. Bell Atlantic
8. BellSouth
9. CALLS
10. CompTel
11. CPI
12. Florida Commission
13. Focal
14. Global Crossing
15. GTE
16. ITTA
17. Indiana Commission
18. Maine Public Utilities Commission (Maine Commission), Massachusetts Dept., and Oregon Public Utilities Commission (Oregon Commission) (collectively, Maine Joint Commenters)
19. Maryland Commission
20. MCI
21. NASUCA
22. National Consumers League (NCL) and Consumer Action (CA)
23. National Hispanic Council on Aging (NHCA)
24. Eliot Spitzer, Attorney General of the State of New York (New York Atty. Gen.)
25. One Call
26. Smithville
27. Sprint
28. Telefónica Larga Distancia de Puerto Rico, Inc. (TLD)
29. United Seniors Health Cooperative (United Seniors)
30. U S West
31. VALOR
32. Washington Utilities and Transportation Commission (Washington Commission)

**III. Low-Volume Notice of Inquiry Proceeding****A. Comments**

1. AARP
2. Ad Hoc
3. Ameritech
4. AT&T
5. Bell Atlantic
6. Bell South
7. City of New York
8. CompTel
9. Excel Communications, Inc.
10. GSA
11. GTE
12. Congressman Baron P. Hill
13. Joint Consumer Commenters
14. Kentucky Payphone Assoc., Michigan Payphone Assoc., and Payphone Assoc. of Ohio (collectively, Kentucky Joint Commenters)
15. MCI
16. Michigan Commission.
17. Pennsylvania Office of Consumer Advocate, Maryland Office of People's Counsel, New Mexico Attorney General, Missouri Office of the Public Counsel, the Connecticut Office of Consumer Counsel, the New Hampshire Office of Consumer Advocate, the Washington D.C. Office of People's Counsel, and the Washington Office of Attorney General) (collectively, Joint Consumer Advocates)
18. Qwest
19. RTC
20. Sprint
21. The Utility Reform Network (TURN)
22. USTA
23. Wisconsin Public Service Commission (Wisconsin Commission)

**B. Reply Comments**

1. AT&T
2. Bell Atlantic
3. GTE
4. Individual Commenters<sup>603</sup>

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<sup>603</sup> Richard A. Arsinow, Bob Beaudoin, Mr. And Mrs. James Besenger, Fred Bethke, Nancy T. Clark, Robert W. Cooper, Jr., Allan DeSmet, Sandra Farrell, D.D.S., Jonathan Freidin, Barbara N. Gibbons, Ms. Frances Gizerian, Frank Griffith, Donald G. Hyatt, Barry D. Johnson, David Krauser, Robert Lehr, Roger Merel, Ruth J. Pelt, Gwen Petitjean, Mark Plemmons, R. Rivera, Paul Schaeffer, Michael Schneider, Robert Sullivan, Richard Stallworthy.

5. Joint Consumer Commenters
6. MCI
7. Pathfinder
8. SBC
9. TRA
10. TURN

**APPENDIX B**  
**AMENDMENTS TO THE CODE OF FEDERAL REGULATIONS**

**PART 54**

**Subpart E - Universal Service Support for Low-Income Consumers**

**§ 54.403 Lifeline support amount.**

- (a) The federal Lifeline support amount for all eligible telecommunications carriers shall equal:
- (1) *Tier One.* The tariffed rate in effect for the primary residential End User Common Line charge of the incumbent local exchange carrier serving the area in which the qualifying low-income consumer receives service, as determined in accordance with § 69.104 or § 69.152(d) and (q), whichever is applicable;
  - (2) *Tier Two.* If the state commission approves an additional reduction of \$1.75 in the amount paid by consumers, additional federal Lifeline support in the amount of \$1.75 will be made available to the carrier providing Lifeline service to that consumer; and
  - (3) *Tier Three.* Additional federal Lifeline support in an amount equal to one-half the amount of any state Lifeline support will be made available to the carrier providing Lifeline service to a qualifying low-income consumer if the state commission approves an additional reduction in the amount paid by that consumer equal to the state support multiplied by 1.5.
- (b) For the qualifying low-income consumer, the federal Lifeline support amount shall not exceed \$3.50 plus the tariffed rate in effect for the primary residential End User Common Line charge of the incumbent local exchange carrier serving the area in which the qualifying low-income consumer receives service, as determined in accordance with § 69.104 or § 69.152(d) and (q), whichever is applicable. Eligible telecommunications carriers that charge federal End-User Common Line charges or equivalent federal charges shall apply Tier One federal Lifeline support to waive Lifeline consumers' federal End-User Common Line charges. Such carriers shall apply any additional federal support amount to a qualifying low-income consumer's intrastate rate, if the state has approved of such additional support. Other eligible telecommunications carriers shall apply Tier One federal Lifeline support amount, plus any additional federal support amount, to reduce their lowest tariffed (or otherwise generally available) residential rate for the services enumerated in § 54.101(a)(1) through (a)(9), and charge Lifeline consumers the resulting amount.
- (c) Lifeline support for providing toll limitation shall equal the eligible telecommunications carrier's incremental cost of providing either toll blocking or toll control, whichever is selected by the particular consumer.

**Subpart H—Administration****§ 54.701 Administrator of universal service support mechanisms.**

- (a) The Universal Service Administrative Company is appointed the permanent Administrator of the federal universal service support mechanisms, subject to a review after one year by the Federal Communications Commission to determine that the Administrator is administering the universal service support mechanisms in an efficient, effective, and competitively neutral manner.
- (b) The Schools and Libraries Corporation and the Rural Health Care Corporation shall merge into the Universal Service Administrative Company by January 1, 1999; provided, however, that the merger shall not take place until the Common Carrier Bureau, acting pursuant to delegated authority, has approved the merger documents, the amended by-laws, and the amended articles of incorporation, as set forth in paragraphs (c) and (d) of this section.
- (c) By December 1, 1998, the Schools and Libraries Corporation, the Rural Health Care Corporation and the Universal Service Administrative Company shall file with the Federal Communications Commission draft copies of all documents necessary to effectuate the merger.
- (d) By December 1, 1998, the Universal Service Administrative Company shall file with the Federal Communications Commission draft copies of amended by-laws and amended articles of incorporation.
- (e) Upon consummation of the merger of the Schools and Libraries Corporation and the Rural Health Care Corporation into the Universal Service Administrative Company, the Schools and Libraries Corporation and the Rural Health Care Corporation shall take all steps necessary to dissolve such corporations.
- (f) The Administrator shall establish a nineteen (19) member Board of Directors, as set forth in § 54.703. The Administrator's Board of Directors shall establish three Committees of the Board of Directors, as set forth in § 54.705: (1) the Schools and Libraries Committee, which shall oversee the schools and libraries support mechanism; (2) the Rural Health Care Committee, which shall oversee the rural health care support mechanism; and (3) the High Cost and Low Income Committee, which shall oversee the high cost and low income support mechanism. The Board of Directors shall not modify substantially the power or authority of the Committees of the Board without prior approval from the Federal Communications Commission.
- (g) The Administrator shall establish three divisions: (1) the Schools and Libraries Division, which shall perform duties and functions in connection with the schools and libraries support mechanism under the direction of the Schools and Libraries Committee of the Board, as set forth in § 54.705(a); (2) the Rural Health Care Division, which shall perform duties and functions in connection with the rural health care support mechanism under the direction of the Rural Health Care Committee of the Board, as set forth in § 54.705(b); and (3) the High

Cost and Low Income Division, which shall perform duties and functions in connection with the high cost and low income support mechanism, and the interstate access universal service support mechanism described in Subpart I of this Part, under the direction of the High Cost and Low Income Committee of the Board, as set forth in § 54.705(c). As directed by the Committees of the Board set forth in § 54.705, these divisions shall perform the duties and functions unique to their respective support mechanisms.

- (h) The Administrator shall be managed by a Chief Executive Officer, as set forth in § 54.704. The Chief Executive Officer shall serve on the Committees of the Board established in § 54.705.

**Sec. 54.702 Administrator's functions and responsibilities.**

- (a) The Administrator, and the divisions therein, shall be responsible for administering the schools and libraries support mechanism, the rural health care support mechanism, the high cost support mechanism, the low income support mechanism, and the interstate access universal service support mechanism described in Subpart I of this Part.
- (b) The Administrator shall be responsible for billing contributors, collecting contributions to the universal service support mechanisms, and disbursing universal service support funds.
- (c) The Administrator may not make policy, interpret unclear provisions of the statute or rules, or interpret the intent of Congress. Where the Act or the Commission's rules are unclear, or do not address a particular situation, the Administrator shall seek guidance from the Commission.
- (d) The Administrator may advocate positions before the Commission and its staff only on administrative matters relating to the universal service support mechanisms.
- (e) The Administrator shall maintain books of account separate from those of the National Exchange Carrier Association, of which the Administrator is an independent subsidiary. The Administrator's books of account shall be maintained in accordance with generally accepted accounting principles. The Administrator may borrow start up funds from the National Exchange Carrier Association. Such funds may not be drawn from the Telecommunications Relay Services (TRS) fund or TRS administrative expense accounts.
- (f) Pursuant to its responsibility for billing and collecting contributions, the Administrator shall compare periodically information collected by the administrator of the TRS Fund from TRS Fund Worksheets with information submitted by contributors on Universal Service Worksheets to verify the accuracy of information submitted on Universal Service Worksheets. When performing a comparison of contributor information as provided by this paragraph, the Administrator must undertake company-by-company comparisons for all entities filing Universal Service and TRS Fund Worksheets.
- (g) The Administrator shall create and maintain a website, as defined in Sec. 54.5, on which applications for services will be posted on behalf of schools, libraries and rural health care providers.
- (h) The Administrator shall file with the Commission and Congress an annual report by March

31 of each year. The report shall detail the Administrator's operations, activities, and accomplishments for the prior year, including information about participation in each of the universal service support mechanisms and administrative action intended to prevent waste, fraud, and abuse. The report also shall include an assessment of subcontractors' performance, and an itemization of monthly administrative costs that shall include all expenses, receipts, and payments associated with the administration of the universal service support programs. The Administrator shall consult each year with Commission staff to determine the scope and content of the annual report.

- (i) The Administrator shall report quarterly to the Commission on the disbursement of universal service support program funds. The Administrator shall keep separate accounts for the amounts of money collected and disbursed for eligible schools and libraries, rural health care providers, low-income consumers, interstate access universal service support, and high cost and insular areas.
- (j) Information based on the Administrator's reports will be made public by the Commission at least once a year as part of a Monitoring Report.
- (k) The Administrator shall provide the Commission full access to the data collected pursuant to the administration of the universal service support programs.
- (l) Pursuant to Sec. 64.903 of this chapter, the Administrator shall file with the Commission a cost allocation manual (CAM) that describes the accounts and procedures the Administrator will use to allocate the shared costs of administering the universal service support mechanisms and its other operations.
- (m) The Administrator shall make available to whomever the Commission directs, free of charge, any and all intellectual property, including, but not limited to, all records and information generated by or resulting from its role in administering the support mechanisms, if its participation in administering the universal service support mechanisms ends.
- (n) If its participation in administering the universal service support mechanisms ends, the Administrator shall be subject to close-out audits at the end of its term.

**Sec. 54.703 and Sec. 54.704 remain unchanged.**

**Sec. 54.705 Committees of the Administrator's Board of Directors.**

- (a) Schools and Libraries Committee.--

(1) Committee functions. The Schools and Libraries Committee shall oversee the administration of the schools and libraries support mechanism by the Schools and Libraries Division. The Schools and Libraries Committee shall have the authority to make decisions concerning:

- (A) How the Administrator projects demand for the schools and libraries support

mechanism;

- (B) Development of applications and associated instructions as needed for the schools and libraries support mechanism;
  - (C) Administration of the application process, including activities to ensure compliance with Federal Communications Commission rules and regulations;
  - (D) Performance of outreach and education functions;
  - (E) Review of bills for services that are submitted by schools and libraries;
  - (F) Monitoring demand for the purpose of determining when the \$2 billion trigger has been reached;
  - (G) Implementation of the rules of priority in accordance with § 54.507(g) of this chapter;
  - (H) Review and certification of technology plans when a state agency has indicated that it will not be able to review such plans within a reasonable time;
  - (I) The classification of schools and libraries as urban or rural and the use of the discount matrix established in § 54.505(c) of this chapter to set the discount rate to be applied to services purchased by eligible schools and libraries;
  - (J) Performance of audits of beneficiaries under the schools and libraries support mechanism; and
  - (K) Development and implementation of other functions unique to the schools and libraries support mechanism.
- (2) Committee composition. The Schools and Libraries Committee shall consist of the following members of the Administrator's Board of Directors:
- (A) Three school representatives;
  - (B) One library representative;
  - (C) One service provider representative;
  - (D) One at-large representative elected by the Administrator's Board of Directors; and
  - (E) The Administrator's Chief Executive Officer.

- (b) Rural Health Care Committee.--

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- (1) Committee functions. The Rural Health Care Committee shall oversee the administration of the rural health care support mechanism by the Rural Health Care Division. The Rural Health Care Committee shall have authority to make decisions concerning:
- (A) How the Administrator projects demand for the rural health care support mechanism;
  - (B) Development of applications and associated instructions as needed for the rural health care support mechanism;
  - (C) Administration of the application process, including activities to ensure compliance with Federal Communications Commission rules and regulations;
  - (D) Calculation of support levels under § 54.609;
  - (E) Performance of outreach and education functions;
  - (F) Review of bills for services that are submitted by rural health care providers;
  - (G) Monitoring demand for the purpose of determining when the \$400 million cap has been reached;
  - (H) Performance of audits of beneficiaries under the rural health care support mechanism; and
  - (I) Development and implementation of other functions unique to the rural health care support mechanism.
- (2) Committee composition. The Rural Health Care Committee shall consist of the following members of the Administrator's Board of Directors:
- (A) Two rural health care representatives;
  - (B) One service provider representative;
  - (C) Two at-large representatives elected by the Administrator's Board of Directors;
  - (D) One State telecommunications regulator, one state consumer advocate; and
  - (E) The Administrator's Chief Executive Officer.
- (c) High Cost and Low Income Committee.--

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- (1) Committee functions. The High Cost and Low Income Committee shall oversee the administration of the high cost and low income support mechanisms and the interstate access universal service support mechanism described in Subpart I of this Part, by the High Cost and Low Income Division. The High Cost and Low Income Committee shall have the authority to make decisions concerning:
- (A) How the Administrator projects demand for the high cost, low income, and interstate access universal service support mechanisms;
  - (B) Development of applications and associated instructions as needed for the high cost, low income, and interstate access universal service support mechanisms;
  - (C) Administration of the application process, including activities to ensure compliance with Federal Communications Commission rules and regulations;
  - (D) Performance of audits of beneficiaries under the high cost, low income, and interstate access universal service support mechanisms; and
  - (E) Development and implementation of other functions unique to the high cost, low income, and interstate access universal service support mechanisms.
- (2) Committee composition. The High Cost and Low Income Committee shall consist of the following members of the Administrator's Board of Directors:
- (A) One low income representative;
  - (B) One state telecommunications regulator;
  - (C) One state consumer advocate;
  - (D) Two incumbent local exchange carrier representatives (one shall represent rural telephone companies, as that term is defined in 47 U.S.C. 153(37) and one shall represent non-rural telephone companies);
  - (E) One interexchange carrier representative;
  - (F) One competing local exchange carrier representative;
  - (G) One commercial mobile radio service representative; and
  - (H) The Administrator's Chief Executive Officer.
- (d) Binding Authority of Committees of the Board.
- (1) Any action taken by the Committees of the Board established in paragraphs (a)

through (c) of this section shall be binding on the Board of Directors of the Administrator, unless such action is presented for review to the Board by the Administrator's Chief Executive Officer and the Board disapproves of such action by a two-thirds vote of a quorum of directors, as defined in the Administrator's by-laws.

- (2) The budgets prepared by each Committee shall be subject to Board review as part of the Administrator's combined budget. The Board shall not modify the budgets prepared by the Committees of the Board unless such modification is approved by a two-thirds vote of a quorum of the Board, as defined in the Administrator's by-laws.

**Secs. 54.706 – 54.714 remain unchanged.**

**Sec. 54.715 Administrative expenses of the Administrator.**

- (a) The annual administrative expenses of the Administrator should be commensurate with the administrative expenses of programs of similar size, with the exception of the salary levels for officers and employees of the Administrator described in paragraph (b) of this section. The annual administrative expenses may include, but are not limited to, salaries of officers and operations personnel, the costs of borrowing funds, equipment costs, operating expenses, directors' expenses, and costs associated with auditing contributors of support recipients.
- (b) All officers and employees of the Administrator may be compensated at an annual rate of pay, including any non-regular payments, bonuses, or other compensation, in an amount not to exceed the rate of basic pay in effect for Level I of the Executive Schedule under 5 U.S.C. 5312.
- (c) The Administrator shall submit to the Commission projected quarterly budgets at least sixty (60) days prior to the start of every quarter. The Commission must approve the projected quarterly budgets before the Administrator disburses funds under the federal universal service support mechanisms. The administrative expenses incurred by the Administrator in connection with the schools and libraries support mechanism, the rural health care support mechanism, the high cost support mechanism, the low income support mechanism, and the interstate access universal service support mechanism shall be deducted from the annual funding of each respective support mechanism. The expenses deducted from the annual funding for each support mechanism also shall include the Administrator's joint and common costs allocated to each support mechanism pursuant to the cost allocation manual filed by the Administrator under § 64.903 of this chapter.

**Sec. 54.717 remains unchanged.**

**Subpart I - Interstate Access Universal Service Support Mechanism [All New]****§ 54.800 Terms and Definitions**

- (a) *Average Price Cap CMT Revenue Per Line Per Month<sub>Study Area</sub>* has the same meaning as that term is defined in § 61.3(d), except that it includes exogenous changes in effect prior to the effective date of a calculation made pursuant to § 54.808 and exogenous changes not yet effective related to the sale or acquisition of exchanges, but excludes any other exogenous changes or other changes made pursuant to § 61.45(i)(4) not yet effective.
- (b) *Base Period Lines* –For purposes of calculations pursuant to this Subpart, Base Period Lines are the number of lines for a given study area or zone as of the end of the quarter ending 6 months prior to the effective date of a calculation pursuant to § 54.808.
- (c) *Interstate Access Universal Service Support Benchmark* shall mean, for residential and single line business lines, \$7.00, and for multi-line business lines, \$9.20.
- (d) *Minimum Adjustment Amount (MAA)* is defined in § 54.806(f).
- (e) *MAA Phase In Percentage* is:  
50% as of July 1, 2000,  
75% as of July 1, 2001  
100% as of July 1, 2002.
- (f) *Minimum Delta (MD)* is defined in § 54.806(d).
- (g) *Minimum Support Requirement (MSR)* is defined in § 54.806(g).
- (h) *Nationwide Total Above Benchmark Revenues* is defined in § 54.806(b).
- (i) *Price cap LEC* is defined in § 54.802(c).
- (j) *Preliminary Minimum Access Universal Service Support<sub>study area</sub>* is the amount calculated pursuant to § 54.804.
- (k) *Preliminary Study Area Universal Service Support (PSAUSS)* is defined in § 54.806(c).
- (l) *Study Area Above Benchmark Revenues* is the sum of all Zone Above Benchmark Revenues for all zones in the study area.
- (m) *Study Area Access Universal Service Support (SAAUS)* is defined in § 54.806(i) and (j).
- (n) *Total National Minimum Delta (TNMD)* is the nationwide sum of all study area Minimum Deltas.
- (o) *Total National Minimum Support Requirement (TNMSR)* is the sum of the MSR for all

price cap incumbent LEC study areas.

- (p) *Zone Above Benchmark Revenues* is defined in § 54.805(a)(2).
- (q) *Zone Average Revenue per Line*. The amount calculated as follows:

Zone Average Revenue Per Line = (25% \* (Loop<sub>zone price</sub> + (Port)<sub>price</sub>))+ U (Uniform revenue per line adjustment) where,

$$U = [(Average\ Price\ Cap\ CMT\ Revenue\ Per\ Line\ Per\ Month_{study\ area} * ILEC\ Base\ Period\ Lines) - (25\% * \sum (ILEC\ Base\ Period\ Lines_{SUNE\ Zone} * ((Loop_{zone\ price} + Port\ Price) \text{ for all zones})))] \div ILEC\ Base\ Period\ Lines_{Study\ Area(s)}$$

### § 54.801 General

- (a) The total amount of universal service support under this Subpart, excluding administrative expenses, for areas served by price cap incumbent LECs as of June 30, 2000, is targeted to be \$650 million per year, if no exchanges, other than those offered for sale prior to July 1, 2000, are sold to non-price-cap LECs or purchased from non-price cap LECs by price cap LECs.
- (b) In the event that all or a portion of a study area served by a price cap LEC is sold to an entity other than a price cap LEC, and the study area or portion thereof was not offered for sale prior to July 1, 2000, then the support that would otherwise be provided under this Subpart, had such study area or portion thereof not been sold, will not be distributed or collected. Subsequent calculations will use the last reported data for the study area or portion thereof that was sold to determine the amount that will not be distributed or collected.
- (c) In the event that a price cap LEC acquires additional exchanges, from an entity other than a price cap LEC, that acquisition should be reported to the Administrator pursuant to § 54.802 and included in the determination of study area support pursuant to § 54.806 for the areas served by the acquiring price cap LEC, beginning with the next support recalculation pursuant to § 54.808.
- (d) In the event that a price cap LEC acquires additional exchanges from an entity that is also a price cap LEC, the acquiring price cap LEC will receive support under this Subpart at the same level as the selling price cap LEC formerly received, and both carriers will adjust their line counts accordingly beginning with the next quarterly report to the Fund Administrator. At the subsequent report to the Fund Administrator for purposes of recalculating support as required by section 54.808, the acquiring and selling price cap LECs will reflect the acquired and sold lines, and will adjust the average CMT Revenue per Line per Month for the affected study areas accordingly.
- (e) The Fund Administrator for the fund created by this subpart shall be the Universal Service Administrative Company.

**§ 54.802 Obligations of LECs and the Fund Administrator**

- (a) Each Eligible Telecommunications Carrier that is providing service within an area served by a price cap LEC shall submit to the Fund Administrator, on a quarterly basis on the last business day of March, June, September, and December of each year line count data showing the number of lines it serves for the period ending three months prior to the reporting date, within each price cap LEC study area disaggregated by UNE Zone if UNE Zones have been established within that study area, showing residential/single line business and multi-line business line counts separately. For purposes of this report, and for purposes of computing support under this Subpart, the aggregated residence/single line business class lines reported include single and non-primary residence lines, single line business lines, ISDN BRI and other related residence class lines. Similarly, the multi-line business class lines reported include multi-line business, centrex, ISDN PRI and other related business class lines assessed the End User Common Line charge pursuant to § 69.152. For purposes of this report and for purposes of computing support under this Subpart, lines served using resale of the price cap LEC's service pursuant to Section 251(c)(4) of the Communications Act of 1934, as amended, shall be considered lines served by the price cap LEC only and must be reported accordingly.
- (b) In addition to the information submitted pursuant to paragraph (a), each price cap LEC must submit to the Fund Administrator, on June 30, 2000, October 15, 2000, and April 16, 2001 and annually thereafter or as determined by the Fund Administrator according to Section 54.808:
- (1) Average Price Cap CMT Revenue Per Line Per Month<sub>Study Area</sub> for each of its study areas;
  - (2) The rates established for UNE Loops and UNE Line Ports, by zone in those study areas where UNE Zones have been established as of the date of filing; and
  - (3) Make available information sufficient to determine the boundaries of each UNE Zone within each of its study areas where such zones have been established;
- provided, however, that after the June 30, 2000 filing, if there have been no changes since its previous filing a company may submit a statement that there have been no changes in lieu of such information, and further provided that, for study areas in which UNE Zones have been newly established since the last filing pursuant to this paragraph, the price cap LEC shall also report the information required by subparagraph (2) and (3) to the Fund Administrator on July 15, 2000, or January 15, 2001, as required.
- (d) An eligible telecommunications carrier shall be eligible for support pursuant to this Subpart only after it has filed all of the information required by paragraphs (a) through (c) of this section, where applicable. An eligible telecommunications carrier shall receive payment of support pursuant to this Subpart only for such months the carrier is actually providing service to the end user. The Administrator shall ensure that there is periodic reconciliation of support payments.
- (e) Upon receiving the information required to be filed in paragraphs (a) and (b) of this section, the Fund Administrator shall:
- (1) Perform the calculations described in sections 54.804 through 54.807 of this section;
  - (2) Publish the results of these calculations showing Interstate Access Universal Service

Support Per Line available in each price cap LEC study area, by UNE Zone and customer class;

- (3) Collect the funds necessary to provide support pursuant to this Subpart in accordance with Subpart H; and
- (4) Distribute support calculated pursuant to the rules contained in this Subpart; and
- (5) Report quarterly to the Commission on the collection and distribution of funds under this Subpart as described in 54.701(g). Fund distribution reporting will be by state and by eligible telecommunications carrier within the state.

### § 54.803 Universal Service Zones

- (a) The zones used for determining interstate access universal service support shall be the same zones that would be used for EUCL deaveraging as described in §69.152(q)(2).
- (b) In a price cap study area where the price cap LEC has not established state-approved prices for UNE loops by zone, the fund administrator shall develop an estimate of the ILEC's Zone Above Benchmark Revenues for transitional purposes, in order to reserve a portion of the fund for that study area. This estimate will be included by the Administrator in the Nationwide Study Area Above Benchmark Revenues calculated pursuant to §54.806.
  - (1) For the purpose of developing this transitional estimate, the loop and port costs estimated by the FCC cost model, or other substitute method if no model is available, shall be used.
  - (2) For the purpose of developing this transitional estimate, the administrator shall construct three zones. Wire centers within the study area will be grouped into these zones in such a way that each zone is assigned approximately one third of ILEC base period lines in the study area, with the lowest cost wire centers assigned to Zone 1, the highest cost wire centers assigned to Zone 3, and the remainder to Zone 2.

### § 54.804 Preliminary Minimum Access Universal Service Support<sub>Study Area</sub> Calculated by the Fund Administrator.

- (a) If Average Price Cap CMT Revenue Per Line Per Month<sub>Study Area</sub> is greater than \$9.20 then: Preliminary Minimum Access Universal Service Support<sub>study area</sub> = (Average Price Cap CMT Revenue Per Line Per Month<sub>study area</sub> x ILEC Base Period Lines x 12) - ((\$7.00 x ILEC Base Period Residential & Single Line Business Lines<sub>Study area</sub> x 12) + (\$9.20 x ILEC Base Period Multi-line Business Lines<sub>Study area</sub> x 12))
- (b) If Average Price Cap CMT Revenue Per Line Per Month<sub>Study Area</sub> is greater than \$7.00 but less than \$9.20 then: Preliminary Minimum Access Universal Service Support<sub>study area</sub> = (Average Price Cap CMT Revenue Per Line Per Month<sub>Study Area</sub> - \$7.00) x (ILEC Base Period Residential & Single Line Business Lines<sub>Study area</sub> x 12)
- (c) If Average Price Cap CMT Revenue Per Line Per Month<sub>Study Area</sub> is less than \$7.00 then the

Preliminary Minimum Access Universal Service Support<sub>study area</sub> is zero.

**§54.805 Zone and Study Area Above Benchmark Revenues Calculated by the Fund Administrator.**

- (a) The following steps shall be performed by the Fund Administrator to determine Zone Above Benchmark Revenues for each price cap LEC.
- (1) Calculate Zone Average Revenue Per Line.
  - (2) Calculate Zone Above Benchmark Revenues. Zone Above Benchmark Revenues is the sum of Zone Above Benchmark Revenues<sub>Residence&SingleLineBusiness</sub> and Zone Above Benchmark Revenues<sub>Multi-lineBusiness</sub>. Zone Above Benchmark Revenues<sub>Residence&SingleLineBusiness</sub> is, within each zone, the product of Zone Average Revenue Per Line minus \$7.00 multiplied by all eligible telecommunications carrier Base Period Line<sub>Residence and Single Line Business</sub> times 12. If negative, the Zone Above Benchmark Revenues<sub>Residence&SingleLineBusiness</sub> for the zone is zero. Zone Above Benchmark Revenues<sub>Multi-lineBusiness</sub> is, within each zone, the product of Zone Average Revenue Per Line minus \$9.20 multiplied by all eligible telecommunications carrier zone Base Period Lines<sub>Multi-lineBusiness</sub> times 12. If negative, the Zone Above Benchmark Revenues<sub>Multi-lineBusiness</sub> for the zone is zero.
- (b) Study Area Above Benchmark Revenues is the sum of Zone Above Benchmark Revenues for all zones in the study area.

**§ 54.806 Calculation by the Fund Administrator of Interstate Access Universal Service Support for Areas Served by Price cap LECs**

- (a) The Fund Administrator, based on the calculations performed in sections 54.804 and 54.805, shall calculate the Interstate Access Universal Service Support for areas served by price cap LECs according to the following methodology:
- (b) Calculate Nationwide Total Above Benchmark Revenues. Nationwide Total Above Benchmark Revenues is the sum of all Study Area Above Benchmark Revenues for all study areas served by price cap ILECs,
  - (c) Calculate Preliminary Study Area Universal Service Support (PSAUSS).
    - (1) If the Nationwide Total Above Benchmark Revenues is greater than \$650 million, then the Preliminary Study Area Universal Service Support (PSAUSS) equals the Study Area Above Benchmark Revenues multiplied by the ratio of \$650 million to Nationwide Total Above Benchmark Revenues (i.e. Preliminary Study Area Universal Service Support = Study Area Above Benchmark Revenues X (\$650 Million / Nationwide Total Above Benchmark Revenues).

- (2) If the Nationwide Total Above Benchmark Revenues is not greater than \$650 million, PSAUSS equals the Study Area Above Benchmark Revenues.
- (d) Calculate the Minimum Delta (MD) by study area. Within each study area the Minimum Delta will be equal to the Preliminary Minimum Access Universal Service Support<sub>Study Area</sub> less the PSAUSS, if the difference is greater than zero. If the difference is less than or equal to zero, the MD is equal to zero.
- (e) Calculate the Total National Minimum Delta (TNMD) by summing all study area Minimum Deltas nationwide.
- (f) Calculate the Minimum Adjustment Amount.
- (1) If the TNMD is greater than \$75 million, then the Minimum Adjustment Amount (MAA) equals the product of the MAA Phase In Percentage times the MD by study area times the ratio of \$75 million to TNMD Or:
- $$\text{Minimum Adjustment Amount} = (\text{MAA Phase In Percentage}) \times (\text{Minimum Delta}) \times (\$75 \text{ million} / \text{Total National Minimum Delta}).$$
- (2) If the TNMD is less than \$75 million, then the MAA equals the product of the MAA Phase In Percentage and the MD by study area.
- (g) Calculate the Minimum Support Requirement (MSR). The Minimum Support Requirement for a study area equals the PSAUSS plus the MAA.
- (h) Calculate the Total National Minimum Support Requirement (TNMSR), which equals the sum of the MSR for all study areas in which the Preliminary Minimum Access Universal Service Support is greater than or equal to the PSAUSS.
- (i) Calculate Study Area Access Universal Service Support (SAAUS) for a study area in which the price cap incumbent LEC has geographically deaveraged state-approved rates for UNE loops:
- (1) For study areas in which the Preliminary Minimum Access Universal Service Support is greater than PSAUSS, and within which the price cap incumbent LEC has established geographically deaveraged state-approved rates for UNE loops, the SAAUS for that study area is the MSR.
- (2) For study areas in which the Preliminary Minimum Access Universal Service Support is less than PSAUSS, and within which the price cap incumbent LEC has established geographically deaveraged state-approved rates for UNE loops, the SAAUS for that study area is equal to:
- $$\text{Preliminary Study Area Universal Service Support} \times (\$650 \text{ million} - \text{TNMSR}) \div (\text{the sum of PSAUSS of study areas where the Preliminary Minimum Access Universal Service Support is less than PSAUSS}).$$
- (j) Calculate Study Area Access Universal Service Support (SAAUS) for a price cap incumbent LEC that has not established geographically deaveraged state-approved rates for UNE loops. In such study areas, the SAAUS shall be the lesser of the Preliminary Minimum Access Universal Service Support or:

- (1) For study areas in which the Preliminary Minimum Access Universal Service Support is greater than PSAUSS, and for which an estimate has been made for deaveraged UNE loop costs, the SAAUS for that study area is the MSR.
- (2) For study areas in which the Preliminary Minimum Access Universal Service Support is less than PSAUSS, and for which an estimate has been made for deaveraged UNE loop costs, the SAAUS for that study area is equal to:

Preliminary Study Area Universal Service Support x (\$650 million – TNMSR) ÷  
(the sum of PSAUSS of study areas where the Preliminary Minimum Access Universal Service Support is less than PSAUSS).

**§ 54.807 Interstate Access Universal Service Support**

- (a) Each Eligible Telecommunication Carrier (ETC) that provides supported service within the study area of a price cap LEC shall receive Interstate Access Universal Service Support for each line that it serves within that study area.
- (b) In any study area within which the incumbent LEC has not established state approved geographically deaveraged rates for UNE loops, the Fund Administrator shall calculate the Interstate Access Universal Service Support Per Line by dividing Study Area Access Universal Service Support by twelve times all eligible telecommunications carriers' base period lines in that study area adjusted for growth during the relevant support period based on the average nationwide annual growth in eligible lines during the three previous years. For the purpose of calculating growth, the Fund Administrator shall use a simple average of annual growth rates for total switched access lines for the three most recent years as reported in the Common Carrier Bureau Report, Statistics of Communications Common Carriers, Table 6.10 – Selected Operating Statistics.
- (c) In any study area within which the incumbent LEC has established state approved geographically deaveraged rates for UNE loops, the Fund Administrator shall calculate the Interstate Access Universal Service Support Per Line for each customer class and zone using all eligible telecommunications carriers' base period lines by customer class and zone adjusted for growth during the relevant support period based on the average nationwide annual growth in eligible lines during the three previous years. For the purpose of calculating growth, the Fund Administrator shall use a simple average of annual growth rates for total switched access lines for the three most recent years as reported in the Common Carrier Bureau Report, Statistics of Communications Common Carriers, Table 6.10 – Selected Operating Statistics. Support shall be allocated to lines in the highest cost UNE zone first, and will “cascade” to lines in lower cost UNE zones to the extent that sufficient funding is available. Beginning with the zone with the highest Zone Average Revenue Per Line, support will be applied in the following order of priority:
  - (1) To all lines in the highest zone, to eliminate the amount per line by which Zone Average Revenue Per Line exceeds the higher of \$9.20 or the Average Revenue Per Line in the next highest zone;
  - (2) If the Zone Average Revenue Per Line in the next highest zone is greater than \$9.20, then to all lines in both zones to eliminate the amount per line by which Zone Average

- Revenue per Line exceeds \$9.20 or the Zone Average Revenue Per Line in the third highest zone. This application of support will continue to additional zones in the same fashion until the amount per line by which Zone Average Revenue Per Line exceeds \$9.20 has been eliminated in all zones, or until the available support has been exhausted;
- (3) To all residential and single line business lines in the highest zone, to eliminate the remaining amount per line that Zone Average Revenue Per Line for these lines exceeds the higher of \$7.00 or Zone Average Revenue Per Line in the next highest zone;
  - (4) If the Zone Average Revenue per Line in the next highest zone is greater than \$7.00, then to all residential and single line business lines in both zones to eliminate the remaining amount per line by which Zone Average Revenue Per Line exceeds \$7.00. This application of support will continue to additional zones in the same fashion until the difference between Zone Average Revenue Per Line and \$7.00 has been eliminated in all zones, or until the available support has been exhausted.
- (d) Notwithstanding the provisions of 54.307(a)(2), the per-line support amount determined within each zone by applicable customer class under paragraph (b) or (c) above is portable among all eligible telecommunications carriers providing service within that zone.

#### **§ 54.808 Transition Provisions and Periodic Calculation.**

Study Area Access Universal Service Support amounts for the area served by each price cap incumbent LEC will be calculated as of July 1, 2000, January 1, 2001, July 1, 2001 and thereafter as determined by the Administrator, but at least annually.

#### **§ 54.809 Carrier Certification**

- (a) *Certification.* Carriers that desire to receive support pursuant to section 54.807 must file a certification with the Administrator and the Commission stating that all interstate access universal service support provided to such carrier will be used only for the provision, maintenance, and upgrading of facilities and services for which the support is intended. Support provided pursuant to section 54.807 shall only be provided to the extent that the carrier has filed the requisite certification pursuant to this section.
- (b) *Certification Format.* A certification pursuant to this section may be filed in the form of a letter from an authorized representative for the carrier, and must be filed with both the Office of the Secretary of the Commission clearly referencing CC Docket No. 96-45, and with the Administrator of the interstate access universal service support mechanism, on or before the filing deadlines set forth below in subsection (c). All of the certifications filed by carriers pursuant to this section shall become part of the public record maintained by the Commission.
- (c) *Filing Deadlines.* In order for a price cap local exchange carrier, and/or an eligible telecommunications carriers serving lines in the service area of a price cap local exchange carrier, to receive interstate access universal service support, such carrier must file an annual certification, as described in subsection (b), on the date that it first files its line count

information pursuant to section 54.802, and thereafter on June 30<sup>th</sup> of each year.

## PART 61 – TARIFFS

### § 61.3 Definitions

- (a) *Act*. The Communications Act of 1934 (48 Stat. 1004; 47 U.S.C. chapter 5), as amended.
- (b) *Actual Price Index (API)*. An index of the level of aggregate rate element rates in a basket, which index is calculated pursuant to § 61.46.
- (c) *Association*. This term has the meaning given it in § 69.2(d).
- (d) *Average Price Cap CMT Revenue per Line month*. Price Cap Common Line, and Marketing Per Residual Interconnection Charge Revenue (CMT Revenue) per month as of July 1, 2000 (adjusted to remove Universal Service Contributions assessed to Local Exchange Carriers pursuant to 54.702) using 2000 annual filing base period demand, divided by the 2000 annual filing base period demand. In filing entities with multiple study areas, if it becomes necessary to calculate the Price Cap CMT Revenue Per Line for a specific study area, then the Price Cap CMT Revenue Per Line for that study area is determined as follows, using base period demand revenues (adjusted to remove Universal Service Contributions assessed to Local Exchange Carriers pursuant to 54.702), Base Factor Portion (BFP) and 2000 annual filing base period lines:

$$\text{PriceCapCMTRevenuePerLineMonth}_{\text{StudyArea}} = \frac{\text{PriceCapCMTRevenue}_{\text{FilingEntity}} \times (\text{BFP}_{\text{StudyArea}} \div \text{BFP}_{\text{FilingEntity}})}{\text{Lines}_{\text{StudyArea}}}$$

Nothing in this definition precludes a price cap local exchange carrier from continuing to average rates across filing entities containing multiple study areas, where permitted under existing rules.

Average Price Cap CMT Revenues Per Line month may be adjusted after July 1, 2000 to reflect exogenous costs pursuant to 61.45(d).

Average Price Cap CMT Revenues Per Line month may also be adjusted pursuant to 61.45(b)(1)(iii).

(e) *Average Traffic Sensitive Charge*.

(1) The Average Traffic Sensitive Charge ("ATS charge") is the sum of the following two components:

(A) The Local Switching (LS) component will be calculated by dividing the proposed Local Switching revenues (End Office Switch, LS trunk ports, Information Surcharge, and signalling transfer point (STP) port) by the base period LS minutes of use (MOUs); and

(B) The Transport component will be calculated by dividing the proposed Transport revenues (Switched Direct Trunk Transport, Signalling for Switched

Direct Trunk Transport, Entrance Facilities for Switched Access traffic, Tandem Switched Transport, Signalling for Tandem Switching and residual per minute Transport Interconnection Charge (TIC) pursuant to §69.155 by incumbent LEC only base period MOUs (including meet-point billing arrangements for jointly-provided interstate access by an incumbent LEC and any other LEC).

(2) For the purposes of determining whether the ATS charge has reached the Target Rate as set forth in 61.3(qq), the calculations should include all the relevant revenues and minutes for services provided under generally available tariffs.

(f) **Band.** A zone of pricing flexibility for a service category, which zone is calculated pursuant to § 61.47.

(g) **Base period.** For carriers subject to §§ 61.41-61.49, the 12-month period ending six months prior to the effective date of annual price cap tariffs. Base year or base period earnings shall exclude amounts associated with exogenous adjustments to the PCI for the lower formula adjustment mechanism permitted by § 61.45(d)(1)(vii).

(h) **Basket.** Any class or category of tariffed service or charge:

- (1) Which is established by the Commission pursuant to price cap regulation;
- (2) The rates of which are reflected in an Actual Price Index; and
- (3) The related revenues of which are reflected in a Price Cap Index.

(i) **Change in rate structure.** A restructuring or other alteration of the rate components for an existing service.

(j) **Charges.** The price for service based on tariffed rates.

(k) **Commercial contractor.** The commercial firm to whom the Commission annually awards a contract to make copies of Commission records for sale to the public.

(l) **Commission.** The Federal Communications Commission.

(m) **Concurring carrier.** A carrier (other than a connecting carrier) subject to the Act which concurs in and assents to schedules of rates and regulations filed on its behalf an issuing carrier or carriers.

(n) **Connecting carrier.** A carrier engaged in interstate or foreign communication solely through physical connection with the facilities of another carrier not directly or indirectly controlling or controlled by, or under direct or indirect common control with, such carrier.

(o) **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.

(p) **Corrections**. The remedy of errors in typing, spelling, or punctuations.

(q) **Dominant carrier**. A carrier found by the Commission to have market power (*i.e.*, power to control prices).

(r) **GDP Price Index (GDP-PI)**. The estimate of the Chain-Type Price Index for Gross Domestic Product published by the United States Department of Commerce, which the Commission designates by Order.

(s) **GNP Price Index (GNP-PI)**. The estimate of the "Fixed-Weighted Price Index for Gross National Product, 1982 Weights" published by the United States Department of Commerce, which the Commission designates by Order.

(t) **Issuing carrier**. A carrier subject to the Act that publishes and files a tariff or tariffs with the Commission.

(u) **Line Month**. Line demand per month multiplied by twelve.

(v) **Local Exchange Carrier**. Any person that is engaged in the provision of telephone exchange service or exchange access as defined in section 3(26) of the Act.

(w) **Mid-size Company**. All price cap local exchange carriers other than the Regional Bell Operating Companies and GTE.

(x) **New service offering**. A tariff filing that provides for a class or sub-class of service not previously offered by the carrier involved and that enlarges the range of service options available to ratepayers.

(y) **Non-dominant carrier**. A carrier not found to be dominant.

(z) **Other participating carrier**. A carrier subject to the Act that publishes a tariff containing rates and regulations applicable to the portion or through service it furnishes in conjunction with another subject carrier.

(aa) **Price cap LEC**. See Part 54.802(c).

(bb) **Local Switching Pooled Revenue**, for certain qualified companies as set forth in §61.48 (m), is the amount of additional Local Switching reductions in the July 2000 Annual filing allowed to be moved and recovered in the Common Line Basket.

(cc) **Price Cap CMT Revenue**. The maximum total revenue a filing entity would be permitted to receive from End User Common Line charges under § 69.152, Presubscribed Interexchange Carrier charges (PICCs) under § 69.153, Carrier Common Line charges under § 69.154, and Marketing under 69.156, using Base Period lines. Price Cap CMT Revenue does not include the

local exchange carrier universal service contributions as of July 1, 2000. The Price Cap CMT revenue does not include the Local Switching Pooled revenue outlined in § 61.3 (bb), above.

(dd) **Price Cap Index (PCI)**. An index of prices applying to each basket of services of each carrier subject to price cap regulation, and calculated pursuant to § 61.45.

(ee) **Price cap regulation**. A method of regulation of dominant carriers provided in §§ 61.41 through 61.49 or §§ 61.41 through 61.49.

(ff) **Price cap tariff filing**. Any tariff filing involving a service subject to price cap regulation, or that requires calculations pursuant to §§ 61.45, 61.46, or 61.47.

(gg) **Productivity factor**. An adjustment factor used to make annual adjustments to the Price Cap Index to reflect the margin by which a carrier subject to price cap regulation is expected to improve its productivity relative to the economy as a whole.

(hh) **Rate**. The tariffed price per unit of service.

(ii) **Rate increase**. Any change in a tariff which results in an increased rate or charge to any of the filing carrier's customers.

(jj) **Rate level change**. A tariff change that only affects the actual rate associated with a rate element, and does not affect any tariff regulations or any other wording of tariff language.

(kk) **Regulations**. The body of carrier prescribed rules in a tariff governing the offering of service in that tariff, including rules, practices, classifications, and definitions.

(ll) **Restructured service**. An offering which represents the modification of a method of charging or provisioning a service; or the introduction of a new method of charging or provisioning that does not result in a net increase in options available to customers.

(mm) **Rural Company**. A company that, as of December 31, 1999, was certified to the Commission as a rural telephone company.

(nn) **Service Band Index (SBI)**. An index of the level of aggregate rate element rates in a service category, which index is calculated pursuant to § 61.47.

(oo) **Service category**. Any group of rate elements subject to price cap regulation, which group is subject to a band.

(pp) **Supplement**. A publication filed as part of a tariff for the purpose of suspending or canceling that tariff, or tariff publication and numbered independently from the tariff page series.

(qq) **Target Rate**. The applicable Target Rate shall be defined as follows:

- (1) For regional Bell Operating Companies and GTE, \$0.0055 per ATS minute of use;

(2) For a holding company with a holding company average of less than 19 Switched Access End User Common Line charge lines per square mile served such company may elect to use a Target Rate of \$0.0095 with respect to all exchanges owned by that holding company on July 1, 2000, or which that holding company is, as of April 1, 2000, under a binding and executed contract to purchase;

(3) For other price cap local exchange carriers, \$0.0065 per ATS minute of use.

(rr) **Tariff**. Schedules of rates and regulations filed by common carriers.

(ss) **Tariff publication, or publication**. A tariff, supplement, revised page, additional page, concurrence, notice of revocation, adoption notice, or any other schedule of rates or regulations filed by common carriers.

(tt) **Tariff year**. The period from the day in a calendar year on which a carrier's annual access tariff filing is scheduled to become effective through the preceding day of the subsequent calendar year.

(uu) **Text change**. A change in the text of a tariff which does not result in a change in any rate or regulation.

(vv) **United States**. The several States and Territories, the District of Columbia, and the possessions of the United States.

(ww) **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).

(xx) **Toll dialing parity**. "Toll dialing parity" exists when there is dialing parity, as defined in § 51.5 of this chapter, for toll services.

(yy) **Loop-based services**. Loop-based services are services that employ Subcategory 1.3 facilities, as defined in § 36.154 of this chapter.

(zz) **Zone Average Revenue per Line**. The Price Cap CMT Revenue per Line allocated to a particular state-defined zone used for deaveraging of UNE loop prices. The Zone Average Revenue per Line is computed according to the following formula:

$$\text{Zone Average Revenue Per Line} = (25\% * (\text{Loop}_{\text{zone price}} + (\text{Port})_{\text{price}})) + U \text{ where,}$$

U(Uniform revenue per line adjustment) =

$$\frac{[(\text{Average Price Cap CMT Revenue Per Line Month}_{\text{study area}} * \text{ILEC Base Period Lines}) - (25\% * \sum (\text{ILEC Base Period Lines}_{\text{UNE Zone}} * ((\text{Loop}_{\text{zone price}} + \text{Port Price}) \text{ for all zones})))]}{\text{ILEC Base Period Lines}_{\text{Study Area(s)}}}$$

where:

Loop<sub>zone price</sub> = the price for unbundled loop in a UNE zone.

Port<sub>Price</sub> = price for switch ports in that UNE zone.

**§ 61.41 Price cap requirements generally.**

(a) Sections 61.42 through 61.49 shall apply as follows:

(1) [reserved]

(2) To such local exchange carriers as specified by Commission order, and to all local exchange carriers, other than average schedule companies, that are affiliated with such carriers; and

(3) On an elective basis, to local exchange carriers, other than those specified in paragraph (a)(2) of this section, that are neither participants in any Association tariff, nor affiliated with any such participants, except that affiliation with average schedule companies shall not bar a carrier from electing price cap regulation provided the carrier is otherwise eligible.

(b) If a telephone company, or any one of a group of affiliated telephone companies, files a price cap tariff in one study area, that telephone company and its affiliates, except its average schedule affiliates, must file price cap tariffs in all their study areas.

(c) The following rules apply to telephone companies subject to price cap regulation, as that term is defined in § 61.3(ee), which are involved in mergers, acquisitions, or similar transactions.

(1) Any telephone company subject to price cap regulation that is a party to a merger, acquisition, or similar transaction shall continue to be subject to price cap regulation notwithstanding such transaction.

(2) Where a telephone company subject to price cap regulation acquires, is acquired by, merges with, or otherwise becomes affiliated with a telephone company that is not subject to price cap regulation, the latter telephone company shall become subject to price cap regulation no later than one year following the effective date of such merger, acquisition, or similar transaction and shall accordingly file price cap tariffs to be effective no later than that date in accordance with the applicable provisions of this part 61.

(3) Notwithstanding the provisions of § 61.41(c)(2) above, when a telephone company subject to price cap regulation acquires, is acquired by, merges with, or otherwise becomes affiliated with a telephone company that qualifies as an 'average schedule' company, the latter company may retain its 'average schedule' status or become subject to price cap regulation in accordance with § 69.3(i)(3) and the requirements referenced in that section.

(d) Local exchange carriers that become subject to price cap regulation as that term is defined in § 61.3(ee) of this chapter shall not be eligible to withdraw from such regulation.

**§ 61.42 Price cap baskets and service categories.**

(a)-(c) [reserved]

(d) Each local exchange carrier subject to price cap regulation shall establish baskets of services as follows:

- (1) A basket for the common line, marketing, and certain residual interconnection charge interstate access elements as described in §§ 69.115, 69.152, 69.153, 69.154, 69.155, 69.156, and 69.157 of this chapter. For purposes of §§ 61.41 through 61.49 of this chapter, this basket shall be referred to as the "CMT basket."
- (2) A basket for traffic sensitive switched interstate access elements. For purposes of §§ 61.41 through 61.49 of this chapter, this basket shall be referred to as the "traffic-sensitive basket."
- (3) A basket for trunking services as described in §§ 69.110, 69.111, 69.112, 69.125(b), and 69.129 of this chapter. For purposes of §§ 61.41 through 61.49 of this chapter, this basket shall be referred to as the "trunking basket."
- (4)
  - (i.) To the extent that a local exchange carrier specified in § 61.41(a) (2) or (3) offers interstate interexchange services that are not classified as access services for the purpose of part 69 of this chapter, such exchange carrier shall establish a fourth basket for such services. For purposes of §§ 61.41 through 61.49 of this chapter, this basket shall be referred to as the "interexchange basket."
  - (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.
- (5) A basket for special access services as described in §§69.114 of this chapter.

(e)(1) The traffic sensitive switched interstate access basket shall contain such services as the Commission shall permit or require, including the following service categories:

- (i.) Local switching as described in § 69.106(f) of this chapter;
- (ii.) Information, as described in § 69.109 of this chapter;
- (iii.) Data base access services;
- (iv.) Billing name and address, as described in § 69.128 of this chapter;
- (v.) Local switching trunk ports, as described in § 69.106(f)(1) of this chapter; and

- 
- (vi.) Signalling transfer point port termination, as described in § 69.125(c) of this chapter.
- (2) The trunking basket shall contain such switched transport as the Commission shall permit or require, including the following service categories and subcategories:
- (i.) Voice grade entrance facilities, voice grade direct-trunked transport, voice grade dedicated signalling transport,
  - (ii.) High capacity flat-rated transport, including the following service subcategories:
    - (A) DS1 entrance facilities, DS1 direct-trunked transport, DS1 dedicated signalling transport, and
    - (B) DS3 entrance facilities, DS3 direct-trunked transport, DS3 dedicated signalling transport.
  - (iii.) Tandem-switched transport, as described in § 69.111 of this chapter; and
  - (iv.) Signalling for tandem switching, as described in § 69.129 of this chapter.
- (3) The Special Access basket shall contain special access services as the Commission shall permit or require, including the following service categories and subcategories:
- (i.) Voice grade special access, WATS special access, metallic special access, and telegraph special access services;
  - (ii.) Audio and video services;
  - (iii.) High capacity special access, and DDS services, including the following service subcategories:
    - (A) DS1 special access services; and
    - (B) DS3 special access services;
  - (iv.) Wideband data and wideband analog services;
- (f) Each local exchange carrier subject to price cap regulation shall exclude from its price cap baskets such services or portions of such services as the Commission has designated or may hereafter designate by order.
- (g) New services, other than those within the scope of paragraph (f) of this section, must be included in the affected basket at the first annual price cap tariff filing following completion of the

base period in which they are introduced. To the extent that such new services are permitted or required to be included in new or existing service categories within the assigned basket, they shall be so included at the first annual price cap tariff filing following completion of the base period in which they are introduced.

### § 61.45 Adjustments to the PCI for Local Exchange Carriers.

(a) Local exchange carriers subject to price cap regulation shall file adjustments to the PCI for each basket as part of the annual price cap tariff filing, and shall maintain updated PCIs to reflect the effect of mid-year exogenous cost changes.

(b)(1)(i) Adjustments to local exchange carrier PCIs, in those carriers' annual access tariff filings, for the CMT basket as described in § 61.42(d)(i), the traffic-sensitive basket described in § 61.42(d)(2), the trunking basket described in § 61.42(d)(3), the Special Access basket described in § 61.42(d)(5) and the Interexchange Basket described in § 61.42(d)(4), shall be made pursuant to the following formula:

$$PCI_t = PCI_{t-1} [1 + w[(GDP-PI - X (g/2))/(1+(g/2))] + Z/R]$$

where the terms in the equation are described:

GDP-PI = For annual filings only, the percentage change in the GDP-PI between the quarter ending six months prior to the effective date of the new annual tariff and the corresponding quarter of the previous year. For all other filings, the value is zero.

X = For the CMT, traffic sensitive, and trunking baskets, for annual filings only, the factor is set at the level prescribed in subsection (b)(1)(ii) and (iii). For the interexchange basket, for annual filings only, the factor is set at the level prescribed in subsection (b)(1)(v). For the special access basket, the factor is set at the level prescribed in subsection (b)(1)(iv). For all other filings, the value is zero.

g = For annual filings for the CMT basket only, 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, all minus 1.

Z = the dollar effect of current regulatory changes when compared to the regulations in effect at the time the PCI was updated to  $PCI_{t-1}$ , measured at base period level of operations.

Targeted Reduction = the actual possible dollar value of the (GDP-PI-X) reductions that will be targeted to the ATS Charge pursuant to 61.45(i)(3). The reductions calculated by applying the (GDP-PI-X) portion of the formula to the CCL element within the CMT basket will contain the "g" component, as defined above.

R = base period quantities for each rate element "I", multiplied by the price for each rate element "I" at the time the PCI was updated to  $PCI_{t-1}$ .

w =  $R + Z$ , all divided by R (used for the CMT, traffic sensitive, trunking, and special access baskets).

$w_{ix}$  =  $R - (\text{access rate in effect at the time the PCI was updated to } PCI_{t-1} \times \text{base period demand}) + Z$ , all divided by  $R$ .

$PCI_t$  = the new PCI value.

$PCI_{t-1}$  = the immediately preceding PCI value.

(b)(1)(ii) The X value applicable to the baskets specified in § 61.42(d)(1), (2), and (3), shall be 6.5%, to the extent necessary to reduce a tariff entity's ATS Charge to its Target Rate as set forth in § 61.33 (qq). Once an ILEC tariff entity's ATS Charge is equal to the Target Rate as set forth in § 61.33 (qq) for the first time (the former NYNEX telephone companies may be treated as a separate tariff entity), then, except as provided in paragraph (b)(1)(iii), X is equal to GDP-PI and no further reductions will be mandated (i.e. if applying the full X-factor reduction for a given year would reduce the ATS Charge below the Target Rate as set forth in § 61.33 (qq), the amount of X-factor reduction applied that year will be the amount necessary to reach the Target Rate as set forth in § 61.33 (qq)). A filing entity does not reach the Target Rate as set forth in 61.3(qq) in any year in which it exercises an exogenous adjustment pursuant to § 61.45(d)(vii). For companies with separate tariff entities under a single price cap, the following rules shall apply:

(A) Targeting amounts as defined in § 61.45(i)(1) shall be identified separately, using the revenue for each of the tariff entities under the cap.

(B) Each tariff entity shall only be required to use the amount of targeting necessary to get to the Target Rate as set forth in § 61.33 (qq).

(b)(1)(iii)(A) Except as provided in subparagraph (B), once the Tariff Entity's Target Rate as set forth in § 61.33 (qq) is achieved, the X-factor for the CMT basket will equal GDP-PI as long as GDP-PI is less than or equal to 6.5% and greater than 0%. If GDP-PI is greater than 6.5%, and an entity has eliminated its CCL and multi-line business PICCs charges, the X-factor for the CMT basket will equal 6.5%, and all End User Common Line charges, rates and nominal caps, will be increased by the difference between GDP-PI and the 6.5% X-factor. If GDP-PI is less than 0, the X-factor for the CMT basket will be 0.

(B) For tariff filing entities with a Target Rate of \$0.0095, or for the portion of a filing entity consolidated pursuant to § 61.48(o) that, prior to such consolidation, had a Target Rate of \$0.0095, in which the ATS charge has achieved the Target Rate but in which the carrier common line (CCL) charge has not been eliminated, the X-factor for the CMT basket will be 6.5% until the earlier of June 30, 2004, or until CCL charges are eliminated pursuant to § 61.45(i)(4) below. Thereafter, in any filing entity in which a CCL charge remains after July 1, 2004, the X-factor for the CMT basket will be determined pursuant to subparagraph (A) as if CCL charges were eliminated.

(b)(1)(iv) For the special access basket specified in § 61.42(d)(5), the value of X shall be 3.0% for the 2000 annual filing. The value of X shall be 6.5% for the 2001, 2002 and 2003 annual filings. Starting in the 2004 annual filing, X shall be equal to GDP-PI for the special access basket.

(b)(1)(v) For the interexchange basket specified § 61.42(d)(4), the value of X shall be 3.0% for all annual filings.

(b)(2) Adjustments to local exchange carrier PCIs and average price cap CMT revenue per line, in tariff filings other than the annual access tariff filing, for the CMT basket described in § 61.42(d)(1), the traffic-sensitive basket described in § 61.42(d)(2), the trunking basket described in § 61.42(d)(3), the interexchange basket described in § 61.42(d)(4), and the special access basket described in § 61.42(d)(5), shall be made pursuant to the formulas set forth in paragraph (b)(1) of this section, except that the "w(GDP-PI-X)" component of those PCI formulas shall not be employed.

(c) Effective July 1, 2000, the prices of the CMT basket rate elements, excluding special access surcharges under § 69.115 and line ports in excess of basic under § 69.157, shall be set based upon Average Price Cap CMT revenue per line month.

(d) The exogenous cost changes represented by the term "Z" in the formula detailed in paragraphs (b) of this section shall be limited to those cost changes that the Commission shall permit or require by rule, rule waiver, or declaratory ruling.

- (1) Subject to further order of the Commission, those exogenous changes shall include cost changes caused by:
  - (i.) The completion of the amortization of depreciation reserve deficiencies;
  - (ii.) Such changes in the Uniform System of Accounts, including changes in the Uniform System of Accounts requirements made pursuant to § 32.16 of this chapter, as the Commission shall permit or require be treated as exogenous by rule, rule waiver, or declaratory ruling;
  - (iii.) Changes in the Separations Manual;
  - (iv.) [removed and reserved];
  - (v.) The reallocation of investment from regulated to nonregulated activities pursuant to § 64.901;
  - (vi.) Such tax law changes and other extraordinary cost changes as the Commission shall permit or require be treated as exogenous by rule, rule waiver, or declaratory ruling;
  - (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 § 69.731 of this chapter. The allocation of LFAM amounts will be allocated pursuant to §61.45(d)(3). This subsection shall not be applicable to tariff filings during the tariff year beginning July 1, 2000, but is applicable in subsequent years;

- (viii.) Inside wire amortizations;
  - (ix.) The completion of amortization of equal access expenses.
- (2) Local exchange carriers specified in § 61.41(a)(2) or (a)(3) of this part shall, in their annual access tariff filing, recognize all exogenous cost changes attributable to modifications during the coming tariff year in the obligations specified in § 61.45(d)(1)(iv) as well as those changes attributable to alterations in their Subscriber Plant Factor and the Dial Equipment Minutes factor, and completions of inside wire amortizations and reserve deficiency amortizations.
- (3) Exogenous cost changes shall be apportioned on a cost-causative basis between price cap services as a group, and excluded services as a group. Total exogenous cost changes thus attributed to price cap services shall be recovered from services other than those used to calculate the ATS charge.
- (e) [reserved]
- (f) The exogenous costs caused by new services subject to price cap regulation must be included in the appropriate PCI calculations under paragraphs (b) and (c) of this section beginning at the first annual price cap tariff filing following completion of the base period in which such services are introduced.
- (g) In the event that a price cap tariff becomes effective, which tariff results in an API value (calculated pursuant to § 61.46) that exceeds the currently applicable PCI value, the PCI value shall be adjusted upward to equal the API value.
- (h) [reserved]
- (i)(1)(A) Price cap local exchange carriers that are recovering revenues through rates pursuant to §§ 69.106, 69.108, 69.109, 69.110, 69.111, 69.112, 69.113, 69.118, 69.123, 69.124, 69.125, 69.129, or § 69.155 of this chapter shall target, to the extent necessary to reduce the ATS Charge to the Target Rate as set forth in § 61.33 (qq) for the first time, any PCI reductions associated with the dollar impact of application of the (GDPPI-X) portion of the formula in 61.45(b) to the CMT, traffic sensitive, and trunking baskets. In order to calculate the actual dollars to transfer to the trunking and traffic sensitive baskets, carriers will first determine the “Targeted Revenue Differential” that will be transferred to the trunking and traffic sensitive baskets to reduce the ATS Charge to the Target Rate as set forth in 61.33(qq). The Targeted Revenue Differential shall be applied only to the trunking and traffic sensitive baskets to the extent necessary to reduce the ATS charge to the Target Rate as set forth in § 61.33 (qq), and shall not be applied to reduce the PCIs in any other basket or to reduced average price cap CMT Revenue per line, except as provided in § 61.45(i)(4).
- (B) For the purposes of paragraph (A), Targeted Revenue Differential will be determined by adding together the following amounts:
- (i.)  $R * (GDP-PI - X)$  for the traffic sensitive basket, trunking basket, and the

CMT basket excluding CCL revenues; and

$$(ii.) \text{ CCL Revenues} * [(GDP-PI - X - (g/2)] / [1 + (g/2)]$$

Where g is defined in § 61.45(b)(1)(i) above.

(2) Until a tariff entity's ATS Charge equals the Target Rate as set forth in § 61.33 (qq) for the first time, the Targeted Revenue Differential will be targeted to reduce the following rates for that tariff filing entity, in order of priority:

- (i) To the residual per minute Transport Interconnection Charge, until that rate is \$0.00; then
- (ii) To the Information Surcharge, until that rate is \$0.00; then
- (iii) To the other Local Switching charges and Switched Transport charges until the tariff entity's ATS Rate equals the Target Rate as set forth in § 61.3(qq) for the first time. In making these reductions, the reductions to Local Switching rates as a percentage of total X-factor reductions must be greater than or equal to the percentage proportion of Local Switching revenues to the total sum of revenues for Local Switching, Local Switching Trunk Ports, Signalling Transfer Point Port Termination, Switched Direct Trunked Transport, Signalling for Switched Direct Trunked Transport, Entrance Facilities for switched access traffic, Tandem Switched Transport, and Signalling for Tandem Switching (*i.e.*, Local Switching gets at least its proportionate share of reductions).

(3) After a price cap LEC reaches the Target Rate as set forth in § 61.3(qq) level, the ATS Rate will be recalculated each subsequent Annual Filing. This process will identify the new ATS Charge for the new base period level. Due to change in base period demand and inclusion of new services for that annual filing, the absolute level of a tariff entity's ATS Charge may change. The resulting new ATS Charge level will be what that tariff entity will be measured against during that base period. For example, if a company whose target is \$0.0055 reached the Target Rate during the 2000 annual filing, that level may change to \$0.0058 in the 2001 annual filing due to change in demand and inclusion of new services. Therefore, it will be the \$0.0058 average rate that the tariff entity will be measured against for all non-annual filings. Likewise, if that same company was at the Target Rate during the 2000 filing, that level may change to \$0.0053 average rate in the 2001 annual filing due to change in demand and inclusion of new services. In that case, it will be at the \$0.0053 average rate that the tariff entity will be measured.

(4) A company electing a \$0.0095 Target Rate will, in the tariff year it reaches the Target Rate, apply any Targeted Revenue Differential remaining after reaching the Target Rate to reduce Average Price Cap CMT Revenue per Line month until the CCL charge is eliminated. In subsequent years, until the earlier of June 30, 2004 or when the CCL charge is eliminated, tariff filing entities with a Target Rate of \$0.0095, or the portion of a filing entity consolidated pursuant to § 61.48(o) that, prior to such consolidation, had a Target Rate of \$0.0095, will reduce Average Price Cap CMT Revenue per Line month according to the following method:

- 
- (i.) Filing entity calculates the maximum allowable carrier common line revenue, as defined in § 61.46(d), that would be permitted in the absence of further adjustment pursuant to this paragraph;
- (ii.) Filing entity identifies maximum amount of dollars available to reduce Average Price Cap CMT Revenue per Line month by the following:
- $$\begin{aligned} & (\text{CMT revenue}_{.0095 \text{ Area}} \text{ less CCL revenue}_{.0095 \text{ Area}}) * (\text{GDPPI-X}) + \\ & (\text{CCL Revenue}_{.0095 \text{ Area}}) * [\text{GDPPI-X} - (g/2)]/[1+(g/2)] \end{aligned}$$
- (iii.) The Average Price Cap CMT Revenue per Line month shall then be reduced by the lesser of the amount described in clause (i) and the amount described in clause (ii), divided by base period Switched Access End User Common Line Charge lines.

### § 61.46 Adjustments to the API.

(a) Except as provided in paragraphs (d) and (e) of this section, in connection with any price cap tariff filing proposing rate changes, the carrier must calculate an API for each affected basket pursuant to the following methodology:

$$API_t = API_{t-1} [S \sum v_i (p_t/p_{t-1})^i]$$

where

API[t] = the proposed API value,

API[t-1] = the existing API value,

P[t] = the proposed price for rate element "i,"

P[t-1] = the existing price for rate element "i," and

v[i] = the current estimated revenue weight for rate element "i," calculated as the ratio of the base period demand for the rate element "i" priced at the existing rate, to the base period demand for the entire basket of services priced at existing rates.

(b) New services subject to price cap regulation must be included in the appropriate API calculations under paragraph (a) of this section beginning at the first annual price cap tariff filing following completion of the base period in which they are introduced. This index adjustment requires that the demand for the new service during the base period must be included in determining the weights used in calculating the API.

(c) Any price cap tariff filing proposing rate restructuring shall require an adjustment to the API pursuant to the general methodology described in paragraph (a) of this section. This adjustment requires the conversion of existing rates into rates of equivalent value under the proposed structure, and then the comparison of the existing rates that have been converted to reflect restructuring to the proposed restructured rates. This calculation may require use of carrier data and estimation techniques to assign customers of the preexisting service to those services (including the new restructured service) that will remain or become available after restructuring.

(d) The maximum allowable carrier common line (CCL) revenue shall be computed pursuant to the following methodology:

$$CCL = CMT - EUCL - \text{Interstate Access Universal Service Support Mechanism Per Line} - PICC$$

where

CMT = Price Cap CMT Revenue as defined in § 61.3(cc).

EUCL = Maximum allowable EUCL rates established pursuant to § 69.152

multiplied by base period lines.

Interstate Access Universal Service Support Per Line = the amount as determined by the Fund Administrator pursuant to §54.807 times the number of base period lines for each customer class and zone receiving Interstate Access USF support pursuant to Part 54, Subpart I.

PICC = Maximum allowable PICC rates established pursuant to § 69.153 multiplied by base period lines.

(e) 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.

### § 61.47 Adjustments to the SBI; pricing bands.

[PUBLISHER'S NOTE: 64 FR 46584, 46590, Aug. 26, 1999, effective Sept. 27, 1999, purported to remove and reserve paragraph (i)(1) in § 61.49. However, this instruction could not be implemented, because the text does not exist within the section. Upon calling the agency, it was determined that the amendment should instead be implemented in § 61.47. In accordance with the apparent intent of the agency, the amendment has been implemented. It is expected that the agency will issue a correction in the Federal Register.]

(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:

$$SBI_t = SBI_{t-1} [S_i v_i (p_t/p_{t-1})^i]$$

where

$SBI[t]$  = the proposed SBI value,

$SBI[t-1]$  = the existing SBI value,

$P[t]$  = the proposed price for rate element "i,"

$P[t-1]$  = the existing price for rate element "i," and

$v[i]$  = the current estimated revenue weight for rate element "i," calculated as the ratio of the base period demand for the rate element "i" priced at the existing rate, to the base period demand for the entire group of rate elements comprising the service category priced at existing rates.

(b) New services that are added to existing service categories or subcategories must be included in the appropriate SBI calculations under paragraph (a) of this section beginning at the first annual price cap tariff filing following completion of the base period in which they are introduced. This index adjustment requires that the demand for the new service during the base period must be included in determining the weights used in calculating the SBI.

(c) In the event that the introduction of a new service requires the creation of a new service category or subcategory, a new SBI must be established for that service category or subcategory beginning at the first annual price cap tariff filing following completion of the base period in which the new service is introduced. The new SBI should be initialized at a value of 100, corresponding to the service category or subcategory rates in effect the last day of the base period, and thereafter should be adjusted as provided in paragraph (a) of this section.

(d) Any price cap tariff filing proposing rate restructuring shall require an adjustment to the affected SBI pursuant to the general methodology described in paragraph (a) of this section. This

adjustment requires the conversion of existing rates in the rate element group into rates of equivalent value under the proposed structure, and then the comparison of the existing rates that have been converted to reflect restructuring to the proposed restructured rates. This calculation may require use of carrier data and estimation techniques to assign customers of the preexisting service to those services (including the new restructured service) that will remain or become available after restructuring.

(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, 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 § 61.3(ee), 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 and Special Access basket)
- (ix.) Audio/Video (special access basket)
- (x.) Total High Capacity (trunking and special access baskets)
- (xi.) DS1 Subservice (trunking and special access baskets)
- (xii.) DS3 Subservice (trunking and special access baskets)
- (xiii.) Wideband (special access basket)

(2) Two percent:

- (i.) Tandem-Switched Transport (trunking basket)

## (ii.) Signalling for Tandem Switching (trunking basket)

(f) A local exchange carrier subject to price cap regulation may establish density zones pursuant to the requirements set forth in § 69.123 of this chapter, for any service in the trunking and special access baskets, other than the interconnection charge set forth in § 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.

(g)-(h) [reserved]

(i)(l) [reserved]

(2) Effective January 1, 1998, notwithstanding the requirements of paragraph (a) of this section, if a local exchange carrier is recovering interconnection charge revenues through per-minute rates pursuant to § 69.155 of this chapter, any reductions to the PCI for the basket designated in § 61.42(d)(3) resulting from the application of the provisions of § 61.45(b)(1)(i) and from the application of the provisions of § 61.45(i)(1) and (i)(2) shall be directed to the SBI of the service category designated in § 61.42(d)(i).

(3) [removed and reserved]

(4) Effective January 1, 1998, the SBI reduction required by paragraph (i)(2) of this section shall be determined by dividing the sum of the dollar amount of any PCI reduction required by § 61.45(i)(1) and (i)(2), by the dollar amount associated with the SBI for the service category designated in § 61.42(e)(2)(vi), and multiplying the SBI for the service category designated in § 61.42(e)(2)(vi) by one minus the resulting ratio.

(5) Effective July 1, 2000, notwithstanding the requirements of paragraph (a) of this section and subject to the limitations of § 61.45(i), if a local exchange carrier is recovering an ATS Charge greater than its Target Rate as set forth in 61.3(qq), any reductions to the PCI for the Traffic Sensitive or Trunking baskets designated in §§ 61.42(d)(2) and (3) resulting from the application of the provisions of § 61.45(b), and the formula in § 61.45(b) and from the application of the provisions of §§ 61.45(i)(1), and (i)(2) shall be directed to the SBIs of the service categories designated in §§ 61.42(e)(1) and (2).

(j) The calculation of the SBI for the service category designated in § 61.42(d)(i) shall include any residual interconnection charge revenues recovered pursuant to §§ 69.153 and 69.155 of this chapter.

(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.

**47 CFR 61.48 Transition rules for price cap formula calculations.**

(a)-(h) [reserved]

(i) Transport and Special Access Density Pricing Zone Transition Rules.

- (1) Definitions. The following definitions apply for purposes of paragraph (i) of this section:

Earlier date is the earlier of the special access zone date and the transport zone date.

Earlier service is special access if the special access zone date precedes the transport zone date, and is transport if the transport zone date precedes the special access zone date.

Later date is the later of the special access zone date and the transport zone date.

Later service is transport if the special access zone date precedes the transport zone date, and is special access if the transport zone date precedes the special access zone date.

Revenue weight of a given group of services included in a zone category is the ratio of base period demand for the given service rate elements included in the category priced at existing rates, to the base period demand for the entire group of rate elements comprising the category priced at existing rates.

Special access zone date is the date on which a local exchange carrier tariff establishing divergent special access rates in different zones, as described in § 69.123(c) of this chapter, becomes effective.

Transport zone date is the date on which a local exchange carrier tariff establishing divergent switched transport rates in different zones, as described in § 69.123(d) of this chapter, becomes effective.

- (2) Simultaneous Introduction of Special Access and Transport Zones. Local exchange carriers subject to price cap regulation that have established density pricing zones pursuant to § 69.123 of this chapter, and whose special access zone date and transport zone date occur on the same date, shall initially establish density pricing zone SBIs and bands pursuant to the methodology in § 61.47(e-f).
- (3) Sequential Introduction of Zones in the Same Tariff Year. Notwithstanding § 61.47(e-f), local exchange carriers subject to price cap regulation that have established density pricing zones pursuant to § 69.123 of this chapter, and whose special access zone date and transport zone date occur on different dates during the same tariff year, shall, on the earlier date, establish density pricing zone SBIs and pricing bands using the methodology described in § 61.47(e-f), but applicable to the earlier service only. On

the later date, such carriers shall recalculate the SBIs and pricing bands to limit the pricing flexibility of the services included in each density pricing zone category, as reflected in its SBI, as follows:

- (i.) The upper pricing band shall be a weighted average of the following:
  - (A) The upper pricing band that applied to the earlier services included in the zone category on the day preceding the later date, weighted by the revenue weight of the earlier services included in the zone category; and
  - (B) 1.05 times the SBI value for the services included in the zone category on the day preceding the later date, weighted by the revenue weight of the later services included in the zone category.
- (ii.) [reserved]
- (iii.) On the later date, the SBI value for the zone category shall be equal to the SBI value for the category on the day preceding the later date.

(4) Introduction of Zones in Different Tariff Years. Notwithstanding § 61.47(e-f), those local exchange carriers subject to price cap regulation that have established density pricing zones pursuant to § 69.123 of this chapter, and whose special access zone date and transport zone date do not occur within the same tariff year, shall, on the earlier date, establish density pricing zone SBIs and pricing bands using the methodology described in § 61.47(e-f), but applicable to the earlier service only.

- (i.) On the later date, such carriers shall use the methodology set forth in paragraphs (a) through (d) of § 61.47 to calculate separate SBIs in each zone for each of the following groups of services:
  - (A) DS1 special access services;
  - (B) DS3 special access services;
  - (C) DS1 entrance facilities, DS1 direct-trunked transport, and DS1 dedicated signalling transport;
  - (D) DS3 entrance facilities, DS3 direct-trunked transport, and DS3 dedicated signalling transport;
  - (E) Voice grade entrance facilities, voice grade direct-trunked transport, and voice grade dedicated signalling transport;

- (F) Tandem-switched transport; and
  - (G) Such other special access services as the Commission may designate by order.
- (ii.) From the later date through the end of the following tariff year, the annual pricing flexibility for each of the subindexes specified in paragraph (i)(4)(i) of this section shall be limited to an annual increase of five percent or an annual decrease of fifteen percent, relative to the percentage change in the PCI for the trunking basket, measured from the levels in effect on the last day of the tariff year preceding the tariff year in which the later date occurs.
  - (iii.) On the first day of the second tariff year following the tariff year during which the later date occurs, the local exchange carriers to which this paragraph applies shall establish the separate subindexes provided in § 61.47(e), and shall set the initial SBIs for those density pricing zone categories that are combined (specified in paragraphs (i)(4)(i)(A) and (i)(4)(i)(C), (i)(4)(i)(B) and (i)(4)(i)(D), and (i)(4)(i)(E) and (i)(4)(i)(G) of this section) by computing the weighted averages of the SBIs that applied to the formerly separate zone categories, weighted by the revenue weights of the respective services included in the zone categories.
- (j) [removed and reserved]
  - (k) [removed and reserved]
  - (l) AverageTraffic Sensitive Revenues.
    - (1) In the July 1, 2000 annual filing, price cap LECs will make an additional reduction to rates comprising ATS Charge, and to associated SBI upper limits and PCIs. This reduction will be calculated to be the amount that would be necessary, when calculated as if all price cap LECs elect to be price cap LECs, to achieve a total \$2.1 billion reduction in carrier common line and ATS rates by all price cap LECs, compared with those rates as they existed on June 30, 2000 using 2000 annual filing base period demand.
    - (i.) The net change in revenue associated with Carrier Common Line rate elements resulting from:

- (A) the removal from access of ILEC contributions to the Federal universal service mechanisms;
- (B) ILEC receipts of Interstate Access USF pursuant to Subpart I of Part 54;
- (C) Changes in End User Common Line Charges and PICC rates;
- (D) Changes in Carrier Common Line charges due to GDPPI-X targeting for \$0.0095 filing entities.

(ii.) Reductions in Average Traffic Sensitive charges resulting from:

- (A) Targeting of the application of the (GDPPI-X) portion of the formula in § 61.45(b), and any applicable “g” adjustments;
- (B) The removal from access of ILEC contributions to the Federal universal service mechanisms;
- (C) Additional ATS charge reductions defined in subparagraph (2) below.

(2) Once the reductions in paragraph (i) and subparagraphs (ii)(A)-(B) are identified, the difference between those reductions and \$2.1 billion is the total amount of additional reductions that would be made to ATS rates of price cap LECs if all price cap LECs were price cap LECs. This amount will then be restated as the percentage of total price cap LEC Local Switching revenues as of June 30, 2000 using 2000 annual filing base period demand (“June 30 Local Switching revenues”) necessary to yield the total amount of additional reductions and taking into account the fact that, if participating, a price cap LEC would not reduce ATS rates below its Target Rate as set forth in § 61.3(qq). Each price cap LEC then reduces ATS rate elements, and associated SBI upper limits and PCIs, by a dollar amount equivalent to the percentage times the June 30 Local Switching revenues for that filing entity, provided that no price cap LEC shall be required to reduce its ATS rates below its Target Rate as set forth in § 61.3(qq). Each carrier can take its additional reductions against any of the ATS rate elements, provided that at least a proportional share must be taken against Local Switching rates.

(m) Local Switching Pooled Revenues.

(1) Price cap local exchange carriers are permitted to pool local switching revenues in their common line basket under one of the following conditions.

(i) Any price cap local exchange carrier that would otherwise have July 1, 2000 price cap reductions as a percentage of Base Period Price Cap Revenues at the holding company level greater than the industry wide total July 1, 2000 price cap revenue reduction as a percentage of Base Period Price Cap Revenues may elect temporarily to pool the amount of the additional reductions above 25% of the Local Switching element

revenues necessary to yield that carrier's proportionate share of a total \$2.1 billion reduction in switched access usage rates on July 1, 2000. The basis of the reduction calculation will be R at PCI<sub>(t-1)</sub> for the upcoming tariff year. The percentage reductions per line amounts will be calculated as follows:

(Total Price Cap Revenue Reduction / Base Period Price Cap Revenues)

Pooled local switching revenue for each filing entity within a holding company that qualifies under this subparagraph (i) will continue until such pooled revenues are eliminated under this subparagraph. Notwithstanding the provisions of section 61.45(b)(1), once the Average Traffic Sensitive (ATS) rate reaches the applicable Target Rate as set forth in § 61.3(qq), the dollar impact of PCI reductions associated with the CMT, traffic sensitive, and trunking baskets' X-factor of 6.5% shall be targeted to reducing pooled local switching revenue until the pooled local switching revenue is eliminated. Thereafter, the X-factor for these baskets will be determined in accordance with § 61.45(b)(1).

(ii) Price cap local exchange carriers other than the Bell companies and GTE with at least 20% of total holding company lines operated by companies that as of December 31, 1999 were certified to the Commission as rural carriers, may elect to pool up to the following amounts:

(A) for a price cap holding company's predominantly non-rural filing entities (*i.e.* filing entities within which more than 50% of all lines are operated by telephone companies other than those that as of December 31, 1999 were certified to the Commission as rural telephone companies), the amount of the additional reductions to Average Traffic Sensitive Charge rates as defined in § 61.48(l)(2), to the extent such reductions exceed 25% of the Local Switching element revenues (measured in terms of June 30, 2000 rates times 1999 base period demand);

(B) for a price cap holding company's predominantly rural filing entities (*i.e.* filing entities with greater than 50% of lines operated by telephone companies that as of December 31, 1999 were certified to the Commission as rural telephone companies), the amount of the additional reductions to Average Traffic Sensitive Charge rates as defined in § 61.48(l)(2).

## (2) Allocation of Pooled Local Switching Revenue to Certain Common Line Elements

(i) The pooled local switching revenue for each filing entity is shifted to the common line basket within price caps. Pooled local switching revenue will not be included in calculations to determine the eligibility for interstate access universal service support.

(ii) Pooled local switching revenue will be capped on a revenue per line basis.

(iii) Pooled local switching revenue is included in the total revenue for the common line basket in calculating the X-factor reduction targeted to the traffic sensitive rate elements, and for companies qualified under § 61.48 (m)(1)(i), to pooled elements after the Average Traffic Sensitive Charge reaches the target level. For the purpose of targeting X-factor reductions, companies that allocate pooled local switching revenue to other filing entities pursuant to § 61.48(m)(2)(vii) shall include pooled local switching revenue in the total revenue of the common line basket of the filing entity from which the pooled local switching revenue originated.

(iv) Pooled local switching revenue shall be kept separate from CMT revenue in the CMT basket. CMT rate elements for each filing entity shall first be set based on CMT revenue per line without regard to the presence of pooled local switching revenue for each filing entity.

(v) If the rates generated without regard to the presence of pooled local switching revenue for multi-line business (MLB) PICC and/or MLB SLC are below the nominal caps of \$4.31 and \$9.20, respectively, pooled amounts can be added to these rate elements to the extent permitted by the nominal caps.

(vi) Notwithstanding the provisions of § 69.152(k), pooled local switching revenue is first added to the MLB SLC until the rate equals the nominal cap (\$9.20) or the pooled local switching revenue is fully allocated. If pooled local switching revenue remains after applying amounts to the MLB SLC, notwithstanding the provisions of § 69.153, the remaining pooled local switching revenue may be added to the MLB PICC until the rate equals the nominal cap (\$4.31) or the pooled local switching revenue is fully allocated. Unallocated pooled local switching revenue may still remain. For companies pooling pursuant to § 61.48(m)(1)(i), these unallocated amounts may not be recovered from the CCL charge, the primary residential and single-line business SLC, a non-primary residential SLC, or from CMT elements in any other filing entity.

(vii) For companies pooling pursuant to § 61.48(m)(1)(ii), pooled local switching revenue that can not be allocated to the MLB PICC and MLB SLC rates within an individual filing entity may not be recovered from the CCL charge, primary residential and single-line business SLC or residential/single line business SLC charges, but may be allocated to other filing entities within the holding company, and collected by adding these amounts to the MLB PICC and MLB SLC rates. The allocation of pooled local switching revenue among filing entities will be re-calculated at each annual filing. In subsequent annual filings, pooled local switching revenue that was allocated to another filing entity will be reallocated to the filing entity from where it originated, to the full extent permitted by the nominal caps of \$9.20 and \$4.31.

(viii) Notwithstanding the provisions of §69.152(k), these unallocated local switching revenues that cannot be recovered fully pursuant to (vii) are first added to the

MLB SLC of other filing entities until the resulting rate equals the nominal cap (\$9.20) or the pooled local switching revenue for the holding company is fully allocated. If the pooled local switching revenue can be fully allocated to the MLB SLC, the amount is distributed to each filing entity with a rate below the nominal cap (\$9.20) based on its below-cap MLB SLC revenue as a percentage of the total holding company's below-cap MLB SLC revenue.

(ix) If pooled local switching revenue remains after applying amounts to the MLB SLC of all filing entities in the holding company, pooled local switching revenue may be added to the MLB PICC of other filing entities. Notwithstanding the provisions of § 69.153, the remaining pooled local switching revenue is distributed to each filing entity with a rate below the nominal cap (\$4.31) based on its below-cap MLB PICC revenue as a percentage of the total holding company's below-cap MLB PICC revenue.

(x) If pooled local switching is added to the MLB SLC but not to the MLB PICC for a filing entity that qualified to de-average SLCs without regard to pooled local switching, the resulting SLC rates can still be de-averaged. Total pooled local switching is added to the de-averaged zone 1 MLB SLC rate until the per line rate in zone 1 equals the rate in zone 2 or until the pooled local switching is fully allocated to the de-averaged MLB SLC rate for zone 1. If pooled local switching revenue remains after the rate in zone 1 equals zone 2, the de-averaged rates of zone 1 and zone 2 are increased until the pooled local switching is fully allocated to the de-averaged MLB SLC rates of zone 1 and 2 or until those rates reaches zone 3 MLB SLC rate level. This process continues until pooled local switching revenue is fully allocated to the zone de-averaged rates.

(n) Establishment of the special access basket, effective July 1, 2000.

(1) On the effective date, the PCI value for the special access basket, as defined in § 61.42(d)(5) shall be equal to the PCI for the trunking basket on the day preceding the establishment of the special access basket.

(2) On the effective date, the API value for the special access basket, as defined in § 61.42(d)(5) shall be equal to the API for the trunking basket on the day preceding the establishment of the special access basket.

(3) Service Category, Subcategory, and Density Zone SBIs and Upper Limits

(i) Interconnection, Tandem Switched Transport, and Signalling Interconnection will retain the SBIs and upper limits and remain in the trunking basket.

(ii) Audio/Video and Wideband will retain the SBIs and upper limits and be moved into the Special Access basket.

(iii) For Voice Grade, the SBIs and upper limits in both baskets will be equal to the SBIs and upper limits in the existing trunking basket on

the day preceding the establishment of the special access basket. Voice Grade density zones in the trunking basket will retain their indices and upper limits. Voice Grade density zones will be initialized in the special access basket when services are first offered in them.

- (iv) For High Cap/DDS, DS1, and DS3 category and subcategories, the SBIs and upper limits in both baskets will be equal to the SBIs and upper limits in the existing trunking basket on the day preceding the establishment of the Special Access basket. SBIs and upper limits for services that are in both combined density zones and either DTT/EF or Special density zones will be calculated by using weighted averages of the indices in the affected zones.
  - (v) For each DTT/EF-related zone remaining in the trunking basket, the values will be calculated by taking the sum of the products of the DTT/EF revenues times the DTT/EF index (or upper limit) and the DTT/EF-related revenues in the combined zone times the combined index (or upper limit), and dividing by the total DTT/EF-related revenues for that zone.
  - (vi) For each Special-related zone remaining in the trunking basket, the values will be calculated by taking the sum of the products of the Special revenues times the Special index (or upper limit) and the Special-related revenues in the combined zone times the combined index (or upper limit), and dividing by the total Special-related revenues for that zone.
- (o) Treatment of acquisitions of exchanges with different ATS Target Rates as set forth in 61.3(qq):
- (1) In the event of that a price cap LEC acquires a filing entity or portion thereof from a price cap LEC after July 1, 2000, and the price cap LEC did not have a binding and executed contract to purchase that filing entity or portion thereof as of April 1, 2000, those properties retain their pre-existing Target Rates as set forth in § 61.3(qq). If those properties are merged into a filing entity with a different Target Rate as set forth in § 61.3(qq), the Target Rate as set forth in § 61.3(qq) for the merged filing entity will be the weighted average of the Target Rates as set forth in § 61.3(qq) for the properties being combined into a single filing entity, with the average weighted by local switching minutes. When a property acquired as a result of a contract for purchase executed after April 1, 2000 is merged with \$0.0095 Target Rate properties, the obligation to apply price-cap reductions to reduce CCL, pursuant to § 61.45(b)(iii) does not apply to the properties purchased under contracts executed after April 1, 2000, but continues to apply to the other properties.
  - (2) For sale of properties for which a holding company was, as of April 1, 2000, under a binding and executed contract to purchase but which close after June 30, 2000, but

during tariff year 2000, and that are subject to the \$0.0095 Target Rate as set forth in 61.3(qq), the Average Traffic Sensitive Rate charged by the purchaser for that property will be the greater of \$0.0095 or the Average Traffic Sensitive Rate for that property.

**PART 69 – ACCESS CHARGES****SEC. 69.4 CHARGES TO BE FILED**

(d) Recovery of Contributions to the Universal Service Support Mechanisms by Incumbent Local Exchange Carriers.

(1) Incumbent local exchange carriers other than price cap LECs (as defined in § 54.802(c)) may recover their contributions to the universal service support mechanisms through carriers' carrier charges.

(i) Price cap local exchange carriers may recover their contributions to the universal service mechanism by exogenously adjusting the price cap indices of each basket on the basis of relative end-user revenues.

(ii) Non-price cap local exchange carriers may recover their contributions to the universal service mechanism by applying a factor to their carrier common line charge revenue requirements.

(2)(i) In lieu of the carriers' carrier charges described in paragraph (d)(1), price cap local exchange carriers may recover their contributions to the universal service support mechanisms through explicit, interstate, end-user charges that are equitable and nondiscriminatory.

(ii) To the extent that price cap local exchange carriers choose to implement explicit, interstate, end-user charges to recover their contributions to the universal service support mechanisms, they must make corresponding reductions in their access charges to avoid any double recovery.

**Sec. 69.115 Special access surcharges.**

(a) Pending the development of techniques to accurately measure usage of exchange facilities that are interconnected by users with means of interstate or foreign telecommunications, a surcharge that is expressed in dollars and cents per line termination per month shall be assessed upon users that subscribe to private line services or WATS services that are not exempt from assessment pursuant to paragraph (e) of this section.

(b) Such surcharge shall be computed to reflect a reasonable approximation of the carrier usage charges which, assuming non-premium interconnection, would have been paid for by average interstate or foreign usage of common lines, end office facilities, and transport facilities, attributable to each Special Access line termination which is not exempt from assessment pursuant to paragraph (e) of this section.

(c) If the association, carrier or carriers that file the tariff are unable to estimate such average usage for a period ending May 31, 1985, the surcharge for such period shall be twenty-five dollars (\$25) per line termination per month. As of June 30, 2000, these rates will remain and be

capped at the current levels until June 30, 2005.

(d) A telephone company may propose reasonable and nondiscriminatory end user surcharges, to be filed in its federal access tariffs and to be applied to the use of exchange facilities which are interconnected by users with means of interstate or foreign telecommunication which are not provided by the telephone company, and which are not exempt from assessment pursuant to paragraph (e) of this section. Telephone companies which wish to avail themselves of this option must undertake to use reasonable efforts to identify such means of interstate or foreign telecommunication, and to assess end user surcharges in a reasonable and nondiscriminatory manner.

(e) No special access surcharges shall be assessed for any of the following terminations:

(1) The open end termination in a telephone company switch of an FX line, including CCSA and CCSA-equivalent ONALs;

(2) Any termination of an analog channel that is used for radio or television program transmission;

(3) Any termination of a line that is used for telex service;

(4) Any termination of a line that by nature of its operating characteristics could not make use of common lines;

(5) Any termination of a line that is subject to carrier usage charges pursuant to Sec. 69.5; and

(6) Any termination of a line that the customer certifies to the exchange carrier is not connected to a PBX or other device capable of interconnecting a local exchange subscriber line with the private line or WATS access line.

### **§ 69.152 End user common line for price cap local exchange carriers.**

[PUBLISHER'S NOTE: Paragraph (h) was added at 64 FR 16353, 16358, Apr. 5, 1999, effective July 1, 1999.]

(a) A charge that is expressed in dollars and cents per line per month shall be assessed upon end users that subscribe to local exchange telephone service or Centrex service to the extent they do not pay carrier common line charges. A charge that is expressed in dollars and cents per line per month shall be assessed upon providers of public telephones. Such charge shall be assessed for each line between the premises of an end user, or public telephone location, and a Class 5 office that is or may be used for local exchange service transmissions.

(b) [Removed and reserved]

(c) The charge for each subscriber line associated with a public telephone shall be equal to the monthly charge computed in accordance with paragraph (k) of this section.

(d)(1) Beginning July 1, 2000, in a study area that does not have deaveraged End User Common Line Charges, the maximum monthly charge for each primary residential or single line business local exchange service subscriber line shall be the lesser of (i) the Average Price Cap CMT Revenue Per Line as defined in § 61.3(d) or (ii):

- (A) On July 1, 2000, \$4.35.
- (B) On July 1, 2001, \$5.00.
- (C) On July 1, 2002, \$6.00.
- (D) On July 1, 2003, \$6.50.

(2) In the event that GDP-PI exceeds 6.5% or is less than 0%, the maximum monthly charge in subsection (d)(1)(ii) and the cap will be adjusted pursuant to § 61.45(b)(1)(iii).

(e)(1) Beginning July 1, 2000, in an study area that does not have deaveraged End User Common Line Charges, the monthly charge for each non-primary residential local exchange service subscriber line shall be the lesser of:

(i) \$7.00, or

(ii) the greater of:

- (A) The rate as of June 30, 2000 less reductions needed to ensure over recovery of CMT Revenues does not occur, or
- (B) Average Price Cap CMT Revenue Per Line.

(2) In the event that GDP-PI is greater than 6.5% or is less than 0%, the maximum monthly charge in subsection (e)(1)(i) and the cap will be adjusted pursuant to § 61.45(b)(1)(iii).

(3) Where the local exchange carrier provides a residential line to another carrier so that the other carrier may resell that residential line to a residence that already receives a primary residential line, the local exchange carrier may collect the non-primary residential charge described in paragraph (e) of this section from the other carrier.

(f) The charge for each primary residential local exchange service subscriber line shall be the same as the charge for each single line business local exchange service subscriber line.

(g) A line shall be deemed to be a residential subscriber line if the subscriber pays a rate for such line that is described as a residential rate in the local exchange service tariff.

(h) [Effective July 1, 1999.] Only one of the residential subscriber lines a price cap LEC provides to a location shall be deemed to be a primary residential line.

(1) [Effective July 1, 1999.] For purposes of § 69.152(h), "residential subscriber line" includes residential lines that a price cap LEC provides to a competitive LEC that resells the line and on which the price cap LEC may assess access charges.

(2) [Effective July 1, 1999.] If a customer subscribes to residential lines from a price cap LEC and at least one reseller of the price cap LEC's lines, the line sold by the price cap LEC shall be the primary line, except that if a resold price cap LEC line is already the primary line, the resold line will remain the primary line should a price cap LEC subsequently sell an additional line to that residence.

(i) A line shall be deemed to be a single line business subscriber line if the subscriber pays a rate that is not described as a residential rate in the local exchange service tariff and does not obtain more than one such line from a particular telephone company.

(j) No charge shall be assessed for any WATS access line.

(k)(1) Beginning on July 1, 2000, for any study area that does not have deaveraged End User Common Line charges and in the absence of voluntary reductions, the maximum monthly End User Common Line Charge for multi-line business lines will be the lesser of:

- (i) \$9.20, or
- (ii) the greater of:
  - (A) the rate as of June 30, 2000, less reductions needed to ensure over recovery of CMT Revenues does not occur, or
  - (B) Average Price Cap CMT Per Line as defined in § 61.3(d).

Except when the incumbent LEC reduces the rate through voluntary reductions, the multi-line business End User Common Line charge will be frozen until the study area's multi-line business PICC and CCL charge are eliminated.

(2) In the event that GDP-PI is greater than 6.5% or is less than 0%, the maximum monthly charge in subsection (k)(1)(i) and the cap will be adjusted pursuant to § 61.45(b)(1)(iii).

(l)(1) Beginning January 1, 1998, local exchange carriers shall assess no more than one End User Common Line charge as calculated under the applicable method under paragraph (e) of this section for Basic Rate Interface integrated services digital network (ISDN) service.

(2) Local exchange carriers shall assess no more than five End User Common Line charges as calculated under paragraph (k) of this section for Primary Rate Interface ISDN service.

(m) In the event the local exchange carrier charges less than the maximum End User Common Line charge for any subscriber lines, the local exchange carrier may not recover the difference between the amount collected and the maximum from carrier common line charges or PICCs.

(n) – (p) [Removed and Reserved]

(q) End User Common Line Charge De-Averaging. Beginning on July 1, 2000, ILECs may geographically deaverage End User Common Line charges subject to the following conditions:

- (1) In order for an ILEC to be allowed to de-average End User Common Line charges within a study area, the ILEC must have state Commission approved geographically deaveraged rates for UNE loops within that study area. Except where an incumbent LEC geographically deaverages through voluntary reductions, before an ILEC may geographically deaverage its End User Common Line rates, its Originating and

Terminating CCL and Multi-line Business PICC rates in that study area must equal \$0.00.

(2) All geographic deaveraging of End User Common Line charges by customer class within a study area must be according to the state commission-approved UNE loop zone. Solely for the purposes of determining interstate subscriber line charges and the interstate access universal service support described in § 54.806 and § 54.807, an ILEC may not have more than four geographic End User Common Line Charge/USF zones absent a review by the Commission. Where an ILEC has more than four state-created UNE zones and the Commission has not approved use of additional zones, the ILEC will determine, at its discretion, which state-created UNE zones to consolidate so that it has no more than four zones for the purpose of determining interstate subscriber line charges and interstate access universal service support.

(3) Within a given zone, Multi-line Business End User Common Line rates cannot fall below Primary Residential and Single Line Business or Non-Primary Residential End User Common Line charges. Non Primary End User Common Line charges cannot fall below Primary Residential and Single Line Business charges.

(4) For any given class of customer in any given zone, the Zone de-averaged End User Common Line Charge in that zone must be greater than or equal to the Zone de-averaged End User Common Line charge in the zone with the next lower Zone Average Revenue Per Line.

(5) The sum of all revenues per month that would be generated from all deaveraged End User Common Line charges in all zones within a study area plus Interstate Access USF Support Per Line (as defined in § 54.807) for the applicable customer classes and zones receiving such support multiplied by corresponding base period lines, divided by the number of base period lines in that study area cannot exceed Average Price Cap CMT Revenue Per Line as defined in § 61.3(d) for that study area. In addition, the sum of revenues per month that would be generated from all deaveraged End User Common Line charges in all End User Common Line charge deaveraging zones within a study area plus revenues per month from all End User Common Line charge, multi-line business PICC and CCL charges from study areas within that study area that have not geographically deaveraged End User Common Line charges plus the sum of all Interstate Access USF Support Per Line (as defined in § 54.807) for the applicable customer classes and zones receiving such support, multiplied by the corresponding base period lines for the applicable customer classes and zones within the study area, divided by the number of total base period lines in the study area cannot exceed Average Price Cap CMT Revenue Per Line as defined in § 61.3(d) for the study area.

(6) Maximum Charge. The maximum zone deaveraged End User Common Line Charge that may be charged in any zone is the applicable cap specified in § 69.152(d)(1), § 69.152(e)(1)(i) or § 69.152(k)(1)(i) Zone Average Revenue Per Line is the Price Cap CMT Revenue Per Line allocated to a particular state-defined zone used for deaveraging of UNE loop prices. The zone average revenue per line is

computed pursuant to § 61.3 (zz).

(7) Minimum Charge. Except where an incumbent LEC chooses to lower the deaveraged End User Common Line Charge through voluntary reductions, the minimum zone deaveraged End User Common Line Charge in any zone in a study area is at least the Minimum EUCL. Minimum EUCL is Zone Average Revenue Per Line for the zone with the lowest Zone Average Revenue Per Line in that study area plus an amount per line calculated to recover the difference between Interstate Access USF Support Per Line (as defined in § 54.807) multiplied by base period lines for the applicable customer class and zones receiving such support and Study Area Above Benchmark Revenues, first from Zone 1 until the End User Common Line Charges in Zone 1 equal to the End User Common Line Charges in Zone 2, and then from lines in Zones 1 and 2 equally until the End User Common Line Charges in those Zones reach Zone 3 (with all End User Common Line Charges subject to the applicable residential and multi-line business lines nominal caps).

(i) For the purposes of this Part, “Study Area Above Benchmark Revenues is the sum of all Zone Above Benchmark Revenues.

(ii) For the purposes of this Part, “Zone Above Benchmark Revenues” is calculated as follows:

Zone Above Benchmark Revenues is the sum of Zone Above Benchmark Revenues<sub>Residence&SingleLineBusiness</sub> and Zone Above Benchmark Revenues<sub>Multi-lineBusiness</sub>. Zone Above Benchmark Revenues<sub>Residence&SingleLineBusiness</sub> is, within each zone, the product of Zone Average Revenue Per Line minus \$7.00 multiplied by all ILEC Base Period Lines<sub>Residence and Single Line Business</sub> times 12. If negative, the Zone Above Benchmark Revenues<sub>Residence&SingleLineBusiness</sub> for the zone is zero. Zone Above Benchmark Revenues<sub>Multi-lineBusiness</sub> is, within each zone, the product of Zone Average Revenue Per Line minus \$9.20 multiplied by all ILEC zone Base Period<sub>multi-line business</sub> lines times 12. If negative, the Zone Above Benchmark Revenues<sub>Multi-lineBusiness</sub> for the zone is zero.

(8) Voluntary Reductions. A “Voluntary Reduction” is one in which the ILEC reduces prices other than through offset of net increases in End User Common Line charge revenues or Interstate Access USF support received pursuant to § 54.807, or through increases in other zone deaveraged End User Common Line charges.

### **§ 69.153 Presubscribed interexchange carrier charge (PICC).**

(a) A charge expressed in dollars and cents per line may be assessed upon the Multi-line business subscriber's presubscribed interexchange carrier to recover revenues totaling Average Price Cap CMT Revenues Per Line times the number of base period lines less revenues recovered through the End User Common Line charge established under § 69.152 and Interstate Access USF Support Per Line (as defined in § 54.807) multiplied by base period lines for the applicable

customer class and zones receiving such support, up to a maximum of \$4.31 per line per month. In the event the ceilings on the PICC prevent the PICC from recovering all the residual common line/marketing and residual interconnection charge revenues, the PICC shall recover all residual common line/marketing revenues before it recovers residual interconnection charge revenues.

(b) If an end-user customer does not have a presubscribed interexchange carrier, the local exchange carrier may collect the PICC directly from the end user.

(c) [Removed and Reserved]

(d) Local exchange carriers shall assess no more than five PICCs as calculated under paragraph (a) of this section for Primary Rate Interface ISDN service.

(e) The maximum monthly PICC for Centrex lines shall be one-ninth of the maximum charge determined under paragraph (a) of this section, except that if a Centrex customer has fewer than nine lines, the maximum monthly PICC for those lines shall be the maximum charge determined under paragraph (a) of this section divided by the customer's number of Centrex lines.

**§ 69.154 Per-minute carrier common line charge. [Effective Jan. 1, 1998.]**

[PUBLISHER'S NOTE: This section was added at 62 FR 31868, 31937, June 11, 1997, effective Jan. 1, 1998.]

(a) Local exchange carriers may recover a per-minute carrier common line charge from interexchange carriers, collected on originating access minutes and calculated using the weighting method set forth in paragraph (c) of this section. The maximum such charge shall be the lower of:

(1) The per-minute rate using base period demand that would recover the maximum allowable carrier common line revenue as defined in § 61.46(d); or

(2) The sum of the local switching, carrier common line and interconnection charge charges assessed on originating minutes on December 31, 1997, minus the local switching charges assessed on originating minutes.

(b) To the extent that paragraph (a) of this section does not recover from interexchange carriers all permitted carrier common line revenue, the excess may be collected through a per-minute charge on terminating access calculated using the weighting method set forth in paragraph (c) of this section.

(c) For each Carrier Common Line access element tariff, the premium originating Carrier Common Line charge shall be set at a level that recovers revenues allowed under paragraphs (a) and (b) of this section. The non-premium charges shall be equal to .45 multiplied by the premium charges.

**§ 69.155 Per-minute residual interconnection charge. [Effective Jan. 1, 1998.]**

[PUBLISHER'S NOTE: This section was added at 62 FR 31868, 31938, June 11, 1997, effective Jan. 1, 1998. 62 FR 56121, 56133, Oct. 29, 1997, revised paragraph (c), effective Jan. 1, 1998.]

(a) Local exchange carriers may recover a per-minute residual interconnection charge on originating access. The maximum such charge shall be the lower of:

(1) The per-minute rate that would recover the total annual residual interconnection charge revenues permitted less the portion of the residual interconnection charge allowed to be recovered under § 69.153; or

(2) The sum of the local switching, carrier common line and residual interconnection charges assessed on originating minutes on December 31, 1997, minus the local switching charges assessed on originating minutes, less the maximum amount allowed to be recovered under § 69.154(a).

(b) To the extent that paragraph (a) of this section prohibits a local exchange carrier from recovering all of the residual interconnection charge revenues permitted, the residual may be collected through a per-minute charge on terminating access.

(c)(1) No portion of the charge assessed pursuant to paragraphs (a) or (b) of this section that recovers revenues that the local exchange carrier anticipates will be reassigned to other, facilities-based rate elements, including the tandem-switching rate element described in § 69.111(g), the three-part tandem switched transport rate structure described in § 69.111(a)(2), and port and multiplexer charges described in § 69.111(l), shall be assessed upon minutes utilizing the local exchange carrier's local switching facilities, but not the local exchange carrier's transport service.

(2) If a local exchange carrier cannot recover its full residual interconnection charge revenues through the PICC mechanism established in § 69.153, and will consequently recover a portion of its residual interconnection charge revenues through per-minute charges assessed pursuant to paragraphs (a) and (b) of this section, then the local exchange carrier must allocate its residual interconnection charge revenues subject to the exemption established in paragraph (c)(1) of this section between the PICC and the per-minute residual interconnection charge in the same proportion as other residual interconnection charge revenues are allocated between these two recovery mechanisms.

**§ 69.156 Marketing expenses.**

Effective July 1, 2000, the marketing expenses formerly allocated to the common line and traffic sensitive baskets, and the switched services within the trunking basket pursuant to §§ 32.6610 of this chapter and 69.403 will now be recovered in the CMT basket created pursuant to §61.42(d)(1). These marketing expenses will be recovered through the elements outlined in §§ 69.152, 69.153 and 69.154.

**§ 69.157 Line port costs in excess of basic, analog service. [Effective Jan. 1, 1998.]**

[PUBLISHER'S NOTE: This section was added at 62 FR 31868, 31938, June 11, 1997, effective Jan. 1, 1998.]

To the extent that the costs of ISDN line ports, and line ports associated with other services, exceed the costs of a line port used for basic, analog service, local exchange carriers may recover the difference through a separate monthly end user charge. As of June 30, 2000, these rates will be capped until June 30, 2005.

**§ 69.158 Universal Service End User Charges**

To the extent the company makes contributions to the Universal Service Support Mechanisms pursuant to § 54.706 and § 54.709 and the ILEC seeks to recover some or all of the amount of such contribution, the ILEC shall recover those contributions through a charge to end users other than Lifeline users. These contributions are not a part of any price cap baskets, and the charge to recover these contributions is not part of any other element established pursuant to Part 69. Such a charge may be assessed on a per line basis or as a percentage of interstate retail revenues, and at the option of the ILEC it may be combined for billing purposes with other end user retail rate elements. An ILEC opting to assess the USF end user rate element on a per line basis may apply that charge using the "equivalency" relationships established for the multi-line business PICC for Primary Rate ISDN service, as per § 69.153(d), and for Centrex lines, per § 69.153(e).

**§§ 69.201-69.205 [Removed]**

**§ 69.206 [Deleted]**

**§ 69.207 [Deleted]**

**§ 69.208 [Deleted]**

**§ 69.209 [Deleted]**

**APPENDIX C  
CHART 1**

**SLC and PICC Caps under current access rules (assumes 2% inflation)**

	Current	7/2000	7/2001	7/2002	7/2003	7/2004
<b>Primary Residential</b>						
SLC	\$3.50	\$3.50	\$3.50	\$3.50	\$3.50	\$3.50
PICC	\$1.04	\$1.56	\$2.09	\$2.63	\$3.18	\$3.74
<b>Non-Primary Residential</b>						
SLC	\$6.07	\$7.19	\$8.33	\$9.51	\$9.96	\$10.16
PICC	\$2.53	\$3.58	\$4.65	\$5.74	\$6.86	\$8.00
<b>Multi-line Business</b>						
SLC	\$9.20	\$9.38	\$9.57	\$9.76	\$9.96	\$10.16
PICC	\$4.31	\$5.90	\$7.52	\$9.17	\$10.85	\$11.57

**SLC and PICC Caps under CALLS (assumes 2% inflation)**

<b>Primary Residential</b>						
SLC	\$3.50	\$4.35	\$5.00	\$6.00	\$6.50	\$6.50
PICC	\$1.04	0	0	0	0	0
<b>Non-Primary Residential</b>						
SLC	\$6.07	\$7.00	\$7.00	\$7.00	\$7.00	\$7.00
PICC	\$2.53	0	0	0	0	0
<b>Multi-line Business</b>						
SLC	\$9.20	\$9.20	\$9.20	\$9.20	\$9.20	\$9.20
PICC	\$4.31	\$4.31	\$4.31	\$4.31	\$4.31	\$4.31

**APPENDIX E**  
**CALLS *Ex Parte* Filings**  
**Modifying the CALLS Proposal**

- Letter from John T. Nakahata, Counsel to CALLS, to Magalie Roman Salas, Secretary, FCC, February 25, 2000.
- Letter from Joel E. Lubin, Vice President, Federal Government Affairs, AT&T, to Magalie Roman Salas, Secretary, FCC, February 25, 2000 (*AT&T February 25 Letter*).
- Letter from Richard Juhnke, General Attorney, Sprint, to Magalie Roman Salas, Secretary, FCC, February 25, 2000 (*Sprint February 25 Letter*).
- Letter from Kathleen M. H. Wallman, Wallman Strategic Consulting, L.L.C., to Magalie Roman Salas, Secretary, FCC, March 30, 2000 (*Wallman March 30 Letter*).
- Letter from Joel E. Lubin, Vice President, Federal Government Affairs, AT&T, to Magalie Roman Salas, Secretary, FCC, March 30, 2000 (*AT&T March 30 Letter*).
- Letter from John T. Nakahata, Counsel to CALLS, to Magalie Roman Salas, Secretary, FCC, April 7, 2000.
- Letter from John T. Nakahata, Counsel to CALLS, to Richard Lerner, Deputy Chief, Competitive Pricing Division, Common Carrier Bureau, FCC, April 14, 2000.
- Letter from John T. Nakahata, Counsel to CALLS, to Magalie Roman Salas, Secretary, FCC, April 14, 2000 (*VALOR April 14 Letter*).
- Letter from John T. Nakahata, Counsel to CALLS, to Magalie Roman Salas, Secretary, FCC, April 24, 2000.
- Letter from John T. Nakahata, Counsel to CALLS, to Magalie Roman Salas, Secretary, FCC, April 28, 2000 (*CALLS April 28 Letter*).
- Letter from John T. Nakahata, Counsel to CALLS, to Magalie Roman Salas, May 2, 2000.
- Letter from John T. Nakahata, Counsel to CALLS, to Jack Zinman, Legal Counsel, Common Carrier Bureau, FCC, May 22, 2000.
- Letter from John T. Nakahata, Counsel to CALLS, to Magalie R. Salas, Secretary, FCC, May 25, 2000.
- Letter from John T. Nakahata, to Jack Zinman, Legal Counsel, Common Carrier Bureau, FCC, May 25, 2000.

## VII. STATEMENT OF COMMISSIONER HAROLD FURCHTGOTT-ROTH, CONCURRING IN PART AND DISSENTING IN PART

*Re: Access Charge Reform, Price Cap Performance Review for Local Exchange Carriers, Low-Volume Long Distance Users, Federal-State Joint Board on Universal Service, Report and Order, CC Docket Nos. 96-262, 94-1, 99-249, 96-45.*

The current structure of interstate access charges is irrational, and substantial revision of the Commission's access charge rules is needed. At present, the price of access to the local exchange carriers' networks bears very little relation to the way in which the costs of access are actually incurred – per-minute charges for access are far higher than they should be, whereas fixed charges are artificially low. As substitutes for traditional circuit-switched long-distance services, such as packet-switched Internet-based telephony, become more widely available, the regulatory distortions created by the Commission's rules are increasingly untenable.

Today's restructure of the access charge regime takes some steps in the right direction, and I concur in those aspects of this decision that permit price-cap local exchange carriers more fully to recover the fixed costs of the local loop through flat-rated charges. Indeed, I would have moved even more aggressively in this regard. I write separately, however, to express my profound disagreement with three aspects of this order.

**The Process Through Which this Order Was Adopted Was Fundamentally Defective.** This order is a product of a proposal that was originally submitted last summer by the Coalition for Affordable Local and Long Distance Service (“CALLS”). The Commission sought comment on this proposal last fall. *See* Notice of Proposed Rulemaking, *Access Charge Reform, Low-Volume Long Distance Users, Federal-State Joint Board on Universal Service*, CC Docket Nos. 92-262, 94-1, 99-249, 96-45 (Sept. 15, 1999).

In ordinary circumstances, the Commission would simply have rendered a decision on the CALLS proposal based on comments submitted by interested parties. The course the Commission took here, however, was very different. In the early part of this year, apparently prompted by objections to the original CALLS proposal raised by groups purporting to represent consumer interests, the Commission, acting chiefly through the Common Carrier Bureau, held a series of meetings with a select group of some – but by no means all – of the parties with interests in this proceeding. The substance of what was discussed at these meetings was not publicly disclosed. And a number of parties with interests in the outcome of this proceeding, including the Ad Hoc Telecommunications Users Committee, Time Warner Telecom, and the Association for Local Telecommunications Services, were not allowed to participate.

The Commission evidently refereed the negotiations at these meetings, and a “modified” CALLS proposal was reached near the end of February. Although this order announces that this “modified proposal” was put forth by members of the Coalition, *see*

Order ¶ 1, it is undeniable that the proposal was a product of the negotiations that took place between the Commission and those parties that were allowed to participate in the negotiations – that is, members of the Coalition and some groups that purport to represent the interests of residential and small-business consumers. The Coalition’s “modified proposal” simply memorialized aspects of the agreement that was reached between these parties and the Commission in the course of the meetings held in January and February of this year.

Even more dismaying, however, is what the “modified proposal” does not disclose. At some point in the course of the CALLS negotiations, proceedings that were unrelated to the issue of access charge reform became part of the negotiations. Incumbent local exchange carrier members of the Coalition apparently contended that they could not commit to certain modifications of the CALLS proposal unless they had confidence that two separate matters – a depreciation waiver item<sup>604</sup> and the pending special access proceeding, which concerns the circumstances in which carriers may purchase combinations of unbundled loops and transport network elements<sup>605</sup> – would be resolved favorably to them. As a consequence, part of the final agreement reached by the participants to the CALLS negotiations concerned these two separate matters. With respect to this depreciation item, the Bureau agreed to recommend to the Commission that it approve the waiver that is the subject of this Notice and terminate the CPR audits. Additionally, the Bureau agreed to recommend to the Commission that it “clarify” the existing rules regarding special access and defer further rulemaking until 2001. The linkage between these unrelated items and the CALLS docket was very clear – at least internally. To brief the Commissioners and their staff regarding the outcome of the CALLS negotiations, the Bureau distributed briefing sheets outlining the incumbent carriers’ concerns and making plain that the depreciation and special access matters had become a key part of the CALLS package. Nothing in this order, however, tells the public of this connection between this order and these other dockets.

In my view, the process by which the original CALLS proposal was modified is fundamentally inconsistent with principles of neutrality and transparency that must govern agency decisionmaking. By participating in the CALLS negotiations, the Commission plainly reached a view as to how the CALLS proceeding should be resolved, and its review of the comments it subsequently received regarding the “modified proposal” could not have been uninfluenced by the role it had played earlier. In addition, it was entirely improper for the Commission to have permitted the unrelated matters of depreciation and special access become part of the negotiations.

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<sup>604</sup> See Further Notice of Proposed Rulemaking, *1998 Biennial Regulatory Review -- Review Of Depreciation Requirements For Incumbent Local Exchange Carriers, Ameritech Corporation Telephone Operating Companies' Continuing Property Records Audit, et al.*, CC Docket Nos. 98-137, 99-117 (Rel. Apr. 3, 2000).

<sup>605</sup> See, e.g., Supplemental Order, *Implementation of the Local Competition Provisions of the Telecommunications Act of 1996*, CC Docket 96-98 (rel. Nov. 24, 1999).

If the Bureau thought it would be helpful to narrow the differences between the various parties with interests in this docket in advance of a formal rulemaking proceeding, it could legally have done so by following the framework set forth in the Negotiated Rulemaking Act, 5 U.S.C. § 561 *et seq.* This statute provides for the formation of a committee that will, with the assistance of the relevant agency, negotiate to reach a consensus on a given issue. 5 U.S.C. § 563. An agency that undertakes a negotiated rulemaking must publish in the Federal Register a notice that, among other things, (1) announces the establishment of the committee; (2) describes the issues and scope of the rule to be developed; and (3) proposes a list of persons that will participate on the committee. 5 U.S.C. § 564(a). In addition, the agency must give persons with interests that will be affected by the new rule an opportunity to apply to participate in the negotiated rulemaking process. *Id.* § 564(b). If the committee reaches a consensus, the statute requires it to transmit to the agency that established the committee a report on a proposed rule. *Id.* § 566(f). Significantly, although the agency may nominate a federal employee to facilitate the committee's negotiations, "[a] person designated to represent the agency in substantive issues *may not* serve as facilitator or otherwise chair the committee." *Id.* § 566(c) (emphasis added).

None of those procedures was followed here. The public generally was not notified that the CALLS negotiations were taking place, nor were a number of parties that wished to be included in these negotiations permitted to participate. Not surprisingly, the final CALLS deal does not reflect the views of parties that were not included in the CALLS negotiations, such as the Ad Hoc Telecommunications Users Committee. For example, Ad Hoc has pointed out, in its comments and in a series of *ex parte* presentations to the Commission, that the retention of the multi-line business presubscribed interexchange carrier charge (or "PICC") imposes substantial costs on multi-line business consumers. *See, e.g.,* Letter from James S. Blasak to Harold Furchtgott-Roth (May 23, 2000). Ad Hoc contended that the multi-line business PICC is often marked up by long-distance carriers, with the result that business subscribers pay more than they otherwise would. It therefore proposed that the multi-line business PICC be consolidated with the multi-line business subscriber line charge (or "SLC") and billed directly from the price-cap LEC to the end-user, to avoid a mark-up by the interexchange carrier. *See* Order ¶¶ 105-110. Elimination of the multi-line business PICC would have been consistent with the approach the Commission took with respect to the residential and single-line PICC. (Notably, groups purporting to represent the interests of residential and small-business consumers *were* at the table when the CALLS negotiations were held.) But the order declines to take Ad Hoc's approach. Had this party been permitted to present its views in the context of a negotiated rulemaking, I think the treatment of the multi-line business PICC might well have been different. And other aspects of this order would have been different as well.

Not only were interested parties excluded from the CALLS negotiations, but also the substance and scope of the CALLS negotiations was not made public, and there is no public record describing whatever consensus was finally reached. And, inconsistent with the policy set forth in 5 U.S.C. § 566(c), the Bureau participated in these negotiations

both substantively *and* as a facilitator. Had the Commission adhered to the statutory requirements set forth in the Negotiated Rulemaking Act, I believe it could have accomplished its goal of reforming the current access charge regime in a way that preserved its neutrality, allowed representatives of *all* interested parties to participate, and kept the public informed about the process taking place.<sup>606</sup>

To be clear, I do not believe that any employee of this agency acted in bad faith, nor do I call into question the propriety of public participation in the Commission's decisionmaking process by making *ex parte* presentations. In addition, I believe that the inefficiencies of the current access charge regime should be eliminated. But I cannot escape the conclusion that the process by which this Notice has been promulgated falls short of certain fundamental principles that govern the behavior of administrative agencies.

**The Universal Service Subsidy Created in this Order Is Illegitimate.** This order establishes a new \$650 million fund universal service subsidy mechanism, which will be paid from contributions made by *all* interstate carriers almost exclusively to price-cap local exchange carriers. The Commission claims that this new subsidy is needed to replace the implicit "universal service" support mechanism currently present in interstate access charges.

It is important to understand what is occurring with the creation of this new subsidy. Until now, it has been interexchange carriers that have paid to local exchange carriers whatever "implicit subsidy" exists in access charges, and local exchange carriers have used this money to subsidize the cost of providing certain types of services within a limited geographical area (typically within a state). Thus, money might flow from a business end-user to a residential user, both within the incumbent's territory. Under this new mechanism, however, *all* carriers that provide interstate services will fund the access subsidy, and the costs of the subsidy will be spread nationwide. Thus, a wireless carrier in California (which is not eligible to receive any support from the \$650 million fund) will now find itself footing the bill to subsidize local exchange carriers nationwide.

I do not think that the creation of this new fund is consistent with the statute's directive that the Commission "preserve and advance" universal service support mechanisms. *See* 47 U.S.C. §254. In my view, the subsidies present in the existing access charge regime do not come within the scope of section 254, and the Commission's reliance on section 254 as a basis for creating this new fund is inconsistent with the statute. Moreover, the only economically rational way for local exchange carriers to recover whatever subsidies are currently included in access charges is to increase the flat fees that subscribers pay for access. Paradoxically, this order decreases those charges. Although consumers may pay less in flat charges in the short term, I believe that this

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<sup>606</sup> Even under the Negotiated Rulemaking Act, however, the Bureau could not have promised that this Commission would abide by the negotiated rulemaking committee's consensus. *See USA Group Loan Servs. Inc. v. Riley*, 82 F.3d 708, 714 (7<sup>th</sup> Cir. 1996).

order does them a great disservice, since they will ultimately wind up paying far more to fund the subsidies that this Commission continues to manufacture in the name of “universal service.”

The Commission’s Requirement that Sprint and AT&T Comply with the Commitments these Companies Made in Letters to the Commission Is Unenforceable. In various letters to Commission, Sprint and AT&T have made “commitments” regarding the CALLS proposal. Among other things, these companies have said they will “pass through” to consumers the savings that they realize in access charge reductions and that they will make various rate plans available to different types of consumers. The Commission orders Sprint and AT&T to comply with all the supposedly “voluntary” commitments they have made in these letters. *See* Order ¶ 247.

In my view, the Commission lacks the power to regulate AT&T’s and Sprint’s rates in this manner. As the Commission recognized in 1996, the long-distance market is a competitive one, and the Commission therefore no longer regulates the rates of any long-distance carrier. Order, *Motion of AT&T To Be Classified as a Non-Dominant Carrier*, 11 FCC Rcd 3271 (1996). In a competitive market, it is consumers – through their buying power – who tell carriers whether their rates are reasonable or not. Government regulation is no longer warranted. I therefore do not see how, even if these carriers fail to live up to their “commitment” letters, the Commission could possibly find these carriers’ rates “unjust” or “unreasonable.”