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MAR 10 1993

FEDERAL COMMUNICATIONS COMMISSION
OFFICE OF THE SECRETARY

BEFORE THE
FEDERAL COMMUNICATIONS COMMISSION
WASHINGTON, D.C. 20554

In the Matter of	)	
	)	
	)	
Simplification of the	)	CC Docket No. 92-296
Depreciation Prescription	)	
Process	)	

TO: The Commission

COMMENTS OF SOUTHWESTERN BELL TELEPHONE COMPANY

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CC Docket No. 92-296

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Southwestern Bell Telephone Company

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SUMMARY[**]

Southwestern Bell Telephone Company supports the Commission's efforts to simplify the depreciation prescription process. However, the true focus of this proceeding should not merely be simplification but development and improvement of the prescription process to obtain the regulatory framework essential for future oriented reform.

All carriers should have the ability to establish capital recovery rates in a manner similar to their competitors in the industry. Only Option IV provides such ability. Option IV is consistent with the Commission's Section 220 Statutory Requirements and truly achieves the Commission's goal for simplification. Speculation about whether the price cap regulation sharing mechanism will impact depreciation decisions is unwarranted because of the existence of Generally Accepted Accounting Principles, Securities and Exchange Commission guidelines, sound business judgment and the Public Notice and comment cycle.

The remaining options fail to achieve the Commission's goal of simplicity and fail to adequately address carrier needs in a competitive market. Option IV should be adopted.

[**] All abbreviations used herein are referenced within the text.

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COMMENTS OF
SOUTHWESTERN BELL TELEPHONE COMPANY

Southwestern Bell Telephone Company (SWBT), by its attorneys, files the following Comments in response to the Commission's Notice of Proposed Rulemaking (NPRM)[1] for simplification of the depreciation prescription process.

I. INTRODUCTION

The current depreciation prescription process, developed in the 1940s, was designed to establish rates that accurately allocate plant costs to expense at a rate representative of actual consumption of plant (i.e., remaining life depreciation procedures).[2] This process was developed when there was no competition and only moderate technological advances in the telephone industry.[3] Consequently, the depreciation process was geared to rely heavily upon historical lives, rather than economic useful lives (i.e., accelerated depreciation methods that recognize

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[1] In the Matter of Simplification of the Depreciation Prescription Process, CC Docket 92-296, Notice of Proposed Rulemaking (released December 29, 1992).

[2] NPRM, at paras. 5 & 7.

[3] NPRM, at para. 7.

useful life expectations based upon technological advancements). The current process is complex and costly for the carriers which must compile and submit voluminous data, as well as for the Commission which must devote significant resources to review carrier depreciation studies.

Therefore, SWBT supports the Commission's efforts to simplify the depreciation prescription process. The true focus of this proceeding however should not merely be simplification, but development and improvement of the process to obtain the regulatory framework essential for future-oriented reform. This type of reform would provide for capital recovery in a transition marketplace, and could be utilized as a mechanism to drive the industry toward the desired investment in the infrastructure, while accommodating carriers' needs to respond to the competitive environment, where rapid technological advancements are materially shortening the economic service lives of existing investments.

The era of intense competition, as noted above, is rapidly becoming a reality. As recently noted by Commissioner Barrett:

> The communications industry is undergoing rapid changes. Advances in technology make the local exchange market and wireless services market fertile ground for companies who seek to provide niche services. Future local exchange markets will continue to be reshaped by an increasing number of competitors seeking new market niches. It is likely that the monopoly local exchange market will eventually evolve into a local multimedia and wireless services market, with multiple competitors.[4]

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[4] Commissioner Barrett's February 2, 1993 presentation at the Institute for International Research in Dallas, Texas.

In addition to the competitors seeking "new market niches," carriers will also be competing against companies like a merged AT&T/McCaw and the Sprint/Centel combination, which are already positioned to market nationally banded wireless services.[5] Further, the Commission has recently initiated the development of rules for the provision of wireless Personal Communications Services, which will have enormous impacts on the competitive equation and regulatory framework for the future local exchange markets.[6] As rapidly advancing technologies enable more sophisticated use of fixed microwave frequencies, proposals for local loop wireless services such as those recently authorized in the United Kingdom will likely appear.[7]

The accelerated pace of technological change in the communications market is hastening the demise of traditional market segments and barriers.[8] The Commission recognized some of these changes in implementing the price cap regulatory plan, which was intended to provide more of the incentives that occur in a competitive market.[9] This same type of forward-looking reform is essential in the depreciation prescription process to streamline

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[5] 1993 Telephony Annual U.S. Review and Forecast, p. 38, Telephony, January 25, 1993.

[6] In the Matter of Amendment of Commission's Rules to Establish New Personal Communications Services, Docket No. 90-314.

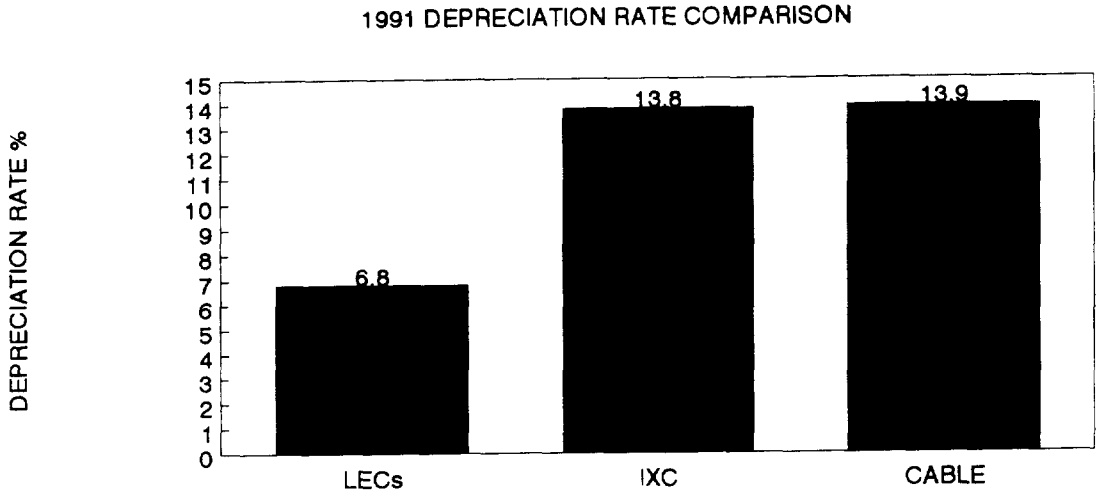
[7] See, Local Loop Alternative Approved, p. 35, Communications Week International, September 21, 1992. (Millicom and Ionica granted licenses to offer wireless local loop services.)

[8] Commissioner Barrett's February 2, 1993 presentation at the Institute for International Research in Dallas, Texas.

[9] Id.

regulatory procedures that currently handicap and restrict a carrier's ability to respond effectively to competition. Carriers should be allowed to make depreciation decisions in the same manner employed by other industry participants, with Commission review and approval of the rates, as mandated by statute.

As indicated on the graph below, the LECs depreciation rates are significantly less than other communication companies:



Note: Comparison was prepared using MR Rates for regulated carriers, and Financial Statement information from Compustat Database for non-regulated companies.

These distinctions in capital recovery rates have been caused in large part by the utilization of different methodologies and assumptions in the depreciation rate development process. Specifically, regulated carriers are required to rely heavily upon historical lives, while nonregulated carriers utilize economic plant life assumptions. This equates to an unfair competitive advantage for nonregulated carriers, as they are continually permitted to recover their investment over shorter periods, thus

continually generating additional funds for upgrading facilities (i.e., ability to obtain the latest technology).

With the emergence of intense competition (i.e., local exchange competition, local wireless access providers, cable TV-telephony networks), the increased pace of economic and technological obsolescence of investments will increasingly demand that carriers have the same ability to accelerate capital recovery. As noted in the latest series of reports by Mercer Management Consultants, "the copper network, which is both the lifeblood of today's networks and one of the biggest capital drains, is not likely to carry LECs into the future."[10] This analysis clearly illustrates that, irrespective of historical trends in obsolescence and retirement, competition and technological advancements will necessitate infrastructure modernization. Therefore, reform of the depreciation prescription process should utilize economic lives, instead of the historical data which is currently heavily relied upon.

AT&T is a "leading indicator" in measuring the results of competition and technology on a regulated entity. As noted in AT&T's recently filed Petition for Waiver of the Commission's Depreciation Rules, rapid technological and competitive changes resulted in substantially reducing the value and economic useful life of AT&T's analog transmission plant, which served to highlight

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[10] Wilson, Carol, The Three Best Things LECs Can Do in 1993, Telephony, January 25, 1993, at p. 20.

the inadequacy of AT&T's existing depreciation rates.[11] Accordingly, at the end of 1988, AT&T, with concurrence from its independent auditors, expensed its analog long-distance network equipment for financial reporting (FR) purposes and, with Commission approval, began to increase its regulated depreciation expense (MR reporting). AT&T also adopted accelerated depreciation methods (for FR purposes) for some accounts, as a measure to avoid subsequent writedowns.[12] In the following years, AT&T dramatically increased its total regulated depreciation expense. AT&T now requests a waiver of the Commission's rules, regardless of the outcome of this docket, in order to compute and record depreciation expenses for regulatory reporting purposes in conformity with the depreciation rates used for FR purposes.[13]

The situation experienced by AT&T in 1988 is similar to the transition currently confronting the LECs. At that time, AT&T presented the analysis of Ronald E. White, Ph.D., supporting their petition for modification of depreciation rate-setting practices. White correctly noted that, "the emergence of competition in markets previously protected by regulatory barriers to entry,

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[11] AT&T Petition for Waiver of the Commission's Depreciation Methods and Procedures, 1/27/93 pp. 12-13. ("AT&T Petition for Waiver").

[12] We neither accept nor condone AT&T's strategic decisions in managing their depreciation policies and practices, we merely point out the consequences of competition and technological advancements on a regulated entity in a transitional environment.

[13] AT&T Petition for Waiver, pg. 1. While SWBT does not oppose AT&T's waiver request, SWBT does reject AT&T's conclusion that the LEC situation is significantly different than AT&T so as not to be afforded equal treatment is setting depreciation rates.

presents a new set of challenges in setting depreciation rates."[14]

White's statement contained the following:

> The opportunity for capital recovery of the competitive carrier still subject to regulatory constraints of its depreciation practices, will be threatened if competitive pricing does not permit a realization of the net revenue contemplated in the prescribed depreciation rates.[15]
>
> The period of transition between partial regulation and total deregulation must be used to eliminate reserve imbalances created by the changing economic and technological forces which have spurred competition. Failure to eliminate these imbalances will systematically deny regulated carriers subject to competition an opportunity to recover its capital invested during previous eras when markets were closed to competition.[16]
>
> Intense competition among interexchange carriers no longer permits AT&T to satisfy the goals of depreciation accounting as they were achieved under regulation. Secondarily, the Commission should consider the capital recovery implications of such pervasive regulation when competitive pricing may not permit recovery of the depreciation expense allowed under prescribed depreciation rates.[17]

The analysis of the AT&T situation, as presented by White and subsequently acknowledged by the Commission in the form of increased regulated depreciation expense, is relevant to the circumstances currently confronting the LECs. Therefore, the Commission should give sufficient consideration to the situation of

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[14] Ronald E. White, Ph.D., Foster Associates, Inc., Statement In Support Of AT&T Petition For Modification Of Depreciation Rate-setting Practices, February 14, 1989, page 9. (White Analysis).

[15] White Analysis, p. 2.

[16] White Analysis, p. 9.

[17] White Analysis, p. 15.

the LECs and put forth a comprehensive effort to reform the depreciation prescription process. Such reform should include providing carriers with the ability to increase depreciation rates based upon the economic realities of a competitive market, as well as providing mechanisms for recovery of embedded investments.

In the past the Commission has recognized that a carrier's shareholders are entitled to the opportunity to earn a fair return on the amount of capital prudently invested in the regulated enterprise, and that depreciation is designed to regain the entire amount the investors paid to purchase it over the service life of the asset.[18] The fact that the combination of changing technologies and a competitive market necessitate the deployment of such new technologies which in turn is reducing the expected service life of existing assets does not make this axiom any less appropriate.[19]

For these reasons the Commission should seize the opportunity available within this proceeding, to not merely simplify the depreciation process, but to develop the framework essential for future-oriented reform (i.e., capital recovery reform

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[18] In the Matter of Amendment of Part 31 So As To Permit Depreciable Property to be Placed in Groups of Units with Expected Equal Life of Depreciation under the Straight-Line Method, Docket No. 20188, 83 FCC 2d 267, 276-277 (1980). ("CC Docket 20188").

[19] See, Docket 20188, 83 FCC 2d. at 276 wherein the Commission notes "when utility property becomes unsuitable by reason of obsolescence before investors have fully recovered their investment in it, the loss is passed on to the consumers". While with price cap regulation, changes in depreciation expense are generally treated by the Commission as endogenous and thus do not affect rates, the general axiom espoused in Docket 21088 is still applicable--LEC shareholders are entitled to the opportunity to recover the full cost of the asset through depreciation over its useful life.

of the depreciation prescription process). In order to achieve this goal, SWBT recommends that the Commission adopt Option IV, the price cap carrier option. Option IV, as outlined by the Commission, recognizes the regulated carriers' need to establish depreciation rates on the same basis used by competitors. At the same time Option IV ensures that the Commission fulfills its statutory duty, through the Public Notice and comment process, to consider the positions of interested parties and prescribe the actual rates. The other options do not allow carriers the ability to establish depreciation rates in a manner consistent with the competition and fail in varying degrees to accomplish the Commission's goal for simplicity.

II. CARRIERS SHOULD BE ALLOWED THE SAME OPPORTUNITIES TO MANAGE THE BUSINESS AS COMPETITORS--OPTION IV SHOULD BE ADOPTED.

1. Option IV Should be Adopted for All Carriers.

The Commission recognizes that the telecommunication industry today is characterized by rapidly changing technology and emerging competition.[20] LEC competitors respond to technological advancements and the competitive market place without the handicap of setting depreciation rates through complex studies and a costly time-consuming approval process. Rather, LEC competitors make management decisions regarding advanced technologies and depreciation rates and practices based upon a myriad of factors, including the economic lives of the assets.

As the communications industry transitions toward a more fully competitive local exchange carrier market, all LECs will

[20] NPRM, at para. 8.

experience competition and the need to establish capital recovery rates in a manner similar to their competitors. Thus, Option IV should not be limited to price cap carriers, but should be available for all carriers.[21] Option IV should be adopted because it is the only option that provides the latitude necessary for all carriers to remain players in an environment evolving from traditional local exchange service to a local multimedia and wireless services market, with multiple competitors.

2. Option IV is Consistent with the Commission's Section 220 Statutory Requirements.

Under Option IV a carrier seeking depreciation rate changes would file information regarding the depreciation rates in effect, the proposed depreciation rates and the change in the depreciation expense they would experience if the rates become effective.[22] The proposed depreciation rates would be placed on Public Notice and each state commission having jurisdiction over the carrier would be notified and given the opportunity to submit comments, as prescribed by Section 220(i) of the Communications Act.[23] Concerns over the fact that depreciation expenses are included in the revenue requirements for rate of return carriers would be addressed during the Public Notice and Comment cycle and subject to close scrutiny. The Commission would prescribe rates,

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[21] Concerns over the fact that depreciation expenses are included in revenue requirements under rate of return regulation would be addressed in the Public Notice and comment cycle when the carrier sought a change in depreciation rates. See Section II.2 below.

[22] NPRM, para. 41.

[23] Id.

based on the carrier's proposal and all comments filed in relation thereto, thus fulfilling the Commission's statutory duty to prescribe the percentages of depreciation under Section 220(b).[24]

In the past, the Commission has conducted three-way meetings with the carrier and state commissions in setting depreciation rates. The Commission requests comment on whether the practice of relying on formal comments filed in the notice and comment process of Option IV would be consistent with the Section 220(i) statutory notification requirement.[25] Section 220(i) provides that:

> The Commission, before prescribing **any requirements as to accounts, record or memoranda**, shall notify each state commission having jurisdiction with respect to any carrier involved, and shall give reasonable opportunity to each such commission to present its views, and shall receive and consider such views and recommendations.[26]

The plain language of the statute does not require a three-way meeting nor has the Commission in the past required meetings with state commissions prior to prescribing "any requirements as to accounts, record or memoranda" pursuant to Section 220(i). Instead, the Commission has proceeded by notifying the state commissions of the existence of the proceeding and giving the state commissions an opportunity to comment.[27] The notice and comment

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[24] See, 47 USC 220(b).

[25] NPRM, at para 42.

[26] 47 USC 220(i). (emphasis added).

[27] See, e.g., Notice of Proposed Rulemaking to amend Part 31, Uniform System of Accounts as it Relates to Treatment of Individual Items of Furniture and Equipment Costing $500 or less, Notice of

(continued...)

process in Option IV fulfills the statutory notification requirements of Section 220(i) in precisely the same manner that the Commission has used in the past when prescribing other "requirements as to accounts, records or memoranda".[28] As acknowledged in the NPRM, the three-way meeting process is merely a "practice" of the Commission - - not a statutory obligation.[29] The notice and comment process of Option IV satisfies the statutory notification requirements of Section 220(i).

Implementation of Option IV would simplify the depreciation prescription process and allow LECs to set depreciation rates in a manner similar to their competitors, while satisfying the Commission's statutory obligation to prescribe rates. Thus, Option IV should be adopted for all carriers.

3. Speculation About Whether the Sharing Mechanism will Impact Depreciation Decisions is Unwarranted.

The Commission notes that under price cap regulation, LECs must share earnings with their customers if earnings fall within a prescribed sharing zone.[30] Depreciation expense derived from rates set pursuant to Generally Accepted Accounting Principles

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[27](...continued)
Proposed Rulemaking, 2 FCC Rcd. 2788, 2792 (1987); Amendment of Annual Report Form M and FCC Form 901, CC Docket 85-308, Notice of Proposed Rulemaking, at para. 34 (Released Oct. 15, 1985); Detariffing of Billing and Collection Services, Notice of Proposed Rulemaking, 100 FCC 2d 607, 615 (1985); Deregulation of Customer Premises Inside Wiring, CC Docket 79-105, Further Notice of Inquiry, 86 FCC 2d. 885, 890 (1981).

[28] See, Id.

[29] See, NPRM, at para. 42.

[30] Id.

(GAAP) is a legitimate recoverable expense, regardless of the carrier's earning level or whether the carrier is in the sharing mode. A change in depreciation expense will inpact earnings just as any other legitimate expense will impact earnings.

Parties wishing to keep the LECs handicapped by complex inflexible depreciation prescription methods and under recovered assets will most likely attempt to weave arguments from this basic fact. Such commentors have the freedom to make capital recovery decisions based on a myriad of factors and accelerate depreciation to accommodate changing technologies and competition, thus giving them a competitive advantage over LECs. To speculate that LECs would manipulate the depreciation process based on the possibility of sharing is to ignore the existence of GAAP, Securities and Exchange Commission guidelines, internal and external audits and sound business judgment.

The concern regarding depreciation manipulation is unwarranted because, regardless of which alternative is adopted, the use of GAAP in deriving depreciation methodologies and assumptions remains constant. GAAP specifically provides that "depreciation be determined in a manner that systematically and rationally allocates the cost of an asset over its estimated useful life."[31] Thus, adherence to GAAP will prohibit carriers from manipulating depreciation expense merely to avoid sharing. Instead, LECs will continue to be motivated to record depreciation based upon reasonable estimates of useful life.[32]

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[31] HBJ Miller Comprehensive GAAP Guide 1993, Section 11.09.

[32] Id.

More significantly, sound business judgment questions the rationality of manipulating depreciation rates merely because of sharing. The LEC would be incurring $1 of depreciation expense to avoid paying at most $.50 through sharing.[33] Such a rationale would not be attractive to shareholders and would be contrary to sound business judgment.

The process of capital recovery is fundamentally a "timing" mechanism that governs when expense is recognized. It prohibits over recovery in that depreciation expense is limited to original costs, net of salvage value and cost of removal. Therefore, depreciation methods and procedures merely (using mathematical formulas) determine when the appropriate levels of expense is recognized. In addition, the use of remaining life depreciation, which would presumably remain an element of Option IV, is designed as a self-correcting mechanism to assure that investments are not over recovered.

Carriers have strong incentives to depreciate investments over the appropriate useful lives:

1. A carrier that recovers its investment too rapidly through the utilization of aggressive depreciation rates, and does not sufficiently reinvest, will be under pressure in future years as market demands may exceed the carrier's capabilities.

2. A carrier that recovers its investment too slowly, will not generate sufficient recovery to fund appropriate infrastructure improvements, and thus may not remain viable in a competitive market.

3. Over or under recovery of depreciation will have adverse financial impacts and will result in

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[33] If interstate sharing were the only concern, $1 of depreciation expense would be incurred to avoid approximately $.13 through sharing.

misleading information to the investment community. This could ultimately affect stock prices.

Speculating that LECs will manipulate the depreciation process because of sharing to arrive at unreasonable rates also ignores that the Commission is still prescribing the depreciation rates, after full consideration of input from all interested parties. If a party is concerned that a proposed change in a depreciation rate is unreasonable or inflated, it has the right to challenge the proposed rate, in the Public Notice cycle, regardless of whether the LEC is at or near the sharing mode. The party challenging the rate will know the prior rate, the proposed rate and the change in depreciation expense. The carrier requesting the change will also file information sufficient to support the requested change which will be available to the party challenging the change. The party challenging the change will also be able to compare the rate with the rates used by other carriers and rates used by the industry in general. If the party challenging the requested change is an IXC or competitor, it can compare the depreciation rate it uses for like plant to the proposed rate and include such comparison in its comments. There is no reason to assume that the Commission will suddenly adopt a "rubber stamp" mentality regarding its duty to review relevant input and prescribe depreciation rates. Rather, it is reasonable to assume that the Commission will review all input, address all comments, including allegations of rate manipulation and rule accordingly.

Under Option IV carriers would follow GAAP and would be setting rates in a manner similar to that of the industry in which they must compete, the difference being that the industry would

have the opportunity to review and comment on the carrier's rates. Option IV thus strikes an equitable balance between the need for reform, the need for simplicity and the statutorily imposed need for the Commission to prescribe carrier depreciation rates, with input from the state commissions and other interested parties. While simplification is important to all carriers and regulators alike, another major benefit obtained under Option IV is the ability to refocus resources and manage the business more efficiently for survival in a competitive environment. SWBT approximates that savings of $2,000,000 annually in travel and preparation expenses will be realized by SWBT if Option IV is adopted.

III. THE REMAINING OPTIONS FAIL TO ADEQUATELY ADDRESS CARRIER NEEDS IN A COMPETITIVE MARKET.

A. The Remaining Options Fail to Achieve the Commission's Goal of Simplicity and Fail to Adequately Address Carrier Needs in a Competitive Market.

The remaining proposed options fail to achieve the Commission's goal of simplicity and do not grant carriers the ability needed in an environment of rapidly changing technologies and competition.

The amount of simplification arising out of the Basic Factor Range Option ("Factor Range Option") and the Depreciation Rate Range Option ("Rate Range Option") is questionable, especially in light of the minimal impact these options will have as a means of reform. Pursuant to the Rate Range Option the carrier would select depreciation rates from ranges dictated by the Commission.[34]

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[34] NPRM, at paras. 26-38.

Pursuant to the Factor Range Option the carrier would select future net salvage, projection life and survivor curve factors from ranges again dictated by the Commission.[35]

Previously, the carriers were allowed to set such factors and provide analysis to support the factors chosen to arrive at the rate.[36] The approach thus switches the process of determining the appropriate factors and the rates from the carrier to the Commission. Thus, instead of the carrier deciding the service life of an asset in light of rapidly changing technology, the Commission is given that responsibility.

The Commission proposes to implement the Factor Range Option or the Rate Range Option by reviewing "industry wide data" to arrive at the ranges.[37] The Commission cites as an example reviewing industry wide data on Motor Vehicles, Account 2112.[38] The Commission's proposal to establish the rate ranges or initial factor ranges through the basic factors underlying the current rates[39] accomplishes little in the way of reform in response to an environment of emerging competition and rapidly changing technologies.

The data should be gathered from the communications industry as a whole, not just those carriers for which the Commission currently prescribes rates. The existing prescribed

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[35] NPRM, at para. 13.

[36] See, Id.

[37] NPRM, at para. 14.

[38] NPRM, at para. 14.

[39] NPRM, at para. 24.

rates simply do not accurately represent the industry in which the LECs must compete. Using existing rates or rate factors merely perpetuate the problems associated with setting depreciation rates in an environment of emerging competition and rapid change in technology using historical lives rather than economic lives.

Since the Commission would need to gather information from the communication industry, the remaining options do not actually further the Commission's goal of simplicity. Rather, the Commission is merely shifting its burden from one methodology to another without lessening the burden. Under the remaining three options the Commission has the burden of gathering information from the industry and trying to determine the future economic life of assets in an environment of rapidly changing technology. Thus, the obligation of demonstrating that the depreciation rates are proper seemingly lies with the Commission under the remaining three options and not with the carrier. Chairman Sikes recognized this fact in questioning whether the FCC staff could examine telephone poles, fiber, switches or software add-ons and have any reasonable idea of what their life is.[40]

The Factor Range Option and the Rate Range also propose a mandated staggered approach for the implementation of the new process. All carriers will be affected by emerging competition and no carrier should be disadvantaged because of their position on the prescription schedule.

In addition, under the Factor Range Option, basic factor ranges would not be established for all accounts because a number

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[40] Telecommunications Reports, December 14, 1992, p. 5.

of accounts are not easily adaptable to ranges because of the divergence "from company to company and from prescription to prescription."[41] The Commission should not waste resources in attempting to develop what is admittedly only a partial fix for the depreciation prescription problem. The Commission should strive to achieve a total fix. Of the options listed in the NPRM, only Option IV has the potential to achieve a total fix for existing depreciation problems.

The final option, the Depreciation Schedule Option, fails to provide the carriers with any meaningful decision-making responsibility regarding their depreciation rates. The Commission would simply dictate a depreciation schedule to be applied to each account. As the Commission notes, the Depreciation Schedule Option offers the greatest degree of simplification and greatest degree of depreciation expense certainty.[42] However, simplicity for simplicity's sake without reform is not a solution to the problems facing the industry.

As the Commission accurately notes, the Depreciation Schedule Option offers the greatest deviation from accuracy in matching allocation of costs with plant consumption.[43] Instead of the carrier making the depreciation rate decision that will best suit its plans for infrastructure investment based on its service area, the depreciation schedule will be mandated by the Commission. Therefore, the Depreciation Schedule Option will put the carrier at

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[41] NPRM, at para. 16.

[42] NPRM, at para. 33.

[43] Id.

a distinct disadvantage in attempting to compete in today's environment because it will be unable to adjust its asset deployment and capital recovery strategies to the competitive marketplace.

The Depreciation Schedule Option also calls for the tracking of accruals by vintage, which will increase the amount of accounting work while at the same time producing less accuracy in the matching of allocations of cost with plant consumption.[44] The Depreciation Schedule also does not adequately take into account future plans for technological improvements. Of the four options proposed, the Depreciation Schedule Option does the least in reforming the prescription process to reflect an environment of competition and rapidly changing technology.

The Commission also requests commentors to address the transitional problems posed by embedded plant under the Depreciation Schedule Option.[45] The Commission suggests development of depreciation schedules for each vintage of embedded plant in a particular account or an aggregate of all embedded plant in an account and determine a composite depreciation schedule for that embedded plant.

SWBT agrees with the Commission's assessment that adjustments may be required for complete reconciliation under the Depreciation Schedule Option. However, SWBT does not believe that this problem is limited solely to the Depreciation Schedule Option. This problem is inherent to all options.

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[44] NPRM, at para. 33.

[45] NPRM, at para. 36.

Specifically, the Commission's goal of introducing competition, coupled with the accelerated pace of technological advancements, is threatening the LECs' ability to recover embedded investment, and thus will severely limit the funds available for infrastructure improvements.[46] As a result, the Commission must address the LECs' at-risk investment within the context of depreciation reform.

For these reasons, Option IV is best suited to meet today's environment and accomplish the Commission's goal for simplification.

B. Of The Remaining Options, The Rate Range Option Is The Only Option That Appears To Further The Commission's Goal Of Simplification, But In Actuality It Does Not Achieve This End.

Pursuant to the Rate Range Option (Option II), the Commission would establish ranges of annual depreciation rates for each plant account using industry-wide data.[47] Carriers would then set depreciation rates for that particular account somewhere within the range. The selection of a composite depreciation rate based on industry data is conceptually sound. The LECs would set depreciation rates comparable to the competition within the industry. As such, the establishment of ranges for rates (Option II) is preferable to ranges for parameters (Option I). However, the establishment of "industry averages" poses significant

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[46] An example that illustrates this point is the Interim Transport Order that does not allow the LECs to price their services consistent with the technology utilized in the existing network. In The Matter of Transport Rate Structure and Pricing, CC Docket No. CC 91-213, 7 FCC Rcd 7006 (1992).

[47] NPRM, at paras. 26-28.

problems. Further problems arise with the application of review cycles.

The usefulness of the Rate Range Option as a method of reform depends to a large extent on how the term "industry" is defined in gathering "industry-wide data". As mentioned above, because of the need to meet competition, ranges should reflect the entire communications industry. Realistically, the information concerning the asset lives of similar assets used elsewhere in the communications industry is not as readily available as the rates of the companies currently regulated by the Commission. As such, it is unclear how the Commission could gather such "industry" data.

Further, it is likely that the Commission's "industry" average will be based partially (if not primarily, due to the above) on LEC data that it currently regulates. The submission of data to the Commission to establish rates will presumably require significant input from the LECs. Unless the information required is significantly abbreviated from what is required today, the degree of simplification is questionable.

Additionally, the Commission proposes to review the rates every five years and seeks comment as to the appropriateness of this time frame. SWBT agrees that a more frequent review does little to meet the goal of simplification. Yet, recognizing a five year window is exactly contradictory to why reform is needed today (i.e. rapidly changing technology and emerging competition). Moreover, simplification is being undertaken to recognize competition. As such, it is questionable how many five-year cycles will actually come to pass. At best, significant work will be