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Before the
FEDERAL COMMUNICATIONS COMMISSION
Washington, D.C. 20554

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In the Matter of	)	
	)	
Implementation of the Local Competition	)	
Provisions in the Telecommunications Act	)	CC Docket No. 96-98
of 1996 - Supplemental Comment Period	)	
	)	
	)	

Comments of John Staurulakis, Inc.

Michael S. Fox
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Date: July 8, 1996

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Summary

John Staurulakis, Inc. ("JSI") submits comments on the Industry Demand and Supply Simulation model. We believe that this model is unworkable in its current incarnation. We recommend a separate model or module for local exchange carriers serving rural areas. This recommendation is based upon evidence showing that rural local exchange markets are significantly different from urban areas. We also express concern regarding the usefulness of this model in attempting to simulate demand and supply in telecommunication markets.

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Implementation of the Local Competition Provisions in the Telecommunications Act of 1996 - Supplemental Comment Period	)	CC Docket No. 96-98
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Comments of John Staurulakis, Inc.

John Staurulakis, Inc. ("JSI") hereby submits comments related to the working copy of the FCC Industry Demand and Supply Simulation Model ("model"). Our comments are filed in accordance with the supplemental comment period designated for CC Docket 96-98 ("96-98").

JSI is a management consulting firm whose principal clients are independent local exchange carriers. While these comments are to be attributed solely to JSI, many of the issues we address will resonate throughout the independent local exchange carrier community.

I. General Issues Related to the Model

While we can comment on the general framework of the model, we cannot demonstrate any simulations with the model because of the incompatibilities we have with the Lotus 3.1 DOS version when used with other spreadsheet programs, including

Lotus 5.0 for Windows. We confirmed with the FCC staff that that the model is temperamental on platforms other than Lotus 3.1 DOS. We encourage the FCC staff to update the model to a current version of software.

Given the completely undocumented nature of the model, it is not entirely clear what the model is attempting to simulate. The public notice related to the model suggests that the model allows the user to "simulate effects in traditional industry segments" using exogenous data inputs. We find this purpose vague and without direction. We admit that because of the nature of the 96-98 proceeding, the model should address the effects of competition in local exchange markets. The FCC staff should be required to clearly define the specific policy goals and or objectives that the model is attempting to measure.

Based upon some segments of the model, such as the consumer surplus modules, we have the impression that the FCC is interested in demonstrating efficiency gains when competition is introduced in the local exchange markets. Our experience in the rural telecommunications industry suggests that the introduction of "unfettered competition" may pose significant financial hardship on telecommunication consumers in rural areas. We are not convinced that an aggregate model of this nature can be useful in dealing with specific LEC competitive issues.

It is the opinion of JSI that this model is currently unworkable in measuring the financial impact of policy implications related to 96-98. We reject the premise that an aggregated model can capture the nuances and uniqueness evident in all parts of the telephone industry. This premise is particularly egregious as national policy issues are translated to rural areas of the country. It is a common misconception that areas served

by rural, independent local exchange carriers of the United States are characterized by posh resort towns and communities. The fact that over 1,500 independent carriers service areas neither desired nor serviced by the original Bell system shows that the vast majority of areas served by independent local exchange carriers are farms and small communities in the heartland of the nation which have typically small population densities and high service costs. These areas are diverse and characteristically different from large towns and cities. The Telecommunications Act of 1996 ("Act") recognized these differences in several provisions for rural exchange carriers. This model is an aggregate model therefore, it doesn't capture any of these distinctions widely recognized in the telecommunications industry. We feel that this is a very serious deficiency with the model and would encourage the FCC staff to develop a model for rural local exchange carriers in conjunction with the development of a Tier 1 model.

We have concerns that in this version of the model, many of the critical "modeling variables" are exogenous values inputted by the user. We would like to see a simulation model that creates a supply schedule for both the retail and wholesale telecommunication markets from underlying cost information rather than requiring the user to input supply information. The demand for various telecommunication services could be combined with this supply schedule to determine an equilibrium price of these services. Because this is a "demand and supply model", we had anticipated that the model would determine a supply and demand equilibrium price based upon user defined inputs. Unfortunately, we find that the model doesn't determine an equilibrium price, rather it uses an input price to reflect the financial impact of the user defined price input. From our viewpoint,

this model seems to be a financial impact model and not a demand and supply simulation model.

Finally, we would like the model to demonstrate the interrelated nature of a multi-product LEC when there are economies of scope in telecommunications.[1] We encourage the FCC staff to explicitly relate scope economies from local service and toll service. This interrelationship will result in a positive network externality for local service and toll service when provided jointly and a negative externality when there are facilities based bypass competitors.

II. Issues Specifically Related to Independents as They Pertain to the Model

This section presents evidence from a selection of studies we have performed for independent local exchange carriers. These studies demonstrate that the effect of "cream skimming" in rural local exchange markets may pose serious financial hardship to telephone customers. The relationships presented in the FCC model are likely to be too modest when determining the impact of cream skimming in these unique rural markets. The table below shows the impact on average local rates if the top 5%, 10%, 15% or 20% of an Incumbent Local Exchange Carrier's (ILEC's) customers were to switch to a new entrant under the scenario where the new entrant purchased the ILEC's unbundled loop and bypassed the ILEC's switch -- this is a very likely scenario faced by the rural local exchange carriers. In all such studies we have performed, the results show that local rates

[1] In a digital switch there are clear economies of scope between local and toll calls. David Gabel and Mark Kennet, *Estimating the Cost Structure of the Local Telephone Exchange Network*, NRRI, October 1991.

will have to increase, or universal service contributions will need to dramatically increase, in order to offset the losses incurred from this type of competition. The majority of the revenue shifts are mostly the result of the bypass of access charge revenues. The FCC model would clearly understate these impact for small rural companies. The following table demonstrates the magnitude of losses when as little as 5% of the top customers are lost to competitive bypass.

Percentage Increase of Local Rates Due To Cream Skimming

Company	Loss Of Top 5% Of Customers	Loss Of Top 10% Of Customers	Loss Of Top 15% Of Customers	Loss Of Top 20% Of Customers
A	139.8%	231.8%	293.7%	342.7%
B	152.3%	257.0%	360.4%	477.6%
C	70.6%	133.4%	195.9%	259.6%
D	77.7%	162.1%	254.0%	367.0%
E	135.2%	273.3%	418.0%	598.6%
F	130.1%	278.5%	446.1%	546.6%
G	141.3%	265.8%	375.8%	507.6%
H	48.6%	87.7%	138.6%	194.0%
I	149.6%	293.4%	453.9%	636.6%

A failure to recognize the unique characteristics of these types of companies will place in jeopardy a substantial revenue flow that may well jeopardize the their ability to fulfill the obligations of carrier of last resort to those customers who have no competitive alternative. Secondly, and not unexpectedly, each of the studies also demonstrates that a small minority of customers account for the vast majority of the independent's regulated revenues. This suggests that if the competitor chooses to cream skim in rural areas, even

a 5% loss of access lines will inflict significant financial harm on the ILEC and, absent a substantial increase in Universal Service funding, these hardships will be borne by those customers who have no competitive alternative.

We have demonstrated that cream skimming in rural areas is significantly different than cream skimming in urban areas where the service area population is large. The model in its aggregate form cannot reflect the financial realities faced by independent local exchange carriers and their customers.

III. Conclusion

Despite the fact that we were not able to examine the simulation relationships under a working model, we have identified several key facts that have been omitted by the model. We encourage the FCC staff to develop an alternative model which closely resembles independent telephone company reality. We recognize that the FCC's primary focus is on the RBOCs; however, we encourage the FCC to pay particular attention to the independent telephone company situation and acknowledge that service in rural America merits at least as careful examination as service in urban areas.

Respectfully submitted,

John Staurulakis, Inc.

By: Michael S. Fox

Michael S. Fox
Director, Regulatory Affairs