concerning the definition of universal service or the method of collecting and distributing universal service support.

(A) USF. NYNEX supports the implementation of separate mechanisms of high-cost assistance for price cap LECs and rate of return LECs, and this support should be limited to residential customers. The support amounts for eligible price cap LECs should be calculated using a "proxy factors" system such as the Benchmark Cost Model ("BCM"). The BCM could be used to effectively target high-cost areas. It would be consistent with price cap or incentive regulation, because it would not require carriers to report actual cost data. It would allow carriers equal treatment regardless of whether they were incumbents or new entrants or whether they maintained large or small study areas, and it would allow portability of support. The subsidy amounts that would be developed through the BCM would be competitively neutral, since any eligible carrier, as defined in Section 214(e) of the Act, would receive the same payment as an incumbent LEC for serving a customer in the same area.

Rate of return carriers should be allowed to use actual study area costs. The BCM may be satisfactory for a carrier that serves a wider geographic area, as any overestimation in some areas will be offset by underestimation in other areas. However, such a model may not accurately portray the costs of a carrier that serves only a limited or a smaller area, and this could cause financial harm to small carriers.

(B) DEM. DEM weighting does not satisfy the requirements of the Act that support for universal service be "explicit" and that all telecommunications providers

contribute on an "equitable and nondiscriminatory" basis [22] The DEM weighting program should be restructured by removing the revenue requirements associated with it from smaller LECs' interstate switched access rates, and by recovering those costs through an explicit federal fund.[23]

(C) LTS. LTS is another form high-cost assistance; it is a fund paid by LECs that are not members of the NECA common line pool to members of the pool.[24] The LTS program is not consistent with Section 254 It does not support the definition of core universal service, as it is designed to help small LECs maintain lower carrier common line (CCL) charges, which only affects rates for interexchange service. Therefore, LTS should be eliminated, and the NECA pooling LECs should recover these costs directly through their CCL charges.[25]

(D) Funding the Programs. High cost support should be funded by all interstate telecommunications carrier Under Section 254, there should be individual funds, such as funds for schools, low income subscribers, and for high cost areas, but the revenues for these funds should be collected through a single mechanism. The funding mechanism should be competitively neutral; it should not favor one technology, service, or company over another. Contributions for the Federal fund should be based on interstate retail revenues. Each contributor's interstate universal service payment should be based on its

[22] *See* 47 U.S.C. Sections 254(b)(5), 254(b)(4), and 254(e).
[23] *See NYNEX Comments* at pp. 9-10
[24] *See* Sections 69.105, 69.503, and 69.502.
[25] *See NYNEX Comments* at pp. 23-25

percentage of total interstate retail revenues. The Commission should specify a surcharge that all interstate carriers would apply to their interstate retail customers' bills.[26]

28. What are the potential advantages and disadvantages of basing the payments to competitive carriers on the book costs of the incumbent local exchange carrier operating in the same service area?

If the Commission defines a LEC's "service area" as the current study area, which typically includes all of the LEC's exchanges in a state, using the book costs of the large LECs to determine universal service support payments to the CLECs would result in windfall profits to the CLECs. This would occur because the CLECs typically concentrate their initial efforts in dense urban areas that have loop costs that are significantly below the state-wide average.[27] For example, in New York, which has state-wide loop close to the national average, loop costs in urban areas are about 72% of the national average, and those in suburban areas are about 87% of the national average.[28] Therefore, providing high cost support to CLECs based on the LEC study area average loop cost would exceed the amount of support that those carriers need to provide universal service. It would also distort competition, because the LECs would have a continuing obligation to serve the high cost areas while competing with subsidized CLECs in the lower cost areas.

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[26] *See NYNEX Comments* at pp. 23-25.

[27] For small LECs, which are currently outside the price cap system, their smaller study areas reduce the ability of the CLECs to target low cost customers in a study area. Therefore, the Commission should use the LEC book costs to determine support levels for non-price cap LECs. See answer to question No. 27

[28] *See* Chart 1 *supra*.

If the Commission adopted a proxy model, such as the BCM, it could target support levels to costs in individual Census Block Groups ("CBGs"). Because CBGs are small, the costs within a CBG should not vary significantly.[29] Therefore, the LEC-based BCM costs could be used to calculate support for CLECs provided that they offered universal service throughout the CBG in the same manner as the LEC.

29. Should price cap companies be eligible for high-cost support, and if not, how would the exclusion of price cap carriers be consistent with the provisions of section 214(e) of the Communications Act? In the alternative, should high-cost support be structured differently for price cap carriers than for other carriers?

The price cap LECs should be eligible for high-cost support. Since the Commission has decided in Docket 96-98 to remove most of the access charge revenue stream from the rates for unbundled network elements, the price cap carriers will need universal service funds to replace the contribution from access charges that they have used to support affordable service to high cost areas.

If the Commission decides to provide high-cost support for price cap carriers, the support should be structured differently for these carriers than for non-price cap carriers. See answer to question No. 27. The Commission could use the BCM as a means of identifying areas served by price cap LECs that are likely to have higher-than-average costs. The BCM is both technologically and competitively neutral, as it does not rely on a company's actual costs of providing service. The BCM treats carriers equally, regardless

[29] The BCM also shows that costs vary significantly even among CBGs within the same wire center. Thus, basing cost support on costs by wire center would still provide CLECs with an incentive to serve primarily the low-cost CBGs in a wire center.

of the size of the area served and regardless of whether they are incumbent LECs or new entrants. In addition, the BCM allows for portability of the subsidy among eligible service providers. As such, the model should be used to calculate universal service support for price cap LECs providing "core" services to residential customers in high-cost areas.

The BCM assumes that the Commission will not disturb the current sources of revenue that the LECs use to provide residential and business services. Both price cap LECs and rate-of-return LECs rely on the contribution from access services, vertical features,[30] and other high-margin services to maintain universal service at affordable prices. NYNEX's previous proposal to establish relatively high Benchmark Cost thresholds for determining the amount of universal service support that a LEC would receive for a particular area assumed that the Commission would not disturb these sources of contribution. However, the Commission's decision in Docket 96-98 to require the LECs to offer unbundled network elements under Section 251(c)(3) of the Act based on total element long run incremental cost ("TELRIC") plus a portion of joint and common costs[31] will remove much of the contribution that the LECs currently rely upon to maintain affordable local exchange rates. This will occur for two reasons. First, the TELRIC methodology, even after addition of joint and common costs, is likely to result in prices that are well below the current level of state and interstate Local Switching access

[30] In a recent speech to the National Association of Regulatory Utility Commissions, Chairman Hundt stated that the cost of vertical features is about 5 cents per month. However, the State commissions have priced vertical features at several dollars per month in order to maintain affordable rates for basic telephone service.

[31] *See* FCC News Release, FCC Docket No. 96-98, Report No. DC 96-75, released August 1, 1996.

charges. Second, the Commission has decided to allow the LECs to apply the carrier common line charge and three fourths of the transport interconnection charge to carriers that purchase switching as an unbundled network element only until the Commission completes the earlier of (1) the universal service and access charge reform investigations; (2) the date that a LEC receives authority to provide in-region interLATA service; or (3) June 30, 1997. Thus, the revenues from these elements, as well as the shortfall in the unbundled price for switching, will either have to be recovered through the universal service fund, or through access charge reform, or both. If these shortfalls were not recovered, it would undermine the ability of the LECs to maintain their current service levels to high-cost areas and to residential customers in all areas.

30. If price cap companies are not eligible for support or receive high-cost support on a different basis than other carriers, what should be the definition of a "price cap" company? Would companies participating in a state, but not a federal, price cap plan be deemed price cap companies? Should there be a distinction between carriers operating under price caps and carriers that have agreed, for a specified period of time, to limit increases in some or all rates as part of a "social contract" regulatory approach?

For interstate universal service purposes, price cap LECs should be defined as those carriers that are not under rate of return regulation in the interstate jurisdiction per Section 61.41(a), and as defined in the Price Cap Performance Review for Local Exchange Carriers.[32]

[32] *See* CC Docket 94-1 released April 7, 1995 paragraph 33 ("The LEC price cap plan is mandatory for the largest LECs, the seven Regional Bell Operating Companies (RBOCs) and GTE. It is optional for other LECs. If a company elects price caps, all of its affiliated companies, with the exception of any average schedule affiliates, must also become price cap carriers. Those LECs electing price caps include United Telephone, Rochester

Companies that participate in a state price cap or incentive regulation plan but that are not price cap carriers in the interstate jurisdiction should not be classified as "price cap carriers" for purposes of determining eligibility for high-cost support. Such carriers are still basing their interstate rates on their costs, and their ability to maintain service in high cost areas may require universal service funding based on their book costs.

31. If a bifurcated plan that would allow the use of book costs (instead of proxy costs) were used for rural companies, how should rural companies be defined?

A rural company is already defined in the Act. The Act defines a rural telephone company as:

"[A] local exchange carrier operating entity to the extent that such entity --

A) provides common carrier service to any local exchange carrier study area that does not include either:

(i) any incorporated place of 10,000 inhabitants or more, or any part thereof, based on the most recently available population statistics of the Bureau of the Census; or;

(ii) any territory, incorporated or unincorporated, included in an urbanized area, as defined by the Bureau of the Census as of August 10, 1993;

B) provides telephone exchange service, including exchange access, to fewer than 50,000 access lines;

C) provides telephone exchange service to any local exchange carrier study area with fewer than 100,000 access lines; or

D) has less than 15 percent of its access lines in communities of more 50,000 on the date of enactment of the Telecommunications Act of 1996."[33]

Telephone, The Lincoln Telephone and Telegraph Company, and Southern New England Telephone.").

[33] *See* Section 3 (47).

If the above definition of a rural carrier as specified in the Act is used, some rate of return carriers may not qualify as rural carriers. Therefore, the Commission should define rural carrier for purposes of receiving universal service support as a carrier that is not under price cap or any other incentive form of regulation in the interstate jurisdiction. Non-price cap LECs are generally small LECs that serve rural areas, while price cap LECs are large carriers that generally serve both rural and urban areas.[34]

32. If such a bifurcated approach is used, should those carriers initially allowed to use book costs eventually transition to a proxy system or a system of competitive bidding? If these companies are transitioned from book costs, how long should the transition be? What would be the basis for high-cost assistance to competitors under a bifurcated approach, both initially and during a transition period?

Carriers that use book costs should transition, on a flash cut basis, to a proxy system when their form of interstate regulation changes from rate of return to price caps or another type of incentive regulation.

Under a bifurcated approach, CLECs should be eligible for the same amount of universal service support as the incumbent carrier serving the area in which the CLEC operates. In other words, in areas served by price cap LECs, the competitor will be eligible for support at level determined by the proxy system; and in areas served by rate of return LECs, the competitor will be eligible for the same assistance per line as the incumbent LEC.

33. If a proxy model is used, should carriers serving areas with subscription below a certain level continue to receive assistance at levels currently produced under the HCF and DEM weighting subsidies?

[34] *See* NYNEX Comments CC Docket 80-286, October 10, 1995 at p 18.

No. The whole point of a proxy system is that it would provide a consistent level of support for all LECs serving high cost areas. It would provide assistance based on high-cost areas rather than high-cost companies; and it would encourage recipients of assistance to control their costs, because the level of assistance would not increase as their costs increased. In a broader sense, it would be consistent with the Act's regulatory trend towards non-cost-based forms of regulation.[35] Moreover, it is unlikely that the NYNEX BCM methodology would provide less high cost assistance to price cap LECs than the current HCF mechanism.[36] It is for this reason that NYNEX proposes that any additional funding should be reflected in a reduction in interstate and state access rates.

Proxy Models

34. What, if any, programs (in addition to those aimed at high-cost areas) are needed to ensure that insular areas have affordable telecommunications service?

To ensure that insular areas have affordable telecommunications service, the Commission should provide targeted universal service funding for high-cost, insular areas. Low income customers should continue to benefit from existing assistance programs, such as the Lifeline and Link-up America programs. These programs have been effective in the past in promoting subscribership. However, they may need to be enhanced to accommodate the effects of increased competition in the local exchange market.[37]

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[35] *See* NYNEX Reply Comments CC Docket 80-286, November 9, 1995 at p 9.
[36] *See NYNEX Comments*, Exhibit A.
[37] *See NYNEX Comments*, pp. i - ii.

In addition, the Commission should rely upon other mechanisms, such as toll limit services, toll blocking services, credit limits, reduced service deposits, and debit cards, to make telephone service accessible to low-income customers in insular areas. This would help the LECs to provide access to such customers as well as to help the customers avoid disconnections for non-payment.

35. US West has stated that an industry task force "could develop a final model process utilizing consensus model assumptions and input data," US West comments at 1). Comment on US West's statement, discussing potential legal issues and practical considerations in light of the requirement under the 1996 Act that the Commission take final action in this proceeding within six months of the Joint's Board's recommended decision.

No comment

36. What proposals, if any, have been considered by interested parties to harmonize the differences among the various proxy cost proposals? What results have been achieved?

No comment.

37. How does a proxy model determine costs for providing only the defined universal service core services?

Proxy model algorithms are designed to calculate a proxy cost for providing customers with access to the core universal services. For instance, if core universal service is defined as voice grade local exchange service, touch tone dialing, and access to other services (see the answer to question No. 39 below), the proxy algorithms would include loop costs and the costs of the local switch that are associated with local calls. Since the

switch provides access to other services, such as long distance calling, the costs of such services do not need to be included in the proxy algorithm.

38. How should a proxy model evolve to account for changes in the definition of core services or in the technical capabilities of various types of facilities?

Proxy models can be updated and improved to account for changes in the definition of core services and advances in telecommunications and information technologies. In fact, updated versions of existing proxy models have already been filed with the Commission in this proceeding. Changes can be incorporated by including additional cost algorithms, using LEC cost-to-investment ratios times the additional investment needed to provide the additional services.

39. Should a proxy model account for the cost of access to advanced telecommunications and information services, as referenced in section 254(b) of the Act? If so, how should this occur?

Proxy models should not account for the cost of access to advanced telecommunications and information services. Under Section 254(c)(1)(B) of the Act, universal service is defined as telecommunications services that are subscribed to by a substantial majority of residential customers. Advanced services, such as Internet access service, data transmission capability, ISDN, optional Signaling System Seven features, or blocking of such features, enhanced services, and broadband services are not subscribed to by a majority of customers at this time. A proxy model should include the costs of the following "core" universal service features; (1) voice grade residential service with the ability to place and receive calls; (2) single party service; (3) touch-tone dialing; (4)

directory listing; (5) access to local and long distance toll calling; (6) access to operator services; (7) access to emergency (911) service; (8) access to Telecommunications Relay Service. These services would provide the loop and switch facilities that a customer would need to subscribe to advanced services. The Commission should consider advanced services as part of its "evolving" definition of universal service under Section 254(c)(1).[38]

> 40. If a proxy model is used, what, if any, measures are necessary to assure that urban rates and rates in rural, insular, and high-cost areas are reasonably comparable, as required in Section 254(b)(3) of the 1996 Act.

The State regulatory commissions have traditionally taken the lead in ensuring that rates for local telephone service are comparable in urban and rural areas. A proxy model, like the BCM, should be used as a backstop for State efforts to support affordable rates. The BCM would promote the statutory objectives of providing support to rural and high cost areas at rates that are comparable to rates in urban areas, which are generally less costly to serve, and of ensuring that rates for telephone service are "affordable" in high cost areas. Under Section 254(f) of the Act, the States can supplement the interstate universal service funding levels with state universal service funds to ensure that the rates in rural and urban areas are comparable.

Because proxy models are based on hypothetical costs, and because they do not represent the actual amount of costs that a LEC or other carrier incurs to provide service, they should not be used to develop a "reasonable" state-wide average price for local exchange service. Proxy models are very good at identifying areas that are relatively more

[38] *See NYNEX Comments*, p. 12.

costly to serve than other areas. Therefore, they are useful in targeting universal service support to the truly high cost areas. However, they are not accurate enough to develop appropriate rate levels for telephone service in urban and rural areas. That responsibility should remain with the States.

41. How should support be calculated for those areas (e.g., insular areas and Alaska) that are not included under the proxy model?

A major portion of these insular areas and Alaska are served by rate of return LECs, which should not be included in a proxy model -- their support levels should be based on their actual costs. A proxy model should only be used for price cap LECs, which generally are the largest LECs. A well-designed proxy system may be satisfactory for a LEC that serves a wider geographic area, as any overestimation in some areas will be offset by underestimation in other areas. However, such a model may not accurately portray the costs of a LEC that serves only a limited or a smaller area, and this could cause financial harm to small LECs. To the extent that insular areas and Alaska are served by price cap LECs, they should be included in a proxy model.

42. Will support calculated using a proxy model provide sufficient incentive to support infrastructure development and maintain quality service?

A proxy model can be a valuable tool in strengthening the ability of the LECs to provide service to high-cost areas as they face increasing competition in low-cost areas. By targeting universal service support to high cost areas, a proxy model would provide an additional incentive for the LECs to invest in those areas. However, the price cap system

would still provide the primary incentive for the LECs to invest in the network, because the LECs can share in the benefits of the productivity improvements that result from the introduction of new technologies.

43. Should there be recourse for companies whose book costs are substantially above the costs projected for them under a proxy model? If so, under what conditions (for example, at what cost levels above the proxy amount) should carriers be granted a waiver allowing alternative treatment? What standards should be used when considering such requests?

No. The advantage of a proxy model, like the BCM, is that it would provide an equitable level of support for price cap LECs that serve high cost areas; it would provide assistance to high-cost areas rather than to high-cost companies; and it would encourage recipients of assistance to control their costs, because the level of assistance would not increase as their costs increased.[39] Under NYNEX's proposal, the proxy model would be limited to price cap carriers which are large companies that have the ability to attract capital and to maintain quality service for all customers. Therefore, they do not need additional support above the level developed through the proxy model.

44. How can a proxy model be modified to accommodate technological neutrality?

A proxy system should not be biased in favor of a particular technology. Instead, the model should approximate the cost for a price cap LEC to provide "core" services to a high-cost area by using the most efficient technology currently available. An example of this is the Benchmark Cost Model. The BCM avoids technological bias by estimating the loop

[39] *See* NYNEX Reply Comments, CC Docket No. 80-286, filed November 9, 1995, p. 9.

investment needed to serve each Census Block Group as if a LEC were constructing a completely new network using current technologies. For both feeder and distribution plant, the model applies either copper facilities or fiber-based facilities on a least-cost analysis. The model can be updated as new technologies are introduced and as supplier prices change.[40] It may be appropriate to include wireless technology in those very remote areas where the cost of wireline facilities is extremely high.

> 45. Is it appropriate for a proxy model adopted by the Commission in this proceeding to be subject to proprietary restrictions, or must such a model be a public document?

If the Commission adopts a proxy model in this proceeding, it must be a publicly available document. In addition, all interested parties in this proceeding must have an opportunity to run and analyze the model and its results, and be able to readily obtain the documentation of the model.

> 46. Should a proxy model be adopted if it is based on proprietary data that may not be available for public review?

No. In order to avoid bias and data anomalies, a proxy model should rely only on data that are publicly available.

> 47. If it is determined that proprietary data should not be employed in the proxy model, are there adequate data publicly available on current book costs to develop a proxy model? If so, identify the source(s) of such data.

[40] *See* NYNEX Comments, FCC Docket No. 80-286, filed October 10, 1996, pp. 27.

Public data sources include ARMIS Data, the Federal-State Joint Board Monitoring Report, Statistics of Communications Common Carriers, and the annual Tariff Review Plans.

48. Should the materiality and potential importance of proprietary information be considered in evaluating the various models?

A proxy model should not employ a LEC's proprietary information.

Competitive Bidding

49. How would high-cost payments be determined under a system of competitive bidding in areas with no competition?

50. How should a bidding system be structured in order to provide incentives for carriers to compete to submit the low bid for universal service support?

51. What, if any, safeguards should be adopted to ensure that large companies do not bid excessively low to drive out competition?

52. What safeguards should be adopted to ensure adequate quality of service under a system of competitive bidding?

53. How is collusion avoided when using a competitive bid?

54. Should the structure of the auction differ if there are few bidders? If so, how?

55. How should the Commission determine the size of the areas within which eligible carriers bid for universal service support? What is the optimal basis for determining the size of those areas, in order to avoid unfair advantage for either the incumbent local exchange carriers or competitive carriers?

Answers to 49 through 55.

NYNEX does not support use of a bidding system to determine the level of interstate high-cost support. Such a system would be difficult to administer, especially if the Commission determined high-cost support levels by CBG. Depending on the

benchmark cost level that the Commission adopts as a threshold for determining whether a CBG is eligible for support the number of CBGs could vary from a few thousand to over 100,000. Competitive bidding for that many areas would be a very time consuming and expensive undertaking. Also, competitive bidding would not necessarily represent a better method of identifying the amount of support that is needed in each high-cost area. It would create large variations in the amount of support that is directed at each area depending on the level of competition and the business objectives of the bidders.[41]

Benchmark Cost Model (BCM)

> 56. How do the book costs of incumbent local exchange carriers compare with the calculated proxy costs of the Benchmark Cost Model (BCM) for the same areas?

We cannot quantify the difference between the BCM cost estimates and a LEC's book costs, since the BCM calculates the loop and local switching costs for providing basic residential service at the CBG level, and the incumbent LECs do not have book costs at the CBG level. However as a general matter, BCM costs tend to be well below the LECs' book costs, because the model is based on the hypothetical costs that a LEC would incur if it were constructing a completely new network using the most up-to-date technologies, rather than on the LEC's actual network investment, which reflects varied technologies and vintages.

> 57. Should the BCM be modified to include non-wireline services? If wireless technology proves less costly than wireline facilities, should projected costs be capped at the level predicted for use of wireless technology?

[41] *See* NYNEX Comments CC Docket 80-286, October 10, 1995, at p. 30.

Yes. Where wireless technology could be used efficiently to provide residential telephone service, it should be incorporated in a proxy model. In rural areas where customers are widely dispersed and very distant from the central office, wireless loop technology may be a less costly alternative to a wireline facility. The BCM assumes that wireline technology would be used for all customers. However, the BCM 2 submitted recently by US West and Sprint applies a $10,000 cap on loop investment to take into account the fact that wireless loops would be more efficient above that level of investment.[42]

58. What are the advantages and disadvantages of using a wire center instead of a Census Block Group as the appropriate geographic area in projecting costs?

NYNEX supports identifying high cost areas on the basis of U.S. Census Block Groups. The U.S. Census Block Group ("CBG"), which contains, on average, about 400 household units, is a discrete geographical unit used by the Department of Commerce in its national population census surveys. It is sufficiently small so as to allow the Commission to target high cost support to specific areas that have above-average costs. The CBG could be applied uniformly to all providers of telecommunications service, incumbents as well as competitors. In addition, it would not be administratively burdensome to distribute USF support by CBG.[43]

Costs to serve end user customers may vary greatly over an exchange or wire center or any other large geographic area due to terrain conditions and the distance an end

[42] *See Ex Parte* filing by US West and Sprint, CC Docket No. 96-45, dated July 3, 1996.
[43] *See* NYNEX Comments CC Docket No. 80-286, filed October 10, 1995, p. 13.

user may live from the serving central office. Even in smaller communities, there are some areas where the cost to serve subscribers are reasonable compared to urban areas, and there are other areas that have costs many times that of urban areas. Accordingly, determining support at the smaller CBG level better targets support to specifically defined high cost areas by eliminating some of the disparities in costs that can occur within a larger area. Additionally, the use of CBGs eliminates the implicit subsidy, inherent with a system where costs would be averaged throughout an entire exchange or wire center, of one group of subscribers by another.

> 59. The Maine PUC and several other State commissions proposed inclusion in the BCM of the costs of connecting exchanges to the public switched network through the use of microwave, trunk, or satellite technologies. Those commenters also proposed the use an additional extra-high-cost variable for remote areas not accessible by road. What is the feasibility and the advisability of incorporating these changes into the BCM?

Since the BCM is primarily designed as a proxy for loop costs, it should not be modified to include the costs of connecting exchanges to the public switched network through the use of microwave, trunk, or satellite technologies. However, since loop facilities to some customers in rural areas may be served more efficiently by wireless technology, the BCM 2 incorporates a maximum investment of $10,000 per wireline loop. This is based on the assumption that, above that level, it would be less costly to provide a wireless loop to serve the customer.

> 60. The National Cable Television Association proposed a number of modifications to the BCM related to switching cost, fill factors, digital loop carrier subscriber equipment, penetration assumptions, deployment of fiber versus copper technology assumptions, and service area interface costs.

Which, if any, of these changes would be feasible and advisable to incorporate into the BCM?

The BCM 2 includes many of the proposed modifications that parties in this proceeding, including the National Cable Television Association, recommended in their comments. However, the BCM 2 does not include all of the recommended modifications. According to the model designers, US WEST and Sprint, the model enhancements in the BCM 2 are designed to more accurately reflect actual engineering practices in the development of a local exchange network. Updating the switching module to include a variety of switch sizes, a user adjustable copper/fiber breakpoint, and business lines in the outside plant architecture, and adopting a road buffer approach to address household distribution assumptions, are among the major BCM 2 enhancements that were noted as areas of concern by the National Cable Television Association.

61. Should the support calculated using the Benchmark Cost Model also reflect subscriber income levels, as suggested by the Puerto Rico Telephone Company in its comments?

Yes. A significant variable that should be included as part of a long-term package of high-cost funding is the inclusion of a general economic needs test. This variable would differentiate areas with low income levels from areas with above-average income levels. High cost assistance should not automatically flow to subscribers just because they reside in areas where it is more costly to provide telephone service. Society does not subsidize the price of commodities for everyone irrespective of income, even when the commodities are considered essential. The same principle should apply to telephone services. This would allow the

Commission to limit the level of high-cost support while targeting it to areas where it is most needed. An income test could also be used to narrow the reach of universal service funding, thereby reducing the total size of the fund.[44] The benchmark cost estimated by BCM model could be related to the average income level in a CBG so that subsidies could be targeted to lower income areas and exclude high income areas.[45]

> 62. The BCM appears to compare unseparated costs, calculated using a proxy methodology with a nationwide local benchmark rate. Does use of the BCM suggest that the costs calculated by the model would be recovered only through services included in the benchmark rate? Does the BCM require changes to existing separations and access charge rules? Is the model designed to change as those rules are changed? Does the comparison of model costs with a local rate affordability benchmark create an opportunity for over-recovery from universal service support mechanisms?

NYNEX proposes the use of a benchmark cost instead of a benchmark rate. Use of the BCM does not suggest that the costs calculated by the model would be recovered only through services included in the benchmark cost. The benchmark cost should be used simply to determine the level of universal service support for a particular area. The universal service funding for each area would be used to by the LEC to maintain its existing state and interstate rates, or to reduce its rates if the BCM funding level exceeded the current level of high cost support in the interstate jurisdiction.

If the Commission decided to use the BCM to provide high-cost support, existing separations and access charge rules would have to be updated. The Part 69 rules concerning Long Term Support and the Part 36 Separations rules concerning DEM weighting and the

[44] *See* NYNEX Comments, CC Docket No. 80-286, filed October 10, 1995, pp. 13-14.
[45] *See* NYNEX Comments, CC Docket No. 80-286, filed October 10, 1995, note 40.

existing universal service fund would have to be replaced with a funding mechanism based on the BCM.

The comparison of model costs with a local rate affordability benchmark does not create an opportunity for over-recovery from universal service support mechanisms. A national cost benchmark would be established to identify CBGs with costs that are significantly above average. The benchmark would be used to control the size of the fund and to target support to areas that are truly high-cost. The difference between the cost estimate and the benchmark would be the number that would be subject to national funding, The actual difference could be weighted by some percentage to reflect the fact that a company should be required to recover some of the difference through its own internal rate averaging. Therefore, the company would not receive the entire difference from the universal service fund, but some percentage of the difference. To the extent that funding from the new USF exceeded the amount from the old USF, that amount would be used by the receiving LEC to reduce its interstate access rates, state access rates, or state toll rates.[46]

63. Is it feasible and/or advisable to integrate the grid cell structure used in the Cost Proxy Model (CPM) proposed by Pacific Telesis into the BCM for identifying terrain and population in areas where population density is low?

No comment. An industry task force is looking into this issue.

Cost Proxy Model Proposed by Pacific Telesis

64. Can the grid cell structure used in the CPM reasonably identify population distribution in sparsely populated areas?

65. Can the CPM be modified to identify terrain and soil type by grid cell?

[46] *See* NYNEX Comments, CC Docket No. 80-286, filed October 10, 1995, pp. 23-24.

66. Can the CPM be used on a nationwide basis to estimate the cost of providing basic residential service?

67. Using the CPM, what costs would be calculated by Census Block Group and by wire center for serving a rural, high-cost state (e.g., Arkansas)?

68. Is the CPM a self-contained model, or does it rely on other models, and if so, to what extent?

No comment to questions 64 through 68.

SLC/CCLC

69. If a portion of the CCL charge represents a subsidy to support universal service, what is the total amount of the subsidy? Please provide supporting evidence to substantiate such estimates. Supporting evidence should indicate the cost methodology used to estimate the magnitude of the subsidy (e.g., long-run incremental, short-run incremental, fully-distributed).

The CCL charge has three distinct categories of costs embedded in it. These costs may be referred to as (1) LTS; (2) Pay Phone; and (3) Base Factor Portion ("BFP").

The common line Pay Phone costs are interstate public pay phone costs that are recovered through the CCL charge. These costs are being dealt with in CC Docket 96-128, and they are not as significant as the common line Base Factor Portion.

The LTS program enables the NECA pool members to maintain a CCL charge equivalent to the CCL charge that would result if all LECs were members of the pool. The LTS fund replaces the revenues lost to the NECA pool members in setting their CCL charges at the nationwide equivalent rate. This amount is determined annually by NECA, which informs each LEC of its obligations to contribute to the fund. In 1995, $44 million of NYNEX's CCL revenues (out of a total of $423 million) represented LTS contributions. See Chart 2 below.

The CCL charge attributable to the common line Base Factor Portion recovers the revenue requirements for the difference between the capped $3.50 single-line business and residence end user common line ("EUCL") charge and the full monthly interstate loop cost. It also recovers the difference between the capped $6.00 multi-line EUCL rate and the interstate full loop cost in the event that the loop cost is above $6.00 per month.

The payphone and LTS portions of the CCL revenue stream clearly represent inter-company or inter-service transfers, and they are implicit subsidies that need to be replaced under the Act.

The remainder of the CCL charge represents nontraffic sensitive costs of providing local loops. If the Commission eliminated the CCL charge without increasing the EUCL charge, then the LECs would not have sufficient revenues to recover their current common line costs.[47] This would have an impact on their ability to continue providing loop services, especially in high-cost areas. Therefore, if the Commission eliminated the CCL charge, it would have to allow another mechanism for recovery of these costs, either through increases in EUCL charges, through other mechanisms, such as bulk-billing, or through the universal service fund. If the Commission did not want to increase the EUCL charges, the most competitively neutral mechanism for recovering these revenues would be the universal service fund.

In Chart 2, NYNEX calculates the interstate loop cost, based on fully distributed costs per the Commission's Separations and Access rules.

[47] The Commission's decision in Docket 96-98 not to apply CCL charges to unbundled network elements after June 30, 1996, or earlier, will also cause a revenue shortfall that will have to be recovered through other mechanisms if the EUCL charges are not increased. See answer to question No. 29 above.