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Before the
Federal Communications Commission
Washington, DC 20554

In the Matter of	)	
	)	
Implementation of the Local Competition Provisions in the Telecommunications Act of 1996	)	CC Docket No. 96-98
	)	
Interconnection between Local Exchange Carriers and Commercial Mobile Radio Service Providers	)	CC Docket No. 95-185

ORDER ON RECONSIDERATION

Adopted: September 27, 1996 Released: September 27, 1996

By the Commission:

I. Summary

1. In the *First Report and Order* we adopted regulations implementing sections 251 and 252 of the Telecommunications Act of 1934, as amended by the Telecommunications Act of 1996, that require local exchange carriers (LECs) to open their networks to competition by providing interconnection, access to unbundled network elements, and retail services at wholesale rates.[1] Pursuant to section 1.108 of the Commission's rules,[2] we here reconsider on our own motion two specific issues addressed in the *First Report and Order*. We expect that parties may raise other issues in petitions for reconsideration. First, we establish a flat-rated default proxy range for the non-traffic sensitive costs of basic residential and business line ports associated with the unbundled local switching element. The default proxy range for

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[1] *Implementation of the Local Competition Provisions of the Telecommunications Act of 1996,* CC Docket No. 96-98, FCC 96-325 (released August 8, 1996) (*First Report and Order*) at paras. 172-224, 226-541, 863-984, *petition for review pending sub nom., Iowa Utilities Board et. al v. FCC*, No. 96-3321 and consolidated cases (8th Cir. filed Sept. 6, 1996).

[2] 47 C.F.R. § 1.108

local switching adopted in the *First Report and Order* will continue to apply to the traffic-sensitive components of the local switching element, including the switching matrix, the functionalities used to provide vertical features, and the trunk port. Second, we clarify that, because the *First Report and Order* concluded that the local switching element includes dedicated facilities, the requesting carrier is thereby effectively precluded from using unbundled switching to substitute for switched access services where the loop is used to provide both exchange access to the requesting carrier and local service by the incumbent LEC. Finally, we make a non-substantive rule change to correct a typographical error.

II. Unbundled Local Switching Default Proxy

2. *Background.* To implement the pricing standards for interconnection and unbundled elements of the 1996 Act, we concluded in the *First Report and Order* that state commissions, in arbitrations, should set interconnection and unbundled element rates pursuant to a forward-looking economic cost pricing methodology.[3] Specifically, we concluded that the prices that new entrants pay for interconnection and unbundled elements should be based on the incumbent LEC's Total Element Long Run Incremental Cost (TELRIC), including a reasonable profit, plus a reasonable share of forward-looking common costs.[4] We concluded in the *First Report and Order* that "a combination of a flat-rated charge for line ports, which are dedicated to a single new entrant, and either a flat-rate or per-minute usage charge for the switching matrix and for trunk ports, which constitute shared facilities, best reflects the way costs for unbundled local switching are incurred and is therefore reasonable."[5] We remain convinced that the pricing methodology and rate structure established in the *First Report and Order* are correct and should be implemented by state commissions in arbitration proceedings.

3. For states that are unable to review or conduct an economic cost study consistent with the methodology we prescribed within the statutory time frame for arbitrating interconnection disputes, we established default proxy price ranges and ceilings that the states could apply, on an interim basis, to set prices for unbundled local switching and other unbundled elements in arbitrations.[6] We did not establish separate default proxy price ranges or ceilings for the dedicated, non-traffic sensitive costs of line ports and the traffic-sensitive costs of the unbundled local switching element. Rather, we stated that states that do not establish the rate for the unbundled local switching element based on a forward-looking economic cost study in compliance with the rules adopted in the *First Report and Order* may, in the interim, set the rate so that the sum of the flat-rated charge for line ports and the product of the minutes of use per port and the usage-sensitive charges for the switching

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[3] *Id.* at paras. 672-732.

[4] *Id.* at paras. 690-703.

[5] *Id.* at para. 810.

[6] *Id.* at paras. 782-827.

matrix and trunk ports, all divided by the projected minutes of use, does not exceed 0.4 cents ($0.004) per minute of use and is not lower than 0.2 cents ($0.002) per minute of use.[7]

4. *Discussion.* We now reconsider on our own motion a limited aspect of that decision and establish a default proxy range for basic residential and business line port costs of the local switching element. We see no reason at this time to revise the default proxy range for unbundled local switching that will apply to the traffic-sensitive components of the local switching element, including the switching matrix, the functionalities used to provide vertical features, and the trunk port. Moreover, we find no basis at this time for modifying the default proxy range for the termination of calls.

5. We relied on several studies in the record to support the default proxy range that we established for both the unbundled local switching element, pursuant to sections 251(c)(3) and 252(d)(1), and termination of calls, pursuant to sections 251(b)(5) and 252(d)(2).[8] These data described a range for the "additional costs" of end office switching, from a low estimate of 0.18 cents ($0.0018) to a high of 1.5 cents ($0.015) per minute of use,[9] with the forward-

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[7] *Id.* at para. 815; 47 C.F. R. 51.513(c)(2). We also observed that states that use our proxy and impose flat-rated charges for unbundled local switching should set rates so that the price falls within the range of 0.2 cents ($0.002) and 0.4 cents ($0.004) per minute of use if converted through the use of a geographically disaggregated average use factor. *Id.*

[8] *Id.* at paras. 803-811, 815, 1060.

[9] As we discussed in the Order (at paras. 803-809), the following data are included in the record: (1) MCI submitted an estimate of the cost of end-office switching, as calculated by the Hatfield 2 model, of 0.18 cents ($0.0018) per minute of use; (2) Cox estimated that, based on the Hatfield 2.2 model that AT&T submitted, the average Total Service Long Run Incremental Cost (TSLRIC) of end office switching for most states clusters around 0.2 cents ($0.002) per minute of use; (3) GTE reports that the Cost Proxy Model (CPM) submitted by Pacific Telesis estimates that the average cost of routing traffic through end office switches is 0.35 cents ($0.0035) per minute of use; (4) Cox asserts that the average incremental cost of inter-office transport and termination of traffic is 0.2 cents ($0.002) per minute of use; (5) USTA claims the average incremental cost of call termination is 1.3 cents ($0.013) per minute of use; (6) U S West asserts that Cox's estimate underestimates the incremental cost of transporting and terminating traffic through a tandem switch is approximately three times the Cox estimate of 0.2 cents ($0.002) per minute of use; (7) AirTouch asserts that the Long Run Incremental Cost (LRIC) of transporting and terminating a call through the tandem switch is 0.49 cents ($0.0049) for the first minute of a call and 0.12 cents ($0.0012) for each additional minute of use; (8) Pacific Bell asserts that the average LRIC for termination of calls under "Feature Group B," which appears to include terminations at tandem switches as well as at end offices, is 0.62 cents ($0.0062) per minute of use; (9) Maryland set a rate of 0.3 cents ($0.003) for terminations at end office switches and 0.5 cents ($0.005) for terminations at tandem switches; (10) Illinois adopted a rate of 0.5 cents ($0.005) for terminations at end office switches and 0.75 ($0.0075) for terminations at tandem switches; (11) In Massachusetts, NYNEX testified that its average marginal cost of end office switching was 0.129 cents ($0.00129) per minute of use; (12) Cox noted that Florida, based on GTE and Centel submissions, estimated the sum of the estimated TSLRIC for end office switching and the LRIC for tandem office switching and transport is 0.25 cents ($0.0025) per minute of use; (13) NYNEX's peak-period interconnection rates are 0.74 cents ($0.0074) per minute of use at end offices and 0.98 cents ($0.0098) per minute of use at tandem switches, and its off-peak rates are 0.27 cents ($0.0027) per minute of use at end offices and 0.29 cents ($0.0029) per minute of use at tandem switches; and (14) Michigan established a rate of 1.5 cents

looking cost studies in the record ranging from 0.18 cents ($0.0018) to 0.35 cents ($0.0035) per minute of use.[10] We determined that the studies in the record supported a default proxy range of 0.2 cents ($0.002) to 0.4 cents ($0.004) per minute of use.[11] Based on further analysis of those studies, we conclude that the default proxy range of 0.2 cents ($0.002) to 0.4 cents ($0.004) per minute that we established using these data is a reasonable approximation of the cost of the usage-sensitive components of the unbundled local switching element, but that none of the cost estimates on which we relied to establish the default proxy range for usage-sensitive local switching included the costs of line ports.[12] Accordingly, we now establish a default proxy ceiling for a charge to recover those costs.

6. The data support the default proxy we established for the termination portion of transport and termination, as defined in section 251(b)(5), because we found that the "additional cost" to the incumbent LEC of terminating a call that originates on another network includes only the usage-sensitive costs, including the switching matrix and the trunk ports, but not the non-traffic sensitive costs of local loops and line ports associated with the local loops. Such non-traffic-sensitive costs, by definition, do not vary in proportion to the number of calls terminating over the LEC's facilities and, thus, are not "additional costs."[13] Since all the studies we discussed in the Order included all the usage-based or "additional costs," these studies fully support our conclusion that the default proxy for traffic termination, in the context of transport and termination, should be in the 0.2 cents ($0.002) to 0.4 cents ($0.004) per minute of use range. Accordingly, as stated, we find no basis at this time for modifying the default proxy range for the termination of calls. By contrast, the unbundled local switching element, as defined in section 251(c)(3), includes not just the usage-sensitive switching matrix and trunk port costs, but the non-traffic sensitive costs of the line ports as well.[14] Thus, we now hold that the default proxy rate of 0.2 cents ($0.002) to 0.4 cents ($0.004) per minute of use should apply only to the traffic-sensitive components of the local switching element, including the switching matrix, the functionalities used to provide vertical features, and the trunk ports, but that line ports should be assessed a separate, flat-rated charge. We reject AT&T's arguments that we should not modify our existing rule.[15] AT&T argues that it is not clear that the existing proxy range fails to include costs attributable to line

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($0.015) per minute of use for calls passing directly through an end office or tandem switch.

[10] *Id.* at para. 812.

[11] *Id.* at para. 811.

[12] *Id.* at paras. 803-809.

[13] *Id.* at para. 1057.

[14] *Id.* at para. 810.

[15] Letter from Brian W. Masterson, Director - Government Affairs, AT&T Corporation to William F. Caton, Acting Secretary, FCC, Sept. 24, 1996.

ports and, even if it does fail to include such costs, LECs could recover their line port costs and the total would still be within the existing range.[16] As previously stated, our conclusion is that the studies we relied upon in setting the existing range did not include a line port increment, and thus we believe that the local unbundled switching proxy must be modified.

7. We have reviewed several examples of rates set by state commissions that had available evidence from forward-looking cost studies. The Illinois Commission set rates of $1.62 and $1.10 per line per month for basic business and residential exchange line ports, respectively, after reviewing a forward-looking cost study submitted by Ameritech.[17] The Florida Commission set interim line port rates of $2.00 for BellSouth.[18] In a subsequent proceeding, the Florida Commission adopted a rate of $6.00 per line port for GTE, but the basis of that rate is not entirely clear.[19] The Connecticut Commission set an interim rate for Southern New England Telephone ("SNET") of $1.90 per line per month, which it estimated was in excess of SNET's forward-looking economic cost.[20] The Oregon Commission set a rate of $1.20 per line port.[21]

8. Based on this record we adopt an interim default price range of $1.10 to $2.00 per line port per month for ports used in the delivery of basic residential and business exchange services. Our default price range is derived from existing state commission decisions based, at least in part, on forward-looking costs. With the exception of the Florida Commission's rates for GTE, state commissions with forward-looking cost data available have set line port rates that range from $1.10 for residential line ports in Illinois to $2.00 per line port in

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[16] *Id.*

[17] Ameritech Tariff, Ill. C.C. No. 20, Part 19, Section 1, issued October 23, 1995.

[18] *See In Re* Resolution of Petition(s) to Establish non-Discriminatory rates, terms, and Conditions for Resale Involving Local Exchange Companies and Alternative Exchange Companies Pursuant to Section 364.161 Florida Statutes (March 29, 1996) at 12.

[19] *In Re Resolution of petition(s) to establish nondiscriminatory rates, terms and conditions for resale involving local exchange companies and alternative local exchange companies and alternative local exchanges companies pursuant to Section 364.161, Florida Statutes*, Docket No. 950981-TP, Order No. PSC-96-0811-FOF-TP (Florida Commission, June 24, 1996). In that order, the Florida commission also set an interim rate of $7.00 per line port for United/Centel. The Florida commission in that proceeding required United/Centel to refile cost studies for all elements, and the basis for the $7.00 rate is even less clear than for GTE.

[20] *In Re* Southern New England Telephone Company, Order No. 95-06-17, 1995 WL 80387 (Conn. D.P.U.C., December 20, 1995) at 70-72.

[21] *See In Re Investigation into the Cost of Providing* Telecommunications Services, Order No. 96-188, (Oregon Commission, July 19, 1996) (price based on long-run incremental cost plus a contribution to joint and common costs) at 78 n.61, Appendix C p. 2.

Florida for BellSouth.[22] We thus set the proxy range between $1.10 and $2.00 per line port, consistent with these state commission decisions. We decline to rely on the Florida commission's decision regarding GTE. We note that that price is more than three times as large as any of the other rates set by state commissions with forward-looking cost studies available. In addition, the basis for that rate is not entirely clear. For example, it appears that the rate included marketing costs, some of which may be retail costs. The inclusion of retail costs would not be consistent with the pricing methodology we adopted in the *First Report and Order*. Under these circumstances, where we are establishing a pricing proxy that is intended for nationwide use by states that are unable to conduct an economic cost study within the time required for arbitrations, we conclude that we should not take this rate into account in setting the interim default proxy range for line ports.

9. We emphasize that we are adopting this proxy range for use only in the event a state commission is unable to set a price pursuant to the forward-looking methodology we outlined in the *First Report and Order* within the statutory arbitration period. States setting prices based on this proxy price range are required to replace those prices when they have approved an economic cost study complying with our rules or when the Commission adopts new proxies. Additionally, we find that states with existing rates for line ports that fall within our default price range need not readopt those rates pending the completion of a forward-looking cost study that complies with the methodology outlined in the *First Report and Order*.

III. Unbundled Local Switching Element

10. Several parties have raised a question as to whether interexchange carriers (IXCs) or competitive access providers (CAPs) may purchase access to an incumbent LEC's unbundled switch in order to originate or terminate interexchange traffic to customers for whom they do not provide local exchange service.[23] Based on these inquiries, it appears that

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[22] We also note that the range we adopt is consistent with the cost estimates derived by the Hatfield Model Version 2, Release 1 and the Cost Proxy Model. *See Hatfield Model, Version 2.2, Release 1*, (Hatfield Associates, Inc., March 1996), submitted by AT&T and MCI on May 30, 1996 (*Hatfield 2.2*); *see also* AT&T reply at Appendix D (Update of the Hatfield Model Version 2.2, Release 1). *See* Letter from Whitney Hatch, Assistant Vice President Regulatory Affairs, GTE, to William F. Caton, Acting Secretary, FCC, July 11, 1996 at Attachment 2 (Economic Evaluation of Version 2.2 of the Hatfield Model), at 16-17 (GTE reports that the Cost Proxy Model estimates that the forward-looking cost of line ports is $1.77 in California).

[23] Letter from Todd F. Silbergeld, Director - Federal Regulatory, SBC Communications, Inc. to William F. Caton, Acting Secretary, FCC, Sept. 19, 1996 (SBC Sept. 19, 1996 *ex parte*); Letter from Genevieve Morelli, Vice President & General Counsel, Competitive Telecommunications Association (CompTel) to William F. Caton, Acting Secretary, FCC, Sept. 23, 1996 (CompTel Sept. 23, 1996 *ex parte*); Letter from Mary L. Brown, Director-Corporate Rates and Federal Regulatory Analysis, MCI Telecommunications Corporation to William F. Caton, Acting Secretary, FCC, Sept. 24, 1996 (MCI Sept. 24, 1996 *ex parte*); Letter from W. Scott Randolph, Director- Regulatory Affairs, GTE Service Corporation to William F. Caton, Acting Secretary, FCC, Sept. 24, 1996 (GTE Sept. 24, 1996 *ex parte*).

some parties believe that the *First Report and Order* could be interpreted to permit carriers to use unbundled switching elements, rather than standard access arrangements, to originate and terminate interexchange traffic to end users.[24] Parties have noted that the *First Report and Order* does not specifically prohibit this, and that, if a carrier is entitled to purchase an unbundled switching element, the *First Report and Order* does not impose restrictions on the use of that element. In light of these inquiries, it appears that our resolution of this issue in the *First Report and Order* may not have been sufficiently explicit. In this Order, we seek to remove any ambiguity that may exist with respect to this issue.

11. In section V.J.2. of the *First Report and Order*, we stated that "when a requesting carrier purchases the unbundled local switching element, it obtains *all* switching features in a single element *on a per-line basis*."[25] The unbundled switching element, as defined in the *First Report and Order*, includes the line card, which is often dedicated to a particular customer.[26] Thus, a carrier that purchases the unbundled local switching element to serve an end user effectively obtains the exclusive right to provide all features, functions, and capabilities of the switch, including switching for exchange access and local exchange service, for that end user.[27] A practical consequence of this determination is that the carrier that purchases the local switching element is likely to provide all available services requested by the customer served by that switching element, including switching for local exchange and exchange access.[28] We further note that the pricing methodology set forth in the *First Report and Order* for the unbundled switching element included costs of components (*e.g.*, line ports) necessary to provide switching for both local exchange and exchange access services,[29] and contemplated that the carrier purchasing the unbundled switch would provide switching for both local exchange and exchange access services.

12. Although we concluded in the *First Report and Order* that requesting telecommunications carriers are permitted under the 1996 Act to purchase unbundled elements for the purpose of providing exchange access,[30] a carrier must, at least with respect to unbundled loops, provide to an end user all of the services that the end user requests. The *First Report and Order* concluded that carriers, "as a practical matter, will have to provide

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[24] *See, e.g.*, CompTel Sept. 23, 1996 *ex parte*; MCI Sept. 24, 1996 *ex parte*; GTE Sept. 24, 1996 *ex parte*.

[25] *First Report and Order* at para. 412 (emphasis added).

[26] *Id*; see also *id.* at para. 810.

[27] *See, e.g.*, *id.* at para. 423.

[28] We reached a similar conclusion with respect to unbundled local loops. *Id.* at para. 357.

[29] *See id.* at para. 810. Although, as noted above, line port costs were not included in the switching proxy, we have concluded that such costs must be included in the price for the unbundled switching element.

[30] *Id.* at para. 356.

whatever services are requested by the customers to whom those loops are dedicated."[31] Similarly, the *First Report and Order* defined the local switching element in a manner that includes dedicated facilities, thereby effectively precluding the requesting carrier from using unbundled switching to substitute for switched access services where the loop is used to provide both exchange access to the requesting carrier and local exchange service by the incumbent LEC.

13. We thus make clear that, as a practical matter, a carrier that purchases an unbundled switching element will not be able to provide solely interexchange service or solely access service to an interexchange carrier. A requesting carrier that purchases an unbundled local switching element for an end user may not use that switching element to provide interexchange service to end users for whom that requesting carrier does not also provide local exchange service. Using unbundled switching elements in such a manner would be inconsistent with our statement in the *First Report and Order* that "a competing provider orders the unbundled basic switching element *for a particular customer line* . . . ."[32]

IV. Miscellaneous

14. We also modify Rule 51.707(b)(2) of our rules to correct a typographical error,[33] by changing "51.513(d)(3),(4), and (5)" to "51.513(c)(3),(4), and (5)."

V. Final Regulatory Flexibility Analysis

15. In the *First Report and Order* we conducted a Final Regulatory Flexibility Analysis, as required by Section 603 of the Regulatory Flexibility Act, as amended by the Contract With America Advancement Act of 1996, Pub. L. No. 104-121, 110 Stat. 847 (1996).[34] The changes we adopt in this order do not affect our analysis of regulatory flexibility in the *First Report and Order*.

VI. Ordering Clauses

16. Accordingly, IT IS ORDERED that pursuant to authority contained in §§ 251 and 252 of the Communications Act of 1934, as amended, 47 U.S.C. §§ 251, 252, and pursuant to § 1.108 of the Commission's rules, 47 C.F.R. § 1.108, the Commission reconsiders its decision in the *First Report and Order* on its own motion to the extent specified herein.

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[31] *Id.* at para. 357.

[32] *Id.* at para. 414 (emphasis added).

[33] 47 C.F.R. § 51.707(b)(2).

[34] *First Report and Order* at paras. 1324-1441.

17. IT IS FURTHER ORDERED that the policies and rules adopted here shall be effective upon publication of a summary in the Federal Register.

Federal Communications Commission

William F. Caton

William F. Caton
Acting Secretary

Appendix--Amendment to Final Rules

PART 51--INTERCONNECTION

1. The authority citation for part 51 continues to read as follows:

Authority: Sections 1-5, 7, 201-05, 218, 225-27, 251-54, 271, 48 Stat. 1070, as amended, 1077; 47 U.S.C. 151-55, 157, 201-05, 218, 225-27, 251-54, 271, unless otherwise noted.

2. Paragraph (c)(2) of Section 51.513 is revised to read as follows:

§ 51.513 Proxies for forward-looking economic cost.

* * * * *

(c) *Proxies for specific elements.*

* * * * *

(2) *Local switching.*

(A) The blended proxy-based rate for the usage-sensitive component of the unbundled local switching element, including the switching matrix, the functionalities used to provide vertical features, and the trunk ports, shall be no greater than 0.4 cents ($0.004) per minute, and no less than 0.2 cents ($0.002) per minute, except that, where a state commission has, before August 8, 1996, established a rate less than or equal to 0.5 cents ($0.005) per minute, that rate may be retained pending completion of a forward-looking economic cost study. If a flat-rated charge is established for these components, it shall be converted to a per-minute rate by dividing the projected average minutes of use per flat-rated subelement, for purposes of assessing compliance with this proxy. A weighted average of such flat-rate or usage-sensitive charges shall be used in appropriate circumstances, such as when peak and off-peak charges are used.

(B) The blended proxy-based rate for the line port component of the local switching element shall be no less than $1.10, and no more than $2.00, per line port per month for ports used in the delivery of basic residential and business exchange services.

3. Paragraph (b)(2) of Section 51.707 is revised to read as follows:

§ 51.707

* * * * *

(b) * * *

* * * * *

(2) *Transport*. The incumbent LEC's rates for the transport of local telecommunications traffic, under this section, shall comply with the proxies described in Section 51.513(c)(3), (4), and (5) of this part that apply to the analogous unbundled network elements used in transporting a call to the end office that serves the called party.