

ILECs' revenues from regulated services, and virtually exempt ILECs from contributing to federal universal service support mechanisms.<sup>52</sup>

While the 1996 Act specifies that telecommunications carriers providing interstate services are required to contribute to the interstate fund, and telecommunications carriers that provide intrastate services are required to contribute to the appropriate intrastate fund(s), if any,<sup>53</sup> the Act does not, as some commenters imply,<sup>54</sup> speak to the *base* of revenues that federal or state regulators should use to determine interstate and intrastate carriers' contributions.

As GTE has noted, Congress did not define the measure of revenues on which universal service contributions should be assessed. The statute implicitly permits the Commission to choose either revenue base.<sup>55</sup> Indeed, Section 2 of the Communications Act does not preclude the FCC from basing universal service contributions on carriers' combined interstate and intrastate telecommunications revenues.<sup>56</sup> Allocating interstate universal service funding responsibilities based on interstate and intrastate revenues is merely a methodology for setting an interstate fee. It is not a foray into intrastate rate setting.

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<sup>52</sup> ILECs' revenues from interstate access charges were roughly a third the size of their intrastate revenues. See *supra*, note 22.

<sup>53</sup> Section 254(d) of the Act specifies that "every telecommunications carrier that provides interstate telecommunications services shall contribute, on an equitable and nondiscriminatory basis, to the specific, predictable, and sufficient mechanisms established by the Commission to preserve and advance universal service." In a parallel fashion, Section 254(f) permits a state to adopt regulations, "not inconsistent with" the federal rules, to preserve and advance universal service, and provides that "[e]very telecommunications carrier that provide intrastate telecommunications services shall contribute, on an equitable and nondiscriminatory basis, in a manner determined by the State to the preservation and advancement of universal service in that State."

<sup>54</sup> See, e.g., Bell Atlantic Comments, at 5.

<sup>55</sup> See GTE Comments, at 65.

<sup>56</sup> See 47 U.S.C. § 152.

Moreover, as a general proposition, the broader the funding base, the more competitively neutral the funding will be.<sup>57</sup> Assessing carriers' contributions based on combined inter- and intrastate revenues would, of course, create a larger funding base than basing assessments on only interstate revenues. This wider funding base should help to mitigate any potential effects of universal service support on competition in various telecommunications service markets by spreading the burden of universal service more among a broader class of carriers and in a uniform manner, regardless of jurisdiction. If intrastate revenues are reserved to support programs designed and administered by each state, a patchwork of fifty different universal support programs, each with different competitive side effects, could result -- notwithstanding Section 254(f)'s implicit requirement that state programs be "not inconsistent with" the federal program.<sup>58</sup>

Time Warner has stated that "it is simply illogical to extend federal funding to intrastate service at a level that will far exceed that which historically has been funded, while restricting the assessment of such support to the much smaller base of interstate-only revenues."<sup>59</sup> USTA similarly notes that "the benefits of universal service funding will flow to the intrastate jurisdiction."<sup>60</sup> USTA also argues correctly that a larger funding base will result in a lower surcharge needed to recover the contribution.<sup>61</sup>

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<sup>57</sup> C.f. GTE Service Corporation Comments, filed December 19, 1996, at 67.

<sup>58</sup> See *supra*, note 54..

<sup>59</sup> Time Warner Comments, filed December 19, 1996, at 9-10.

<sup>60</sup> USTA Comments, at 17.

<sup>61</sup> *Id.* For example, assume a universal service funding obligation of \$1 billion, on combined intrastate and interstate telecommunications revenues of \$100 billion, of which interstate revenues are \$25 billion. In this example, if combined intrastate and interstate revenues are used as the

For all of the foregoing reasons, Ad Hoc submits that combined intrastate and interstate revenues constitute the appropriate revenue base for funding all universal service obligations, including not only funding for schools and libraries (as explicitly recommended by the Joint Board<sup>62</sup>), but also funding for high-cost areas and low-income consumers.

**III. ONLY ENTITIES PROVIDING COMMON CARRIER SERVICES SHOULD BE REQUIRED TO CONTRIBUTE TO THE UNIVERSAL SERVICE FUND.**

In its Comments, Ad Hoc noted certain ambiguities in the Joint Board's discussion of the entities that must contribute to the Universal Service Fund, and requested that the Commission clarify that the universal service contribution obligation does not apply to private carriers and parties to sharing arrangements. Several commenters have expressed support for a contribution obligation that is spread across a broad pool of carriers.<sup>63</sup> Ad Hoc found no comments, however, that advocated extending universal service contribution requirements to private carriers or parties participating in sharing arrangements. Notwithstanding the apparent consensus on this issue, Ad Hoc reiterates its request that the Commission clearly indicate that the contribution obligations will apply only to those entities that provide common carrier services.

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revenue base, a burden rate of 1% would be sufficient to allocate the obligation among all carriers, since 1% of \$100 billion is \$1 billion. If, however, only interstate revenues are used as the revenue base, a burden rate of 4% would be required to collect the same \$1 billion universal service funding requirement, since 4% of \$25 billion is \$1 billion.

<sup>62</sup> Recommended Decision at ¶ 817.

<sup>63</sup> See, e.g., Georgia Department of Administrative Services Comments, filed December 19, 1996, at 2.

IV. NO REDUCTION IN THE SLC SHOULD BE MADE UNLESS AND UNTIL ALL OTHER NON-ECONOMICALLY EFFICIENT SOURCES OF COST RECOVERY HAVE BEEN ELIMINATED.

As discussed at length in the Ad Hoc's December 19, 1996 Comments, the Joint Board's tentative proposal to reduce the Subscriber Line Charge (SLC) in the event carrier contributions to the universal service fund are based on both intra- and interstate revenues<sup>64</sup> is contrary to the fundamental economic principles of cost causation and to the Joint Board's own findings and recommendations concerning the Carrier Common Line Charge (CCLC).<sup>65</sup> Consistent with Ad Hoc's analysis, there is widespread agreement among commenters that it would be economically inefficient to reduce the SLC.<sup>66</sup>

Notwithstanding the overwhelming economic justification for at least retaining (and probably increasing) the SLC under the new competitive paradigm the 1996 Act has set in motion, the National Association of State Utility Consumer Advocates ("NASUCA") supports the Joint Board's ill-conceived recommendation to reduce the SLC. NASUCA argues that the SLC should be reduced regardless of whether the revenue base for universal service funding is comprised of both intra- and interstate revenues or interstate only revenues.<sup>67</sup>

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<sup>64</sup> Recommended Decision, at ¶ 772.

<sup>65</sup> Ad Hoc Comments, at 22-26.

<sup>66</sup> See, e.g., AT&T Comments, at 13; MCI Comments, at 14-15; Sprint Comments, at 16; USTA Comments, at 20; Bell Atlantic Comments, at 22; SBC Comments, at 35; BellSouth Comments, at 4, note 9.

<sup>67</sup> NASUCA Comments, filed December 19, 1996, at 2-3.

NASUCA apparently believes that the SLC forces basic exchange customers to bear an unreasonable share of interstate common loop costs.<sup>68</sup> NASUCA argues that “Section 254(k) stipulates that the services included in the definition of universal service ‘should bear no more than a reasonable share of joint and common costs.’”<sup>69</sup> Because NASUCA includes the SLC within the category of universal service, it asserts that Section 254(k) encompasses the SLC and requires that it be reduced.

According to NASUCA, a “fair share” of loop costs recoverable through the SLC would be a maximum of 50%, whereas the SLC currently recovers more than 66% of interstate common line costs.<sup>70</sup> On this basis, NASUCA argues that it is “a matter of law” that the Commission must reduce the SLC, and NASUCA further recommends that the Commission reduce the SLC “to a level that would limit recovery of interstate common line costs to 50%.”<sup>71</sup>

Ad Hoc strongly disagrees with NASUCA. As Ad Hoc and others have discussed in earlier comments, and as the Joint Board has recognized, it is economically efficient to recover fixed costs (such as loop costs) on a flat-rate basis from the end user (as occurs with the SLC). Conversely, it is economically inefficient to recover fixed loop costs on a usage-sensitive basis (as occurs with the CCLC). Furthermore, the entirety of loop costs is appropriately viewed as a direct cost of end user basic local exchange service, and accordingly, the correct allocation of loop costs to the end user is 100% -- not 50% as argued by NASUCA,

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<sup>68</sup> *Id.* at 3.

<sup>69</sup> *Id.* at 5.

<sup>70</sup> *Id.* at 6-7.

<sup>71</sup> *Id.* at 7.

nor the 66% currently allocated to the SLC. Categorizing loop costs as a direct cost of basic local exchange service, and thus allocating all of the loop cost to basic service, is consistent with economic principles of cost causation, since a change in demand for basic service actually causes a change in the cost of the underlying loop facilities.<sup>72</sup> This is not true of other services (*i.e.*, usage) provided over loop facilities. Reduced demand for usage rated service will not lower the cost of the underlying loop facilities.

In support of its position that the Commission treat the SLC as a charge paid by a customer to receive universal service, NASUCA explains:

The magnitude of the SLC cannot be reduced by any action taken by the customer who is trying to economize. The SLC could not be avoided by an end user who did not make a single telephone call, but maintained a telephone only for receiving calls or for use in emergencies. The SLC is incurred automatically by virtue of having a telephone in a home or business. It is part and parcel of a telephone service customer's bill for universal service.<sup>73</sup>

Ironically, the very attributes NASUCA describes above are precisely the ones that make the SLC an economically efficient and equitable charge for the recovery of non-traffic sensitive loop costs accrued when a customer subscribes to basic local exchange service.

NASUCA argues that an increase in the SLC is tantamount to a rate increase for end users, and that such an increase could be considered "rate rebalancing," as it would be intertwined with proposals to restructure access

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<sup>72</sup> See New Jersey Board of Public Utilities, Local Exchange Competition for Telecommunications Services, Docket No. TX95120631, Testimony of Patricia D. Kravtin (Exh. NJCTA 1) at 17; Testimony of Brian Staihr (Exh. Sprint 2) at 3-4; Testimony of William Taylor (Exh. Bell Atlantic 16) at 24-25; Tr. 9/9/96 at 97; Tr. 9/11/96 at 88-107; Tr. 9/12/96 at 118-126.

<sup>73</sup> NASUCA Comments, at 3.

charges. NASUCA contends that either increasing and rebalancing rates would exceed the scope of this proceeding.<sup>74</sup> NASUCA reasons that to the extent such rate increases and rate rebalancing would render telephone service less affordable and cause subscribership to decline, increases in the SLC would be contrary to the 1996 Act's mandate for universal service.<sup>75</sup>

NASUCA is again off the mark in its reasoning and its fervor to decrease the SLC. It is the bottom line on the customer's bill that will most directly affect the affordability of telecommunications services. Whether the bottom line is increased by an increase in the SLC or by imposition of an equivalent flat-rate CCLC, the result to the consumer is the same. Similarly, lower rates for long distance services (resulting from the economically rational elimination of the CCLC) could be expected to offset higher local rates that might result from an increase in the SLC. As correctly stated by Commissioner Chong:

Any policy that, in essence, shifts or perpetuates the recovery of these [non-traffic sensitive] costs from interstate providers can, at best, be described as an inefficient "shell game" on consumers. It is a shell game because in the competitive interstate telecommunications market, service providers will have to pass these costs along to consumers in the form of either flat rated charges or higher rates on long distance bills. Any potential savings that consumers would receive from a SLC reduction on their local phone bills may well be offset by an increase to their long distance bills.<sup>76</sup>

The critical issue in this context -- which Congress made clear in Section 254 -- is whether the charges to recover loop costs should be hidden (as in the case of a flat-rated CCLC or other offsetting increases in long distance rates) or evident to the end user (as in the case of the SLC). Both economic efficiency and equity

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<sup>74</sup> *Id.* at 2.

<sup>75</sup> *Id.*

<sup>76</sup> Statement of Commissioner Chong, at 12.

considerations strongly support the latter. Consumers should know what it costs them to support universal service.

Moreover, as discussed in Ad Hoc's earlier comments, evidence suggests that the vast majority of subscribers would find telephone service affordable even if the SLC is increased.<sup>77</sup> The implementation of economically inefficient reductions to the SLC would be a very poor substitute for a properly targeted universal service funding mechanism. To the extent some subscribers need more support to afford basic telephone service, they should get it. Lowering the SLC, however, would not further Congress's universal service goals, but would only exacerbate the economic efficiency inherent in the current artificially low SLC.

A reduction in the SLC would be rational *only* after an overall reduction in interstate revenue requirements permitted full elimination of the non-economically justified CCLC and above-cost pricing of other access charge elements.<sup>78</sup> MCI's analysis, which indicates common line charges to be roughly \$5-billion above economic cost, suggests this very possibility.<sup>79</sup> Ad Hoc disagrees, however, with MCI's proposal to spread any overall reduction in common line cost (resulting from the Commission's anticipated reliance on economic costs) proportionately between the CCLC and the SLC for the reasons discussed above.<sup>80</sup> Before it even

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<sup>77</sup> Ad Hoc Comments, at 26-28.

<sup>78</sup> This could occur if, as contemplated in the access charge reform proceeding, the cost of regulated telephone services are brought down to forward-looking economic cost levels. See *In the Matter of Access Charge Reform*, CC Docket No. 96-262, FCC 96-488 (released December 24, 1996).

<sup>79</sup> See MCI Comments, at 15-16.

<sup>80</sup> See *id.* at 16.

considers reducing the SLC, the Commission should first focus on eliminating all other non-economically efficient sources of loop cost recovery.

#### V. SUPPORT FOR SCHOOLS AND LIBRARIES.

Ad Hoc has traditionally supported public policy decisions based on sound public finance principles. Several commenters raised valid concerns about whether the Joint Board's response to Section 254(h)(1)(B)'s mandate (requiring discounted telecommunications service rates for schools and libraries) is rational and supported by such principles.<sup>81</sup> In light of these concerns, Ad Hoc recommends that the Commission closely examine these and other issues, including the appropriate size and allocation of the fund, the estimated cost of the program, and the allocation of future support once the cap has been exceeded.

In addition, Ad Hoc proposes that the Commission re-evaluate the program every five years to determine whether the system is meeting the Commission's desired goal of guaranteeing "affordable access to and use of such [advanced telecommunications] services."<sup>82</sup> Periodic review will give the Commission the opportunity to determine, for example, whether the cap should be augmented or reduced, whether discount tiers should be readjusted, or whether technology changes warrant a revised definition of supported services. With the advent of local competition and access reform, changes in the telecommunications services and equipment markets may be fast and furious.

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<sup>81</sup> See, e.g., AT&T Comments, at 21; NYNEX Comments, at 37-39; USTA Comments, at 36; People of the State of California and the Public Utilities Commission of the State of California Comments, filed December 18, 1996, at 17.

The universal service support system must adapt to these changes if it is to provide a maximum benefit to those needing such support.

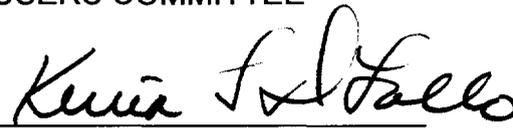
**CONCLUSION**

For the foregoing reasons, the Ad Hoc Telecommunications Users Committee respectfully requests that the Commission take actions in this docket that are consistent with the recommendations discussed above and in Ad Hoc's initial Comments.

Respectfully submitted,

AD HOC TELECOMMUNICATIONS  
USERS COMMITTEE

By:



Economic Consultants:

Patricia Kravtin  
Economics and Technology, Inc.  
One Washington Mall  
Boston, MA 02108-2617  
617-227-0900

James S. Blaszak  
Kevin S. DiLallo  
Janine F. Goodman  
Levine, Blaszak, Block & Boothby  
1300 Connecticut Avenue, N.W.  
Suite 500  
Washington, D.C. 20036-1703  
202-223-4980

January 10, 1997

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## Certificate of Service

I, Andrew Baer, hereby certify that true and correct copies of the preceding Comments of the Ad Hoc Telecommunications Users Committee in the Matter of Federal-State Joint Board on Universal Service, CC Docket No. 96-45, were served this 10th day of January, 1997 upon the following:



Andrew Baer

January 10, 1997

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The Honorable Reed E. Hundt  
Chairman  
Federal Communications Commission  
1919 M Street, NW  
Room 814  
Washington, DC 20554

The Honorable Rachelle B. Chong  
Commissioner  
Federal Communications Commission  
1919 M Street NW, Room 844  
Washington, DC 20554

The Honorable Susan Ness, Commissioner  
Federal Communications Commission  
1919 M Street, NW, Room 832  
Washington, DC 20554

The Honorable Julia Johnson, Commissioner  
Florida Public Service Commission  
2540 Shumard Oak Blvd.  
Gerald Gunter Building  
Tallahassee, FL 32399-0850

The Honorable Kenneth McClure, Commissioner  
Missouri Public Service Commission  
301 W. High Street, Suite 530  
Jefferson City, MO 65101

The Honorable Sharon L. Nelson, Chairman  
Washington Utilities and Transportation  
Commission  
PO Box 47250  
Olympia, WA 98504-7250

The Honorable Laska Schoenfelder  
Commissioner  
South Dakota Public Utilities Commission  
State Capitol, 500 E. Capitol Street  
Pierre, SD 57501-5070

Martha S. Hogerty  
Public Counsel for the State of Missouri  
PO Box 7800  
Jefferson City, MO 65102

Paul E. Pederson, State Staff Chair  
Missouri Public Service Commission  
PO Box 360  
Jefferson City, MO 65102

Lisa Boehley  
Federal Communications Commission  
2100 M Street, NW, Room 8605  
Washington, DC 20554

Charles Bolle  
South Dakota Public Utilities Commission  
State Capitol, 500 E. Capitol Street  
Pierre, SD 57501-5070

Deonne Bruning  
Nebraska Public Service Commission  
300 The Atrium  
1200 N. Street, PO Box 94927  
Lincoln, NE 68509-4927

James Casserly  
Federal Communications Commission  
Office of Commissioner Ness  
1919 M Street, NW, Room 832  
Washington, DC 20554

John Clark  
Federal Communications Commission  
2100 M Street, NW, Room 8619  
Washington, DC 20554

Bryan Clopton  
Federal Communications Commission  
2100 M Street, NW, Room 8615  
Washington, DC 20554

Irene Flannery  
Federal Communications Commission  
2100 M Street, NW, Room 8922  
Washington, DC 20554

Daniel Gonzalez  
Federal Communications Commission  
Office of Commissioner Chong  
1919 M Street, NW, Room 844  
Washington, DC 20554

Emily Hoffnar  
Federal Communications Commission  
2100 M Street, NW, Room 8623  
Washington, DC 20554

L. Charles Keller  
Federal Communications Commission  
2100 M Street, NW, Room 8918  
Washington, DC 20554

Lori Kenyon  
Alaska Public Utilities Commission  
1016 West Sixth Avenue, Suite 400  
Anchorage, AK 99501

David Krech  
Federal Communications Commission  
2025 M Street, NW, Room 7130  
Washington, DC 20554

Debra M. Kriete  
Pennsylvania Public Utilities Commission  
PO Box 3265  
Harrisburg, PA 17105-3265

Diane Law  
Federal Communications Commission  
2100 M Street, NW, Room 8920  
Washington, DC 20554

Mark Long  
Florida Public Service Commission  
2540 Shumard Oak Blvd.  
Gerald Gunter Building  
Tallahassee, FL 32399

Robert Loube  
Federal Communications Commission  
2100 M Street, NW, Room 8914  
Washington, DC 20554

Samuel Loudenslager  
Arkansas Public Service Commission  
PO Box 400  
Little Rock, AR 72203-0400

Sandra Makeef  
Iowa Utilities Board  
Lucas State Office Building  
Des Moines, IA 50319

Philip F. McClelland  
Pennsylvania Office of Consumer Advocate  
1425 Strawberry Square  
Harrisburg, PA 17120

Michael A. McRae  
DC Office of the People's Counsel  
1133 15<sup>th</sup> Street, NW, Suite 500  
Washington, DC 20005

Tejal Mehta  
Federal Communications Commission  
2100 M Street, NW, Room 8625  
Washington, DC 20554

Terry Monroe  
NY Public Service Commission  
3 Empire Plaza  
Albany, NY 12223

John Morabito  
Deputy Division Chief  
Accounting and Audits  
Federal Communications Commission  
2000 L Street, NW, Suite 812  
Washington, DC 20554

Mark Nadel  
Federal Communications Commission  
2100 M Street, NW, Room 8916  
Washington, DC 20554

John Nakahata  
Federal Communications Commission  
Office of the Chairman  
1919 M Street, NW, Room 814  
Washington, DC 20554

Lee Palagyi  
Washington Utilities and Transportation  
Commission  
1300 South Evergreen Park Drive, SW  
Olympia, WA 98504

Kimberly Parker  
Federal Communications Commission  
2100 M Street, NW, Room 8609  
Washington, DC 20554

Barry Payne  
Indiana Office of the Consumer Counsel  
100 North Senate Avenue, Room N501  
Indianapolis, IN 46204-2208

Jeanine Poltronieri  
Federal Communications Commission  
2100 M Street, NW, Room 8924  
Washington, DC 20554

James Bradford Ramsay  
National Association of Regulatory Utility  
Commissioners  
PO Box 684  
Washington, DC 20044-0684

Brian Roberts  
California Public Utilities Commission  
505 Van Ness Avenue  
San Francisco, CA 94102

Gary Seigel  
Federal Communications Commission  
2000 L Street, NW, Suite 812  
Washington, DC 20554

Richard Smith  
Federal Communications Commission  
2100 M Street, NW, Room 8605  
Washington, DC 20554

Pamela Szymczak  
Federal Communications Commission  
2100 M Street, NW, Room 8912  
Washington, DC 20554

Lori Wright  
Federal Communications Commission  
2100 M Street, NW, Room 8603  
Washington, DC 20554

Ms. Sheryl Todd\*  
Common Carrier Bureau  
Room 8611  
2100 M Street, N.W.  
Washington, D.C. 20554

International Transcription Service  
Room 140  
2100 M Street, N.W.  
Washington, D.C. 20037