MCI Communications Corporation
1801 Pennsylvania Avenue, NW
Washington, DC 20006
202 887 2375

Kimberly M. Kirby
Senior Manager
FCC Affairs

EX PARTE OR LATE FILED

ORIGINAL

RECEIVED

MAY 5 1997

May 5, 1997

Mr. William F. Caton, Acting Secretary
Federal Communications Commission
1919 M Street, NW Room 222
Washington, DC 20554

Re: Ex Parte Presentation in CC Docket No. 96-262 and CC Docket No. 96-45

Dear Mr. Caton:

Please file the attached document, transmitted via e-mail (electronic mail) from Mary Brown to Dan Gonzalez on May 4, 1997, as part of the record in this proceeding. This information was requested by the Office of Commissioner Chong and will therefore not count against MCI's page limit in this proceeding.

Two copies of this Notice are being submitted to the Secretary of the FCC in accordance with Section 1.1206(a)(1) of the Commission's rules the next business day.

Sincerely,

Kimberly M. Kirby

Kimberly M. Kirby

Attachment

cc: Regina Keeney
Tom Boasberg
John Nakahata
Jim Coltharp
Jim Casserly
Dan Gonzalez
Kathy Franco
Larry Atlas

No. of Copies rec'd 0+3
List ABCDE

Draft MCI Mail
Subject: MCI Ex Parte -- Access Charges/Chong

To: dan gonzalez|EMS: Internet|MBX: dgonzalez@fcc.gov
cc: james casserly|EMS: Internet|MBX: jcasserly@fcc.gov
cc: regina keeney|EMS: Internet|MBX: rkeeney@fcc.gov
cc: james coltharp|EMS: Internet|MBX: jcoltharp@fcc.gov
cc: tom boasberg|EMS: Internet|tboasberg@fcc.gov
cc: john nakahata|EMS: Internet|jnakahata@fcc.gov
cc: larry atlas|EMS: Internet|MBX: latlas@fcc.gov
Subject: MCI Ex Parte -- Access Charges/Chong

Dan Gonzalez
Legal Advisor
Office of Commissioner Chong
Federal Communications Commission
1919 M St. NW
Washington, D.C. 20554

Re: EX PARTE in CC Docket No. 96-262 and CC Docket No. 94-1

Dear Dan:

Pursuant to your request, MCI is reiterating its views on the policy reasons supporting a downward adjustment in price cap index levels, as well as the legal authority for making such an adjustment.

MCI has been assiduously working for the past two years to convince the Commission that its 1995 interim price cap decision produced rates that were too high relative to trends in incumbent local exchange carrier (ILEC) productivity, as well as failing to move access charges toward levels that would be reflected in a competitive market. The passage of the Telecommunications Act of 1996 caused the Commission to set aside its active consideration of this long-pending docket, and to schedule its price cap review to coincide with its May 1997 review of access and universal service reform. This decision, while a matter of Commission discretion by law, has caused long distance carriers to overpay access charges by potentially billions of dollars. The long distance industry, and long distance ratepayers, should not be disadvantaged by Commission's decision to defer action on the price cap review docket.

Many parties in the access reform proceeding -- consumer groups, business users, the Department of Justice, the National Telecommunications and Information Administration, and other long distance companies -- agree that today's access rates far exceed the level that would be found if true competition existed in the local exchange and exchange access market. As you know, MCI has advocated that price cap ILECs be subject to a price cap productivity offset of 10 percent, and a coalition of consumers, business users, and long distance companies have recommended an offset of 9 percent.

MCI believes that, as part of access reform, the Commission should finalize its review of the price cap productivity offset by substantially increasing the offset. We further believe that the Commission should make a one-time, prospective adjustment to the price cap indices to reflect that the interim price cap productivity offsets were too low since 1995.

As part of our examination of this issue, MCI has also been asked to discuss the legal authority for requiring a one-time, prospective downward adjustment in the price cap indexes to reflect the differential between the interim productivity factors and a larger price cap productivity factor that the Commission might adopt as part of access reform.

The Commission's Interim Price Cap Order was upheld by the D.C. Circuit against a plethora of legal challenges. Bell Atlantic Telephone Companies v. FCC, 79 F.3d 1195 (D.C. Cir. 1996). In particular, the appellate court rejected attacks on the Commission's decision to continue to set the productivity factor only on an interim basis until better productivity data were developed. Id. at 1203. None of the petitioners argued that the Commission lacked legal authority under the Communications Act to take this approach, and they should not be heard now to complain that the Commission proposes to do exactly what it said it would do.

A decision in 1997 to adjust access rates for the two years in which the productivity factor has been too low is not a refund, but a one-time downward adjustment to the price cap to ensure that the price cap ILECs are facing the correct set of price incentives prospectively. This is no different than the Commission's 1995 decision to make a one-time prospective price cap index adjustment to account for its 1995 finding that the productivity factor selected in the initial price cap decision in 1990 was erroneously low. In both cases, the purpose of the adjustment is to ensure that price cap ILECs face the correct incentives for productivity growth.

It is not surprising that no price cap ILEC challenged the Commission's authority to prescribe an interim productivity factor subject to a later upward or downward adjustment because its authority to do so is settled. Section 4(i) confers authority for the Commission to order refunds if interim rates turn out to be too high, or higher rates if interim rates turn out to be too low. Virgin Islands Tel. Corp. v. FCC, 989 F.2d 1231, 1233-34 (D.C. Cir. 1993); Lincoln Tel. & Tel. Co. v. FCC, 659 F.2d 1092, 1107-08 & n.76 (D.C. Cir. 1981) (section 4(i) gives Commission authority to establish interim arrangement "subject to later adjustment") (citing United States v. Southwestern Cable Co., 392 U.S. 157 (1968), and Trans Alaska Pipeline Rate Cases, 436 U.S. 631, 654-655, (1978) (approving ICC's establishment of interim rate refund mechanism notwithstanding absence of express statutory authority)). Section 4(i) applies in the price cap context as well as in a ratemaking context.

The rule against retroactive ratemaking has no application to a Commission decision to adjust price cap levels down on a going-forward basis. That rule is intended to address situations in which an agency order may require a carrier to make refunds if its rates were subsequently determined to be too high, but to deny them additional compensation if its rates were later determined to be too low. Virgin Islands Tel. Corp. v. FCC, 989 F.2d 1231, 1233 (D.C. Cir. 1993); AT&T v. FCC, 836 F.2d 1386, 1389 (D.C. Cir. 1988). Here, no such potential unfairness exists because the Interim Price Cap Order gave price cap ILECs an opportunity to obtain additional revenues for prior years. Indeed, many of the price cap ILECs selected the highest productivity factor and had the opportunity to earn and retain earnings to whatever level achieved. Even those price cap ILECs that did not select 5.3 as a productivity factor had an opportunity to earn and retain earnings several percentage points higher than the prescribed 11.25 percent cost of capital that is the benchmark for price cap sharing mechanisms. This kind of two-way true-up is an "obvious example" of a scheme consistent with standard ratemaking principles. Virgin Islands Tel. Corp. v. FCC, 989 F.2d 1231, 1234 (D.C. Cir. 1993)(internal citations omitted).

MCI is hopeful that as part of the access reforms that the Commission will adopt, beginning with its initial decision on May 7, 1997, the current unjustified, above-cost level of interstate access charges will be recognized, and corrective steps taken to avoid what will otherwise be an impediment to local and long distance competition. As the NTIA ex parte of April 24, 1997, stated, a decision to increase the price cap productivity factor, and to make a one-time, prospective adjustment to the price cap index to reflect that the productivity offset has been too small for two years, would make an initial "down payment" against overcharges that long distance ratepayers have shouldered.

Sincerely,

Mary L. Brown

cc: Tom Boasberg
John Nakahata
James Coltharp
James Casserly
Regina Keeney
Larry Atlas