Julia L. Johnson
Chairman

State of Florida

DOCKET FILE COPY ORIGINAL

Gerald L. Gunter Building
2540 Shumard Oak Boulevard
Tallahassee, FL 32399-0850
(904) 413-6044
FAX (904) 413-6019

Public Service Commission

April 22, 1997

RECEIVED
MAY 22 1997
Federal Communications Commission
Office of Secretary

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

EX PARTE OR LATE FILED

Re: CC Docket 96-45 - Universal Service; CC Docket 96-262 - Access Charge Reform; and CC Docket 96-98 - Implementation of the Local Competition Provisions - EX PARTE FILING

Dear Mr. Caton:

Pursuant to Rule 1.1206, an original and one copy of the filing are enclosed. Chairman Julia L. Johnson and staff are meeting with the Chairman and the other Commissioners and their aides Tuesday, April 22, 1997, to discuss and to disseminate her response to the principles distributed by the Common Carrier Bureau. The staff attending the meeting are Bridget Duff, Walter D'Haeseleer, Mark Long, David Dowds, and Dale Mailhot.

Sincerely,

Cynthia B. Miller
Senior Attorney

CBM:ml

Enclosure

cc: Chairman Reed Hundt

No. of Copies rec'd 2
List ABCDE

The FCC Common Carrier Bureau staff has requested that state commissioners comment on a number of proposed principles related to the implementation of universal service and access charge reform. The following comments are those of Commissioner Julia L. Johnson, Chairman of the Florida PSC, and are not necessarily the opinions of the Florida PSC as a whole.

1) ***FCC Principle***: State commissioners support an FCC commitment to establish a planned, sensible transition to move the telephone industry to the world of competition envisioned by the 1996 Telecom Act.

Response: I fully support a planned, sensible transition to competition. The priority, in my view, should be to ensure that any transitional mechanism, as well as any permanent mechanism to implement the requirements of the Act, promotes both consumer interests and equitable competition. Depending on the course of action the FCC chooses to take, we may or may not agree as to whether such action is the most sensible mechanism for the transition.

Suggested Language: Combine #1 and #3 as follows:

State commissioners support an FCC commitment to establish a planned, sensible transition to move the telephone industry to the world of competition envisioned by the 1996 Telecom Act, provided that consumers will be able to benefit from competition and are not adversely affected by changes occurring as a result of the 1996 Act. Further, state commissioners may or may not agree that a particular plan chosen by the FCC is the most sensible course of action for the transition.

2) ***FCC Principle***: State commissioners support FCC efforts to maintain support for small and rural incumbent LECs during this transition period.

Response: I agree that small and rural LECs should continue to receive current HCF, LTS, and DEM weighting during the transition period. In the March 27, 1997 letter that I sent to Chairman Hundt, I suggested that the current HCF mechanism, with some modifications, be kept in place for such LECs until January 1, 2000. The modifications are: (1) assessment should be based on revenues rather than access lines; (2) disbursement should be available to all qualifying carriers based on incumbent LECs' costs for the interim period; and (3) the calculation of HCF support should be based on the *calculated* amount of income taxes instead of on the *per book* amount of income taxes, which is the current practice. I also proposed that after January 1, 2000, the small LECs should move to the LEC Joint Association Transition Plan, which would further transition them to a permanent mechanism.

I have general concerns regarding the fair and proper treatment of rural companies under several FCC orders implementing the 1996 Act. I am particularly concerned about the possible negative impact that the FCC's August 1, 1996 interconnection order may have on small companies. More specifically, Rules 51.405 (c) and (d) apply to the burden of proof required of incumbent LECs to justify a continued exemption under section 251(f)(1) of the Act, or to justify a suspension or modification under section 251(f)(2) of the Act. The Act permits state commissions to grant exemptions, suspensions, or modifications if they determine that the requirements of sections 251(b) and/or (c) are "unduly economically burdensome." The aforementioned FCC rules, however, are more prescriptive than the statutory language. The rules require incumbent LECs to prove that the application of the requirements of sections 251(b) and/or 251(c) of the Act would likely "cause undue economic burden beyond the economic burden that is typically associated with efficient competitive entry." I assume this language is meant to prevent a rural LEC from arguing that it will lose customers or have to incur new costs to justify indefinite postponement of requirements that it open its network to competition. However, I believe there could be some situations where the loss of a lucrative customer or customers to a new competitor, or the need to absorb new costs, may be enough to place the incumbent in a precarious economic circumstance. In such instances, the incumbent LEC would then likely increase its universal service support requirements. This instance could be avoided if states did not have to follow the requirement that the burden must be beyond that typically associated with efficient competitive entry. I believe the language of the Act clearly gives the states the authority to determine what constitutes an undue economic burden, and states could incorporate the FCC's parameter into their analyses. However, the states should not be constrained by FCC rules in their determinations as to what is "unduly economically burdensome." Such determinations should be made on a case-by-case basis, and should incorporate any parameters the states deem appropriate for the particular circumstance.

Suggested language: State commissioners support FCC efforts to maintain current HCF, LTS, and DEM weighting support mechanisms for small and rural incumbent LECs during this transition period. However, the current HCF mechanism should be modified in the following manner: (1) assessment should be based on revenues rather than access lines; (2) disbursement should be available to all qualifying carriers based on incumbent LECs' costs for the interim period; and (3) the calculation of HCF support should be based on the *calculated* amount of income taxes instead of on the *per book* amount of income taxes, which is the current practice. Further, in order to ensure that competition develops in a fair and equitable manner in rural areas, the FCC should modify Rules 51.405 (c) and (d) to delete language requiring LECs to prove undue economic burden, "beyond the economic burden that is typically associated with

efficient competitive entry."

3) ***FCC Principle:*** State commissioners urge the commission to shape such a transition so that consumers will be able to benefit from competition and are not adversely affected by changes occurring as a result of the 1996 Act.

Response: I couldn't agree more with this point; in fact, I believe it should be the first and foremost objective in implementing any transitional or permanent mechanism. Again, however, we may disagree as to what policies will or will not adversely affect consumers (see my response to the next point).

Suggested language: See suggested language for #1.

4) ***FCC Principle***: State commissioners agree that usage charges to recover NTS costs keep per-minute interstate toll charges at artificially high levels and, for this reason, support an FCC decision to recover these NTS costs in an economically efficient manner.

Response: I agree with the first part of the principle - i.e., that usage charges to recover NTS costs keep per-minute interstate toll charges at artificially high levels. However, I do not think that a per-line flat rate charge is the <u>most</u> appropriate means of recovering such costs, as Chairman Hundt has suggested with his idea of a FERC. While the per-line charge would more accurately reflect underlying costs than minute-of-use charges, the fact remains that by nature, NTS costs are incurred in large blocks and do not have a one-to-one relationship with access lines. Therefore, a per-line charge would not accurately reflect how the underlying costs are incurred. Furthermore, as I stated in my March 27 letter, I believe such a method would allow the per-line charges to be too easily passed through to consumers as a separate line item charge on their bills, thereby appearing to be a local rate increase. The better approach would be to bulk bill the costs to the IXCs. This method would make it more difficult for IXCs to pass the NTS costs on to consumers as a separate line item charge, and would give the IXCs an incentive to monitor these costs so the amount assessed to them decreases as costs decrease. If they could bill the costs as a separate line item to consumers, they would have no such incentive and would be reluctant to remove the line item even if costs decrease.

I am also not convinced that competition will force the IXCs to compete the charge away. I believe it possible that if every IXC separately bills the charge, they as a group may initially elect to compete on the per-minute long distance charges rather than on the flat line item charge, because the separate line item charge would be a guaranteed, known source of revenue. This is especially true if the charge is referred to as an FCC-imposed charge on the bill, thereby

implying that it is a mandatory charge imposed by regulators. Alternatively, an IXC may waive the separate line item charge for certain high-volume customers and continue to levy it on low-volume customers. If the costs are bulk billed, the companies could still pass them on in the form of a line item charge, but they would have to develop the rates. In this instance, there could be competition among the carriers not only as to whether to pass the costs on in the form of a line-item charge, but also as to the amount of the line item charge. The amount would not be simply handed to them by the FCC in the form of a per-line assessment; instead, the marketplace would determine how these NTS costs are recovered.

Should the FCC require a per-line assessment, the method of assessment should be structured to avoid any negative impact on the price a consumer pays for basic local telephone service.

Suggested language: State commissioners agree that usage charges to recover NTS costs keep per-minute toll charges at artificially high levels, and such costs should be recovered in an economically efficient manner. However, the preferred method of recovery should not encourage imposition of additional end-user surcharges. If the FCC requires a per-line assessment, the method of such assessment should be structured to avoid any negative impact on the price a consumer pays for basic local telephone service.

5) ***FCC Principle***: State commissioners conclude that the responsibility for creating, sizing, and defining sources of funding for a permanent high cost support mechanism is shared jointly by the FCC and state commissions.

Response: I believe that this principle is too ambiguous and could easily be misinterpreted. Specifically, I am not sure what is meant by "responsibility" and "shared jointly." My fear is that the statement could be construed to endorse intra/interstate universal service assessments during the interim transition period. As I stated in my March 27 letter, many parties have raised legal issues regarding the FCC's authority to assess intrastate revenues; others have expressed concerns as to the magnitude of the subsidy dollars flowing from their states, as well as the impact that inter/intrastate assessments would have on their ability to create their own intrastate universal service fund. I stated that the issue will and should be decided by the courts. For these reasons, I suggested that the better policy decision for the interim would be to assess only interstate revenues. However, I also stated that in the long run, assessment of inter-and intrastate revenues is appropriate, for the following reasons. First, the definition of universal service has been expanded to include services not previously included, and many of the newly included services are more intrastate than interstate in nature. Second, states will be allowed to assess both inter- and

intrastate revenues for any intrastate universal service funds that are developed. Third, assessing both sources of revenues will discourage companies from declaring interstate revenues as intrastate to avoid assessment. Finally, as competition develops over time, state and federal jurisdictional distinctions will become more blurred.

Suggested language: State commissioners conclude that the creation of a permanent high cost support mechanism, and determinations as to its size and sources of funding should be jointly undertaken by the FCC and state commissions through the federal/state Joint Board process and continuing dialogue between state and federal regulators.

6) ***FCC Principle***: State commissioners, recognizing the fact that each of the models filed in the proceeding has flaws that prevent its use as part of the mechanism for defining and sizing universal service high cost support, recommend that state and federal regulators work together to craft a mechanism for defining and sizing universal service high cost support that meets the goals of section 254.

Response: I fully agree that the cost models are not ready for use at present, but we should not preclude the possibility that they may be workable at some point in the future if one or more of them continue to be refined. Therefore, I agree that state and federal regulators should work together to craft a mechanism for defining and sizing universal service high cost support, and part of that exercise should include continuing work on proxy models. However, I also support exploring other competitively neutral mechanisms that can meet the goals of section 254 of the Act.

Suggested language: State commissioners, recognizing the fact that each of the models filed in the proceeding currently has flaws that prevent its use as part of a permanent mechanism for defining and sizing universal service high cost support by May 8, 1997, recommend that state and federal regulators continue to work together to craft a mechanism for defining and sizing universal service high cost support that meets the goals of Section 254 of the Act. Such work should include continued refinement of a proxy model or models, as well as exploration of other competitively neutral mechanisms.

7) ***FCC Principle***: State commissioners agree that the same forward-looking economic cost principles should govern cost studies developed to size high cost support funding and cost studies developed to determine the rates for unbundled network elements.

Response: I fundamentally disagree with this principle. I believe there are

numerous reasons why *different* forward-looking cost principles should be used to govern cost studies for universal service than those used for interconnection/UNEs. The basic reason for using different principles is related to the assumption that cost studies for universal service contemplate different network architectures, technologies, and input prices different from the current ILEC network's, which are to be unbundled for UNE purposes. For purposes of determining costs for funding high cost support, it is reasonable to base cost studies on a theoretical "efficient design" network principle that assumes the ability to instantaneously build an optimal, cost-efficient network capable of satisfying all existing demand at that point in time. This is because the Act envisions competition on a going-forward basis from multiple providers using different types of networks, and requires that universal service support mechanisms should be explicit and competitively neutral. If the funding for universal service were based on, for example, the costs associated with the incumbent LECs' (ILECs) networks, alternative local providers whose costs were lower could receive excessive compensation. To be competitively neutral thus requires that a universal service mechanism be provider-neutral. Therefore, it makes sense that a purely hypothetical network should be used to approximate costs for a permanent high cost funding mechanism.

For purposes of interconnection and UNEs, however, the goal in determining costs is much different than the goal in determining costs for purposes of designing and sizing a permanent high cost funding mechanism. In the case of interconnection and UNEs, the goal is to determine the costs of pieces and parts of an actual existing network. UNEs such as unbundled loops will be provided by a LEC using an in-place network, not some hypothetically constructed network. However, while the appropriate cost analysis reflects the LEC's actual loop characteristics (such as length, quantity, geographic location, etc.), forward-looking technology is modeled and current input prices are used. If a purely hypothetical network were the basis of cost studies used for interconnection/UNEs, the resulting costs likely would be lower than if cost studies were based on the existing LEC network. Consequently, there would likely be little incentive for new entrants to build their own networks, since "scorched" network design would result in prices for using the incumbents' networks equal to or lower than the costs of building a new network. Beyond the incentive to use the least cost option, firms strive to maximize their exposure to risk. Building facilities inherently carries investment risks and delays market entry. These factors make it all the more important to send the proper pricing signals to potential entrants. Finally, if a hypothetical network were the basis for UNE cost studies, it is more likely that the incumbent LECs would claim an illegal taking of property on the basis that they are not being adequately compensated for the true costs of their networks.

Suggested language: State commissioners agree that forward-looking economic cost principles should govern both cost studies developed to size high cost support funding and those developed to determine the costs of unbundled network elements; however, we disagree that the same forward-looking principles should govern both types of cost studies.

8) ***FCC Principle***: State commissioners support an FCC commitment to adopt the Joint Board's recommendation that there be federal funding sufficient to assure that telecommunications services, including inside wiring and access to the Internet be available to schools and libraries at discounted rates.

Response: I generally agree with the concept here, but I would be more specific as to what was in the Joint Board's recommendation. The statement should specify that the annual funding amount be capped, and that the schools and libraries receive the discounted rates contained in the matrix proposed by the Joint Board.

Suggested language: State commissioners support an FCC commitment to adopt the Joint Board's recommendation that there be federal funding capped at $2.25 billion per year for provision of telecommunications services, as well as inside wiring and access to the Internet, to schools and libraries at the discounted rates contained in the matrix proposed by the Joint Board.

I very much appreciate the FCC's efforts to codify a unifying set of principles to guide the implementation of universal service and access charge reform. In thinking through my comments to the FCC staff's proposed principles, some others came to mind. I would therefore respectfully suggest that the following principles be added to the list:

1) Any restructuring of access charges should be carefully planned to ensure that:

   a) It does not create a mechanism that results in LEC over-recovery; and

   b) Assessments to the IXCs cannot be readily passed through to customers as a separate line item on their bills; and

   c) If IXCs do pass assessments on to customers in the form of per-line charges, there is a mechanism in place whereby the amounts of such charges are periodically examined to determine if they should be continued.

2) To ensure that consumers benefit to the greatest extent possible from the Act, the FCC is committed to examining current price cap levels and productivity