business lines will, on average, decrease from 1998 to 1999, and for every year thereafter, and will fall to less than $1.00 by 2001.

60. To the extent that the ceilings on SLCs and PICCs do not allow recovery through flat charges of all common line revenues, LECs shall be permitted to impose a per-minute CCL charge assessed on originating minutes.[54] As the PICC cap for non-primary residential and multi-line business lines increases -- and as revenues transferred from primary residential and single-line businesses fall to zero -- the per-minute CCL charge will fall to zero, too. Eventually, we anticipate that most, if not all, price cap LECs will be able to recover the full per-line revenues associated with non-primary residential and multi-line business lines through the SLC, after taking into account the assistance provided through the explicit high-cost universal service support mechanisms. In addition, residual TIC revenues will also be recovered through the PICC on non-primary residential and multi-line business lines. As described more fully below, to the extent that the PICC ceilings prevent full recovery of the residual TIC, the remaining amount will be recovered through a per-minute residual TIC.

B. Other Rate Structure Changes

61. *Switching*. The traffic-sensitive costs of local switching will continue to be recovered through per-minute local switching charges.

62. For price cap LECs, the NTS costs associated with line ports will no longer be included in the local switching charge, and instead will be recovered through the flat-rated common line charges discussed above. Price cap LECs will also assess a monthly flat-rated charge directly on end users that are subscribing to integrated services digital network services, digital subscriber line, or other services that have higher line port costs than basic, analog service. This charge recovers the amount by which the cost of the line port exceeds the cost of a line port for basic, analog service. Costs of local switching attributable to trunk ports are moved to a separate service category within the traffic-sensitive basket. These costs will be recovered through flat-rated monthly charges collected from users of dedicated trunk ports and per-minute, traffic-sensitive charges assessed on users of shared trunk ports. The new rate structure also includes an optional call set-up charge.

63. *Transport*. Effective July 1, 1998, the unitary rate structure option for tandem-switched transmission is eliminated and the costs of tandem-switched transmission must be recovered through the existing three-part rate structure. For price cap LECs, a new flat-rated monthly charge recovers the NTS costs of tandem switching attributable to dedicated ports. A

[54] To the extent that the sum of a LEC's originating local switching charge and any residual per-minute CCL, TIC, and marketing expense (see section IV.D) charges exceeds the sum of its originating local switching, CCL, and TIC charges on December 31, 1997, the excess shall be collected through a per-minute charge on terminating access. We expect that this will only apply to a few LECs, and to none beyond 1998.

new per-minute rate element recovers the costs of multiplexers used between tandem switch DS-1 port interfaces and the DS-3 circuits used to transport traffic from tandem to end offices. For all incumbent LECs, the formula used to compute the tandem-switched transport rate is based on actual usage of the circuit, rather than an assumed 9000 minutes of use per month.

64. For all incumbent LECs, certain costs currently recovered through the TIC are reassigned to specified facilities charges, including tandem-switching rates. For price cap LECs, those costs of the TIC that remain (the "residual TIC") are recovered through the PICC. To the extent that the PICC ceiling prevents recovery of the entire residual TIC through the flat-rated PICC, the remaining portion will be collected through a per-minute residual TIC. As the ceilings on the PICCs increase, a larger percentage of the residual TIC will be recovered through the PICC. Beginning in July 1997, price cap reductions will be targeted to the per-minute residual TIC until it is eliminated. We expect that the per-minute TIC charge will be eliminated in two to three years. Residual per-minute TICs shall be assessed only on incumbent LEC transport customers, and therefore shall no longer be assessed on competitive access providers (CAPs) that interconnect with the LEC switched network at the end office.

65. *SS7 Signalling*. Price cap LECs may, but are not required to, adopt a rate structure for SS7 signalling that unbundles SS7 signalling functions, as was permitted in the *Ameritech SS7 Waiver Order*.[55]

66. *Retail Marketing Expense*. Price cap LECs may no longer recover certain marketing expenses through per-minute access charges assessed on IXCs. These expenses are recovered from end users through per-line charges on second and additional residential lines and multi-line business lines, subject to ceilings on SLCs. Any residual shall be recovered through the PICCs on these lines and then through per-minute charges on originating access, subject to the exception described in Section III.A, below.

III. RATE STRUCTURE MODIFICATIONS

A. Common Line

1. Overview

67. In the 1983 *Access Charge Order*, the Commission established a comprehensive mechanism for incumbent LECs to recover the costs associated with their provision of access

[55] Ameritech Operating Companies Petition for Waiver of Part 69 of the Commission's Rules to Establish Unbundled Rate Elements for SS7 Signalling, Order, 11 FCC Rcd 3839 (1996) (*Ameritech SS7 Waiver Order*).

service required to complete interstate and foreign telecommunications.[56] The access plan distinguished between traffic sensitive costs and NTS costs incurred by an incumbent LEC to provide interstate access service An incumbent LEC's NTS costs of providing interstate access, or costs that do not vary with the amount of usage, include the common line, or "local loop," which connects an end user's home or business to a LEC central office.[57]

68. In the *Access Charge Order,* the Commission emphasized that its long range goal was to have incumbent LECs recover a large share of the NTS common line costs from end users instead of carriers, and to recover these costs on a flat-rated, rather than on a usage-sensitive, basis.[58] The Commission recognized, however, that a sudden increase in the flat rates imposed by LECs on end users could have a detrimental effect on universal service. For this reason, the rules adopted in 1983 apportioned charges for common line costs between a monthly flat-rated end-user SLC and a per-minute CCL charge assessed to the IXCs. The SLC is based on average interstate-allocated common line costs, which the incumbent LEC may average over an entire region or over a study area,[59] depending on how it files its interstate tariff. These charges currently are the lesser of the per-line average common line costs allocated to the interstate jurisdiction or $3.50 per month for residential and single-line business users, and $6.00 per month for multi-line business users.[60] Any remaining common line revenues permitted under our price cap rules are recovered by incumbent price cap LECs

[56] MTS and WATS Market Structure, CC Docket No. 78-72, Third Report and Order, 93 F.C.C. 2d 241 (1983) (*Access Charge Order*), modified, 97 F.C.C. 2d 682 (1983) (*Reconsideration Order),* further modified, 92 F.C.C. 2d 834 (1984) (*Second Reconsideration Order),* aff'd in principal part and remanded in part sub nom. *NARUC v. FCC,* 737 F.2d 1095 (D.C. Cir. 1984), *cert. denied,* 469 U.S. 1227 (1985).

[57] See, e.g., *Access Charge Order*, 93 FCC 2d at 268-69.

[58] *Id.* at 268-269.

[59] A "study area" is usually an incumbent LEC's existing service area in a given state. The study area boundaries are fixed as of November 15, 1984. *MTS and WATS Market Structure: Amendment of Part 67 of the Commission's Rules and Establishment of a Joint Board, Decision and Order,* 50 Fed. Reg. 939 (*1985 Lifeline Order*).

[60] Revenues permitted under our price cap rules for common line services may be significantly different from the interstate allocated costs assigned to the common line access element by our Part 36 and Part 69 cost allocation rules. For each price cap basket, the rates allowed are determined based on price cap formulas, without reference to interstate allocation of costs. We measure the earnings of price cap carriers by comparing revenues to interstate allocated costs. See 47 C.F.R. §§ 61.45(c), 65.702, & 69.104. The data indicate that only two study areas served by price cap LECs, (Bell Atlantic in the District of Columbia, and GTE in Minnesota) have interstate-allocated common line costs that are less than the current $3.50 SLC. These two study areas represent less than two percent of subscriber lines nationwide. *See* Supporting Material filed with 1996 Annual Access Tariff Filing, filed with Commission on April 2, 1996. (*1996 LEC Annual Access Tariff Forecast Data.*) This LEC forecast data were used by LECs to set SLC rates that became effective on July 1, 1996.

through per-minute CCL charges assessed on the IXCs, and are ultimately recovered by IXCs from end-users through long distance toll charges.[61]

69. Because common line and other NTS costs do not increase with each additional minute of use transmitted over the loop, the current per-minute CCL charge that recovers loop costs represents an economically inefficient cost-recovery mechanism and implicit subsidy. A rate structure that recovers NTS costs through per-minute charges creates an incentive for customers to underutilize the loop by requiring them to pay usage rates that significantly exceed the incremental cost of using the loop. Additionally, a rate structure that forces high-volume customers to pay significantly more than the cost of the facilities used to service them is not sustainable in a competitive environment because high-volume customers can migrate to a competitive LEC able to offer an efficient combination of flat and per-minute charges, even if the competitive LEC has the same or higher costs than the incumbent LEC.

70. The Federal-State Universal Service Joint Board stated, in its *Recommended Decision*, that primary residential and single-line business lines are essential to the provision of universal service,[62] and that current rates for local services are generally affordable based on subscribership levels.[63] The Joint Board also concluded that the SLC, as a charge assessed directly on local telephone subscribers, has an impact on universal service concerns such as affordability,[64] and recommended that the Commission leave the current SLC ceilings in place for primary residential and single-line business lines.[65] In our companion *Universal Service Order,* consistent with that recommendation, we conclude that we should not raise the current $3.50 SLC ceiling on primary residential and single-line business lines.[66]

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[61] The data indicate that incumbent price cap LECs recover approximately 10.4 billion dollars in total common line revenue. Approximately $7 billion of the common line costs are recovered through the SLC, and approximately $3.4 billion are recovered through the CCL charge. Thus, incumbent price cap LECs recover approximately one-third of their common line costs through per-minute CCL charges. *1996 LEC Annual Access Tariff Forecast Data.*

[62] Federal-State Joint Board on Universal Service, CC Docket No. 96-45, Recommended Decision, 12 FCC Rcd 87, 132-133 (rel. Nov. 8, 1996) (*Joint Board Recommended Decision*).

[63] *Id.* at 154. The Joint board noted that "[s]ubscribership levels, while not dispositive on the issue of affordability, provide an objective criterion to assess the overall success of state and federal universal service policies in maintaining affordable rates." *Id.*

[64] *Id.* at 472.

[65] *Id.*at 463. *See also* Separate Statement of FCC Commissioner Rachelle B. Chong, (dissenting from the Joint Board's recommendation that the Commission should lower the SLC for primary residential and single-line business lines). *Id.* at 556.

[66] *Universal Service Order*, Section XII.C.

71. We adjust the SLC ceilings for multi-line business lines and residential lines beyond the primary connection. Adjusting the SLC ceilings for multi-line business lines and non-primary residential lines will permit incumbent LECs to recover directly from end users more of the common line revenues permitted under our price cap rules for those lines and will reduce the amount of NTS costs related to these lines that are currently recovered through CCL charges. Where the SLC ceilings do not allow the incumbent LEC to recover its price cap common line revenues through end-user charges, the remaining, or "residual" amount will be recovered through flat, per-line charges assessed to each customer's presubscribed interexchange carrier. This presubscribed interexchange carrier charge, or "PICC", will increase gradually until the incumbent price cap LECs' full interstate-allocated common line revenues permitted under our price cap rules are recovered through a combination of flat-rated SLCs and PICCs. To the extent that the flat-rated charges do not recover, during the initial phase, the full interstate-allocated common line revenues permitted under our price cap rules, incumbent LECs may continue to assess the IXCs a per-minute CCL charge based on the costs not recovered through flat-rated charges. This per-minute charge, however, will be generally much lower than today's CCL charge and will be eliminated once all common line revenues are recovered through a combination of SLCs and PICCs.

2. Subscriber Line Charge

a. Background

72. In the NPRM, we proposed to increase the ceiling on the SLC for second and additional lines for residential customers, and for all lines for multi-line business customers, to the per-line loop costs assigned to the interstate jurisdiction.[67] Alternatively, we proposed to eliminate the ceiling for multi-line business customers and for residential connections beyond the primary connection, especially where the incumbent LEC has entered into interconnection agreements and taken other steps to lower barriers to actual or potential local competition.[68] We sought comment on these proposals.[69] We also invited parties to comment on whether any changes that we adopt to the ceiling on SLCs for incumbent price cap LECs should be extended to incumbent rate-of-return LECs, and on the relationship of any such changes to the *Joint Board Recommended Decision.*[70] We sought comment on whether to establish a transition mechanism for this increase if the ceilings on SLCs for multi-line business lines and residential lines beyond the primary connection are increased and whether such a transition

[67] NPRM at ¶ 65.

[68] *Id.*

[69] NPRM at ¶ 65.

[70] *Id.*

could be implemented consistent with section 254, the Act's universal service provision.[71] We sought comment on whether geographic averaging of SLCs is an implicit subsidy that is inconsistent with the requirements of section 254(e), and thus on whether we are required to deaverage SLCs.[72]

b. Discussion

73. The Commission has had the longstanding goal of ensuring that all consumers have affordable access to telecommunications services.[73] In its *Recommended Decision*, the Joint Board stated that current rates for local telephone services are generally affordable and that the SLC, as a charge assessed directly on local telephone subscribers, has an impact on universal service concerns such as affordability.[74] The Joint Board further recommended that the Commission maintain the current SLC ceilings for primary residential and single-line business lines,[75] and we adopt that recommendation in our companion *Universal Service Order*.[76] Numerous parties in this proceeding argue that we should raise or eliminate the SLC ceiling on all lines to permit LECs to recover the full interstate allocated costs of the local loop from end-users.[77] This would increase the average SLC for all residential and single-line business lines from $3.50 per month to $6.10 per month.[78] We conclude that it would be inappropriate to make significant changes to the SLC cap for primary residential and single-

[71] *Id.* at ¶ 66.

[72] *Id.* at ¶ 67.

[73] *See, e.g.*, MTS and WATS Market Structure, Amendment of Part 67 of the Commission's Rules and Establishment of a Joint Board, CC Docket Nos. 78-72, 80-286; Decision and Order, FCC 85-643 (rel. Dec. 27, 1985).

[74] *Joint Board Recommended Decision*, 12 FCC Rcd at 472.

[75] *Id.* at 463.

[76] *Universal Service Order* at Section XII.C.

[77] *See, e.g.*, GTE Service Corporation (GTE) Comments at 26-29, Reply at 20-21; Southwestern Bell Telephone Company (SWBT) Comments at 37-38; Cincinnati Bell Telephone Company (Cincinnati Bell) Comments at 6-7; AT&T Corporation (AT&T) Comments 51-54, Reply at 25-26; Frontier Corporation (Frontier) Comments at 4, 5-7; Sprint Corporation (Sprint) Comments at 11-15; 50-51; Ad Hoc Telecommunications Users Committee (Ad Hoc) Reply at 4; General Services Administration/United States Department of Defense (GSA/DOD) Comments at 9-11, Reply at 5, 7; Tele-Communications, Inc. (TCI) Comments at 10; Reply at 4-5; Time Warner Communications Holdings, Inc. (Time Warner) Comments at 4-5; WorldCom, Inc. (WorldCom) Comments at 30-31.

[78] As discussed below, the data indicate that nationwide, the average interstate allocation of common line costs is $6.10 per line. *1996 LEC Annual Access Tariff Forecast Data.*

line business lines. Primary residential and single-line business lines are central to the provision of universal service. Because of concerns about affordability, and in light of the significant changes that are still underway in this proceeding, in the federal universal service support proceeding, and possible future changes to the separations process, we conclude that the current SLC for these lines should not be raised. Consistent with the Joint Board's recommendation and our conclusion in the *Universal Service Order*, therefore, the ceiling on the SLC for primary residential and single-line business lines will remain at $3.50 or the permitted price cap common line revenues per line, whichever is less.

74. With regard to multi-line users, the Joint Board suggested in its *Recommended Decision* that universal service support should not be extended to non-primary residential lines and multi-line business lines because it found that cost of service is unlikely to be a factor that would cause multi-line users not to subscribe to telephone service.[79] Subsequently, the state members of the Joint Board filed a report with the Commission in which they proposed that we retain high cost support for all lines served in high cost study areas during a transition to a forward-looking cost methodology.[80] Consistent with that proposal, we adopt, in our *Universal Service Order*, a modified version of the existing high-cost support system and continue support for all residential and business connections in areas currently receiving high cost support until at least January 1, 1999.[81] We therefore continue to provide high cost support for non-primary residential and multi-line business lines at this time, by allocating a lower portion of these costs to the intrastate jurisdiction than would otherwise be the case.[82] In that order, we also express our concern, however, that providing universal service support for non-primary residential and multi-line business lines in high-cost areas may be inconsistent with our long-term universal service goals, and that overly expansive universal service support mechanisms potentially could harm all consumers by increasing the expense of telecommunications services for all.[83] We state that we will continue to evaluate the Joint Board's recommendation to limit universal service support to primary residential connections and businesses with single connections.[84]

75. We conclude here that it is necessary to adjust the ceilings on the interstate SLCs on both non-primary residential and multi-line business lines in order to create a rate structure

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[79] *Joint Board Recommended Decision,* 12 FCC Rcd 87 at 133.

[80] State Members Report on the Use of Cost Proxy Models at 3 (dated Mar. 26, 1997).

[81] *Universal Service Order* at Section IV.D and VII.D.

[82] *Universal Service Order* at Section VII.D.

[83] *Universal Service Order* at Section IV.D.

[84] *Universal Service Order* at Section IV.D.

that supports our long-term universal service goals, is pro-competitive, and is sustainable in a competitive local exchange market. Section 254 of the Act requires that all consumers have access to basic telephone service at just, reasonable, and affordable rates that are comparable among different regions of the nation.[85] This section of the Act also requires that universal service support be achieved through support mechanisms that are "specific, predictable, and sufficient."[86] Because universal service concerns about ensuring affordable access to basic telephone services are not as great for non-primary residential and multi-line business lines as they are for primary residential and single-line business lines, we must take action to remove the implicit subsidies contained in our current interstate access charges. Thus, we are adopting a rate structure that will permit LECs to recover greater amounts of their costs on a flat-rated basis from end users and to reduce the amount of revenues they must recover through per-minute access charges. Our initial implementation improves upon the current rate structure because it reduces subsidies by recovering more costs from the cost causer. It also creates a rate structure that is more pro-competitive than the existing one by providing for greater flat-rated recovery of NTS costs. Without these modifications, new entrants, which are not subject to the non-cost-causative rate structure requirements, would be in a position to target the incumbent LECs' most profitable, high-volume customers based on regulatory requirements. A loss of profitable customers would increase the incumbent LECs' costs of providing service to the rest of their customers, especially to those in high-cost areas. Consistent with our universal service goal of ensuring that all consumers receive affordable rates that are comparable in different parts of the nation, however, the SLC adjustments will be subject to ceilings to prevent end-user customers in high-cost areas from paying SLCs that are significantly higher than in other parts of the country.

76. In virtually all cases, current SLC ceilings do not permit incumbent LECs to recover their average per-line interstate-allocated common line costs.[87] As a result of the existing SLC ceilings, which have been in place for the past decade, incumbent LECs must recover the shortfall through usage-sensitive CCL charges assessed on IXCs. The IXCs in turn recover most or all of these costs from toll users in the form of per-minute charges, keeping toll rates artificially high and discouraging demand for interstate long distance services. The high per-minute toll charges also create support flows between different classes of customers. For example, because end-user customers vary widely in their use of interstate long distance services, low-volume toll users do not pay the full cost of their loops while high-volume toll users contribute far more than the total cost of their loops. In addition high-

[85] 47 U.S.C. § 254(b)(3).

[86] 47 U.S.C. § 254(b)(5).

[87] The data indicate that only two study areas served by price cap LECs, (Bell Atlantic in the District of Columbia, and GTE in Minnesota) have interstate-allocated common line costs that are less than the current $3.50 SLC. These two study areas represent less than two percent of subscriber lines nationwide. *See 1996 LEC Annual Access Tariff Forecast Data.*

volume toll users, who include significant numbers of low-income customers, effectively support non-primary residential and multi-line business customers.[88]

77. In order to create a rate structure that supports our long-term universal service goals, is pro-competitive, and is sustainable in a competitive market, we modify our rate structure requirements to permit incumbent LECs to recover costs in a manner that more accurately reflects the way those costs are incurred. Because common line costs do not vary with usage, these costs should be recovered on a flat-rated instead of on a per-minute basis. In addition, these costs should be assigned, where possible, to those customers who benefit from the services provided by the local loop. Accordingly, the SLC ceilings for non-primary residential and multi-line business lines will be adjusted generally to a level that permits incumbent LECs to recover, directly from the end user, their average per-line interstate common line revenues.[89]

78. For multi-line business lines, the SLC will be adjusted to recover the average per-line interstate-allocated common line costs beginning July 1, 1997. To the extent incumbent price cap LECs, mostly in rural areas, have common line costs that significantly exceed the national average, we establish a ceiling on SLCs for multi-line business lines of $9.00, adjusted annually for inflation. To ameliorate any possible adverse impact of adjustments in SLC ceilings for non-primary residential lines, we adopt an approach that will gradually phase in adjustments in the SLC ceilings for these lines. The SLC for non-primary residential lines will be adjusted initially beginning January 1, 1998. For the first year, beginning January 1, 1998, the SLC ceiling for non-primary residential lines will be adjusted to the incumbent LEC's average per-line interstate-allocated costs, but may not exceed $1.50 more than the current SLC ceiling. Beginning January 1, 1999, the monthly SLC ceiling for these lines will be adjusted for inflation and will increase annually by $1.00 per-line, until the SLC ceiling for non-primary residential lines is equal to the ceiling permitted for multi-line business lines.

79. The data indicate that the long term ceilings we are establishing will permit incumbent price cap LECs to recover their average per-line common line revenues[90] from 99

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[88] *See* Robert W. Crandall, *Universal Service Subsidies and Consumer Welfare: Long-distance Access Charges*," Brookings Institution (April, 1997), Table 1, (showing that roughly 30 percent of households with income under $10,000 spend more on long-distance calls than do 50 percent of the households with income over $75,000).

[89] As discussed in Section IV.D, below, in addition to the average per-line interstate-allocated common line costs, price cap LECs may include, in the SLC for non-primary residential and multi-line business lines, certain marketing expenses attributable to these lines.

[90] As discussed in Section III.A.3. below, when the multi-line PICC no longer recovers common line revenues, the calculation of the SLC will be changed from one based on interstate allocated *costs* to one based on common line *revenues* permitted under our price cap rules.

percent of their non-primary residential and multi-line business lines.[91] For the few incumbent price cap LECs that have common line costs in certain study areas that exceed the ceiling, the ceiling will serve as an economic safeguard for those customers who would otherwise pay significantly higher SLCs.[92] We conclude that maintaining a ceiling for non-primary residential and multi-line business customers in high-cost areas is a reasonable response to a legitimate universal service concern because, consistent with section 254(b)(3), it ensures that these customers have access to telecommunication services at rates that are comparable to rates charged for similar services in urban areas.[93]

80. We believe that the approach we adopt should prevent widespread discontinuance of lines by multi-line customers. The record indicates that nationwide, the average interstate allocation of common line costs is only $6.10 per line, and that for more than half of multi-line business lines, the interstate common line costs are below the existing $6.00 ceiling.[94] Therefore, when the SLC ceiling is adjusted July 1, 1997, more than half of multi-line business lines will see no immediate increase in their SLC. The $5.00 SLC ceiling for non-primary residential lines for the first year is a net increase of $1.50 per month and the gradual increase, if any, in subsequent years, is designed to allow these customers time to adjust to the new rate structure. Moreover, we expect the rate structure modifications we adopt in this order to benefit the majority of multi-line customers through reductions in per-minute long distance rates. Thus, for many customers, the access restructuring will lead to an overall reduction in their telephone bill. We also note that, because we are adjusting the SLC on non-primary residential lines only to a level that recovers the average interstate allocated costs attributable to the line, to the extent that a customer chooses not to purchase an additional line because of the SLC increase, it is because the benefits of the second line to that customer are less than the average cost of the line.

81. Many parties contend that adjusting the SLC ceiling for non-primary residential lines and multi-line business lines will affect economic development in rural areas.[95] To

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[91] *See 1996 LEC Annual Access Tariff Forecast Data.*

[92] The data indicate that twelve study areas served by three price cap LECs (GTE, U S West, and Citizens Utilities) have average common line costs that exceed $9.00. These areas represent less than two percent of subscriber lines nationwide. *See 1996 LEC Annual Access Tariff Forecast Data.*

[93] 47 U.S.C. § 254(b)(3).

[94] *See 1996 LEC Annual Access Tariff Forecast Data.*

[95] *See, e.g.,* Harris, Skrivan & Associates, LLC (Harris, Skrivan & Associates) Comments at 6; TCA-Inc.-Telecommunications Consultants (TCA) Comments at 4; GVNW Inc./Management (GVNW) Comments at 7; John Staurulakis, Inc. (Staurulakis) Comments at 7-9; Western Alliance Comments at 22-24; ITCs, Inc. (ITC) Comments at 3; National Exchange Carrier Association, Inc. (NECA) Comments at 13, Reply at 7-9; Rural Telephone Coalition (Rural Tel. Coalition) Comments at 8; Pennsylvania Internet Service Providers Comments at

respond to this concern, with the limited exception of cost allocation to new elements, discussed in Section V, below, we are limiting application of the rate structure modifications we adopt in this Order to incumbent price cap LECs only. Most consumers in rural areas are served by small rate-of-return LECs that are not affected by the SLC adjustment we are adopting. We will review rate structure modifications affecting small, rural carriers in a separate proceeding when we address access charge reform for those carriers. To the extent there are incumbent price cap LECs that serve high-cost areas of the country and have common line costs that exceed the national average, we are maintaining a ceiling on the SLCs for these lines to ensure that subscribers do not pay rates that greatly exceed the national average.[96]

82. We are not persuaded by arguments that an upward adjustment to a SLC ceiling that was set over a decade ago, and that has never been adjusted for inflation, would violate section 254(b)'s requirement that consumers in all regions of the nation have affordable access to telecommunications and information services at rates that are reasonably comparable to those services provided in urban areas.[97] The data indicate that if the SLC ceilings for business and residential lines had been adjusted annually for inflation since they became effective in 1984 and 1989, respectively, the $6.00 business SLC ceiling would have increased by 1996 to $9.00 per line, and the $3.50 residential and single-line business SLC ceiling would have increased to $4.39 per line.[98] Thus, for multi-line business customers, the SLC ceiling we adopt today is not significantly different from what it would have been, if it had been adjusted for inflation annually. Moreover, to adopt a ceiling lower than $9.00 would effectively create an additional impermissible subsidy for a class of customers not enumerated by Congress in section 254 of the 1996 Act as beneficiaries of fundamental universal service goals. We find that the $9.00 ceiling we adopt today strikes a reasonable balance between our desire to establish a more efficient interstate access charge rate structure consistent with our long-term universal service goals in a competitive local exchange environment, and the need to avoid precipitous rate increases to consumers in high cost areas. Although SLCs in

8-9; Commercial Internet Exchange Association (CIEA) Comments at 13; Reply at 10.

[96] We will address access charge modifications as they apply to rate-of-return rural LECs in proceeding later this year. *See* Section V.A, below.

[97] *See, e.g.,* ITC Comments at 3; Rural Tel. Coalition Comments at 8, Reply at 11; TDS Telecommunications Corporation (TDS) Comments at 3-4, Reply at 4; Western Alliance Comments at 23; TCA Comments at 3-4.

[98] Calculations are based on Consumer Price Index for "All Items," *Trends in Telephone Service*, Table 6, (March 28, 1997).

some areas may ultimately be lower than SLCs in high-cost areas, we conclude that $9.00 SLCs remain "reasonably comparable" to those in urban areas.[99]

83. We are also not persuaded that we should maintain the current SLC ceiling for non-primary residential lines because of claims that incumbent LECs will be unable to identify second lines for purposes of billing different SLCs to these lines. Additional telephone lines are a well-established telecommunications product marketed by LECs. This product is supported by a marketing and billing infrastructure that will enable LECs to distinguish non-primary residential lines for purposes of billing different SLCs. We note that we are not defining "primary" or "non-primary" lines in this Order. In a further notice of proposed rulemaking in the Universal Service proceeding, we will address this issue, and release an order defining "primary"and "non-primary" residential lines by the end of the year.[100]

84. We are unpersuaded by arguments that we should forgo these changes on the grounds that increasing the SLC ceilings for non-primary residential lines will create undue incentives for subscribers to order their primary lines from the incumbent LEC and their additional lines from competitors. The changes we adopt in this Order are intended to permit incumbent LECs to move their prices for non-primary residential and multi-line business lines toward more economically efficient levels by substantially reducing implicit subsidies flowing between different classes of customers. Once these subsidies are eliminated and the new universal service regime is fully implemented, incumbent LECs will be able to recover their common line costs from customers through a rate structure that accurately reflects the manner in which these costs are incurred, and through a targeted, portable universal service contribution where necessary. At that point, both incumbent LECs and new entrants should be able to compete efficiently in the local exchange market. Subscribers, therefore, should not have an incentive to use other carriers for their additional lines unless a competitor is operating more efficiently and can offer local exchange service at a lower rate than the incumbent LEC is able to offer. Indeed, the ability of a competitive local exchange carrier to offer local exchange service at a lower rate is precisely the type of competition envisioned by the 1996 Act: it will encourage the incumbent LEC to reduce its costs of providing service in order to meet or beat the prices of its competition.

85. To address the concerns of some commenters that charging a higher SLC for second and additional residential lines will encourage subscribers to order their additional line from competitors, we will permit LECs to charge competitors the higher SLC when the

[99] In Section IV.D, below, we conclude that price cap LECs may recover certain marketing expenses through the SLC on non-primary residential and multi-line business lines. That, however, does not affect the SLC ceilings for these lines.

[100] *Universal Service Order* at Section IV.D.

competitor provides a customer with a second line through resale of an incumbent LEC offering. If prior to the development of full competition, we find that disparity between SLC charges on primary and additional residential lines becomes a significant problem, we will reexamine this issue in conjunction with further reforms we adopt in an upcoming order.

86. Certain incumbent LECs have requested that any rule that increases the SLC ceiling for non-primary residential lines should be optional for LECs.[101] We adopt this proposal in part and will not require LECs to charge a higher SLC for non-primary residential lines. Thus, if an incumbent LEC finds that charging higher SLCs leads to a large number of disconnections, it is free to charge less. To the extent price cap LECs choose to charge a SLC that is less than the maximum allowed, however, they may not recover these foregone revenues through the PICC or CCL charges. This restriction is consistent with our current price cap rules, which prevent LECs from transferring SLC costs to the CCL charge.[102]

87. Several incumbent price cap LECs argue in favor of deaveraging SLCs, stating that an averaged SLC creates cross-subsidies between high-cost and low-cost areas, in violation of section 254 of the Act.[103] We will resolve this issue, along with issues concerning the timing and degrees of geographic deaveraging, pricing flexibility, and ultimate deregulation in an upcoming order.

3. Carrier Common Line Charge

a. Background

88. Because we are retaining the $3.50 ceiling on SLCs for primary residential and single-line business customers, virtually all price cap LECs will be unable to recover, through the SLC, all of their common line revenues permitted under our price cap rules. In the NPRM, we sought comment on possible revisions to the current CCL charge structure that would allow incumbent price cap LECs to recover these NTS common line costs in a way that reflects the way costs are incurred. We proposed a recovery mechanism suggested by the Joint Board in its *Recommended Decision*[104] that would permit incumbent LECs to recover common line costs not recovered from SLCs through a flat, per-line charge assessed against

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[101] *See, e.g.*, Bell Atlantic Telephone Companies and NYNEX (BA/NYNEX) Comments at 33-34; Pacific Telesis (PacTel) Reply at 22; Citizens Utilities Company (Citizens Utilities) Comments at 28-29.

[102] 47 C.F.R. § 69.104.

[103] *See, e.g.*, U S West Comments at 56; Ameritech Comments at 12-13; BellSouth Comments at 32; GTE Comments at 30-31.

[104] *Joint Board Recommended Decision*, 12 FCC Rcd at 474.

each end-user's presubscribed interexchange carrier.[105] The Joint Board suggested that the Commission allow incumbent LECs to collect the flat-rated charge directly from end users who have not selected a primary interexchange carrier ("PIC.")[106] We sought comments on this approach and also invited parties to discuss any potential problems created when end-user customers have selected PICs, but use other IXCs for Internet, fax, interexchange, or other interstate services by "dialing-around" the PIC.[107]

89. We also sought comment on several alternative approaches to the per-minute recovery of interstate NTS loop costs proposed by the Competition Policy Institute (CPI), including a "bulk billing" method that would assess a charge against the IXC based upon its percentage share of interstate minutes of use or revenues, a "capacity charge," a "trunk port charge," and a "trunk port and line port" charge.[108] We invited parties to comment on whether any changes that we adopt to the recovery of interstate NTS local loop costs for price cap LECs should be extended to rate-of-return LECs, and on the relationship of interstate NTS loop cost recovery to the universal service mechanisms proposed in the *Joint Board Recommended Decision.* We asked parties to address how such an extension to rate-of-return LECs would affect small business entities, especially small incumbent LECs.[109]

90. Additionally, we asked parties to address whether an alternative mechanism for recovering common line costs currently recovered through the CCL charge would be necessary if we were to eliminate the SLC ceiling for certain lines. We asked interested parties to address the extent to which any proposed alternative recovery mechanism for recovering common line costs currently recovered through the CCL charge would affect small business entities, including small incumbent price cap LECs and new entrants. We also sought comment on whether section 254(g) precludes an IXC from charging its customers the flat, per-line monthly rate assessed on that line if the amount of that charge varied among customers in different areas within a state or among customers in different states, and if so, whether conditions exist sufficient to require us to forbear from the application of section 254(g) to IXC recovery of flat-rate CCL charges.[110]

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[105] NPRM at ¶¶ 59-63.

[106] *Joint Board Recommended Decision,* 12 FCC Rcd 87 at 474.

[107] NPRM at ¶ 60. Customers are able to "dial-around" their presubscribed interexchange carrier by dialing 10XXX before their area code and 7-digit exchange number.

[108] *Id.* at ¶ 61

[109] *Id.*

[110] *Id.* at ¶¶ 62-63.

b. Discussion

91. The $3.50 SLC ceiling for primary residential and single-line business customers prevents most incumbent price cap LECs from recovering, through end-user charges, all of the common line revenues permitted under our price cap rules.[111] To the extent that common line revenues are not recovered through SLCs, incumbent LECs will be allowed to recover these revenues through a PICC, a flat, per-line charge assessed on the end-user's presubscribed interexchange carrier.

92. We adopt the Joint Board's recommendation that incumbent LECs may collect directly, from any customer who does not select a presubscribed carrier, the PICC that could otherwise be assessed against the presubscribed interexchange carrier. Assessing the PICC directly against end users that do not presubscribe to a long distance carrier should eliminate the incentive for customers to access long-distance services solely through "dial-around" carriers in order to avoid paying long-distance rates that reflect the PICC. Several parties argue that this type of billing arrangement will create administrative difficulties because it will require LECs to prorate charges for both the end user and the IXC when a customer leaves an IXC in the middle of the billing cycle. To avoid any potential administrative difficulties resulting from customers leaving their presubscribed interexchange carriers in the middle of a billing cycle, we will permit LECs to assess the full PICC at the beginning of each billing cycle.

93. We recognize that this flat, per-line PICC will not prevent customers from "dialing around" their presubscribed long distance carrier to obtain interstate service. Collecting a PICC from a customer, however, in and of itself, creates no incentive for a customer to presubscribe to one carrier and use "dial-around" service of another. If the presubscribed carrier is an efficient competitor, it should be able to offer usage-based rates comparable to the prices of a competitor, thus eliminating any artificial benefits of "dial-around" capability. A combination of lower per-minute long distance rates and attractive long-distance pricing packages that reward customers for increasing their usage of the presubscribed interexchange carrier's services should also help deter customers from using separate long-distance carriers for various services solely because of regulation. There is customer contact value in being a customer's presubscribed interexchange carrier. Regulators have long concluded that the convenience of making a long-distance call by simply dialing "1+" conveys certain advantages.[112] And the advantages of "1+" dialing will only increase if, as many predict, we move to a world in which "one-stop shopping" for a multiplicity of services becomes the primary paradigm for provision of telecommunication services. We conclude that the record does not support a finding that assessing a charge on the

[111] *See* n.32, above.

[112] *See, e.g., Local Competition Order*, 11 FCC Rcd at 15511.

presubscribed carrier will artificially encourage "dial-around" traffic to such a degree that we should not adopt access charge modifications that will move substantially toward efficient pricing for common line elements and lower usage charges for long-distance service. If evidence appears to us that our rules do substantially contribute to undue use of "dial-around" capabilities to circumvent presubscribed interexchange services, we stand ready to revisit this issue at a later time.

94. The rate structure we are adopting calls for the single-line PICC ultimately to recover the difference between revenues collected through the SLC and the per-line common line revenues for primary residential lines and single-line business lines permitted under our price cap rules.[113] In order to provide incumbent LECs and IXCs with adequate time to adjust to this rate structure change, we cap the PICC for primary residential and single-line business lines at $0.53 per month for the first year, beginning January 1, 1998, and establish ceilings on increases thereafter. We note that the monthly $0.53 PICC is approximately equal to the current presubscribed per-line charges that are assessed to IXCs for the Universal Service Fund and Lifeline Assistance plan,[114] which are being eliminated in our *Universal Service Order*.[115] Beginning January 1, 1999, the ceiling on the monthly PICC on primary residential and single-line business lines will be adjusted for inflation and will increase by $0.50 per year until the sum of the SLC plus the flat-rated PICC is equal to the price cap LEC's permitted common line revenues per line. In no event shall the sum of the single-line SLC and PICC exceed the sum of the maximum allowable multi-line SLC and multi-line PICC.

95. Sprint asserts that if LECs recover NTS common line costs through deaveraged rates assessed on IXCs, we must forbear from applying section 254(g)[116] to the extent it requires an IXC to average geographically any flat charges an IXC passes on to its customers.[117] WorldCom asserts that IXCs should be permitted to recover their costs in any manner the market will allow, and that unless the Commission forbears with respect to the application of section 254(g) to these costs, IXCs that operate nationally will be forced to

[113] As discussed in Section III.B, below, line port costs will be reassigned from the local switching rate element to the common line rate element. As discussed in Section III.D, price cap LECs may also recover residual TIC revenues through PICCs.

[114] IXCs currently pay $0.0991 for the Lifeline Assistance and $0.4380 for the Universal Service Fund, a total of $0.5371. NECA Transmittal No. 729, F.CC. Tariff No. 5, (filed Nov. 15, 1996).

[115] *See Universal Service Order*, at Sections VII.C and XIII.F.

[116] Section 254(g) requires that "rates charged by providers of interexchange telecommunications services to rural and high cost areas shall be no higher than the rates charged by each such provider to its subscribers in urban areas." 47 U.S.C. § 254 (g).

[117] *See, e.g.*, Sprint Reply at 27.

average together numerous subscribers' loop costs, and thus use long-distance rates as a vehicle for cross-subsidies that run counter to the overall policies of section 254(b) and (c).[118] We conclude that the information in the record before us does not demonstrate that we are required, by section 10(a) of the Act,[119] to forbear from enforcing section 254(g) as it relates to the manner in which IXCs recover their costs.

96. Section 10(a) of the 1934 Act requires the Commission to forbear from applying any regulation or provision of the Communications Act of 1934 if: (1) enforcement of that provision is unnecessary to ensure that the relevant charges and practices are just and reasonable and not unjustly or unreasonably discriminatory; (2) enforcement of that provision is unnecessary to protect consumers; and (3) forbearance from applying such provision or regulation is consistent with the public interest.[120] We conclude that, on the basis of the current record, IXCs have not demonstrated that forbearance of section 254(g) is warranted at this time.

97. We find that establishing a broad exception to section 254(g) to permit IXCs to pass through flat-rated charges on a deaveraged basis may create a substantial risk that many subscribers in rural and high-cost areas may be charged significantly more than subscribers in other areas. Accordingly, we cannot conclude that enforcing our rate averaging requirement is unnecessary to ensure that charges are just and reasonable. In addition, because assessing subscribers flat-rated charges on a deaveraged basis could lead to significantly higher rates for subscribers in high-cost areas, we find no basis in this record to conclude that it is unnecessary to enforce section 254(g) to ensure protection of consumers or to protect the public interest. In contrast, IXCs cite no countervailing public interest considerations but merely make broad, unsupported assertions of the need to deaverage rates in light of the varying PICC amounts expected to be assessed by incumbent LECs. We also note that IXCs now pay access charges that often vary from location to location and from incumbent LEC to incumbent LEC, and still maintain geographically averaged rates. We therefore conclude that, based on the record before us, the IXCs have not met the test set forth in section 10(a) of the Act, and forbearance of section 254(g) is not warranted.

98. We note that we will continue to examine the issue of whether conditions exist that require us to forbear from application of section 254(g) as it relates to recovery of the PICC costs from subscribers. We will resolve this and other specific issues concerning the timing and degrees of pricing flexibility and ultimate deregulation in an upcoming order.

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[118] WorldCom Comments at 34.

[119] 47 C.F.R. § 160.

[120] *Id.*

99. To the extent that the SLC ceilings on all lines and the PICC ceilings on primary residential and single-line business lines prevent recovery of the full common line revenues permitted by our price cap rules, incumbent price cap LECs may recover the shortfall through a flat-rated, per-line PICC on non-primary residential and multi-line business lines.[121] The incumbent LECs will calculate this additional charge by dividing residual permitted common line revenues by the number of non-primary residential and multi-line business lines served by the LEC. For the first year, the ceiling on the PICC will be $1.50 per month for non-primary residential lines and $2.75 per month for multi-line business lines. To the extent that these PICCs do not recover an incumbent LEC's remaining permitted CCL revenues, incumbent LECs will be allowed to recover any such residual common line revenues through per-minute CCL charges assessed on originating access minutes. The per-minute charges shall be calculated based on forecasts of originating access minutes as currently provided in our rules.[122]

100. We generally will not permit incumbent LECs to recover residual common line revenues through per-minute CCL charges assessed on terminating access minutes, because terminating minutes are not likely to be subject to as much competitive pressure as originating access minutes. As discussed in Section III.D, below, we are similarly adopting a rule that requires that incumbent LECs be allowed to recover certain residual transport interconnection charge costs through access charges assessed on originating minutes. In placing these various residual costs on originating minutes only, however, we do not want to destroy the salutary effects of our access charge reforms by creating higher prices for originating minutes than exist under our current access charge rules. To the extent, therefore, that the sum of local switching charges, the per-minute CCL charge, the per-minute residual TIC, and any per-minute charges related to marketing expenses[123] exceed the current sum of local switching charges and the per-minute CCL charge and TIC assessed on originating minutes, the excess may be recovered through charges assessed on terminating minutes. We emphasize that any such amounts recovered through charges assessed on terminating minutes would be temporary and would be phased out as the non-primary residential SLC ceilings and the PICC ceilings are adjusted, and in any event, no later than July 1, 2000.

101. Beginning January 1, 1999, the PICC will be adjusted for inflation and will increase by a maximum of $1.00 per year for non-primary residential lines and $1.50 per year for multi-line business lines, until incumbent LECs recover all their permitted common line

[121] As discussed in Sections III.D and IV.D, price cap LECs may also recover residual TIC revenues and certain marketing expenses through PICCs on non-primary residential and multi-line business lines, subject to the ceilings described below.

[122] 47 C.F.R. § 69.105.

[123] *See* Section IV.D, below.

revenues through a combination of flat-rated SLC and PICCs. These increases will cease as the PICCs on primary residential and single-line business lines recover more of the common line revenues permitted under price cap rules. In addition, as the incumbent price cap LECs increase their PICCs for primary residential and single-line business lines, they shall reduce the amount recovered from the residual per-minute CCL charges and reduce their PICCs on non-primary residential and multi-line business lines by a corresponding amount in accordance with the procedures described below. While the plan we adopt today does not eliminate, even on a flat-rated basis, transitional higher rates for business users, it redistributes collection from a very few high-volume users to business users generally. This will permit the charges to be sustainable while we finish refining access charges and implement a forward-looking cost-based universal service mechanism for rural, insular, and high cost areas. We also acknowledge that our plan will require customers with multiple telephone lines to contribute, for a limited period, to the recovery of common line costs that incumbent LECs incur to serve single-line customers. We conclude that this aspect of the plan is a reasonable measure to avoid an adverse impact on residential customers.

102. As the PICC ceilings on primary residential and single-line business lines increase, the residual per-minute CCL charge will decrease until it is eliminated. After the residual per-minute CCL is eliminated, incumbent LECs shall make further reductions due to the increase in the PICC ceilings for primary residential and single-line business lines, first to the PICCs on multi-line business lines until the flat-rated PICCs for those lines are equal to the flat-rated PICCs for non-primary residential lines. Thereafter, incumbent LECs shall apply the annual reductions to both classes of customers equally until the combined SLC and PICCs for primary residential and single-line business lines recover the full average per-line common line revenues permitted under our price cap rules, and the additional flat-rated PICCs on non-primary residential and multi-line business lines no longer recover common line revenues.[124] If the incumbent LEC's per-line common line revenues permitted by our price cap rules exceed the SLC ceiling for non-primary residential lines and multi-line businesses, the flat-rated charges will continue to apply to those lines so that the sum of the SLCs and flat-rated charges is equal to the permitted common line revenues. Once the multi-line PICC no longer recovers any common line revenues, the calculation of the SLC will be changed from the average per-line interstate allocation of revenue requirement[125] to the average per-line common line revenues permitted by our current price cap rules. With this change, the LEC will not be able to recover more than the average per-line common line revenues permitted under our price cap rules from any access line. We note that at least one party contends that

[124] As discussed in Sections III.D and IV.D, below, the PICC will recover TIC revenues and certain marketing expenses in addition to common line revenues. Therefore, multi-line PICCs may continue to recover non-common line revenues, even though SLCs and PICCs for primary residential and single-line business lines recover the average per-line common line revenues permitted under our price cap rules.

[125] 47 C.F.R. § 69.104(c)

under our current rules, certain price cap carriers could be required to charge negative carrier common line charges, if the revenues recovered through the SLC, which continues to be developed on a cost-of-service basis, exceed the PCI for the common line basket.[126] This adjustment to the calculation of the SLC will solve any such problem.

103. We are concerned that assessing PICCs on multi-line business lines may create an artificial and undue incentive for some multi-line customers to convert from switched access to special access to avoid the multi-line PICC charges. A migration of multi-line customers to special access could significantly reduce the amount of revenue that could be recovered through per-minute charges, and would result in higher PICCs for the non-primary residential and multi-line business lines remaining on the switched network. We tentatively conclude that we should therefore apply PICCs to purchasers of special access lines as well. The NPRM, however, may not have provided sufficient notice to interested parties that we might apply certain rate structure modifications to special access lines. We therefore seek comment on this issue in Section VII.A, below.

104. We reject claims that a flat-rated, per-line recovery mechanism assessed on IXCs would be inconsistent with section 254(b)[127] which requires "equitable and nondiscriminatory contribution to universal service" by all telecommunications providers.[128] The PICC is not a universal service mechanism, but rather a flat-rated charge that recovers local loop costs in a cost-causative manner. Numerous commenters responding to the NPRM support a flat-rated cost recovery mechanism,[129] and we conclude that the PICC is preferable to the other proposals made in the NPRM. We agree with MCI and the Minnesota Independent Coalition that proposals based on the number of trunks or ports that an IXC purchases from the incumbent LEC may encourage IXCs to use fewer trunks or ports than are needed and thereby

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[126] *See* Letter from Albert Shuldiner, Counsel for Aliant Communications Co. to William F. Caton, Acting Secretary, FCC, April 30, 1997.

[127] 47 U.S.C. § 254(b).

[128] Sprint Comments at 15-16; AT&T Reply at 28-29.

[129] *See, e.g.,* United States Telephone Association (USTA) Comments at 55-56; BA/NYNEX Comments at 35-36; BellSouth Comments at 68, Reply at 10-11; PacTel Comments at 64, Reply at 21; U S West Comments at 54; Citizens Utilities Comments at 27-28; Roseville Telephone Company (Roseville Tel.) Comments at 4, 8; Rural Tel. Coalition Comments at 6, Reply at 9; Competitive Telecommunications Association (CompTel) Comments at 29; Cable and Wireless, Inc. (Cable & Wireless) Comments at 10; Excel Telecommunications, Inc. (Excel) Comments at 11; LCI International Telecom Corp. (LCI) Comments at 20-21, Reply at 6; MCI Telecommunications Corporation (MCI) Comments at 77; Public Service Commission of the District of Columbia (District of Columbia Commission) Comments at 3-4; South Dakota Public Utilities Commission (South Dakota Commission) Comments at 3; National Association of Regulatory Utility Commissioners (NARUC) Comments at 13; National Cable Telephone Association, Inc. (NCTA) Comments at 26; American Communications Services, Inc. Reply at 17.

have an adverse effect on service quality. We decline to adopt the bulk billing approach set out in the NPRM, as well as Ameritech's proposed Loop/Port Recovery charge and the approach proposed by the Competition Policy Institute, because these mechanisms are substantially affected by usage and do not reflect the NTS manner in which common line costs are incurred. The Alliance for Public Technology's proposed "facilities charge," which is a hybrid system that accounts both for level of use and intensity of use by all telecommunication carriers that use the local network, is flawed because it is based partly on usage and is complex and administratively burdensome. A cost-recovery mechanism that recovers common line costs through flat-rated charges imposed on end-user customers and IXCs is an administratively simple mechanism. Further, under our plan, interstate common line access charges will become more closely aligned with allocated interstate costs than they would be under any of the alternative proposals.

105. The plan we describe above should move us from the pricing scheme that has been in place for more than a decade to a flat-rated pricing scheme that seeks to promote competition, while balancing universal service considerations. We recognize that the modifications we adopt in this Order do not eliminate all the existing support flows. The modifications, however, do move to eliminate subsidies built into the current rate structure, to an extent that is compatible with preserving the universal service goals of providing support to primary residential and single-line business and to customers in high-cost areas pursuant to the mandate of section 254. As we set final support levels for universal service, address any legal issues related to the transition from embedded to forward-looking economic costs, and factor in the development of competition, we will identify and deal with any remaining legal issues relating to the recovery of these revenues. In addition, the plan we are adopting allows incumbent price cap LECs to recover costs in the manner that reflects the way in which they are incurred. We believe that this realignment of rates with costs will reduce the per-minute access charges assessed on IXCs and benefit consumers through lower long-distance rates, as well as create a pro-competitive local exchange market in which LECs will be able to compete more efficiently.

4. Common Line PCI Formula

a. Background

106. When we adopted price cap regulation in 1990, we established a separate common line basket in order to balance the price cap goal of economically efficient prices with important goals, such as universal service, that were reflected in common line rates prior to the adoption of price caps. Because common line costs are non-traffic sensitive, growth in demand leads to a reduction in average per-minute common line charges. Therefore, in the *LEC Price Cap Order*, we established a price cap index ("PCI") formula for the price cap basket that differed from the PCI formula we established for the other three baskets, to ensure

that carrier common line charges declined as common line demand increased.[130] Specifically, we added a term, "g/2," to the common line PCI formula, to represent half the growth in demand per line in the prior year.[131] This adjustment was made because we originally concluded that both LECs and IXCs have the ability to influence common line growth, and that both LECs and IXCs should benefit from increases in demand.[132]

107. In the *LEC Price Cap Performance Review*, we found that incumbent LECs in fact have little influence over per-minute common line demand, and tentatively concluded that we should remove the "g" term from the common line formula,[133] because including an industry-wide moving average X-Factor in the common line formula might tend to double-count demand growth. We sought comment, in the *Price Cap Fourth Further NPRM*, whether to apply the same PCI formula to the common line basket that we use for the other baskets if we were to adopt a TFP-based X-Factor.[134] We also invited comment on whether we could eliminate g/2 from the common line formula if we retain a separate common line formula.[135] In this Order, we adopt a plan that should quickly convert the CCL charge from a per-minute charge to a flat-rated per-line charge assessed on interexchange carriers. We also revise the common line formula to reflect the phase out of the CCL charge.

b. Discussion

108. We conclude that the separate common line PCI formula should be eliminated, and that the PCI formula for the traffic-sensitive and trunking baskets should be used for the common line basket, once traffic-sensitive CCL charges have been eliminated. In this Order, we have reduced substantially traffic-sensitive CCL charges, and replaced them with the per-line PICC. The remaining traffic-sensitive CCL charges imposed by incumbent price cap LECs will be reduced and then eliminated over the next two or three years. Once common line costs are recovered solely through per-line charges, increased minutes will not affect

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[130] *LEC Price Cap Order*, 5 FCC Rcd at 6793, 6795.

[131] *LEC Price Cap Order*, 5 FCC Rcd at 6795. The Commission did not adopt a common line formula based on an average of the per-line and per-minute approaches, because in some circumstances, this would have produced the anomalous result of CCL rates increasing in response to increases in demand. *Id.* at 6795. The mathematics of the common line formula are explained in detail in Appendix E of the *LEC Price Cap Order*, 5 FCC Rcd at 6942-44.

[132] *LEC Price Cap Order*, 5 FCC Rcd at 6795.

[133] *LEC Price Cap Performance Review*, 10 FCC Rcd at 9079.

[134] *Id.* at 13680.

[135] *Price Cap Fourth Further NPRM*, 10 FCC Rcd at 1368.

common line recovery. Therefore, when the traffic-sensitive CCL charges have been eliminated, it will no longer be necessary to ensure that CCL rates decline as per-minute demand increases. Incumbent price cap LECs that no longer assess per-minute CCL charges will use the same PCI formula for the common line basket as they use for the traffic-sensitive and trunking baskets.

109. In the *LEC Price Cap Order*, we established "g/2" as the common line PCI formula because we believed that because both LECs and IXCs contributed to encouraging common line demand growth, both LECs and IXCs should share in the benefits of common line demand growth.[136] In the *LEC Price Cap Performance Review,* we tentatively concluded that IXCs contributed more to common line demand growth, but declined to revise the common line formula at that time because we were contemplating eliminating the common line PCI formula completely, and because we did not wish to create unnecessary rate churn.[137] To avoid unnecessary rate churn here, we decide to retain "g/2" while carriers continue to charge per-minute CCL charges.

110. We revise sections 61.45(c) and 61.46(d), which govern the common line PCI and API, respectively, to reflect our revisions to the common line rate structure in the common line PCI formula. First, we redesignate section 61.45(c) as 61.45(c)(1) and adopt a new section 61.45(c)(2) that requires price cap LECs to use the separate common line formula only while they continue to charge per-minute CCL charges. Section 61.45(c)(2) also states that the common line PCI will be governed by the same PCI formula LECs use for the traffic-sensitive and trunking baskets. Second, we redesignate section 61.46(d) as 61.46(d)(1), and amend section 61.46(d)(1) to recognize that LECs now impose PICC charges as well as CCL charges on IXCs. We also adopt a new section 61.46(d)(2) to govern PICC charges once per-minute CCL charges have been phased out. These revisions are set forth in Appendix C of this Order.

[136] *LEC Price Cap Order,* 5 FCC Rcd at 6795.

[137] *LEC Price Cap Performance Review*, 10 FCC Rcd. at 9079-80.

5. Assessment of SLCs and PICCs on Derived Channels

a. Background

111. Integrated services digital network (ISDN) services permit digital transmission over ordinary local loops through the use of advanced hardware and software.[138] ISDN offers data transmission at higher speeds and with greater reliability than standard analog service. Most incumbent LECs currently offer two types of ISDN service, Basic Rate Interface (BRI) service and Primary Rate Interface (PRI) service. BRI service allows a subscriber to obtain two voice-grade-equivalent channels and a signalling/data channel over an ordinary local loop, which generally is provided over a single twisted pair of copper wires.[139] PRI service allows subscribers to obtain 23 voice-grade-equivalent channels and one data signalling channel over two pairs of twisted copper wires.[140] BRI service generally is used by individuals and small businesses, and PRI service generally is used by larger businesses. LEC services other than ISDN use derived channel technology to provide multiple channels over a single facility.[141] The LECs also use derived channel technologies within their networks, for example, to provide customers with individual local loops. In such situations, the end user has not generally requested derived channel service and thus most likely is not aware that the LEC is using this technology.

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[138] In order for a LEC to provide ISDN, it must have a digital switch in the central office serving the customer, and substitute an ISDN line or trunk card for the standard cards that would otherwise be used in the central office with the loop facilities serving the customer. The customer also must use special ISDN-capable customer premises equipment.

[139] The two voice-grade-equivalent channels, which are called bearer or B channels, can be used for voice local exchange service or for data transmission at speeds up to 64 kbps. The third channel is a 16 kbps data channel, called the delta or D channel, which is used for signalling and packet data services. The Bell Atlantic Telephone Companies Petition for Waiver of Section 69.104 of the Commission's Rules in Connection with ISDN Services (filed Feb. 10, 1995) at 4 n.8 (*Bell Atlantic Waiver Petition*).

[140] In the case of PRI ISDN, the 23 B channels and the D channel can transmit voice or data at speeds up to 64 kbps. When a customer has more than one PRI connection at a given location, all of the B channels can share a single D channel, permitting the customer to obtain 24 voice-grade-equivalent channels for each PRI connection after the first one. *Bell Atlantic Waiver Petition* at 4, n.8

[141] For example, NYNEX Telephone Companies (NYNEX) uses derived channel technology to provide FLEXPATH service, which provides a customer with 24 digital voice-grade-equivalent trunk channels over a T-1 facility between a suitably equipped central office and a digital PBX. PBX Conversion Service, another NYNEX offering, provides digital trunking capability, with up to 24 trunk access lines, between a customer's digital PBX and an analog-to-digital interface located at the central office switch. NYNEX's Data Over Voice service provides customers with a voice-grade channel and a data channel over a single copper pair. Memorandum Opinion and Order, NYNEX Telephone Companies Revisions to Tariff F.C.C. No. 1, 7 FCC Rcd 7938 n.11 (Com. Car. Bur. 1992), *aff'd on recon.*, 10 FCC Rcd 2247 (1995). Several other LECs provide similar services using derived channel technology. *See, e.g.*, Cincinnati Bell Comments at 6.

112. On May 30, 1995, we released a Notice of Proposed Rulemaking seeking comment on the application of SLCs to ISDN and other derived channel services.[142] In that NPRM, we noted that our current rules, which assess one SLC per derived channel, may discourage efficient use of ISDN services,[143] and we sought comment on several options, ranging from continuation of the current rules applying one SLC to each derived channel to requiring LECs to assess one SLC per each pair of copper wires or each physical facility.[144] Other options presented in the NPRM included: (1) basing the application of SLCs on a ratio of the average LEC cost of providing a derived channel service, including the trunk or line card costs, to the average cost of providing an ordinary local loop or T-1 facility; (2) applying one SLC for every two derived channels; (3) reducing the number of SLCs applied to derived channel services while increasing slightly the SLC rates; or (4) giving LECs flexibility concerning the number of SLCs they assess for derived channel services, at the same time adjusting the price cap rules to prevent an increase in CCL charges.[145]

113. In addition to the comments filed in response to the ISDN SLC NPRM, several BOCs provided data on the relative NTS costs of single and derived channel services.[146] The cost data included information about all NTS cost components, including components located in the central office, such as line cards. As shown in Table 1 below, the cost data indicates that the ratio of NTS loop costs of BRI ISDN to standard analog service is approximately 1 to 1. The ratio of NTS loop costs of PRI ISDN to standard analog service, excluding NYNEX's

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[142] End User Common Line Charges, CC Docket No. 95-72, Notice of Proposed Rulemaking, 10 FCC Rcd 8565 (1995) (*ISDN SLC NPRM*).

[143] Section 69.104 of the Commission's rules, 47 C.F.R. § 69.104, provides for a monthly per line charge for end users that subscribe to local exchange service, stating that surcharges shall be assessed for each line between the customer's premises and a Class 5 Office that is or may be used for local exchange transmissions. In 1992, NYNEX which had been charging a SLC for each of the voice-grade-equivalent channels provided on a T-1 facility, filed a tariff in which it proposed to assess only one SLC for each T-1 facility used to provide a customer with certain services, even though the T-1 facility provided that customer with up to 24 voice-grade-equivalent channels. The Common Carrier rejected the Transmittal, finding that it did not comply with the commission's Part 69 rules governing assessment of SLCs. The Commission affirmed the Bureau's conclusion that Section 69.104 of the rules requires assessment of a SLC for each derived channel. Memorandum Opinion and Order, NYNEX Telephone Companies Revisions to Tariff F.C.C. No. 1, 7 FCC Rcd 7938, ¶ 2 (Com. Car. Bur. 1992) *aff'd on recon.*, 10 FCC Rcd 2247 (1995).

[144] *ISDN SLC NPRM* at ¶ 21.

[145] *Id.* at ¶¶ 22-23, 27-30, 32-34.

[146] In their responses, three of the BOCs, BellSouth, NYNEX, and Southwestern Bell, asked for confidential treatment of portions of the information submitted. NYNEX publicly filed the information we requested, but submitted as confidential additional information that contained more detailed cost data. The confidential data were not necessary to perform our analysis, and the following tables only include data that was filed on the public record. We have returned to the respective companies data for which confidential treatment was sought.