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Before the
FEDERAL COMMUNICATIONS COMMISSION
Washington, D. C. 20554

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OFFICE OF THE SECRETARY

In the Matter of	)	
	)	
Tariffs Implementing	)	CC Docket No. 97-250
Access Charge Reform	)	
	)	

DIRECT CASE

BELLSOUTH TELECOMMUNICATIONS, INC.

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Date: February 27, 1998

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SUMMARY

In this proceeding, the Commission is investigating the access reform tariff filings of various LECs. For BellSouth, the items subject to investigation are the primary and non-primary residential line definitions and counts; the methodology used to identify exogenous cost change amounts; the methodology used to allocate the COE and Marketing expense changes to baskets and service categories; the recalculation of tandem-switched transport rates and the exogenous change associated therewith; and the allocation of the Universal Service Fund exogenous cost change to the related baskets and service categories. In this Direct Case, BellSouth demonstrates that its filings, including the definitions and methodologies under investigation, are reasonable and appropriate and that the Commission should not require BellSouth to make the revisions it tentatively has concluded should be required.

The Access Reform rule changes, and the work effort underlying their implementation, have been massive. Although the Commission's Access Reform Order established new rules, in many areas the Commission left LECs free to implement those rules without specific, detailed guidance. This is particularly the case with respect to the definitions of primary and non-primary line counts. As BellSouth discusses herein, BellSouth utilized, for the purpose of its Access Reform tariff filing, the only definitions it could administer by the January 1, 1998 deadline. While these definitions were not the ones which BellSouth preferred, they are reasonable and implementable. Given the confusion within the industry and among customers regarding the distinction which the Commission's new rules make between primary and non-primary lines, however, BellSouth urges the Commission, in its Defining Primary Lines proceeding, to abandon

the distinction. In the meantime, LECs, such as BellSouth, which have adopted reasonable definitions should be permitted to retain them without further revision pending withdrawal of the rule. With regard to non-primary line counts, BellSouth shows that its quantities are within the range which the Commission expected based upon published estimates. BellSouth demonstrates that the difference in the Commission's calculation from BellSouth's filing and the published data results from the use of different comparisons and time periods.

The Commission likewise should permit BellSouth's exogenous cost amounts to stand as identified by BellSouth. The Commission did not require that any particular methodology be used for identifying such costs, except in the few instances cited, and BellSouth followed a reasonable approach, based upon historical precedence, for their quantification. Where the Commission did specify a particular methodology, BellSouth followed those requirements.

For the allocation of the exogenous costs associated with COE maintenance and Marketing expenses, BellSouth demonstrates that it performed the requisite allocations in accordance with the Commission's directives. For the trunking basket change, Marketing expenses appropriately were removed from those services other than special access, and the exogenous cost change was allocated based upon the percentage of switched transport revenues in the service bands. For the COE change, BellSouth properly allocated the change based upon the Commission-approved TRP methodology. The Commission's tentative conclusion that such changes should have been allocated to the TIC based upon the June 30, 1997 TIC rather than the existing TIC defies the traditional TRP methodology, which relies upon existing revenues -- not earlier revenues-- and the Commission should not penalize LECs retroactively for not having followed a new procedure which it now, for the first time, contemplates.

For the tandem-switched transport recalculation, BellSouth shows that it properly recalculated the rates. The Commission's concern that only the circuit loadings, and not the copper-fiber ratios or DS3 and DS1 rates, should have been changed is without merit. Indeed, BellSouth's revision of such ratios and rates had virtually no effect on the resulting tandem-switched transport rates. Rather, the removal of a multiplexer from the existing tandem-switched transport rates and the creation of the new multiplexer rate element using that multiplexer as well as an additional multiplexer from the TIC had a much greater rate impact. The impact of the recalculation was not to increase the TIC as the Commission fears, but was just the opposite, as BellSouth fully demonstrates.

Finally, BellSouth shows that it properly allocated the USF exogenous cost change to the various baskets and service categories which generate end user revenues. BellSouth explains that the difference in the proportions shown in its tariff filing and those obtained from its Form 457, Universal Service Worksheet, are the result of different time periods as well as an erroneous assumption used when completing the worksheet which will be corrected.

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Access Charge Reform	)	
	)	

DIRECT CASE

BellSouth Telecommunications, Inc. ("BellSouth") hereby submits its Direct Case in the above-captioned investigation regarding the recent access reform tariff filings of several local exchange carriers ("LECs") made in compliance with the Commission's Access Reform Order, the 1997 Annual Filing Investigation Order, the GSF Order and the USF Contribution Revision Order.[1]

The Commission is investigating a variety of issues it believes to have been raised by these filings. Two tariff transmittals filed by BellSouth are at issue: Transmittal No. 434, filed November 26, 1997, and Transmittal No. 435, filed December 17, 1997. The Commission's

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[1] In the Matter of Access Charge Reform, Price Cap Performance Review for Local Exchange Carriers, Transport Rate Structure and Pricing, End User Common Line Charges, CC Docket Nos. 96-262, 94-1, 91-213, 95-72, *First Report and Order*, 12 FCC Rcd 15982 (1997) ("Access Reform Order"); In the Matter of 1997 Annual Access Tariff Filings, CC Docket No. 97-149, *Memorandum Opinion and Order* (FCC 97-403), released December 1, 1997 ("1997 Annual Filing Investigation Order"); In the Matter of Access Charge Reform, Transport Rate Structure and Pricing, CC Docket Nos. 96-262 and 91-213, *Third Report and Order* (FCC 97-401), released November 26, 1997 ("GSF Order"); In the Matter of Federal-State Joint Board on Universal Service, CC Docket No. 96-45, *Third Order on Reconsideration* (FCC 97-411), released December 16, 1997 ("USF Contribution Revision Order").

Access Reform Suspension Order suspended the filed tariff pages and allowed them to take effect on January 1, 1998 subject to an accounting requirement.[2]

The Commission's Designation Order[3] requires the LECs whose tariffs are subject to this investigation to respond to various designated issues in their Direct Cases to be filed on this date. In the sections which follow, BellSouth responds to those issues which relate to its Transmittal Nos. 434 and 435. BellSouth demonstrates that its filings, including the definitions and methodologies under investigation, are reasonable and appropriate and that the Commission should not require BellSouth to make the revisions it tentatively has concluded should be required.

I. COMMON LINE ISSUES

The Commission is investigating the definitions used by several price cap LECs for primary and non-primary residential lines as well as the line counts shown by all price cap LECs subject to this investigation. These are discussed in sections I.A. and B. below.

As a preliminary matter, BellSouth notes that the Commission's requirement that residential local exchange service lines be delineated into primary lines and non-primary lines, for purposes of the application of subscriber line charges ("SLC") and the Presubscribed Interexchange Carrier Charges ("PICC"),[4] has caused substantial confusion within the industry.

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[2] In the Matter of Tariffs Implementing Access Charge Reform, CC Docket No. 97-250, *Memorandum Opinion and Order* (DA 97-2724), released December 30, 1997 ("Suspension Order").

[3] In the Matter of Tariffs Implementing Access Charge Reform, CC Docket No. 97-250, *Order Designating Issues for Investigation and Order on Reconsideration* (DA 98-151), released January 28, 1998 ("Designation Order").

[4] 47 C.F.R. Sections 69.152 and 69.153.

especially among customers. Contributing to this confusion is not only the fact that both the primary/non-primary distinction and the PICC charges are new, but also the fact that the Commission has not established a definition of primary and non-primary lines to be used by the industry as a whole.

Several parties have urged the Commission to revise its rules and abandon the notion that primary and non-primary lines should receive different treatment for purposes of the SLC and PICC charges.[5] BellSouth agrees, and urges the Commission to do so as a part of its Defining Primary Lines NPRM proceeding. As will be seen from the discussion below in Section I.A. of this Direct Case, BellSouth presently distinguishes between primary and non-primary lines using the only criteria which it could implement in time for the January 1, 1998 effective date of the new rules. The basis for the distinction is grounded in certain technical arrangements which are embedded in BellSouth's network and billing systems arrangements which provide for designation of the facilities associated with one line at any given residential premises as the primary line. While this definition is a reasonable and implementable one, customers are confused by the change in the applicable charges resulting from the Commission's new rules.

In the Defining Primary Lines NPRM proceeding, BellSouth advocated that the Commission adopt a different definition of primary and non-primary lines.[6] BellSouth supported a definition which would permit each subscriber to a residential local exchange service at a service address to obtain a primary line from any given telephone company. If a subscriber with a

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5 In the Matter of Defining Primary Lines, CC Docket No. 97-181, *Notice of Proposed Rulemaking*, 12 FCC Rcd 13647 (1997), ("Defining Primary Lines NPRM"), Comments of Sprint, filed on September 25, 1997, and Reply Comments of AT&T, filed October 6, 1997.

6 Defining Primary Lines NPRM, BellSouth Comments filed September 25, 1997 at 6-7.

primary residential line at a service address obtained an additional residential local exchange service at that address from the same telephone company, the additional service would be that subscriber's additional line for purposes of SLC and PICC charges. Because of the considerable records and systems modifications that would be required, BellSouth emphasized that it would not be able to implement this definition until six months after adopted by the Commission, due to the fundamental changes in its systems and procedures which would be required. This is still the case.

While either of these definitions distinguishing primary and non-primary lines are reasonable, BellSouth now urges the Commission to abandon the notion that any distinction should be made in the first place. In this manner, the substantial customer confusion regarding the difference in treatment of residential lines would be abated. In addition, both LECs as well as interexchange carriers (who desired to pass on the PICC charges to their customers on a per-line basis) would no longer have the tedious task of tracking which charge applies to which line for which customer. The Commission should establish uniform, SLC charges for all residential lines. In addition, the PICC charges should be the same for all residential and business lines other than ISDN.

In the following subsections of this Direct Case, BellSouth discusses the specific issues which the Commission has designated for investigation regarding line definitions and line counts.

A. Primary and Non-primary Residential Line Definitions

The Commission is investigating the reasonableness of definitions used by certain LECs, including BellSouth, in their Access Reform tariff filings in the absence of a Commission-prescribed definition, and the consistency with which the LEC applied its definition. Tentatively concluding that BellSouth's primary line definition is unreasonable and "circular[]," the Commission requires BellSouth to explain the definition and any assumptions underlying it and to submit revisions if necessary.[7]

As the Commission observes, BellSouth included, in the definitions section of its tariff, the following definitions:

> Primary Residential Local Exchange Service Line or Trunk -- This term denotes the Residential Local Exchange Service line or trunk provided by the Telephone Company or a reseller of Telephone Company-provided local exchange service lines or trunks which is assessed the Primary Residential PICC or EUCL Charge.[8]
>
> Additional Residential Local Exchange Service Line or Trunk -- This term denotes a local exchange service line or trunk provided by the Telephone Company or a reseller of Telephone Company-provided local exchange service lines or trunks at a residential premises to which the Additional Residential Local Exchange Service Line or Trunk PICC or EUCL charge applies.[9]

BellSouth's tariff also provided further delineation between primary and non-primary lines in Section 4 thereof. The tariff states as follows:

> When an end user is provided local exchange residence service by the Telephone Company,...the Primary Residential EUCL Charge as set forth in 4.7(A)(1) will apply to one local exchange residence line at the premises. Each additional local exchange

7 Designation Order, para. 15.

8 Transmittal No. 434, Section 2.6, page 2-67.

9 Transmittal No. 434, Section 2.6, page 2-50.

residence line at the same premises will be billed at the Additional Residential EUCL Charge as set forth in 4.7(A)(2)....[10]

BellSouth believes that this definition provides a reasonable distinction between primary and non-primary residential lines and applies the primary and non-primary residential line charge. The primary line charge applies to one line at the premises and the non-primary line charge applies to all other lines at the premises. No further explanation as to which lines receive primary treatment and which are non-primary is necessary.

However, in order to provide further clarification and detail, BellSouth offers the following revised definitions:

> Primary Residential Local Exchange Service ("Primary Residential Line"). This term denotes the earliest ordered Residential Local Exchange Service ("residential line") provided by the Telephone Company or a reseller of a Telephone Company-provided residential line at an end user's residential premises. In the case that multiple residential lines are ordered at the same time at a residential premises without existing residential lines, the Primary Residential Line is that residential line to which the first telephone number is assigned. The Primary Residential Line PICC or EUCL charge is assessed to the Primary Residential Line. In the event that the Primary Residential Line is disconnected, the associated facilities will continue to be deemed the Primary Residential Line until a new or remaining subscriber contacts the Telephone Company and requests either 1) new residential local exchange service at that premises, in which case when the new service is established the Primary Residential Line facilities will be used and the new service will be considered to be the Primary Residential Line; or 2) that its existing residential line service be given the Primary Residential Line treatment, in which case that existing service will be deemed to be the Primary Residential Line rather than an Additional Residential Line; whichever of these two events occurs earlier.[11]

[10] Transmittal No. 434, Section 4.6(J), page 4-4. The rate set forth in Section 4.7(A)(1) is the rate for "Primary Residential Local Exchange Service line or trunk" of $3.50, and the rate set forth in Section 4.7(A)(2) is the rate for "Additional Residential Local Exchange Service line or trunk" of $5.00. Transmittal No. 434, page 4-6.

[11] The new provision contained in this last sentence is included to reflect the fact that BellSouth's systems are unable to recognize the involved Additional Residential Lines at the time of the disconnection of a Primary Residential Line belonging to another subscriber at the same premises. BellSouth is currently attempting to determine the costs to modify its systems to eliminate this problem, but believes that such modifications may not be needed in the event that the Commission in the Defining Primary Lines proceeding prescribes definitions of Primary and

Additional Residential Local Exchange Service ("Additional Residential Line"). This term denotes any residential local exchange service ("residential line") provided by the Telephone company or a reseller of Telephone Company-provided residential line at a residential premises other than the Primary Residential Line, as defined above. The Additional Residential Local Exchange Service Line or Trunk PICC and EUCL charges applies to such residential lines.

For purposes of the above definitions, the following apply:

1) a residential premises is an individual residential service address within a building; provided, however, that college, university or school dormitories served by central office-based (e.g., CENTREX) local exchange service shall be considered residential premises.[12]

2) ISDN local exchange service is not considered to be a Primary Residential or Additional Residential Line for the purpose of the application of EUCL or PICC charges.[13]

3) Central office-based (e.g., CENTREX) local exchange services provided to college, university or school dormitories are considered to be Primary Residential Lines.[14]

As can be seen, these definitions necessarily involve both definitional and rate regulation aspects. Therefore, should the Commission require BellSouth to revise its tariff to include these provisions, BellSouth would at that time determine the proper placement within its various

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Additional Residential Lines which are different than those in use by BellSouth at the present time or eliminates the distinction altogether.

12 See Transmittal No. 434, Tariff Section 2.6, Definitions, "Premises," and Sections 3.8.6 and 4.6(C)(4). Under BellSouth's local exchange service tariffs, central office-based local exchange services provided to college, university or school dormitories are considered to be residential lines for this purpose. The Commission has recognized that a determination of the residential or non-residential status of a service is a state matter. 47 C.F.R. Section 69.152(g).

13 The Commission's rules establish separate caps for SLC and PICC charges for ISDN local exchange services. 47 C.F.R. Section 69.152(l) and 69.153(f).

14 See n. 12, supra.

related tariff provisions as well as the appropriate true-up of existing tariff provisions as necessary.

Although BellSouth believes that revisions to its present tariff definitions should not be required, it is true that the foregoing definitions provide a more detailed description of the manner in which BellSouth identifies primary and non-primary lines. As indicated above, these are the only definitions which BellSouth could implement by January 1, 1998. BellSouth historically has identified additional lines installed subsequent to the first line at a residential premises,[15] by use of the Additional Line ("ADL") Field Identifier ("FID"). As it was, BellSouth underwent a major effort to confirm the accuracy of the ADL FID designation in preparation for the Access Reform filings under investigation here, and this resulted in the true-up described in BellSouth's Reply to petitions filed against its Transmittal No. 434[16] and the correction made in Transmittal No. 435.[17]

To the extent that the Commission leans toward requiring BellSouth to revise its definition of primary and non-primary lines to an entirely different means of distinguishing the two, it should bear several points in mind. First, BellSouth would not be able to implement any other definition immediately, but would require six months at a minimum. Second, if anything, the Commission should abandon the notion that any distinction would benefit either subscribers, carriers or the public interest and, as such, it should permit LECs to treat all residential lines in

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15 Or in the case of multiple lines ordered at the same time at a premises without any residential local exchange service, the additional lines would be the lines other than the one to which a telephone number was first assigned.

16 BellSouth Reply, filed December 17, 1997, p. 8.

17 Transmittal No. 435, Description and Justification, at 1-2.

like manner. Third, the Commission should not penalize LECs such as BellSouth for having adopted definitions other than that which the Commission may eventually adopt, if it pursues the course of distinguishing the two types of lines. Given that the Commission had not prescribed a definition for use in LECs' access reform filings and given the limited time in which BellSouth had to implement any definition of the new access reform rules, BellSouth had no choice but to adopt for purposes of its access reform filing the only definition which it could implement. BellSouth's filed definition, in fact, is a reasonable, implementable definition under the circumstances.[18] The Commission cannot overlook the fact that the reasonableness standard embraces a range of permissible outcomes. Merely because the Commission could devise an alternative means of delineating primary and non-primary lines does not invalidate BellSouth's tariff. The fact of the matter is that BellSouth's tariff is not inconsistent with any Commission rule and is nondiscriminatory in application. These are the essential characteristics of a reasonable tariff, and accordingly the Commission should find BellSouth's tariff to be reasonable.

B. Primary and Non-Primary Residential Line Counts

As to line counts, the Commission observes that non-primary residential line counts are lower than "various published estimates and LEC public statements regarding the growth of second line penetration."[19] It suggests that LECs may have under-identified non-primary lines

[18] In a conference call between United States Telephone Association and FCC Common Carrier Bureau Competitive Pricing Division staff members, James Schlichting, Judy Nitsche and Rich Lerner, these staff members advised that a premise-based definition (first line at a premise as primary and additional lines at the same premise as non-primary) would be an acceptable definition.

[19] Designation Order, para. 16.

either due to definitional problems or because their definitions were not applied in a reasonable manner. The Commission requires each price cap LEC to identify the number of primary residential, single-line business, non-primary residential and BRI ISDN lines and to complete the worksheets provided in Appendix B of the Designation Order.

As a preliminary matter, the Commission is correct in its observation that the publicized non-primary percentages to which the Commission refers and the percentages obtainable from BellSouth's filing are different. This is because the percentages which the Commission has calculated and the other percentages to which it refers are based upon different comparisons as well as data from different time periods. The percentage which the Commission has calculated from BellSouth's filing, 8.7%,[20] is based upon the ratio of non-primary residential and BRI ISDN to all residential and single line business lines. In contrast, the percentages which BellSouth releases to the public are generally based upon the ratio of non-primary lines to primary lines in an attempt to approximate the percentage of residential customers with additional residential lines. Additionally, the 8.7% calculated by the Commission from BellSouth's filing is based upon annualized 1996 line counts, i.e., averaged 1996 counts, whereas the publicly released data to which the Commission presumably refers in comparison is based upon late calendar year 1997 data.[21] Using the Commission's calculation methodology and end of 1997 line count data, the BellSouth percentage of non-primary residential and BRI-ISDN lines to the total of all residential and single line business lines is approximately 11.5%. However, the non-primary to primary

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[20] Designation Order, para. 7, Figure 1.

[21] The Designation Order, n. 40, refers to a Salomon Brothers report dated November 28, 1997. This report lists BellSouth's non-primary percentage as 14%.

ratio for BellSouth, based upon end of calendar year 1997 data, was 13.5%, a figure that would appear to be in-line with the Commission's expectations and published estimates.

In response to the Commission's specific requests for information, BellSouth is providing herewith the quantification of lines and the completed worksheets from Appendix B of the Designation Order. These are attached hereto as Appendix A.

Line counts for Primary Residential Lines, for Single Line Business Lines, for Non-Primary Residential Lines and BRI-ISDN Lines are shown in Appendix A the first column of Exhibit 1, "Quantity." This is self-explanatory. The numbers shown match the numbers from BellSouth's Transmittal No. 435.[22]

The sources from which the line count data was obtained are shown in the second column of Exhibit 1, "Sources." As can be seen, the source for all four categories was "D1" and "D3," i.e., "Billing Records" and "Specific USOC/CRIS Field Indicate (FID) or ADL designations." For Single Line Business and Non-Primary Residential Lines, BellSouth includes reference also to "D8," i.e., "Results of estimates/projections based on study." This reference was included to account for the studies performed by BellSouth to true-up its line counts to which BellSouth referred in its Reply to petitions against Transmittal No. 434,[23] and for which corrections were made in Transmittal No. 435.[24] A description of these true-ups is provided on Exhibit 1 by footnote.

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[22] Transmittal No. 435, Description and Justification, Appendix A, Workpaper DEM-4, Access Reform End User Common Lines.

[23] Transmittal No. 434 Reply at 8-9 and n. 21.

[24] Transmittal No. 435, Description and Justification at 1-2.

The next column of Exhibit 1, "Search" has to do with the method used by BellSouth to calculate the line count totals for each of the four categories. As Exhibit 1 shows, BellSouth counted individual lines for Single Line Business, Non-Primary Residential Lines, and BRI-ISDN Lines. BellSouth obtained its count of Primary Lines using method "S2." BellSouth counted total Residential Lines and subtracted from that total the total of all Non-Primary Residential Lines and BRI- ISDN Lines at residential premises.

The next column on Exhibit 1, "Collection," has to do with the level of aggregation at which the data used by BellSouth was available. For all of the four service categories, the data was available and counts were obtained on a state-level basis, thus the "C2" designation.

The next column on Exhibit 1, "Time Period," reflects the time frame that the line count represents. For BellSouth, the line count represents annualized 1996 amounts, and thus the "T2" designation.

The Commission's Appendix B worksheets also require LECs to indicate the sequence in which various criteria were used to identify lines in each of the four categories. As BellSouth's Appendix A, Exhibit 1 shows, for Primary Residential Lines and Non-Primary Residential Lines, BellSouth first used "L2," described by the Commission as "Residential/commercial address where lines are located including those separated by units, apartment, room, suite or other sub-classification for multiple unit addresses." This conforms to BellSouth's Primary and Non-Primary Lines definition which identified groupings of lines to which the first ordered would be the Primary Line and all additional would be Non-Primary Lines based upon the residential premises, including individual residential premises inside a single building. The second criteria used by BellSouth for Primary and Non-Primary Lines is "AO/R5," for a combination of "Number Codes" (date ordered or first telephone number assigned) and "Residential Lines Identifier" (the ADL FID). As has been explained previously in this Direct Case, once BellSouth identified the residential premises, it used the ADL FID to identify Non-Primary Lines, subject to BellSouth's additional investigation in which residential premises without any Primary Lines were identified and the first ordered (or, in the case of multiple lines, the first telephone number assigned) was then removed from the Non-Primary Line count and included in the Primary Line count. For dormitories served by Central Office - based services such as CENTREX, all lines are considered to be primary residential.

For Single Line Business Lines, BellSouth has indicated the first criteria to be location and, specifically, "LO" for state and "B3" for "Customer/Subscriber - Other." For BellSouth, the first criteria in determining whether a line should receive Single Line Business treatment (in lieu of multiple line business treatment) is whether or not a particular business has additional local exchange business line service from BellSouth in the same state. When a customer calls BellSouth to order business service, the service representative first checks to see if that business has other local exchange business service from BellSouth at that location. If there is, the new order would not be treated as a Single Line Business Line but rather as multi-line business service. In addition, the service representative checks to see if the business has other local exchange business service from BellSouth in the same state. If the business does, the new order would not be treated as a Single Line Business Line but rather as multi-line business service. This process necessarily involves determining the legal identity of the business and whether other businesses of the same or similar names are, in fact, the same business entity.

If the line is determined to be a Single Line Business Line, a USOC code of 9LM, for single line, is assigned as well as a business indicator. Thus, BellSouth has completed the Commission's worksheet by indicating the second criteria to be "NO" for a "Number Code" of "Other," i.e., the unique USOC code. In searching for its count of Single Line Business Lines, BellSouth has merely to search for those 9LM USOC codes which also have the business indicator.

For BRI ISDN, BellSouth shows the designation "NO" or a "Number Code[]" of "Other." For BellSouth, BRI ISDN lines are identifiable by unique USOC and service code combinations. Thus, BellSouth can obtain the count of BRI ISDN lines directly from billing records, specifically, its Customer Records Information System ("CRIS") records. No other criteria are applicable.

The final information which the Commission's Appendix B requires LECs to supply is the non-primary and primary classifications which they would apply to the example shown on page 5 of the worksheet. BellSouth provides this information in Appendix A, Exhibit 2. As can been seen, the example includes two residential premises and, thus, there are two non-primary lines, each of which is the first installed at its premises. All of the remainder of the lines are considered to be non-primary.

II. METHODOLOGY FOR CALCULATING EXOGENOUS COST CHANGES FOR LINE PORTS AND END OFFICE TRUNK PORTS

The Commission's Access Charge Reform Order required price cap LECs to remove from the Local Switching element the costs associated with line side and trunk side ports.[25]

[25] 47 C.F.R. Sections 69.106(f) and 69.306(d).

Exogenous cost adjustments were to be made to reflect these changes: downward adjustments to the traffic sensitive basket and the local switching service category; upward adjustments to the common line basket; and the creation of the new trunk port service category in the traffic sensitive basket. The Commission, noting that it has "never adopted by rulemaking a single methodology for computing exogenous cost changes that result from a reallocation of cost recovery among price cap service categories, baskets, or rate elements,"[26] seeks comments on the appropriate methodology which should have been used by LECs. The Commission tentatively concludes that the "best measure" of the costs recovered through a price cap element is revenues, not Part 69 revenue requirements, but that if revenue requirements are used, the actual basket earnings rather than an 11.25% rate of return should be used.[27]

In addition, the Commission asks whether its proposed methodology should be used for other reallocations which the Access Charge Reform Order requires, in addition to port costs. It asks parties to quantify the results of "using this method consistently for all such reallocations." It also asks parties to include a comprehensive list of all exogenous adjustments made since it entered price cap regulations "that had the purpose of reallocating costs among baskets, categories, rate elements, or between price cap and non price cap services."[28]

Finally, the Commission tentatively concludes that if costs are removed from Local Switching to Common Line based upon revenues that, nevertheless, the BFP revenue

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26 Designation Order, para. 47.

27 Designation Order, para. 48

28 Designation Order, para. 51.

requirement should be "recalculated" based on Part 69 revenue requirements "pursuant to fully-distributed embedded costs and revenue requirements."[29]

BellSouth calculated the exogenous cost changes made in the filings at issue here using two basic methodologies. Unless the Commission specified a different methodology, BellSouth utilized a revenue requirement at an 11.25% rate of return analysis.[30] Where the Commission did specify a different methodology, BellSouth followed those instructions.

The only items included in Transmittal Nos. 434 and 435 for which the Commission specified a methodology different from a revenue requirement analysis were for the exogenous cost changes associated with the remaining 80% of the tandem revenue requirement, the tandem-switched reinitialization, and equal access. For the tandem revenue requirement, BellSouth identified the amount based upon the relationship between the TIC established in its Local Transport Restructure ("LTR") filings and the LTR tandem revenue requirement.[31] For the tandem-switched reinitialization, BellSouth recalculated the associated revenues, and made exogenous changes accordingly, based upon updated factors, including the use of actual circuit loadings in lieu of the assumed 9000 minutes of use which had been required for the LTR tariffs.[32] For the equal access exogenous cost change, which was not technically a part of access reform but was included in BellSouth's Transmittal No. 435, the exogenous change was required

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29 Designation Order, para. 52.

30 The one exception to BellSouth's use of a revenue requirement methodology in the absence of a Commission-specified methodology was the use of revenues (rates x demand) for STP port terminations. This was the only exogenous cost change related to an existing service for which rates had already been established.

31 Access Reform Order, para. 197.

32 Access Reform Order, paras. 206-208.

to be based upon the amount of the exogenous change identified at the inception of price caps, adjusted by the growth in revenues since that time.[33] For each of these items, the methodology to be followed was specified by the Commission.

Except for the one instance where rates for a service being moved already existed,[34] the remainder of the changes were accomplished by identification of the revenue requirement associated with the change. This involved the identification of the investment, with the addition of a return component calculated at the authorized return of 11.25%, and expenses.[35] For those items, such as marketing and COE maintenance changes, where no investment was involved, identification of expenses, only, was required.

The Commission should not require BellSouth to revise the exogenous cost change amounts resulting from the use of the revenue requirement approach. As a preliminary matter, although the Commission referred on numerous occasions in the Access Reform Order to the identification and movement of "costs," the only instances in which it specifically required a particular cost methodology for the filings at issue here was for the three items discussed above. If the Commission had intended that specific methodologies be used for the remainder of the cost changes, it would have specifically so indicated as it did for these items.

BellSouth used the revenue requirement approach based on an analysis of the Commission's rules relating to access reform and a reliance on precedent where the Commission

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[33] 1997 Annual Filing Investigation Order, paras. 109-120.

[34] See n. 30 supra.

[35] In preparing this Direct Case, BellSouth discovered an error in the calculation of the exogenous cost change associated with excess ISDN line ports. BellSouth plans to correct these amounts in a filing expected to be made on March 4, 1998. The corrected amounts are included in the quantities displayed in Appendix B.

had approved this approach for similar changes in the past. Prior to access reform, the development of exogenous adjustments had been limited to two basic approaches. Appendix B, Exhibit 1 lists the pre-Access Reform exogenous cost changes for BellSouth. As can be seen, in all cases but one, BellSouth utilized a revenue requirement analysis at 11.25% return. That one instance involved the deregulation of pay telephones for which specific instructions were imposed.[36] The use of a revenue requirement analysis, at an 11.25% return, for access reform follows the historical pattern for exogenous cost changes for which specific requirements were not imposed by the Commission. Given the fact that the Commission established no specific requirements in the Access Reform Order regarding the manner in which exogenous calculations at issue were to be made and given that BellSouth's methodologies follow the pattern of historical exogenous cost changes, the Commission should not at this point in time require any changes to be made.

BellSouth believes that the use of a revenue requirement methodology was appropriate, especially given that the Commission's Access Reform Order, over and over, again discussed the use of "costs" to determine such changes. Under the Commission's Part 32 and 36 rules, the means for categorizing and separating "costs" is prescribed.[37] BellSouth's revenue requirement approach uses the Part 36 definitions for determining the investment and expenses involved. It is

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[36] In the Matter of Implementation of the Pay Telephone Reclassification and Compensation Provisions of the Telecommunications Act of 1996, CC Docket No. 96-128, *Report and Order*, 11 FCC Rcd 2054 (1996), paras. 180-187 and In the Matter of Implementation of the Pay Telephone Reclassification and Compensation Provisions of the Telecommunication Act of 1996, CC Docket No. 96-128, *Order on Reconsideration*, 11 FCC Rcd 21233 (1996), *aff'd in part and rev'd in part sub nom. Illinois Pub. Telecommunications Ass'n v FCC*, 117 F.3d 555 (D.C. Cir. 1997), paras. 197-208.

[37] 47 C.F.R. Sections 36.1 and 36.2.

precisely these "costs" that are then categorized into service elements through Part 69 of the Commission's rules. Changes to the Part 69 rules, as required in Access Reform, are the source of the exogenous impacts BellSouth was required to determine. Following the Commission's rules outlined above, BellSouth quantified the Part 69 cost changes ordered by the Commission, calculated the revenue requirement impact as defined in Part 69 of the Commission's rules,[38] and reflected the resulting exogenous adjustments in its Part 61 price cap revenues. For these items, the data necessary to make the required exogenous adjustment was not available from Part 69 service category results alone, and, thus, the revenue requirement methodology was a reasonable approach, consistent with past exogenous cost calculations, in the absence of Commission-mandated requirement otherwise.

The Commission requests LECs to quantify the results of using the Commission's "revenue" methodology to identify the exogenous cost changes at issue.[39] It should be noted that in referring to a "revenue" methodology, the Commission does not specifically define the methodology to be used. Indeed, the Commission misses the fact that, for the items involved, there are not determinable "revenues" associated with the exogenous changes because there are no rates for the various items prior to the time the exogenous cost is being determined. Of course,

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38 The Commission's Part 69 rules define "annual revenue requirement" as "the sum of the return component and the expense component." 47 C.F.R. Section 69.2(c). The "expense component" is "the total expenses and income charges for an annual period that are attributable to a particular element or category." 47 C.F.R. Section 69.2(o). The "return component" is the "net investment attributable to a particular element or category multiplied by the authorized annual rate of return." 47 C.F.R. Section 69.2(ff). The Commission has not revised the authorized rate of return of 11.25% in effect for price cap LECs since the inception of price cap regulation. In the Matter of Price Cap Performance Review for Local Exchange Carriers, CC Docket No. 94-1, *Fourth Further Notice of Proposed Rulemaking*, 10 FCC Rcd 13659, (1995), para. 35 and n. 56.

39 Designation Order, para. 51.

where there is an existing service and rates associated therewith, the exogenous cost change is appropriately determined based upon the revenues (rates x demand) associated with the service. This is the approach taken by BellSouth for the one service, STP port terminations, where this was the case. However, the Commission cannot detach revenues from the provision of a service or create revenues where a service and its associated rates do not exist. Without existing rate elements and rates, a direct calculation of revenue (i.e., rate times demand) is not possible. Furthermore, the data necessary to make the required exogenous adjustments is not available through Part 69 categories.

BellSouth's objections notwithstanding, the calculations of the various alternatives discussed above are presented in appendix B, Exhibits 2 through 4, using methodologies which it believes the Commission may have intended. Exhibit 2 represents a summary of the exogenous adjustments included by BellSouth in its original filing. Exhibit 3 represents the calculation of the exogenous adjustment determined by reallocating revenues based on the percentage of direct investment removed from each category as determined in the original filing and shows the specific calculations supporting these adjustments. This appears to be the methodology used by AT&T and MCI in developing their comments.[40] Exhibit 4 shows the results of the Commission's alternative methodology using revenue requirement calculated at 1996 actual basket earnings.

Finally, the Commission tentatively concludes that any change in exogenous cost calculation methodology should not impact the Base Factor Portion ("BFP") of the common line basket. BellSouth agrees. Indeed, the Commission only just recently concluded its investigation

[40] Designation Order, paras. 41 and 42.