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FEDERAL COMMUNICATIONS COMMISSION
OFFICE OF THE SECRETARY

Magalie Roman Salas
Secretary
Federal Communications Commission
1919 M Street, NW
Room 222
Washington, DC 20554

Ex Parte Notice -CC Docket No. 96-262

Dear Ms. Salas:

Enclosed is a copy of a letter delivered today to Jane Jackson, Chief of the Competitive Pricing Division; Richard Metzger, Chief of the Common Carrier Bureau; and Richard Lerner and Tamara Preiss of the Common Carrier Bureau.

Two copies of this notice and the letter are being filed in the Office of the Secretary. Please include this notice in the public record of these proceedings.

Respectfully submitted,

Frank McKennedy
Director - Legal & Regulatory Affairs

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UNITED STATES
TELEPHONE
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May 11, 1998

Ms. Jane Jackson
Chief, Competitive Pricing Division
Common Carrier Bureau
Federal Communications Commission
1919 M Street, NW
Room 518
Washington, D.C. 20554

RE: Ex Parte Docket No. 96-262

Dear Ms. Jackson

On April 22, a number of USTA representatives met with Rich Lerner and other Common Carrier Bureau Staff to discuss the need for Commission action on USTA's Petition for Reconsideration (PFR) in the above referenced proceeding[1]. The primary PFR issue USTA discussed was the need for relief from the requirement in the price cap rules that the 6.5% productivity factor be applied to the Price Cap LECs' Universal Service funding (USF) obligations.

During the discussion, Rich Lerner asked USTA to provide an analysis of the net impact of both the application of the productivity factor and demand growth under the current rules on the price cap LECs in the upcoming annual price cap tariff filing. USTA estimates that the net impact is a negative $1.9 million. The productivity factor will cause an aggregate negative impact of $32.4 and aggregate demand growth will create a positive impact of $30.6.

In the aggregate for all price cap LECs, applying the productivity factor to the USF obligation in this year's annual price cap tariff filing will in large part be offset by demand growth in this first year of application. However, because of the ongoing reduction of the higher-growth usage-based Carrier Common Line access charge and the resulting significantly higher proportion of recovery of USF costs from the lower-growth access-line based PICC charge, and the growing impacts of competition on both line and usage growth, the negative impact of these rules may increase substantially. Without a change in the rules, the price cap LECs will not have the opportunity to recover these costs that the unregulated IXCs have clearly been able to employ.

USTA strongly believes that the Commission must reconsider its rules.

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[1] See USTA Ex Parte notice dated April 23, 1998, CC Docket No. 96-262.

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Continued application of the productivity factor to the USF obligation is counter to the Commission's universal service principals which require that the recovery of the USF costs be competitively neutral.

To the degree that the price cap LECs opportunity to recover their USF obligations is reduced because of price cap regulation while the competing CLECs and wireless carriers, and the the IXCs have no such restraint on their pricing to recover these costs is the competitive neutrality sought by the Communications Act of 1996 thwarted. (The IXCs have actually increased their charges to their toll customers to recover these costs and also have implemented a surcharge to recover the PICC charges. On the other hand, the IXCs have not reduced their prices to reflect the LECs' substantial decrease in price for usage based access charges.) As LEC usage based demand is reduced both by competitive losses and movement to flat rate SLCs and PICCs, offsetting demand growth will greatly impair the LECs' opportunity to recover their USF costs.

For these reasons, USTA urges the Commission to act expeditiously to resolve the inequity of the price cap rules that require the application of the productivity factor on the LECs USF obligation.

Frank McKennedy

Director, Legal & Regulatory Affairs

cc: R. Metzger
R. Lerner
T. Preiss