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FEDERAL COMMUNICATIONS COMMISSION
OFFICE OF THE SECRETARY

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

In the Matter of	)	
	)	
Federal-State Joint Board on Universal Service	)	CC Docket No. 96-45
	)	
Forward-Looking Mechanism for High Support for Non-Rural LECs	)	CC Docket No. 97-160
	)	

REQUEST FOR WAIVER

Ameritech Michigan hereby requests waiver in connection with the cost study filed this day in the above-captioned matter on behalf of the Michigan Public Service Commission ("MPSC").

In its order in Case No. U-11635, a copy of which is attached ("U-11635 Order"), the MPSC approved a forward-looking economic cost study for use in the State of Michigan in connection with the Federal Communications Commission's ("FCC's") and any Michigan state universal support mechanism for Ameritech high cost areas. The MPSC ordered Ameritech to file the cost study with the FCC.

In the U-11635 Order, the MPSC found that the cost study satisfies the 10 criteria set forth by the FCC in its Universal Service Order,[1] with the exception of criteria number 5: Economic lives and future net salvage percentages used to calculate depreciation expenses must be within the FCC authorized ranges. Specifically, 11 of the 15 plant categories used in the

[1] *In the Matter of Federal-State Joint Board on Universal Service,* CC Docket No. 96-45, Report and Order, FCC 97-157 (released May 8, 1997) ("Universal Service Order") at ¶250.

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universal service cost study fall outside the FCC life ranges:

UG Cable-Met 5C
Intra-Bldg. CA-Met 12C
Arial Cable-Met 22C
Buried Cable-Met 45C
UG Cable-NonMet 85C
Operator Systems 117C
Sub Pair Gain 257C
Digital Circuit 357C
Digital Switch 377C
Arial Cable-NonMet 822C
Buried Cable-NonMet 845C.

The cost study approved in the U-11635 Order is the same as approved by the MPSC in its January 28, 1998, order in Case No. U-11280 ("U-11280 Order") dealing with establishing total service long run incremental cost ("TSLRIC") in connection with rates for Ameritech's provision of unbundled network elements in the State of Michigan. In the U-11280 Order, a copy of which is also attached, the MPSC specifically found, with respect to those depreciation lives:

> On reconsideration of this issue, the Commission is persuaded that the asset lives proposed by Ameritech Michigan are more forward-looking than those that the Commission initially adopted in the July 14, 1997 order. As such, the Commission concludes that they are more reasonable than the FCC prescription lives, which more closely resemble cost-based regulation than TSLRIC principles. The Commission agrees with Ameritech Michigan and the Staff that, in a more competitive environment, the development of new technologies and a greater sensitivity to customers' needs can be expected to stimulate new investment and hasten the obsolescence of existing equipment. The Commission also finds that Ameritech Michigan's proposal is a reasonable means of recognizing this trend. . .[2]

In the context of the pricing of unbundled elements on the basis of forward-looking costs, the MPSC's determination in this regard is clearly reasonable.

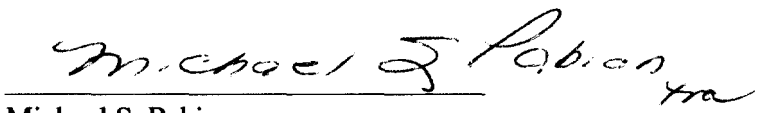
[2] U-11280 Order at 7.

Moreover, approving the same cost study for universal service purposes is consistent with the FCC's own view:

> We also affirm that state-conducted cost studies have the advantage of permitting states to coordinate the basis for pricing unbundled network elements and determining universal service support. This coordination can improve regulatory consistency and avoid such marketplace distortions as unbundled network element cost calculations unequal to universal service cost calculations for the elements that provide supported services. Such marketplace distortions may generate unintended and inefficient arbitrage opportunities.[3]
>
> We also encourage a state, to the extent possible and consistent with the above criteria, to use its ongoing proceedings to develop permanent unbundled network element prices as a basis for its universal service cost study. This would reduce duplication and deminish arbitrage opportunities that might arise from inconsistencies between the methodologies used for setting unbundled network element prices and for determining universal service support levels.[4]

Since the MPSC has approved, for universal service purposes, the entire cost study applicable to the pricing of unbundled network elements in the State of Michigan, the FCC should permit that study to be used, in its entirety, for federal universal service purposes as well -- including depreciation lives that fall outside the FCC's authorized ranges -- and should grant a waiver to that effect.

Respectfully submitted,



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Dated: May 26, 1998
[MSP0137.doc]

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[3] Universal Service Order at ¶247.

[4] *Id.* at ¶251.

STATE OF MICHIGAN

BEFORE THE MICHIGAN PUBLIC SERVICE COMMISSION

* * * * *

In the matter of the application of **AMERITECH MICHIGAN** for approval of its forward-looking economic cost study for use in determining federal universal service support.	)	Case No. U-11635

At the May 11, 1998 meeting of the Michigan Public Service Commission in Lansing, Michigan.

PRESENT: Hon. John G. Strand, Chairman
Hon. John C. Shea, Commissioner
Hon. David A. Svanda, Commissioner

OPINION AND ORDER

I.

HISTORY OF PROCEEDINGS

The Federal Communications Commission (FCC) issued an order dated May 7, 1997, In the Matter of Federal-State Joint Board on Universal Service, CC Docket No. 96-45 (Universal Service Order). In that order, and the rules adopted by it,[1] the FCC identified the services and functionalities to be supported by universal service support mechanisms. The FCC also determined that "high cost" would be determined by the amount a provider's cost exceeds a nationwide benchmark. Those carriers having high costs under the FCC definition could be eligible for cost support. Costs for nonrural carriers, such as Ameritech Michigan, would be determined utilitizing forward-looking

[1] 47 C.F.R. Section 54.101.

economic principles as determined by either a yet-to-be-adopted FCC cost model or pursuant to cost studies approved by state commissions.

On July 14, 1997, the Commission issued an order in Case No. U-11280, which, among other things, approved a cost methodology for Ameritech Michigan to determine its total service long run incremental costs (TSLRIC). Ameritech Michigan was directed to file TSLRIC and related studies and tariffs 14 days thereafter.

On August 13, 1997, the Commission, consistent with FCC deadlines, advised the FCC that it would utilize the TSLRIC standard legislatively mandated in Michigan, MCL 484.2102(ff); MSA 22.1469(102)(ff), for determining universal service costs. On November 3, 1997, Ameritech Michigan filed an application for approval of a forward-looking economic cost (FLEC) study in Case No. U-11573.

In response to petitions for rehearing filed by Ameritech Michigan and other parties, the Commission modified its July 14, 1997 order in Case No. U-11280 on January 28, 1998. That order addressed four items related to Ameritech Michigan's TSLRIC studies: cost of capital, depreciation lives, fill factors, and shared and common cost allocations. The Commission left unchanged its July 14, 1997 rulings related to cost of capital, fill factors, and shared and common cost for unbundled network elements. The Commission adopted Ameritech Michigan's proposals related to depreciation lives.

Also on January 28, 1998, the Commission dismissed Ameritech Michigan's application in Case No. U-11573. It ordered the company to file a new study in a new docket that would be used for federal universal service support for high cost areas and to complete the Commission's comprehensive review of Ameritech Michigan's TSLRICs. Ameritech Michigan's filing in this docket is in response to that order. Today's order is consistent with the schedule established by that order and

will permit Ameritech Michigan to timely file its FLEC study by May 26, 1998, the date established by the FCC.[2]

Attorney General Frank J. Kelley (Attorney General), the Commission Staff (Staff), AT&T Communications of Michigan, Inc. (AT&T), and MCI Telecommunications Corporation (MCI) filed comments on Ameritech Michigan's filing on March 11, 1998. AT&T, the Staff, and Ameritech Michigan filed reply comments by March 26, 1998. Ameritech Michigan, AT&T, MCI, the Attorney General, and the Staff filed additional responses on April 6, 1998.

This order addresses the issues of Ameritech Michigan's retail shared and common cost study and the geographic disaggregation of the TSLRIC study approved by this Commission in Case No. U-11280 on July 14, 1997 and January 28, 1998.

II.

FCC CRITERIA FOR COMPUTING FLEC

In the Universal Service Order, the FCC specified the following ten criteria that any cost methodology used to calculate the FLEC of providing universal service must satisfy:

(1) Assume the use of forward-looking technologies for supported services, i.e., least-cost, most-efficient, and reasonable technologies that are currently being deployed, based on characteristics of incumbent local exchange companies (ILECs) wire centers such as the location of switches, line counts, and actual average loop lengths.

(2) Any network function or element such as loop, switching, transport, and signaling used to provide a supported service must have an associated cost.

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[2]April 23, 1997 Order, CC Docket 96-45. The Commission is not aware of the FCC's having selected a default cost methodology for determining FLECs. However, any determination by the FCC would appear to impact only the filing date for the Ameritech Michigan study, not the methodology used in Michigan.

(3) Only long-run forward-looking economic costs may be included, using a sufficiently long-run period that all costs may be treated as variable or avoidable. The studies must rely on the current purchase prices of plant and equipment.

(4) Use of the authorized federal rate of return on interstate services of 11.25% or the state's prescribed rate of return on intrastate services.

(5) Economic lives and future net salvage percentages used to calculate depreciation expenses must be within the FCC authorized ranges.

(6) The cost study or model for supported services must reflect the level of services demanded by all customers within a geographic region.

(7) A reasonable allocation of joint and common costs must be assigned to supported services.

(8) Cost studies and all underlying data, formulae, computations, and software must be available to all interested parties for review and comment. Inputs should be verifiable, engineering assumptions should be reasonable, and outputs should be plausible.

(9) Cost studies or models must include the capability to examine and modify critical assumptions and engineering principles such as the cost of capital, depreciation rates, fill factors, input costs, overhead adjustments, retail costs, structure sharing percentages, fiber-copper cross-over points, and terrain factors.

(10) Cost studies must deaverage support calculations to the wire center serving area level.[3]

Consistent with the records upon which this case is based and subject to the modifications to Ameritech Michigan's studies delineated in this order, the Commission finds that the studies approved today, in concert with those approved in Case No. U-11280, satisfy the FCC's FLEC criteria, with the exception of criteria 5. The Commission notes that these studies are approved for the purpose of satisfying the geographic disaggregation of Ameritech Michigan's network for the purpose of universal service support mechanisms for high cost areas.

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[3]May 7, 1997 order, CC Docket No. 96-45, paragraph 250.

Approval of these FLEC studies is not intended to overturn, modify, or in any way reconsider issues previously determined in Case No. U-11280 or the parts of this order related to the allocation of shared and common costs. Further, the FLEC study is not intended in any way to be an update to the previously approved study methodology or inputs from Case No. U-11280.

With respect to criteria 5, Ameritech Michigan acknowledges,[4] and the parties appear to concur, that the depreciation lives and net salvage values are not within FCC authorized ranges. By issuing this order approving Ameritech Michigan's FLEC studies, the Commission is neither explicitly nor implicitly seeking a waiver of the requirement of criteria 5 on behalf of Ameritech Michigan. Because the Commission approved Ameritech Michigan's proposal on depreciation issues in Case No. U-11280, the burden of convincing the FCC on this matter lies squarely with Ameritech Michigan.

III.

COST METHODOLOGY ISSUES

As established in its order commencing this proceeding, the Commission identified two areas to be addressed. The first was Ameritech Michigan's retail shared and common cost study. The second was the geographic disaggregation of the Case No. U-11280 cost study to produce a wire center by wire center cost analysis for use in the FCC universal service support mechanism for high cost areas. In the area of geographic disaggregation, the parties and the Commission have identified eight issues that need to be resolved.

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[4]Reply Comments of Ameritech Michigan, Case No. U-11635, p. 30, footnotes 9 and 10.

Shared and Common Costs

The public accounting firm of Arthur Andersen was retained by Ameritech Michigan in June 1996 to perform a study of shared and common costs for use in Case No. U-11280. Arthur Andersen was again retained by Ameritech Michigan to complete a study of shared and common costs for Ameritech Michigan's retail services. The latter is a part of Ameritech Michigan's presentation of its FLEC study.

On the issue of common costs, the Commission notes that it addressed common costs previously. In its Principle No. 5[5], the Commission defined common costs[6] as follows:

> [C]ommon overheads are those costs that are common to all services or output of a firm. These costs cannot be readily identified with specific services or group of services. An example would be the president's desk. [Emphasis added.]

The Commission has previously reviewed the issue of common costs for unbundled network elements in Case No. U-11280. Further, in light of its Cost Principle No. 5, the Commission is not convinced by this record that its Cost Principle No. 5 is in error or was incorrectly applied in Case No. U-11280. The Commission therefore determines that the common cost multiples or mark-ups for Ameritech Michigan retail services should be set at the level approved in its July 14, 1997 order in Case No. U-11280.

Shared costs as proposed by Ameritech Michigan continue to be based on budgeted data. Calendar year 1997 budget information is hardly what the Commission envisioned when adopting its forward-looking principles in Cases Nos. U-10620 and U-11103.

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[5]September 8, 1994 order, Case No. U-10620, Exhibit A, page 5.

[6]The terms common costs and common overheads are used interchangeably in this order.

The result of a TSLRIC analysis is the "economic" cost of providing a service or function. It is intended to identify a forward-looking cost. To reduce a TSLRIC study to an analysis of embedded cost or historical accounting costs or results simply perpetuates the use of a business-as-usual approach to cost analysis. The objective of a TSLRIC study is to reflect the most efficient means of providing a service or function within the parameters previously outlined by the Commission.[7]

Because Ameritech Michigan's retail shared cost study suffers from the same flaws as its study in Case No. U-11280, the Commission must determine a level of shared costs that, at this time, would reasonably reflect the Commission's TSLRIC principles.

The parties commenting on this issue present several "discounts" or reductions to Ameritech Michigan's proposal. Ameritech Michigan responds that any reduction in its proposed costs would have the company experience a drastic underrecovery of its costs.

The Commission concludes that a 20% reduction in Ameritech Michigan's shared costs would result in a reasonable representation of Ameritech Michigan's shared costs. This reduction is consistent with the percentage reduction in similar Michigan Exchange Carriers Association cost studies that were also based on budget data. The 20% is an approximation of increased efficiencies of Ameritech Michigan's operations as required by the TSLRIC concepts of optimum and efficient operation.

Geographic Disaggregation of Costs

The purpose of this phase of the proceeding is simply to disaggregate the TSLRIC study approved in Case No. U-11280 to produce results that could be used by the FCC in the administra-

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[7]September 8, 1994 order, Case No. U-10620; FCC FLEC Criteria 3, paragraph 250, CC Docket 96-45.

tion of the universal service support mechanism for high cost areas. In addressing the issues related to the disaggregation, the Commission will not consider proposals that call into question the validity of the results produced in Case No. U-11280. Further, the Commission intends to resolve the matters in dispute in a manner that will permit Ameritech Michigan and this Commission to meet the recently extended FCC deadline of May 26, 1998 for FLEC studies.[6] With these factors in mind, the Commission rejects all recommendations by commenting parties that the FLEC study be totally recomputed.

The Commission also believes additional justification for rejection of a total restudy is that Ameritech Michigan must use one TSLRIC study for its entire network, e.g., unbundled network elements, retail, and FLEC. At this time, the results of Case No. U-11280 present the best opportunity to achieve that goal. The specific issues in dispute related to disaggregation are:

1. Use of closing factors.
2. Placement of the serving area interface (SAI).
3. Vintage of cable.
4. Use of data from other states or other exchanges.
5. Level of uncollectibles or treatment of uncollectibles.
6. Fill factors.
7. Attorney General items.
   a. AFAM model's use of "error filtering" system.
   b. Use of inefficient and embedded technology of UDLC instead of integrated digital loop carrier.
   c. Use of highly subjective difficulty factors for cable installation.
   d. Inclusion of bridge tap cable overstates loop lengths and are not forward-looking.
   e. Crossover point between copper and fiber may not reflect an efficient forward-looking network confirmation.
   f. Application of a 15% - 20% reduction of loop costs if above 6 items are not recognized in a revised study.
8. Miscellaneous issues
   a. Disaggregation should include not only loops but also ports and switching costs.

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[6]CC Docket No. 96-45, CC Docket No. 97-160, April 23, 1998.

b. Some recognition should be given to switching equipment used in switching cost for large metropolitan areas and small rural areas.
c. Study should include information from or recognize latest vendor contracts rather than the 1992 data utilized by Ameritech Michigan.

Many of these disputed issues have merit in that they provide a level of detail that may have been missing from the study in Case No. U-11280 that was to be disaggregated in this proceeding. The most telling of these issues is the use of closing factors. Absent these factors, Ameritech Michigan could not disaggregate its network in a manner that had the sum of network parts equal the entirety of the network. In effect, Ameritech Michigan has created costs or network synergy where the sum of the network parts exceeds the network as a whole. Closing factors essentially scale down the disaggregated study results to a level equal that in Case No. U-11280. The Commission is concerned with the existence and use of closing factors, but that concern must be tempered with the realization that the FCC's new FLEC study filing deadline provides little time for a comprehensive recalculation of Ameritech Michigan's FLECs. Additionally, the Commission does not intend to revisit its TSLRIC methods approved in Case No. U-11280 prior to the normal biennial review. The Commission therefore concludes, despite the shortcomings, that the use of Ameritech Michigan's closing factors for this case is reasonable and will be permitted. The Commission, however, puts Ameritech Michigan on notice that its future biennial TSLRIC studies must not incorporate closing factors or any similar approach.

Having permitted the use of closing factors in this case, many of the remaining issues may add only false precision to a result that can be deemed reasonable. Therefore, the Commission does not adopt the commenting parties' positions. On the other hand, in its next biennial TSLRIC filing, Ameritech Michigan must justify its proposals as they relate to the placement of the SAIs, use of data from other states, uncollectibles, fill factors (and effective fill factors), and level of disaggrega-

tion in terms of ports and switches and cable vintage, in addition to the normal proofs it would present.

Administrative Issues

The FCC has directed the states to submit FLEC studies. The FCC also established a filing format to be used by all states to simplify and standardize the submission and review of cost studies. The Commission directs Ameritech Michigan to complete the necessary data in the format prescribed by the FCC. The Commission directs Ameritech Michigan to work with the Staff to prepare the data and supporting information. The information should be prepared in a manner that recognizes Michigan statutes and Commission orders. Prior to Ameritech Michigan's filing at the FCC, the Staff is to notify the Commission that, in the Staff's opinion, the FLEC study to be submitted is consistent with Michigan law and Commission action and includes the proper general and supporting information. This notification shall be served on all commenting parties and filed in this docket.

Finally, the Commission also notes that the next biennial TSLRIC filing for Ameritech Michigan is due in January 1999. Until approval of that study, Ameritech Michigan shall utilize the results of Case No. U-11280 and this docket in regulatory matters in Michigan.

The Commission FINDS that:

a. Jurisdiction is pursuant to 1991 PA 179, as amended by 1995 PA 216, MCL 484.2101 et seq.; MSA 22.1469(101) et seq.; the Communications Act of 1934, as amended by the Telecommunications Act of 1996, 47 USC 151 et seq.; 1969 PA 306, as amended, MCL 24.201 et seq.; MSA 3.560(101) et seq.; and the Commission's Rules of Practice and Procedure, as amended, 1992 AACS, R 460.17101 et seq.

b. Shared and common costs should be recalculated in a manner consistent with this order.

c. The Ameritech Michigan FLEC study should be approved for use in the FCC's universal service support mechanism for high costs areas.

d. Ameritech Michigan and the Staff should prepare the filing for submission to the FCC by May 26, 1998.

e. The Staff should notify the Commission and the commenting parties that the study filing is consistent with Michigan law and Commission orders and includes proper general and supporting information.

f. The next biennial TSLRIC filing for Ameritech Michigan is due in January 1999.

g. Disputed issues related to geographic disaggregation, as discussed in this order, should be addressed and justified by Ameritech Michigan in its January 1999 TSLRIC filing.

THEREFORE, IT IS ORDERED that:

A. Shared and common costs shall be recalculated in a manner consistent with this order.

B. The Ameritech Michigan FLEC study is approved for use in the Federal Communications Commission's universal service support mechanism for high costs areas.

C. Ameritech Michigan and the Commission Staff shall prepare the filing for submission to the Federal Communications Commission by May 26, 1998.

D. The Commission Staff shall notify the Commission and the commenting parties that the study filing is consistent with Michigan law and Commission orders and includes proper general and supporting information.

E. The next biennial total service long run incremental cost filing for Ameritech Michigan is due in January 1999.

F. Disputed issues related to geographic disaggregation, as discussed in this order, should be addressed and justified by Ameritech Michigan in its January 1999 total service long run incremental costs filing.

The Commission reserves jurisdiction and may issue further orders as necessary.

MICHIGAN PUBLIC SERVICE COMMISSION

/s/ John G. Strand
Chairman

(SEAL)

/s/ John C. Shea
Commissioner, concurring and dissenting in a separate opinion.

/s/ David A. Svanda
Commissioner

By its action of May 11, 1998.

/s/ Dorothy Wideman
Its Executive Secretary

STATE OF MICHIGAN

BEFORE THE MICHIGAN PUBLIC SERVICE COMMISSION

* * * * *

In the matter of the application of **AMERITECH MICHIGAN** for approval of its forward-looking economic cost study for use in determining federal universal service support.	)	Case No. U-11635

CONCURRING AND DISSENTING OPINION OF COMMISSIONER JOHN C. SHEA

(Submitted on May 11, 1998 concerning order issued on same date.)

I concur with the accompanying order to the extent that it completes the task of approving a part of the total service long run incremental cost study of Ameritech Michigan pursuant to Section 304a of the Michigan Telecommunications Act, MCL 484.2304a; MSA 22.1469 (304a).

I dissent from the accompanying order to the extent that it purports to exercise federal authority concerning the federal universal service program.

While the federal universal service program is no doubt a worthy program, the majority, I believe, has erred in issuing the accompanying order for the reason that the Michigan Legislature has seen fit to deny to this Commission the power to implement any universal service program.

By enacting the Michigan Telecommunications Act ("MTA"), the Michigan Legislature expressly limited the Commission in the exercise of its authority. See, MCL 484.2201(2); MSA 22.1469(201)(2) ["In administering this act, the Commission shall be limited to the powers and duties prescribed by this act"]. Elsewhere, the MTA provides that the Commission shall create a task force "to study changes occurring in the federal universal service fund and the need for the

establishment of a state universal service fund," MCL 484.2202(e); MSA 22.1469(202)(e) [emphasis added], and to "issue a report to the legislature and governor on or before December 31, 1996 containing . . . findings and recommendations." Id. The state universal service report has been completed and sent to the Michigan Legislature but, as of this date, no legislative action has been completed that would implement a universal service fund program. Without such statutory authority, this Commission can not act. See, Union Carbine Corp v PSC, 428 NW2d 322, 431 Mich 135 (1988).

John C. Shea, Commissioner

STATE OF MICHIGAN

BEFORE THE MICHIGAN PUBLIC SERVICE COMMISSION

* * * * *

In the matter, on the Commission's own motion, to consider the total service long run incremental costs and to determine the prices of unbundled network elements, interconnection services, resold services, and basic local exchange services for AMERITECH MICHIGAN.	)	Case No. U-11280

At the January 28, 1998 meeting of the Michigan Public Service Commission in Lansing, Michigan.

PRESENT: Hon. John G. Strand, Chairman
Hon. John C. Shea, Commissioner
Hon. David A. Svanda, Commissioner

ORDER ON REHEARING

On July 14, 1997, the Commission issued an order modifying and approving a total service long run incremental cost (TSLRIC) study methodology for Ameritech Michigan and approving rates, terms, and conditions for Ameritech Michigan to provide unbundled network elements, interconnection services, and resale services. On July 24, 1997, Ameritech Michigan submitted tariff sheets to implement the order.

In response to petitions for rehearing filed by Ameritech Michigan, AT&T Communications of Michigan, Inc. (AT&T), and MCI Telecommunications Corporation (MCI), the Commission granted partial rehearing on September 30, 1997. The Commission defined the scope of rehearing by identifying eight issues. Those issues included the four cost inputs to the TSLRIC

models: (1) cost of capital, (2) depreciation lives, (3) fill factors, and (4) shared and common cost allocations. The other four issues are (5) whether the unbundled local switching charges recover the cost of vertical features, precluding the use of separate charges to recover those costs, (6) the terms and conditions for providing common transport as an unbundled network element, (7) the propriety of the resale discount percentages, and (8) unexplained differences between proposed tariffs submitted by Ameritech Michigan with its initial cost studies on January 21, 1997 and those submitted on July 24, 1997. The Commission denied rehearing in all other respects. The order established filing deadlines for the moving parties' proposals on rehearing and three additional rounds of comments.

On October 21, 1997, Ameritech Michigan, MCI, and AT&T filed their proposals on the rehearing issues.

In its proposal, Ameritech Michigan requested relief with respect to six of the eight issues. For issue (1), Ameritech Michigan proposed that the 10.6% cost of capital required in the July 14, 1997 order be replaced by the confidential cost of capital used in the original cost studies that it filed at the beginning of this case (in January 1997). With respect to issue (2), Ameritech Michigan proposed that the asset lives developed under the Federal Communications Commission's (FCC) prescription approach and adopted in the July 14, 1997 order for depreciation purposes be replaced by the accelerated asset lives used in the original Ameritech Michigan cost studies. On issue (4), which relates to shared and common costs, Ameritech Michigan proposed that the percentage markup approved in the Commission's order be replaced with the specific dollar allocations used in its original cost studies.

For issue (5), Ameritech Michigan claimed that the workpapers submitted with its original cost studies demonstrate that the pricing of its unbundled local switching element does not cover the additional costs associated with the vertical features of a local switch port. Ameritech Michigan approached issue (6) by denying that it has an obligation under federal law to provide common transport as an unbundled network element. With respect to issue (7), Ameritech Michigan proposed adjustments to the computation of the resale discounts that would lower the discount percentages to 19.83% (from 25.96%) if the competing provider does not use Ameritech Michigan's operator services and directory assistance (OS/DA) and 19.71% (from 19.96%) if the provider purchases Ameritech Michigan's OS/DA services.

MCI's initial proposals addressed issues (3), fill factors, and (6), common transport. With respect to issue (3), MCI proposed that the fill factors supported by Ameritech Michigan and adopted by the Commission be replaced by the higher factors that MCI and AT&T had proposed in their comments filed prior to the July 14, 1997 order. For issue (6), MCI proposed that Ameritech Michigan be required to offer common transport at a usage-sensitive rate of $0.000109 per minute of use. MCI discussed matters relating to unbundled local switching and nonrecurring charges. AT&T also addressed Ameritech Michigan's tariff submissions with respect to those issues.

On the November 10, 1997 deadline for initial comments on the rehearing proposals, Ameritech Michigan, AT&T, MCI, the Michigan Exchange Carriers Association, Inc. (MECA), Attorney General Frank J. Kelley (Attorney General), and the Commission Staff

(Staff) filed comments. On November 21, 1997, the same parties, except for MECA, filed response comments. On December 5, 1997, the parties, except for MECA, filed reply comments.

Having reviewed the parties' comments on rehearing, the Commission observes that much of the discussion addresses issues that are outside the scope of rehearing. Some of the other comments, when addressing issues designated for rehearing, did not bring new or different information to the Commission's attention, but instead repeated or expanded arguments made prior to the July 14, 1997 order or supplemented those arguments with information that could have been advanced during the earlier phases of this case.

The Commission reminds the parties that the current proceeding is on rehearing from the determinations made in the July 14, 1997 order. As noted in the September 30, 1997 order at 1-2, the Commission's rehearing standard does not permit the parties to raise any argument that they choose, but imposes the following limitations:

> Rule 403 of the Commission's Rules of Practice and Procedure, 1992 AACS, R 460.17403, provides that a petition for rehearing may be based on claims of error, newly discovered evidence, facts or circumstances arising after the hearing, or unintended consequences resulting from compliance with the order. A petition for rehearing is not merely another opportunity for a party to argue a position or to express disagreement with the Commission's decision. Unless a party can show the decision to be incorrect or improper because of errors, newly discovered evidence, or unintended consequences of the decision, the Commission will not grant a rehearing.

The Commission reaffirms that Rule 403 governs this proceeding. Information and arguments that do not meet this standard are not entitled to consideration.

In the September 30, 1997 order at 7-8, the Commission defined the scope of proceedings on rehearing as follows:

> To summarize, the scope of further proceedings on rehearing shall be limited to the four cost inputs to the TSLRIC models . . . , the recovery of the cost of vertical features as part of unbundled local switching, unbundled common transport, resale, and certain tariff matters. *The Commission finds that the parties' petitions for rehearing should be denied in all other respects and should not be relitigated in this case.*
>
> . . . .
>
> Except for the issue of unbundled common transport (for which Ameritech Michigan acknowledges a responsibility to comply with the FCC's order), *the party seeking rehearing on an issue will have the burden of specifically demonstrating why the July 14, 1997 order was in error and how it should be changed.* To meet this burden, it must file a proposal to resolve the issue by the October 20, 1997 deadline. *The proposals as well as the subsequent comments or affidavits should not merely restate a party's position in general terms, but they should supply new information that was not previously in the record.*

(Emphasis added; footnote deleted). Because much of the discussion in the comments submitted during the rehearing phase of this case does not comply with the Rule 403 standard or the September 30, 1997 order, the Commission has determined that it should disregard those comments in resolving this case. Consequently, this order will focus only on the arguments that are within the proper scope of rehearing. Although already stated in the September 30, 1997 order, the Commission reiterates that the findings and conclusions in the July 14, 1997 order will continue to be effective, except as specifically modified in this order.

Cost of Capital

Ameritech Michigan has not presented new arguments or different information to support its position that the cost of capital should be higher than the 10.6% rate approved in the July 14, 1997 order. Moreover, the Commission remains persuaded that the July 14, 1997 order reached the appropriate result regarding the cost of capital. Therefore, the Commission will not alter this determination.

In addition, the Commission rejects the Attorney General's attempts to reargue his position that the cost of capital should be reduced to 9.74%. The Attorney General exercised his opportunity to develop this position in his earlier comments, which failed to persuade the Commission in its July 14, 1997 order. To the extent that he asserts that those arguments have been improved with new or different information, the information is neither material nor persuasive. The Attorney General's attempt to lower the cost of capital continues to rely on book values and is not forward-looking as required by a TSLRIC analysis.

Depreciation

In support of its depreciation proposal, Ameritech Michigan argues that the longer asset lives adopted in the July 14, 1997 order are based on historical data and are not sufficiently forward-looking for a TSLRIC analysis. Ameritech Michigan argues that the accelerating pace of technological change in a more competitive environment means that equipment and systems will become obsolete more quickly than in the past. Ameritech Michigan notes that the Staff's earlier comments in this case characterized Ameritech Michigan's proposal as being within the range of reasonableness.

In reply, AT&T argues that Ameritech Michigan has not presented any evidence showing that the rate of obsolescence has in fact increased, but that Ameritech Michigan continues to use equipment that is many years old. AT&T further contends that Ameritech Michigan has failed to address how the demands of new market entrants for unbundled network elements will affect the rate of replacement of the network or to identify any new technologies that will render current technologies obsolete in the near future. According to AT&T, local exchange carriers' average rate of accrual of depreciation reserves has increased faster in recent years than their

rate of retirement of depreciable assets. From this trend, AT&T infers that the FCC's prescription rates for depreciation are accurate and err, if anything, on the side of overstating actual depreciation expense.

The Attorney General agrees with AT&T's assessment that Ameritech Michigan has failed to show that forward-looking asset lives would be significantly less than lives based on current experience. According to the Attorney General, Ameritech Michigan's reliance on expected changes in the future is inconsistent with its use of embedded plant and existing technology in its cost study network configuration, which are less efficient and more costly than the new technologies it assumed as the basis for its proposed depreciation lives.

MECA opposes the FCC prescription lives on the ground that they are not forward-looking. MECA recommends using asset lives of 10 years for switching equipment, 8 years for circuit equipment, 15 years for buried cable, and 17½ years for buried fiber.

On reconsideration of this issue, the Commission is persuaded that the asset lives proposed by Ameritech Michigan are more forward-looking than those that the Commission initially adopted in the July 14, 1997 order. As such, the Commission concludes that they are more reasonable than the FCC prescription lives, which more closely resemble cost-based regulation than TSLRIC principles. The Commission agrees with Ameritech Michigan and the Staff that, in a more competitive environment, the development of new technologies and a greater sensitivity to customers' needs can be expected to stimulate new investment and hasten the obsolescence of existing equipment. The Commission also finds that Ameritech Michigan's proposal is a reasonable means of recognizing this trend and that the July 14, 1997 order failed to give due attention to these competitive considerations. Ameritech Michigan's cost study

methodology should be revised to incorporate the asset lives that it proposed for depreciation purposes.

Fill Factors

Although MCI and AT&T continue to advocate increased fill factors based on percentages of usable capacity that approach 100% in many instances, the Commission finds that they have not advanced any material new information or compelling rationale to support this position, which the Commission rejected in the July 14, 1997 order. Although MCI argues on rehearing that the target fill factors it excerpted from Ameritech Corporation's internal documents make adequate provision for administrative and spare capacity, MCI has not demonstrated that the internal documents are current or make the cost assumptions appropriate to a TSLRIC analysis.

Shared and Common Costs

Ameritech Michigan argues for adoption of the shared and common cost allocations used in its original cost studies. Reiterating that it based the cost assumptions used in those studies on preliminary budget data for 1997, Ameritech Michigan claims that a comparison of the cost assumptions to the actual expenditures for the first part of 1997 and final budget data for the remainder of 1997 shows that the assumptions were understated. Ameritech Michigan adds that, contrary to suggestions in the July 14, 1997 order, a new study of retail shared and common costs performed later in 1997 shows that more of those costs have been allocated to retail services than to unbundled network elements.

Ameritech Michigan also criticizes the Commission's order for adopting a fixed percentage allocator. Ameritech Michigan contends that it is more appropriate to identify a fixed pool (in