UNITED STATES GOVERNMENT

memorandum

DATE: June 2, 1998

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FEDERAL COMMUNICATIONS COMMISSION
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REPLY TO
ATTN OF: Jane Whang

SUBJECT: Documents for Public Record

TO: Magalie Roman Salas

Please find enclosed documents to be placed on the record. These documents were submitted for the en banc on June 8, 1998, in the docket proceedings numbered 96-45, 97-160, and DA 98-715.

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RICHARD KOLB

DIRECTOR - UNIVERSAL SERVICE

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FEDERAL COMMUNICATIONS COMMISSION
OFFICE OF THE SECRETARY

EDUCATION:

- **BS** University of Illinois
- **MBA** Loyola University
- **JD** John Marshall Law School

PROFESSIONAL AFFILIATIONS:

Illinois State Bar Association
Counsel to Firm of Zamparo and Goldstein, Northbrook. Illinois

WORK EXPERIENCE:

32 Years With Ameritech and Predecessors with Assignments in Plant, Controllers, Information Systems, Finance, Personnel and Regulatory.

Regulatory assignments and responsibilities have included state policy development, advocacy, and implementation oversight for a wide variety of issues, including measured service, price cap plans, Customers First initiative, and 271 compliance.

Currently responsible for Universal Service and Access Reform Federal and State policy development and advocacy for Ameritech.

What Actions Should the FCC Undertake?

- The FCC should undertake to stay the course as proposed in the 25/75 split - in other words, a smaller fund will best (note: even 25/75 fund is larger than current support levels -- $1.7B to $2.5B based BCPM model calculation using the FCC "common inputs")
  - incent state action to rebalance rate structures (rational cost based rates)
  - incent state action to investigate affordability after rebalancing
  - focus explicit support to handle highly targeted needs only

  These three things will, in turn, accelerate the development of facilities based competition for residential customers by providing the proper economic incentives for investment

- Funding should commence 1/1/99 for non-rurals only
- Funding basis should remain interstate only
- FCC, in conjunction with state commissions should monitor the non-rural fund for 12-18 months following introduction to evaluate state actions, the need for super benchmark support, and to evaluate the cost/benefit of such support flows
- During the 12-18 month period, the FCC should undertake to define/develop a modified plan to appropriately and specifically target "super" benchmark needs in conjunction with state action
- Deal with rurals in light of lessons learned from the non-rural introduction at a later date -- in the interim, current interstate high cost support levels should be maintained (without offsetting reductions to their access charges)

Ameritech Statement on Federal High Cost Fund

In reviewing the thoughts of the commentors who have engaged in the debate regarding the size and mechanics of the Federal High Cost Fund, one is struck with the diversity of views and proposed solutions. Little, if any, common ground is present upon which one might begin to build a consensus.

Generally Absent from the Lively Debate Has been:

- Any showing of enhanced or special need to justify the often dramatic increases in support from the federal arena
- Any showing or rationale as to how increased support advances the goal of vibrant local competition
- A public policy rationale and linkage
- Empirical evidence that even the current level of support is necessary or warranted
- Clear/Universal state commission commitment to work intrastate USF equations so as to help reduce funding demands/pressures, and to help evaluate cost/benefit effectiveness of current support flows

It is Ameritech's View that Federal High Cost Fund Debate is Best Framed with Four Basic Questions:

- What High Cost Fund size is appropriate?
- How should alternative proposals be evaluated?
- What are the implications for state jurisdictions?
- What Actions should the FCC undertake?

What High Cost Fund Size is Appropriate?

- One which best aligns with public policy principles in that it best replicates existing levels of support, the existing state/federal partnership while incenting state USF reform
- One which best preserves USF by minimizing carrier, end user and societal support burdens
- One which best incents competition – economically rationale rates, and minimal intercompany support flows
- One which maximizes end user benefits by fostering market driven rates, minimal support burdens and proper economic signals for products and services as well as additional residential market entry and investment

How Should Alternative Proposals be Evaluated?

- Definition grounded in sound public policy principles such as those offered by the Chairman on February 9
- Amount of disruption of the federal/state partnership – Congress did not intend Section 254 to change the current balance of USF obligation
- How well proposal aligns with fund purpose to preserve and advance USF
- Amount of regulatory intrusion into the emerging competitive marketplace

What Are the Implications for State Jurisdictions?

Expansion of current federal support levels is premature absent state action to reform intrastate support flows and a demonstration that such reform will lead to unaffordable rates, subscribership loss, etc. – states must undertake rate rebalancing and affordability studies

What Actions Should the FCC Undertake?

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Susan M. Baldwin, a Vice President for Economics and Technology, Inc. (ETI), has worked nineteen years in public policy, thirteen of which have been in telecommunications. She is an expert in diverse telecommunications areas including universal service, cost proxy models, numbering issues, alternative regulation, network modernization, local exchange competition, cost methodology, and rate design. (ETI specializes in telecommunications economics, regulation, and public policy.) Ms. Baldwin has participated in numerous state and federal telecommunications policy proceedings, has testified as an expert witness before state regulatory commissions, and has served as an advisor to several state regulatory commissions and consumer advocates. Ms. Baldwin served four years as the Director of the Telecommunications Division for the Massachusetts Department of Public Utilities, where she advised and drafted decisions for the Commission in numerous proceedings and directed a staff of nine. In addition, Ms. Baldwin has worked with local, state, and federal officials on energy, environmental, budget, and welfare issues. [Master of Public Policy, Harvard University's John F. Kennedy School of Government; Bachelor of Arts, Mathematics and English, Wellesley College, nominee, Rhodes Scholar.]

EXECUTIVE SUMMARY OF TIME WARNER COMMUNICATIONS HOLDINGS INC. COMMENTS REGARDING UNIVERSAL SERVICE METHODOLOGY; CC DOCKET NOS. 96-45, 97-160, DA 98-715

Wherever possible, the FCC should avoid subsidizing rates in rural, insular and high cost areas where cost-based rates are affordable. This policy approach comports with Section 254(b)(1) and sound policy. Wealth transfers to consumers with relatively high incomes advance absolutely no identifiable social goal.

In a paper submitted in this proceeding, "Defining the Universal Service 'Affordability' Requirement: A Proposal for Considering Community Income As a Factor in Universal Service Support" ("ETI Study"), Economics and Technology, Inc. ("ETI") quantifies the harm in not recognizing that consumers in the top 30 percent income bracket can easily afford cost-based rates. The ETI Study analyzes average income by census block group ("CBG") in conjunction with cost model results to determine universal service funding requirements in high-cost, high-income areas. It demonstrates that approximately 20-30% of the high-cost universal service fund could be eliminated if support were limited to households with incomes below the 70th income percentile. This could result in up to $4.5 billion in savings nationally.

Thus, the FCC should work toward eliminating federal universal service funding for CBGs with average median incomes above an appropriate threshold, for example the 70th percentile. The elimination of these subsidies will of course result in lower compensation for the carrier serving these high-cost areas. In many states, incumbent LECs do not have the flexibility to raise rates to account for the elimination of the federal subsidy. A state could respond to this problem either by gradually phasing in cost-based rates to avoid rate shock (the preferred outcome) or by increasing the state subsidy to make up for the loss of federal funds. In any event, the decision to subsidize high-income areas should be made by and paid for by the states. In addition, as the ETI Study acknowledges, certain consumers in a particular high income CBG may not have the ability to pay cost-based local telephone rates without serious difficulty. Accordingly, where a state has transitioned to cost-based rates, it may be necessary to establish a "safety net" for those consumers. Finally, the FCC should consider establishing a cost-based local service "cap" beyond which all costs would be subsidized at the federal level, so as to avoid any consumer shouldering an extraordinarily burdensome monthly local telephone bill.

Ernest L. Bush

Biographical Sketch

Ernest Bush, Assistant Vice President - Regulatory Policy and Planning, BellSouth Telecommunications. Ernest began his telephone career in Macon, Georgia with Southern Bell in 1970 after graduating from the Georgia Institute of Technology, Atlanta, Georgia with a degree in Industrial Management. Ernest has held a number of positions within the Southern Bell Comptrollers department in Macon and Atlanta including operations and methods staff assignments. From March 1977 to January 1980 Ernest worked for AT&T in New Jersey in the Comptrollers Operations-CRIS (Customer Records Information System) department. Ernest returned to Southern Bell in February 1980 working in the CRIS group in Atlanta, Georgia. In April 1985 he was appointed Director-Federal Regulatory for BellSouth in the company's Washington office. Ernest returned to Atlanta in January, 1990 as Assistant Vice President-Regulatory, BellSouth Services. On October 1, 1991 he became Assistant Vice President-Regulatory Policy and Planning. He is currently responsible for the provision of staff support for regulatory policy and planning activities for BellSouth Telecommunications.

BIOGRAPHY

Joel B. Shifman

- Senior Advisor - Maine Public Utilities Commission
- Staff of 80-286 (Separations) Joint Board
- Lead Commenter for the "Rural States Group" in the § 254 Universal Service Joint Board Docket
- Leader of the Regulatory Methodologies Issue Group of the NARUC Staff Subcommittee on Communications
- Formally General Counsel of Maine Public Advocate
- Worked for 10 years as a Telecommunications Attorney with West Virginia Public Service Commission
- Bachelors Degree from Carnegie Mellon University - 1970 Pittsburgh, Pennsylvania
- Law Degree from West Virginia University - 1975 Morganstown, West Virginia

Hobbies: Telecomm History

Biographical Information on Peter Bluhm
May 28, 1998

Peter Bluhm holds a law degree from Albany Law School and a Master of Public Administration from S.U.N.Y. at Albany. For twenty years Peter has lived in Vermont and has worked for Vermont state government. For ten years he served as Legislative Draftsman and Committee Counsel to the Vermont Legislature. He also has worked as Vermont Assistant Attorney General for the Department of Mental Health, General Counsel to the Vermont State Board of Education, and as Vermont Deputy Secretary of Administration.

Currently Peter is employed as Director of Regulatory Policy at the Vermont Public Service Board where he directs the Board's legislative program and is the head of the Board's Telecommunications Team. He also serves as a hearing officer on cases from a variety of industries and is responsible for overseeing Vermont's Universal Service Fund for telecommunications.

Peter is also the Immediate Past-President of the Vermont School Boards Association.

VITA of
WARREN L. WENDLING

Mr. Wendling has been a member of the Staff of the Colorado Public Utilities Commission for 16 years and now serves in the capacity of the Supervising Professional Engineer. Mr. Wendling received his Bachelor of Science Degree in Electrical Engineering, Masters of Electrical Engineering, and Master of Business Administration from the University of Colorado, Boulder. He is a registered Professional Engineer in the State of Colorado.

Mr. Wendling has testified on numerous occasions before the Colorado Commission and Colorado State Courts as an expert witness. His testimony has addressed utility operating practices, and engineering issues, including outside plant construction. Since 1983, he has been involved primarily in telecommunications matters brought before the Colorado Commission. His work includes performing and advocating cost-of-service studies for telecommunications services.

Since 1990, Mr. Wendling has served as the lead Staff member in designing, advising and administering the Colorado High Cost Fund.

USWEST

Glenn Brown

Executive Director - Public Policy

Washington, D.C. Office

U S WEST, Inc.

Glenn Brown is presently Executive Director - Public Policy for U S WEST, Inc. in Washington, D.C. He began his career with Mountain Bell in 1971 in the Engineering Department, and in 1973 moved to the Rates and Tariffs organizations where he held a variety of assignments related to the pricing, costing and regulation of telecommunications services. Mr. Brown has presented testimony in over fifty state and federal commission proceedings on the pricing of a wide variety of telecommunication services. In 1985 Mr. Brown founded the first marketing organization within Mountain Bell focused on Interexchange Carrier customers. In 1990 he returned to the Public Policy organization where he was responsible for managing the Federal Regulatory staff. In 1993 he relocated to Washington, D.C. where he is responsible for managing a variety of public policy issues related to the introduction of local exchange competition and the preservation of universal service. Mr. Brown is active within the United States Telephone Association where he has served as Vice- Chairman of the Regulatory Policy Committee.

Mr. Brown has a Bachelor of Science degree in Industrial Engineering from Lehigh University and a Master of Business Administration degree for the University of Colorado.

Rev. May 28, 1998

"INTERSTATE HIGH COST AFFORDABILITY PLAN"

A Proposal by U S WEST
April 27, 1998

The Interstate High Cost Affordability Plan (IHCAP) is being proposed by U S WEST to assure the availability of affordable basic telephone service and network access to all Americans, particularly those living in rural and other high cost areas. We believe that this plan can form a workable alternative to the plan previously proposed by the Commission which assigned 25% of the explicit high-cost funding responsibility to the federal jurisdiction, and the remaining 75% to the states. We appreciate the FCC's intention, expressed in their April 10, 1998 Report to Congress, to reconsider this issue.

In their May 8, 1997 order, the FCC laid out a plan for accomplishing the directives of the Act. They defined a "benchmark" level (roughly $30 for residential customers) above which explicit universal service support would be required to assure affordable service. They also directed that a "proxy cost model" be developed to determine the cost of serving customers by "small areas of geography", such as Census Block Groups, Wire Centers or Grids. Costs for customers above the benchmark level would be aggregated and recovered from an explicit universal service mechanism. Recovery of these costs would be split into two pieces, with 25% of these costs recovered from an Interstate fund, and the remaining 75% of the costs recovered from separate State funds developed and administered by each state. The problem is that, for some states, removing all of the present implicit support and making it explicit would result in surcharges which could, themselves, threaten the basic concept of affordability. Generally, the states which will have the most difficulty have significant numbers of high-cost customers, but do not have large low-cost urban areas over which to spread these costs

The IHCAP plan solves this problem by defining a second "super-benchmark" to identify the "very-high" cost customers. Costs between the basic-benchmark ($30/month) and the super-benchmark (say, $50/month) would be handled the same as in the FCC's proposed plan, with 25% of the funding responsibility assigned to the interstate jurisdiction, and the remaining 75% assigned to the states. Costs above the super-benchmark would be assigned 100% to the interstate jurisdiction. Based upon our analysis to date, removing these "super-high" costs from the intrastate equation would appear to level the playing field, and leave each state with a more solvable problem.

One advantage of the IHCAP plan is that it leaves the primary role for rebalancing rates, defining the need for explicit support, and assuring the continued availability of affordable service with the people who know the local customers and the local markets best - the State regulators. The size of the interstate fund is kept smaller by assuming full support responsibility only for those costs in excess of $50/month (states would still be responsible for 75% of the costs between $30 and $50). Said another way, the interstate fund would cover 25% of costs between $30 and $50, and 100% of customer costs in excess of $50. Most of the customers who would be eligible for funding under the single-benchmark proposal, and a significant portion of the funding need, is due to customers slightly above the $30 benchmark but shy of the $50 super-benchmark. By leaving responsibility for most of these costs with state regulators, they will be able to devise rate rebalancing and/or explicit funding plans which are right for their markets. This plan also reduces the burden on customers in lower cost states, since it only requires them to contribute support to those customers who unquestionably will require some sort of assistance to retain affordable service.

The need for a plan like IHCAP is not limited to the western states served by U S WEST. Southern states, such as Mississippi, Kentucky and Alabama, New England states such as Vermont, New Hampshire and Maine, and Appalachian states like West Virginia have similar problems with many high cost customers and relatively few low cost customers. The IHCAP plan has been designed to benefit all Americans.

Lower cost states also benefit from IHCAP for two reasons. First, all states have some customers who are costly to serve. The IHCAP fund will support very high cost customers in all states, reducing the size of the problem that each state must deal with. Second, customers in all areas of the country benefit from ubiquitous access to all people and businesses nationwide. High cost and rural areas possess agricultural, energy and recreational resources on which urban areas depend. Rural areas contain many customers for goods and services produced in urban areas. IHCAP assures affordable service for all Americans, consistent with the directives of the 1996 Act.

BIOGRAPHY

JOEL E. LUBIN

AT&T Government Affairs

295 N. Maple Avenue
Room 5462B3
Basking Ridge, NJ 07920
Tel: (908) 221-7319 Fax: (908) 221-4628

Joel E. Lubin is Regulatory Vice President in the Law and Public Policy Organization at AT&T. He is responsible for developing public policy at the Federal and State levels. In particular, he formulates regulatory policies associated with access issues, universal service, local exchange competition and LEC regulation.

Prior to his present assignment, Joel held various positions in Federal Regulatory, Marketing, Service Cost and Rates, Long Lines and Bell Telephone Laboratories.

Joel received a BA degree in Mathematics from Wilkes College in 1969, an MS in Operations Research from Columbia University in 1972, and an MBA from Fordham University in 1976.

EXECUTIVE SUMMARY OF AT&T'S USF PROPOSAL

1. Local service revenues *alone* cover all universal service costs in the vast majority of the major non-rural LECs' (the RBOCs, GTE, and SNET) study areas. And this holds true without even counting the numerous other sources of support they have available such as intrastate toll services, yellow pages, and wireless services. These large LECs do not require *any* federal universal service support under present conditions. Therefore, regardless of what fund distribution methodology the Commission ultimately adopts, it should immediately cancel all federal payments to the major non-rural LECs until these LECs can show that the contribution they receive from the revenue sources that they enjoy due to their position as incumbent local monopolists has fallen below the forward-looking economic cost of universal service.

2. Under such circumstances it would be especially ironic if federal USF support to nonrural carriers would increase on January 1, 1999. Yet this appears likely to occur if support is calculated on a wire center or below basis. Not only will such a mechanism needlessly increase the size of the USF by allowing these large carriers to receive substantial payments for their minimal numbers of high-cost wire centers, but it also will allow these LECs to bank as pure profit all of the above-cost revenues that they receive from their lower-cost wire centers.

3. Because significant increases in the federal fund are not needed for universal service purposes. And because such increases would retard the development of local competition, and would damage both political support for the fund and its ability to be competitively

neutral, the Commission should calculate universal service support on no finer than a study area basis.

4. In addition, the Commission should consider deferring implementation of the new system. The assumed predicate for the new system was the widespread development of local competition, but such local competition has not yet arrived. Under these conditions, implementation of a new plan is not immediately necessary and, indeed, would be counterproductive if federal funding increases as a result.

SPRINT'S FEDERAL UNIVERSAL SERVICE FUND PROPOSAL

I. Existing, implicit subsidies must be eliminated. To the extent that subsidies are required, they should be funded through an explicit, competitively neutral USF.

- The elimination of explicit subsidies is required by the Telecommunications Act of 1996
- Existing, implicit access subsidies:
  - are not competitively neutral (only IXCs/toll users fund subsidies);
  - thwart facilities-based local competition; and
  - uneconomically and inequitably burden long distance users.

II. Principles upon which the federal USF plan should be based:

- ***Support should be based on forward looking costs***
  - Using a forward-looking cost methodology as the starting point in calculating the support amount is appropriate since it enables the Commission to arrive at a rate that emulates competitive market conditions. Facilities-based competition will not develop unless the sum of revenues and subsidies is predictable and accurate. Using forward-looking costs is the only way the marketplace will send the correct signals to potential entrants.
    - If costs are under-estimated, that will artificially attract inefficient entry that should not occur.
    - If costs are over-estimated, that will discourage efficient entry that should occur.

- ***Federal USF should be a national fund, based on both state and interstate retail revenues***
  - The Commission has stated, both in its May 8th Order and in its recent Report to Congress, that Section 254 grants it the authority to create a national fund made up of contributions from intrastate as well as interstate revenues.
  - In order to ensure competitive neutrality, as well as sufficient support flow between states, a national fund is not only reasonable, but essential.
  - To assess USF contributions on only interstate revenues would effectively exempt ILECs from contributing to universal service support.

- ***Where a cost-based rate might be considered prohibitive, the federal benchmark should be based on the maximum affordable local service rate***
  - Since the benchmark is intended to be a measure of "affordability" the appropriate standard is the basic local service rate, not average revenues.
  - Income considerations should be excluded, since low income households are addressed directly through the Lifeline/Link-up programs.
  - The federal benchmark rate should be set at a level representing the maximum affordable local service rate – a rate which is considerably higher than the below-cost local service rates that exist today

- ***Implementation of the plan should be revenue neutral at its inception***
  - Any new USF funding (i.e., funding in excess of current levels of high cost support) to a company should be offset, dollar–for-dollar, with reductions in access charges

- ***USF fund obligations should be recovered through a surcharge on end users' retail charges.***
  - The end user surcharge is the key to any workable USF plan. Without it, competitive neutrality, both in terms of contribution levels and recovery, is a virtual impossibility.
  - Because implicit subsidies exist today, end users are already supporting the universal service fund. Consequently, the removal of these implicit subsidies, replaced with the explicit surcharge, will not result in an overall increase in consumer charges.
  - In its recent order regarding Local Number Portability cost recovery, the Commission found that it was appropriate to allow LECs to recover their LNP costs through a monthly end user surcharge. The Commission should apply the same reasoning to USF cost recovery.

- ***States are free to adopt intrastate USF plans if they desire***
  - Employing a lower benchmark affordable rate, the state plan would act as a safety net for those areas where the federal benchmark rate may, in the state's opinion, prove burdensome.
  - Funding for state plans must come solely from intrastate retail revenues.