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July 17 1998

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FEDERAL COMMUNICATIONS COMMISSION
OFFICE OF THE SECRETARY

Ms. Magalie R. Salas
Secretary
Federal Communications Commission
1919 M Street, N.W.
Room 222
Washington, D.C. 20054

Re: *Ex Parte* - CC Docket Nos. 96-45, 97-160, DA 98-715, Federal State Board on Universal Service

Dear Ms. Salas:

On July 14, 1998, Dennis Weller of GTE sent the attached letter to Commissioner Julia Johnson of the Florida PUC. In accordance with Section 1.1206(a)(2) of the Commission's Rules, 47 C.F.R. section 1.1206(a)(2) (1991), please include this letter in the record of the above proceeding. Please contact me if you have any questions.

Sincerely

Alan Ciamporcero

Attachment

13 July 1998 HQE01J25

Ms. Julia Johnson
Chairman
Florida Public Service Commission
2540 Shumard Oak Boulevard
Talahassee, Florida, 32399-0850

Dear Ms. Johnson,

I greatly enjoyed the opportunity to meet with you last Friday, and to discuss the issues with respect to universal service which the Joint Board must address. I am writing to follow up on our conversation, and to put in writing a suggestion we discussed during that conversation.

It was clear to me during the recent Joint Board en banc hearing of 8 June that the Joint Board members share a sense of frustration over the FCC's inability to ensure that reductions in access charges will be passed through to consumers in the form of reductions in their long distance bills. As I made clear in my presentation to the Joint Board on that occasion, one of the objectives of the new Federal universal service plan should be to replace the implicit support generated today by interstate access charges. When such a plan is implemented, interstate access would be reduced dramatically, and consumers should accordingly benefit from a reduction in the rates they pay for long distance service. In our meeting on Friday, I showed you an analysis that indicates that, on average, consumers at every income level would be made better off by this reform of universal service funding.

However, consumers can only benefit if the reductions in access charges are passed through in the form of reductions in long distance charges. At the en banc, Chairman Wood of Texas asked representatives of AT&T and Sprint if they would pass through reductions in access charges – made possible by a new universal service fund – to their customers on a uniform basis. The answer was that IXCs would not do so. This prompted considerable discussion among the Commissioners. Chairman Wood expressed a strong concern that his constituents would be aware only of their contributions to a new universal service fund, and would not see the benefits that ought to result from the new plan. He asked the industry representatives present at the en banc to consider how the benefits could be passed through to consumers in an explicit manner on their bills, so that they could see how their contributions were being used.

You then focused the issue more sharply for me. You asked the AT&T representative why IXCs should automatically receive the benefit of any new universal service fund. On the way home from the en banc, I wondered if we had been asking the question of the IXCs in precisely the right way. In effect, Chairman Wood had assumed in his questions that IXCs would receive access charge reductions, and that they would have discretion over how those reductions would be passed through.

At one point in this discussion, Chairman Kennard of the FCC actually went so far as to suggest that the FCC's deregulation of AT&T – which had given them this discretion over their rates – might have been a mistake. I don't think any of us really wants to propose that the long distance market should be re-regulated. But it may be possible to construct an incentive plan under which IXCs would voluntarily pass through access charge reductions in a uniform way. This would involve asking the IXCs a different question: would they choose to receive access reductions, if those reductions were made conditional on a passthrough, or would they choose to forego the reductions entirely? I believe that, presented with such a choice, IXCs would choose to pass through uniform reductions to their customers.

I suggest that it would be entirely reasonable for the FCC, acting on the recommendation of the Joint Board, to condition its offer of access reductions in this way. After all, the reductions would not be made possible by anything the IXCs themselves had done, but rather by the contributions of millions of ratepayers. The FCC will have required these contributions in order to accomplish certain public policy goals, including the establishment of explicit, competitively neutral support for universal service, and the elimination of today's system of implicit support. If one of the goals established by the FCC and the Joint Board is the removal of implicit support payments from consumers' long distance bills, then it is reasonable for the FCC to require such removal as a condition for an IXCs' receipt of the access charge reductions made possible by consumers' contributions into the plan.

I suggest the following incentive plan to ensure that long distance customers receive the passthoughs they deserve:

1) The current interstate switched access tariffs of the ILECs would remain in place (as modified over time in accordance with the requirements of the FCC's price cap plan.) Call these Schedule A.
2) When a new Federal universal service plan is adopted, the funds the ILECs receive from this plan would be used to create a second, and much lower, interstate switched access tariff, which reflected – in addition to the normal price cap reductions -- a dollar-for-dollar passthrough by the ILEC of the new USF funds it receives. Call this second tariff Schedule B. (Of course, the FCC may choose to provide some of the new Federal funding to the states, to be used to replace implicit support generated today by state rates. The reductions in Schedule B would reflect only that portion of the new Federal fund that the FCC chose to apply toward interstate access reductions.)
3) An IXC could qualify to purchase access from Schedule B by agreeing to meet certain conditions:
    - The reductions in access the IXC received would be passed through to its end users in the form of a uniform, across-the-board reduction for all of the IXC's customers.
    - The reduction for each customer would appear as a separate credit on that customer's long distance bill, calculated as a uniform percentage of the customer's long distance expenditures. This would address Chairman Wood's concern that the reduction should be clearly visible to consumers. At the same time, it would address the concern raised by

IXCs at the en banc that it would be difficult for them to change all of the different rate plans these carriers offer. By the same token, showing the reduction as a separate line item would make it easy for the FCC to verify that the IXC had indeed met the conditions, without having to analyze the IXC's rates in detail.

4) If an IXC chooses not to accept the conditions, or if it fails to carry them out, then that IXC would purchase its access from Schedule A.

I believe that this incentive approach could provide the means to address the passthrough issue in a constructive way. The IXCs would continue to do business as non-dominant carriers. The access reductions made possible by universal service funding would be presented to them as an option, which they could take advantage of by agreeing to certain simple conditions. I believe that, when presented with this choice, all of the major IXCs would "take the pledge," and agree to pass through the benefits uniformly to their customers. However, this plan would not involve any new regulation of the long distance market, since IXCs would agree to these provisions voluntarily. Further, the benefits made possible by explicit universal service funding would be clearly visible to consumers, in the form of a separate credit on their long distance bills.

The FCC and the Joint Board have before them a historic opportunity to eliminate the current implicit support scheme, which is inefficient, unsustainable, and harmful to consumers. Unless and until this system is changed, competition for local residence telephone service in this country will be preempted, since the current implicit support is not portable to new carriers. As we discussed last Friday, the data indicate that consumers at every income level will benefit from a new, explicit, system that is more efficient and more competitively neutral. I recognize that the development of a new system will involve difficult choices, and the piecing together by the FCC and the Joint Board of a complex and delicate puzzle. The passthrough issue is an integral part of this puzzle, and I hope that the proposal I have outlined here may present part of the solution.

I would welcome any comments you may have, and the opportunity to work with you to further develop the ideas we have discussed. I may be reached by phone at 972 718-3489, and by email at dennis.weller@telops.gte.com. Thank you again for being so generous with your time, and for your willingness to discuss these important issues.

Very truly yours,

Dennis Weller
Chief Economist

CC: Mark Sievers
Alan Ciamporcero