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Before the
FEDERAL COMMUNICATIONS COMMISSION
Washington, DC 20554

In the Matter of	)	
	)	
Access Charge Reform for Incumbent	)	CC Docket No. 98-97
Local Exchange Carriers Subject to	)	
Rate-of-Return Regulation	)	

Comments of Harris, Skrivan & Associates, LLC to the Notice of Proposed Rulemaking on Access Reform for Carriers Subject to Rate-of-Return Regulation.

Harris, Skrivan & Associates, LLC (HSA) provides financial and regulatory consulting services to Incumbent Local Exchange Carriers Subject to Rate-of-Return Regulation throughout the United States. These comments are supported by the following incumbent local exchange carriers: Illinois Consolidated Telephone Company, Cross Telephone Company, Pottawatomie Telephone Company, Cimarron Telephone Company, Carnegie Telephone Company, Wilson Telephone Company, Bijou Telephone Cooperative Assn., Inc., Smithville Telephone Company, Wamego Telephone Company, Dobson Telephone Company, McLoud Telephone Company, Silver Star Telephone Company, Teton Communications, Home Telephone Company

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SUMMARY

Rate of Return Carriers are not like Price Cap Companies. As data filed in this proceeding by USTA demonstrates, the cost characteristics of rate-of-return carriers are very different than the cost characteristics of price cap carriers. Loops are longer, serving less populated subscriber areas, switches are smaller, yet require the same software and sophistication as do switches of price cap carriers, and the transport facilities required to serve rural customers are longer and subject to lower economies of scale than is true for price cap carriers. Therefore, while it is desirable to restructure rates for certain services, such revisions must reflect the underlying cost differences between price cap and rate-of-return carriers.

The Commission must evaluate the impact of implementing Subscriber Line Charges (SLCs) and Primary Interexchange Carrier Charges (PICCs) caps on the customers served by rate-of-return carriers. Due to the nature of the areas served by rate-of-return carriers, the costs of service are higher, which results in higher uncapped SLCs and PICCs for rate-of-return carriers. In order to approximate the impact that access restructure has had on the customers of price cap carriers, the Commission should cap SLCs and PICCs for rate-of-return carriers at the average SLCs and PICCs of the price cap carriers. In so doing, the Commission must recognize that there are only three feasible methods to recover the Common Line costs assigned to the interstate jurisdiction: 1) through flat-rated charges such as SLCs and PICCs; 2) through per minute rates such the Carrier Common Line (CCL); or through Universal Service Funding.

Many of the rate structure changes and new access rate elements should be made optional for carriers under rate-of-return regulation. The economic principles that apply to price cap companies are equally applicable to rate-of-return carriers. However, the cost/benefit ratio of implementing the new rate structures may be different due to the higher relative costs for smaller companies to track and gather data, and develop, file and defend the new rates proposed in the Notice. Therefore, the Commission should review each proposed rate element and make as many such rates optional as possible. To the extent that rates cannot be made optional, the Commission should designate default allocation factors to be used until such time as individual carriers develop their own allocation factors. For example, until such time as carriers

have had the opportunity to update Central Office Equipment Continuing Property Records, a default allocation of COE Category 3 to Line and Trunk Ports should be established. The Commission should establish the various allocators which could use default allocators and establish such defaults in a later portion of this proceeding.

The nature of NECA pooling will have an impact on Access Reform, as it relates to moving costs, revenues and/or residuals out of the Traffic Sensitive Pool and into the Common Line Pool. Price cap carriers can easily move revenues from one basket to another. It is less simple for rate-of-return carriers, particularly when an individual company may participate in the NECA Common Line Pool but not in the NECA Traffic Sensitive Pool. For example, under Commission rules for price cap carriers, the Transport Interconnection Charge (TIC) is to be reduced by application of the productivity offset to this element, then it is to be recovered through SLCs and PICC on non-primary lines, then it is to be recovered through the CCL, subject to CCL caps, and if these processes do not recover the TIC, the remainder is to be "sent back" to the Transport Basket to be recovered through a residual TIC. This is an impossible situation for companies with their own Traffic Sensitive tariffs but who participate in the NECA Common Line Pool.

The impact of access reform on the economic development of rural communities must be fully considered. One of the considerations of expanding businesses, in deciding where to location new operations, is the availability and cost of modern telecommunications. This was recognized by the Telecommunications Act of 1996, which requires reasonably comparable services be offered in high cost and rural areas of the Nation at rates reasonably comparable to rates for such service in urban areas. To the extent that SLCs and PICCs for rural areas served by rate-of-return carriers are higher than the SLCs and PICCs of price cap carriers, this is a highly noticeable distinction which could cause such companies not to locate business expansions in rural communities.

SPECIFIC RECOMMENDATIONS

This section will address specific questions, issues, proposals and tentative conclusions in the Notice.

In paragraph 4 of the Notice, the Commission requests comment on whether the implementation transition should be varied, as compared to the schedule for price cap carriers. HSA recommends that the Commission cap SLCs and PICCs for rate-of-return carriers at the nationwide average SLC and PICC rates for price cap carriers. This is simple to calculate and results in fair treatment of all subscribers in the Nation.

In paragraph 5 of the Notice, the Commission suggests that pricing flexibility and alternative regulation be addressed in a future Notice. HSA supports pricing flexibility alternative regulation concepts and urges the Commission to pursue such a proceeding in the very near future, perhaps on a parallel track to access reform. HSA notes that alternative regulation for midsize companies is in need of reform, as indicated by the lack of interest by midsize carriers in filing incentive tariffs under Section 61.50 of the Commission's rules. HSA suggests that the Commission revise its rules to make incentive regulation, as described in Section 61.39 of the Commission's rules, available to all companies with less than $100 million in annual operating revenues.

In paragraph 11 of the Notice, the Commission notes that economic efficiency is promoted when traffic sensitive costs are recovered through traffic sensitive rate elements, and non-traffic sensitive are recovered through flat-rated elements. HSA agrees with this principle, but cautions the Commission to move slowly, and balance the principle of economic efficiency against other principles such as reduction of regulatory burden and promotion of universal service.

In paragraph 12 of the Notice, the Commission notes that entry of competition into rural areas may be delayed due to the provisions of Section 251(F). HSA notes that there is nothing in Section 251(f) to prevent a facility-based carrier from entering a rural market, providing service, and interconnecting with the incumbent rural LEC. Such a competitor might be prevented from collocating or purchasing unbundled network elements, through the rural exemptions offered under Section 251(f). Such a competitor will be able to resell the incumbent LECs services, although it may not receive wholesale discounts on resold services. Further, while a few states have granted rural exemptions

to rural LECs under the 2% rule, there is very little, if any, evidence of a competitive LEC, which has been stymied from serving a rural area by such exemptions. Therefore, rural carriers cannot rely on Section 251(f) to protect them from having their most profitable customers taken by competitive LECs, especially if the rural carrier is located near a larger town.

In paragraph 17 of the Notice, the Commission notes that "average schedule recovery reduces the cost to small rate-of-return LECs of conducting separate cost studies by providing compensation based on cost estimates derived from comparable cost companies." While this is certainly true, and may have been the original purpose of the development of average schedule settlements, HSA notes that the operation of average schedule settlements is very similar to that of price cap regulation. Just like price cap carriers, average schedule carriers' revenue is based on demand for their services. Just like price cap carriers, annual operating efficiencies are reflected in lower rates (settlements) except that in recent years the implicit productivity offset for average schedules has exceeded that of the price cap carriers. Further, average schedule carriers have less downside protection than price cap carriers as average schedule carriers have no lower earnings threshold. HSA urges the Commission to consider the use of average schedules to be a form of incentive regulation and to make this option available to more rate-of-return carriers, with limitations implemented to prevent carriers from "gaming" the system.

In paragraph 32 of the Notice, the Commission notes the limits of the CCL charge for price cap carriers. The limit discussed is that the CCL, combined with the local switching, per minute TIC and per-minute marketing charges, does not exceed the sum of local switching, the per-minute CCL and the TIC assessed on originating minutes on December 31, 1997. In paragraph 35 of the Notice, the Commission proposes to adopt a similar rate structure for rate-of-return carriers. Due to the higher amounts of CCL revenue requirements for the rate-of-return LECs, the Commission needs to carefully analyze the amount of revenue requirements and rate development for rate-of-return carriers. For example, it makes sense, in rural areas, to leave the $.01 cap on originating CCL rates. This has served to prevent uneconomic bypass of the incumbent LECs facilities encouraged by the existing rate structure for recovery of Common Line costs.

In paragraph 35 of the Notice, the Commission tentatively concludes to adopt the same access rate structure for rate-of-return LECs as it did for price cap LECs. HSA supports this general conclusion, subject to limiting the caps on SLCs and PICCs, making many of the new rate elements optional and providing default allocators for rate-of-return carriers until such carriers can develop the data for their own allocators.

In paragraph 36 of the Notice, the Commission notes that it will take longer to align rates for rate-of-return carriers. HSA agrees with this conclusion and has worked with USTA to develop the data to quantify the amount of PICCs, SLCs, and/or CCL required by rate-of-return carriers to implement the access restructuring proposed by the Commission.

In paragraph 40 of the Notice, the Commission requests comment on how SLCs and PICCs should be capped for rate-of-return carriers. HSA recommends that SLCs and PICCs for rate-of-return carriers be capped at the average SLCs and PICCs of the price cap carriers. It would reduce the administrative burden to use the nationwide averages, rather than regional averages or the average of the nearest price cap LEC. Also, if regional averages are used, NECA would be required to file different SLCs and PICCs for member companies in different regions of the country. The mechanism of the pooling process was designed to provide average rates for pool members, therefore the pooled rates, based on national averages would be more appropriate.

In paragraph 45 of the Notice, the Commission asks for comment on whether it should take a single approach for all rate-of-return carriers. HSA recommends that the Commission take a single approach to rate-of-return carriers. There is no evidence of a need to treat rate-of-return LECs differently due to size or geography served. However, should the Commission find it necessary to make distinctions between the large and small rate-of-return LECs, the distinction should be made at the $100 million annual revenue **as** described in Section 32.9000 of the FCC's rules, under the definition for **"Indexed revenue threshold for a given year"** means $100 million, adjusted for inflation, as measured by the Department of Commerce Gross Domestic Product Chain-type Price Index ("GDP-CPI"), for the period from October 19, 1992 to the given year.

In paragraph 45 of the Notice, the Commission asks if there are concerns specific to NECA pooling companies that need to be addressed. There are several issues in the

proposal that will need to be specifically addressed for pooling companies prior to implementation of access restructure. The basic issue, which must be dealt with, is the movement of costs between the Common Line Pool and the Traffic Sensitive Pool. This is made more difficult by the limits on SLCs, PICCs, and CCL, which may result in the rate level impacting the amount of costs to be moved from one pool to another.

The movement of Traffic Sensitive marketing costs to the Common Line pool is easily accomplished from a cost allocation standpoint, but the implication on rate levels may make it difficult to recover the costs through the Common Line rate elements for rate-of-return carriers. HSA supports USTA's recommendation that marketing costs be left in the Traffic Sensitive Pool, due to the impact on Common Line rates of moving the costs to the Common Line Pool.

The movement of Line Port costs from Traffic Sensitive Local Switching to Common Line will require careful coordination between the NECA Common Line Pool and rate-of-return carriers which file their own Traffic Sensitive tariffs. In the Access Reform Order for price cap carriers, the Commission required that line cards, protectors and the main distribution frame be moved from Local Switching to Common Line. For many rate-of-return carriers, this change will required significant resources in order to perform the required analysis. Therefore, HSA recommends that the Commission establish a default allocation factor to be used until companies have developed their own factors. Similar rules should be developed to identify the trunk port portion of the Local Switching, which the Commission proposes to move to a flat-rated element.

The Commission's proposal to move the TIC from Transport to Common Line presents major difficulties for rate-of-return carriers. First, the transfer of the TIC to Common Line seems to be predicated on an erroneous belief that the TIC represents uneconomic costs, the source of which is an over-allocation of costs to the interstate jurisdiction, based on faulty separations rules. The assumptions seem to be that separations reform will fix this allocation problem. HSA does not believe the TIC will be fixed by revised separations rules, nor do we accept the theory that the TIC represents uneconomic costs. The separations treatment of interexchange plant is already rational. (HSA does note that separations may under-allocate costs of interexchange circuit equipment to Private Line, resulting in an overall appropriate allocation of costs to

interstate, but an under-allocation of interstate costs to Special Access.) The rules require that actual investment in interexchange facilities be identified and jurisdictionally allocated on the actual use of the facilities. HSA believes the true reason for the existence of the TIC is due to under-allocation of costs to Special Access, either through the circuit termination count issues or through other Part 69 allocators. This under-allocation of costs to Special Access results in lower Special Access rates, lower Tandem Switched Transport rates and lower Direct Trunked Transport rates. The TIC represents the difference between the Local Transport revenue requirement and the anticipated revenues from the other Local Transport rate elements. Therefore, if Special Access is under-priced, this will increase the TIC. **The TIC represents real interstate transport costs and ought to be recovered through interstate transport rate elements.**

Should the Commission elect to move the TIC from Local Transport to Common Line, it will introduce an extremely difficult rate-making problem for NECA's Common Line pool. First, the TIC is not an access element with associated rate base and revenue requirements. Rather, the TIC is a residual revenue shortfall, which is the difference between a company's Local Transport revenue requirement and the revenue a company can expect to receive through its transport rates – as develop by use of Special Access rates.

Secondly, under price cap access rules, the TIC is allocated to Common Line only to the extent SLCs, PICCs, and CCL rates do not exceed their associated caps. The remainder of the TIC is recovered through a residual TIC. While this process is slightly awkward for price cap carriers, it is nearly impossible in a pooled environment. For example, each company will have a different TIC, so how does the Pool decide how much of each company's TIC can be recovered through capped rates? This proposal is difficult enough for companies which participate in both the Common Line and Traffic Sensitive Pools, but even more problematic for companies which file their own Traffic Sensitive Tariffs. Furthermore, the existence of residual costs in the Common Line Pool would create quite a challenge in the measurement of reporting of Pool earnings. This is because the TIC is a residual revenue shortfall, not a revenue requirement with rate base and expenses.

In paragraph 46 of the Notice, the Commission requests comment on the use of the same SLC and PICC equivalency ratios for rate-of-return carriers as was prescribed for price cap carriers. HSA supports the use of the same ratios. There is no need to develop additional record for this item.

In paragraph 50 of the Notice, the Commission identifies the current process of allocating Local Switching costs between the state and interstate jurisdictions. In this proceeding, the Commission has proposed rate restructures which would significantly reduce the per-minute Local Switching rates. However, the Commission should take note that there are several proposals in Separations Reform, which would allocate more costs to the interstate traffic sensitive portion of Local Switching. First, under existing separations rules, Local Switching costs are allocated to interstate based on Dial Equipment Minutes (DEM). DEM is actually a measurement of the usage of the line ports on a switch and counts local minutes twice and interstate minutes once. If separations rules are revised to reflect the sub-categorization of Local Switching (Central Office Equipment Category 3) into Line Ports, Trunk Ports and Shared Investment (the usage sensitive portion), it is likely that the usage sensitive portion of the switch will be/should be jurisdictionally allocated in a more rational manner, using switch minutes of use. This would increase the allocation of Local Switching costs to interstate. Second, if the jurisdictional nature of Internet is determined to be interstate, a significant additional portion of Local Switching will be allocated to interstate. Therefore, the Commission should consider coordinating the implementation of access reform for rate-of-return carriers with the implementation of separations reform.

In paragraph 67 of the Order, the Commission tentatively concludes that rate-of-return carriers should recover trunk ports used to terminate dedicated trunks on the serving wire center side of the tandem switch through flat-rated charges. The Commission further requests comment on whether rate-of-return LECs should have the option of using the same rates as were developed for the Local Switching trunk ports. HSA supports the use of the tandem switch trunk portion element, and supports the option of mirroring the Local Switching trunk port rates.

In paragraph 68 of the Notice, the Commission proposes to require rate-of-return carriers to implement a multiplexing element to recover costs associated with tandem

switching that were reassigned from TIC costs. The Commission further requests comment on whether to allow rate-of-return LECs to mirror the multiplexing rate from their Special Access tariffs. HSA supports the implementation of an option rate element to recover multiplexing equipment associated with the tandem switch. HSA further supports the optional use of the multiplexing charge developed for Special Access.

In paragraph 70 of the Notice, the Commission requests comment on its proposal to move residual TIC to Common Line. HSA opposes this proposal. The main drawback to this proposal is that the TIC represents real interexchange transport costs. As described earlier, the main source of the TIC is the under-allocation of costs to Special Access. If the Commission desires to eliminate the TIC as a separate rate element, the best course of action would be to allocate the TIC among the following interstate access elements: Tandem Switched Transport; Direct Trunked Transport; and the interexchange portion of Special Access, specifically the Channel Mileage Termination and Channel Mileage Facilities rate elements. This allocation will recover the TIC, which represents real transport costs, from the interstate interexchange rate elements. HSA notes that this reallocation will need to become a permanent part of the interstate rate development rules for rate-of-return carriers. Unlike price cap carriers, rate-of-return carriers cannot eliminate a cost element by means of a one-time transfer to other rate elements.

In paragraph 82 of the Notice, the Commission proposes to implement new General Support Facility (GSF) allocation rules, to move more of the costs of GSF to the interstate Billing and Collection element. For those carriers, which have GSF investment associated with billing services, it is reasonable for such investment to be associated with the billing services provided. However, this proposal by the Commission to revise the treatment of GSF simply adds insult to injury for the erroneous allocation of the interstate portion of Other Billing & Collection (OB&C) Costs primarily to the Billing & Collection element. OB&C is the process of preparing and mailing bills to customers. The primary purpose of such billing is to bill for basic services such as for the Common Line. **As such, the primary nature of the OB&C costs are Common Line costs, very similar to the loop costs which are allocated to interstate and assigned to the Common Line category.** The Commission has concluded that the portion of OB&C assigned to interstate is primarily associated with the provision of toll billing services to

interexchange carriers. HSA strongly recommends that the Commission revise its Part 69 cost allocation procedures, for rate-of-return carriers, to allocate the majority of interstate OB&C costs to Common Line. This is consistent with the nature of the costs and sound economic theory. The primary purpose of billing is to recover fees for basic services. Basic services are required for both state and interstate services. This makes the cost of bill rendering a Common Line cost. Should a rate-of-return carrier provide no billing services to interexchange carriers, it is likely that such a rate-of-return LEC would continue to bill for basic services. However, should such a LEC discontinue the need to bill for basic services, it is very unlikely it would continue to render long distance bills for interexchange carriers. Therefore, the primary purpose of the OB&C costs relate to Common Line billing and Part 69 allocations ought to reflect this reality. Only after these changes have been made, will it make any sense to allocate GSF costs to match the use of GSF facilities to provide billing services.

In paragraph 86 of the Notice, the Commission tentatively concludes that marketing costs should be recovered through the Common Line recovery mechanism. It appears that the Commission wants to move Marketing costs to Common Line in anticipation of the separations reform which, under Commission proposals, would assign Marketing costs primarily to the state jurisdiction. However, HSA notes that the primary purpose of marketing costs is to promote basic services. This includes access to the network and vertical features, such as touch tone calling and Caller ID services. HSA notes that the basic services are required in order for subscribers to use either state or interstate services, and therefore the promotion of such basic services is actually a common cost, properly associated with the Common Line. HSA has recommended in its comments on separations reform that Marketing cost be treated in the same manner as Common Line costs, with the same interstate allocator and the same assignment to Common Line through the Part 69 Process. Until such separations rules are enacted, however, it is consistent to treat the current portion of interstate Marketing costs as Common Line. Therefore, HSA supports the assignment of all interstate Marketing costs to Common Line, due to the nature of such costs as common costs of adding subscribers to the public switched network.

In paragraph 90 of the Notice, the Commission asks for comments on its price cap proposal to implement a PICC for Special Access services. The Commission asks whether, if it implements a PICC for Special Access for price cap carriers, should it also implement PICCs for Special Access for rate-of-return carriers. HSA opposes the implementation of PICCs on Special Access for either price cap or rate-of-return carriers.

In paragraph 92 of the Notice, the Commission requests comment on any other cost allocation modifications required in this proceeding. HSA reiterates its recommendation that the Commission review its Part 69 cost allocation procedures for rate-of-return carriers related to OB&C expenses. HSA recommends that since the primary purpose of OB&C is to provide billing for basic services and since basic services are a common cost of access to state and interstate services, that the majority of OB&C costs assigned to interstate should be assigned to the Common Line category.

Respectfully Submitted,

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