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Federal Communications Commission

DA 98-1733

DISPATCHED BY

Before the
Federal Communications Commission
Washington, D.C. 20554

In the Matter of)	CC Docket No. 96-45
)	
Kendall Telephone, Inc. and)	
Wisconsin Bell, Inc.)	
)	
Definition of "Study Area" Contained)	
in the Part 36 Appendix-Glossary)	
of the Commission's Rules)	
)	
Kendall Telephone, Inc. Petition for Waiver of)	
Sections 61.41(c)(2), 69.3(e)(6), and 69.3(g)(2))	
of the Commission's Rules)	

MEMORANDUM OPINION AND ORDER

Adopted: September 15, 1998

Released: September 15, 1998

By the Chief, Accounting Policy Division:

I. INTRODUCTION

1. On May 13, 1998, Kendall Telephone, Inc. ("Kendall") and Wisconsin Bell, Inc. ("Ameritech Wisconsin") filed a petition for waiver of the definition of "Study Area" contained in the Part 36 Appendix-Glossary of the Commission's rules. The requested waivers would allow Kendall and Ameritech Wisconsin to alter their Wisconsin study area boundaries to reflect the sale of 19 local telephone exchanges from Ameritech Wisconsin to Kendall. Kendall also seeks a waiver of section 61.41(c)(2) of the Commission's rules which would permit Kendall to continue to be regulated under rate-of-return regulation after acquiring exchanges that are currently under price cap regulation. In addition, Kendall seeks a waiver of section 69.3(e)(6) of the Commission's rules, so that it may withdraw from the National Exchange Carrier Association, Inc. ("NECA") traffic sensitive pool and participate in the Telephone Utilities Exchange Carriers Association ("TUECA") traffic sensitive pool.¹ Kendall also seeks waiver of section 69.3(g)(2) to permit more than 50,000 access lines to enter the NECA common line pool.

¹ TUECA is an association of several affiliated telephone operating companies that, like Kendall, are owned by Pacific Telecom, Inc.

2. On May 27, 1998, the Common Carrier Bureau ("Bureau") released a public notice soliciting comments on the petition.² No comments were filed.³ In this Order, we grant the relief requested, as explained below.

II. DISCUSSION

A. Study Area Waivers

3. A study area is a geographic segment of an incumbent local exchange carrier's ("incumbent LEC") telephone operations. Generally, a study area corresponds to an incumbent LEC's entire service territory within a state. Thus, incumbent LECs operating in more than one state typically have one study area for each state. The Commission froze all study area boundaries effective November 15, 1984,⁴ and an incumbent LEC must apply to the Commission for a waiver of the study area boundary if it wishes to sell or purchase an exchange.

4. Universal service support currently is awarded to carriers based on the average cost of providing service throughout the carrier's study area. The Commission's *Universal Service Order* altered the method used to determine the distribution of universal service support for buyers of high cost exchanges.⁵ In the *Universal Service Order*, the Commission recognized that "[u]ntil support for all carriers is based on a forward-looking economic cost methodology, . . . potential universal service support payments may influence unduly a carrier's decision to purchase exchanges from other carriers."⁶ To discourage carriers from transferring exchanges merely to increase universal service support, the Commission concluded that a "carrier making a binding commitment on or after May 7, 1997 to purchase a high cost exchange should

² Kendall Telephone, Inc. and Wisconsin Bell, Inc. Filed Petition for Waiver of Sections 61.41(c), 69.3(e)(6), 69.3(g)(2) and the Definition of "Study Area" in Part 36 of the Commission's Rules, *Public Notice*, DA 98-1000, (rel. May 27, 1998).

³ Prior to the filing of the petition, several hundred members of the Communications Workers of America union sent letters to FCC Chairman William E. Kennard regarding this transaction.

⁴ 47 C.F.R. § 36 app. (defining "study area"). See MTS and WATS Market Structure, Amendment of Part 67 of the Commission's Rules and Establishment of a Joint Board, *Recommended Decision and Order*, 49 Fed. Reg. 48325 (Dec. 12, 1984) ("*1984 Joint Board Recommended Decision*"); *id.*, *Decision and Order*, 50 Fed. Reg. 939 (Jan. 8, 1985) ("*1985 Order Adopting Recommendation*"); see also Amendment of Part 36 of the Commission's Rules and Establishment of a Joint Board, *Notice of Proposed Rulemaking*, 5 FCC Rcd 5974 (Oct. 10, 1990) ("*Study Area Notice*").

⁵ See Federal-State Joint Board on Universal Service, CC Docket No. 96-45, *Report and Order*, 12 FCC Rcd 8776, 9002, 9054-62, 9139-45 (1997) (*Universal Service Order*), as corrected by Federal-State Joint Board on Universal Service, *Errata*, CC Docket No. 96-45, FCC 97-157 (rel. June 4, 1997).

⁶ *Universal Service Order*, 12 FCC Rcd 8942, ¶ 308.

receive the same level of support . . . as the seller received prior to the sale."⁷ For example, if a rural carrier acquires an exchange from another rural carrier, the acquired lines will continue to receive the per-line support that the selling company received prior to the sale.⁸ Eventually, support for all carriers will be based on a forward-looking economic cost methodology allowing carriers to receive support for all high-cost exchanges, including exchanges acquired from other carriers, based on the forward-looking economic cost methodology.⁹

5. Ameritech Wisconsin, an incumbent LEC that currently serves 2,135,407 access lines in Wisconsin, proposes to sell 19 exchanges that serve approximately 85,000 access lines in northern and central Wisconsin.¹⁰ Ameritech Wisconsin seeks a waiver of the rule freezing study area boundaries to allow it to remove these exchanges from its study area. Kendall, a wholly-owned subsidiary of Pacific Telecom, Inc. ("PTI"), is an incumbent LEC that currently serves 586 access lines in Wisconsin.¹¹ Kendall seeks a waiver of the rule freezing study area boundaries to allow the addition of the 19 exchanges to its existing study area.¹²

6. The petitioners state that the transfer of the 19 exchanges from Ameritech Wisconsin to Kendall will promote the public interest because it will provide the customers in the affected exchanges with additional and improved services from a carrier that specializes in meeting the communications needs of rural and small urban communities.¹³ Kendall is planning additional infrastructure investment and service upgrades in the purchased exchanges, such as offering long-distance service and introducing voice mail and local Internet dial-up access.¹⁴ Finally, the petitioners assert that under the Commission's *Universal Service Order*, Kendall is entitled to receive only the same amount of high cost assistance for the 19 exchanges that Ameritech Wisconsin received before the transfer.¹⁵ Ameritech

⁷ *Id.*

⁸ *Id.*

⁹ *Id.*

¹⁰ Petition at 1. *See also* NECA Universal Service Fund 1997 Submission of 1996 Study Results filed October 1, 1997.

¹¹ PTI is a wholly-owned subsidiary of Century Telephone Enterprises, Inc., which owns a total of ten local telephone companies operating in Wisconsin. Petition at 3.

¹² Petition at 1.

¹³ *Id.* at 10.

¹⁴ *Id.* at 11.

¹⁵ *Universal Service Order*, 12 FCC Rcd 8942, ¶ 308.

Wisconsin states that it receives no support from the high cost fund, and therefore, Kendall does not expect to receive any such support for the 19 exchanges after it acquires them.

7. Waiver of a Commission rule is appropriate only if special circumstances warrant deviation from the general rule and such a deviation will serve the public interest.¹⁶ In evaluating petitions seeking a waiver of the rule freezing study area boundaries, the Commission employs a three-prong standard: first, the change in study area boundaries must not adversely affect the universal service fund;¹⁷ second, no state commission having regulatory authority over the exchanges to be transferred may oppose the transfer; and third, the transfer must be in the public interest.¹⁸

8. The transfer of exchanges from Ameritech Wisconsin to Kendall meets each of the requirements of the three-prong test established by the Commission. First, the transfer will not affect universal service support. Under the *Universal Service Order*, Kendall is entitled to receive only the same amount of high cost support for the purchased exchanges that Ameritech Wisconsin received before the transfer, which in this case is no support. Second, the Public Service Commission of Wisconsin does not object to the requested waivers.¹⁹ Third, grant of the requested study area waivers will promote the public interest. Kendall plans to upgrade facilities and improve customer service in the acquired exchanges. Thus, the petitioners have demonstrated that the customers in these exchanges will likely be well served by Kendall.²⁰ In summary, we find that the three-prong standard for granting study area waivers has been met in this instance and that the waiver requests should be granted.

¹⁶ 47 C.F.R. § 1.3. *Northeast Cellular Tel. Co. v. FCC*, 897 F.2d 1164, 1166 (D.C. Cir. 1990); see also *WAIT Radio v. FCC*, 418 F.2d 1153, 1159 (D.C. Cir. 1969).

¹⁷ See 1984 Joint Board Recommended Decision, *supra* note 4, ¶ 66. The Commission created the universal service fund to preserve and promote universal service. See Amendment of Part 67 of the Commission's Rules and Establishment of a Joint Board, *Decision and Order*, 96 FCC 2d 781 (1984). The universal service fund allows incumbent LECs with high local loop plant costs to allocate a portion of those costs to the interstate jurisdiction, thus enabling the states to establish lower local exchange rates in study areas receiving such assistance. See 47 C.F.R. § 36.631.

¹⁸ See *US WEST Communications, Inc., and Eagle Telecommunications, Inc., Petition for Waiver of the Definition of "Study Area" Contained in Part 36, Appendix-Glossary of the Commission's Rules, Memorandum Opinion and Order*, 10 FCC Rcd 1771, ¶ 5 (1995) ("*US WEST-Eagle Study Area Order*").

¹⁹ See Letter from, Lynda L. Door, Secretary to the Public Service Commission of Wisconsin, to A. Richard Metzger, Jr., FCC, dated May 11, 1998.

²⁰ Petition at 10.

B. Price Caps Waiver

9. Section 61.41 of the Commission's rules provides that, when a cost company²¹ acquires a price cap company,²² the acquiring company, and any incumbent LEC with which it is affiliated, shall become subject to price cap regulation within a year of the transaction.²³ The Commission stated that this "all-or-nothing" rule applies not only to the acquisition of an entire incumbent LEC but also to the acquisition of part of a study area.²⁴ Ameritech Wisconsin is a price cap company; hence, absent a waiver, Kendall's acquisition of Ameritech Wisconsin exchanges would normally obligate Kendall to become subject to price cap regulation.

10. The Commission nonetheless recognized that a narrow waiver of section 61.41(c)(2) might be justified if efficiencies created by the purchase and sale of a few exchanges outweigh the threat that the transfer is designed to, or does, thwart the Commission's rules.²⁵ Such a waiver would not be granted unconditionally, however. Rather, the Commission has held that waivers would be granted subject to the condition that the

²¹ Cost companies are those incumbent LECs that receive compensation for the use of their facilities in originating and terminating telecommunications services on the basis of their actual costs. Although Kendall currently is an average schedule company, it states that it intends to convert to a cost company simultaneously with the closing of the purchase of the 19 exchanges.

²² Price cap companies are those incumbent LECs that receive compensation for the use of their facilities originating and terminating interstate telecommunications services on the basis of the Commission's price cap rules. 47 C.F.R. §§ 61.41-61.49.

²³ 47 C.F.R. § 61.41(c). See Policy and Rules Concerning Rates for Dominant Carriers, *Second Report and Order*, 5 FCC Rcd 6786, 6821 (1990), *Erratum*, 5 FCC Rcd 7664 (Com. Car. Bur. 1990) ("*LEC Price Cap Order*"), *modified on recon.*, *Order on Reconsideration*, 6 FCC Rcd 2637 (1991) ("*LEC Price Cap Reconsideration Order*"), *aff'd sub nom. National Rural Telecom Ass'n v. FCC*, 988 F.2d 174 (D.C. Cir. 1993), *petitions for further recon. dismissed*, 6 FCC Rcd 7482 (1991), *further modification on recon.*, Amendments of Part 69 of the Commission's Rules Relating to the Creation of Access Charge Subelements for Open Network Architecture, Policy and Rules Concerning Rates for Dominant Carriers, *Report and Order and Order on Further Reconsideration and Supplemental Notice of Proposed Rulemaking*, 6 FCC Rcd 4524 (1991) ("*ONA Part 69 Order*"), *further recon.*, *Memorandum Opinion and Order on Second Further Reconsideration*, 7 FCC Rcd 5235 (1992).

²⁴ See *LEC Price Cap Reconsideration Order*, *supra* note 23, ¶ 149 n. 207. The Commission explained that, if these two types of acquisitions were not treated the same under the all-or nothing rule, a carrier could avoid the rule by selling all but one of its exchanges. *Id.*

²⁵ See *LEC Price Cap Reconsideration Order*, *supra* note 23, ¶ 148. The Commission explained that the rules under section 61.41(c)(2) are intended to address a concern regarding mergers and acquisitions involving price cap companies. Absent these rules, an incumbent LEC may attempt to "game the system" by switching back and forth between rate-of-return regulation and price cap regulation. For example, a price cap company may have incentive to increase earnings by opting out of price cap regulation, building up a large rate base under rate-of-return regulation so as to raise rates and, then, after returning to price caps, cutting costs back to an efficient level. *Id.* ¶ 149, note 207.

selling price cap company make a downward adjustment to its price cap indices to reflect the change in its study area.²⁶ That adjustment is needed to remove the effects of the transferred exchanges from rates that have been based, in whole or in part, upon the inclusion of those exchanges in the study areas subject to price cap regulation.²⁷

11. Kendall seeks a waiver of section 61.41(c)(2) so that it may continue to operate as a rate-of-return incumbent LEC, rather than a price cap incumbent LEC. A primary purpose of section 61.41(c)(2) is to prevent gaming by shifting back and forth between price cap regulation and rate-of-return regulation. There is not any evidence or allegation that either party is pursuing this exchange as a means to circumvent the Commission's rules. Moreover, requiring Ameritech Wisconsin to make an exogenous cost reduction eliminates inappropriate incentives to sell high-cost areas, and so gives additional protection against gaming. We therefore find there is good cause to grant Kendall a waiver to permit it to remain under rate-of-return regulation after acquiring the exchanges that currently are under price cap regulation. This waiver is subject to the condition that Ameritech Wisconsin shall make a downward adjustment to its price cap indices to reflect the removal of the 19 exchanges from its Wisconsin study area.²⁸

C. Waiver of Section 69.3(e)(6)

12. Kendall seeks a waiver of section 69.3(e)(6) of the Commission's rules. That rule requires that any company electing to participate in a non-NECA tariff must notify NECA of such election no later than December 31 of the year preceding such action. Kendall seeks a waiver in order to participate in a non-NECA traffic sensitive tariff upon consummation of the transaction. Kendall proposes to withdraw from the NECA traffic sensitive pools and to participate in the Telephone Utilities Exchange Carriers Association²⁹ traffic sensitive pools coincident with its acquisition of the 19 exchanges.³⁰ The petitioners state that granting the waiver will produce administrative efficiencies for Kendall and will not adversely impact the NECA traffic sensitive pool.³¹ In addition, Kendall states that it has contacted NECA regarding

²⁶ See Price Cap Performance Review for Local Exchange Carriers, *First Report and Order*, 10 FCC Rcd 8961, 9104-05, ¶ 328, 9105-06 ¶ 330 (1995) ("*LEC Price Cap Review Order*"). The Price Cap Indices, which are the upper bounds for rates that comply with price cap regulation, are calculated pursuant to a formula specified in the Commission's rules for price cap carriers. See 47 C.F.R. § 61.45.

²⁷ See *LEC Price Cap Review Order*, *supra* note 26, ¶ 330.

²⁸ Ameritech Wisconsin estimates that the downward adjustment in its price cap index will be approximately \$1.2 million. See Letter from Julian P. Gehman, Mayer, Brown & Platt, to Adrian Wright, FCC, dated July 14, 1998.

²⁹ See *supra* note 1.

³⁰ Petition at 16.

³¹ *Id.*

its intention to withdraw from the NECA traffic sensitive pool coincident with its acquisition of the 19 exchanges. Kendall states that NECA expressed no objection to Kendall's withdrawing from the NECA traffic sensitive tariff.³² NECA confirmed that it did not object to Kendall withdrawing its 586 access lines from the NECA traffic-sensitive pool.³³ NECA further stated that the withdrawal would not have a significant impact on NECA's calculation of its traffic-sensitive revenue requirement and should not prejudice NECA or any pool member.³⁴ We conclude that there is good cause to grant Kendall a waiver of section 69.3(e)(6) because NECA's traffic sensitive pool will not be adversely affected.

D. Waiver of Section 69.3(g)(2)

13. Kendall also seeks a waiver of section 69.3(g)(2) of the Commission's rules. Under section 69.3(g)(2), a NECA common line tariff participant that is a party to an acquisition may include telephone properties it acquires in the NECA common line tariff, provided that the net addition of common lines to NECA tariff resulting from the transaction does not exceed 50,000 access lines and provided further that if any of the common lines involved in the acquisition are returned to the NECA common line tariff then all of them must be returned. Kendall proposes to comply with the second requirement of the rule, but needs a waiver of the 50,000 access line cap in order to do so. Kendall states that it wants to include all of its access lines in the NECA common line tariff.³⁵ Kendall argues that the 50,000 access line cap was intended to be waived in the case of mergers or acquisitions that would not have an adverse impact on the overall common line pooling structure.³⁶

14. Kendall asserts that no entity will experience a significant increase in its universal service obligations if this waiver is granted, because the impact on the revenue requirement for the NECA common line pool is expected to be insignificant. Kendall states that, based on current NECA pooling data and projected demand and cost data, Kendall's acquisition of the 19 exchanges would produce an impact on the common line pool revenue requirement of no more than 0.07%.³⁷ Kendall states that it has informed NECA of its intent to return all of its lines to the common line pool, and NECA has indicated that it anticipates that any impact on the pool

³² See Letter from Perry Goldschein, NECA, to Adrian Wright, FCC, dated July 15, 1998.

³³ *Id.*

³⁴ *Id.*

³⁵ Petition at 17.

³⁶ Amendment of Part 69 of the Commission's Rules Relating to the Common Line Pool Status of Local Exchange Carriers Involved in Mergers or Acquisitions, *Report and Order*, 5 FCC Rcd 231 (1989).

³⁷ Petition at 21.

would be insignificant.³⁸ NECA confirmed that it does not object to Kendall adding all of the access lines it is acquiring from Ameritech Wisconsin to the NECA common line tariff.³⁹ NECA further stated that such inclusion should not have a substantial adverse effect of the NECA common line pool on other LECs.⁴⁰ We conclude that there is good cause to grant Kendall a waiver of section 69.3(g)(2) because NECA's common line pool will not be adversely affected,⁴¹ and there will be no significant increase in the long-term support or transitional support obligations of the remaining non-pooling LECs.⁴²

III. ORDERING CLAUSES

15. Accordingly, IT IS ORDERED, pursuant to sections 1, 4(i), 5(c), 201 and 202 of the Communications Act of 1934, as amended, 47 U.S.C. §§ 151, 154(i), 155(c), 201 and 202, and sections 0.91, 0.291, and 1.3 of the Commission's rules, 47 C.F.R. §§ 0.91, 0.291, and 1.3, that the petition of Kendall Telephone, Inc. and Wisconsin Bell, Inc. for waiver of Part 36, Appendix-Glossary, of the Commission's rules, 47 C.F.R. Part 36 Appendix-Glossary IS GRANTED.

16. IT IS FURTHER ORDERED, pursuant to sections 1, 4(i), 5(c), 201 and 202 of the Communications Act of 1934, as amended, 47 U.S.C. §§ 151, 154(i), 155(c), 201 and 202, and sections 0.91, 0.291, and 1.3 of the Commission's rules, 47 C.F.R. §§ 0.91, 0.291, and 1.3, that the petition of Kendall Telephone, Inc. for waiver of sections 61.41(c)(2), 69.3(e)(6), and 69.3(g)(2) of the Commission's rules, 47 C.F.R. §§ 61.41(c)(2), 69.3(e)(6), and 69.3(g)(2) ARE GRANTED.

17. IT IS FURTHER ORDERED, pursuant to sections 1, 4(i), 5(c), 201 and 202 of the Communications Act of 1934, as amended, 47 U.S.C. §§ 151, 154(i), 155(c), 201 and 202, and sections 0.91, 0.291, 1.3, and 61.43 of the Commission's rules, 47 C.F.R. §§ 0.91, 0.291, 1.3, and 61.43, that Ameritech Wisconsin SHALL ADJUST its price cap indices as discussed in paragraph 11 above, to reflect in its annual price cap filing, cost changes resulting from this transaction.

³⁸ *Id.*

³⁹ *See also* Letter from Perry Goldschein, NECA, to Adrian Wright, FCC, dated July 16, 1998.

⁴⁰ *Id.*

⁴¹ *Id.*

⁴² Petition at 20.

18. IT IS FURTHER ORDERED, pursuant to sections 1, 4(i), 5(c), 201 and 202 of the Communications Act of 1934, as amended, 47 U.S.C. §§ 151, 154(i), 155(c), 201 and 202, and sections 0.91, 0.291, and 1.3 of the Commission's rules, 47.C.F.R. §§ 0.91, 0.291, and 1.3, that this Order IS EFFECTIVE IMMEDIATELY UPON RELEASE.

FEDERAL COMMUNICATIONS COMMISSION



Lisa S. Gelb
Chief, Accounting Policy Division
Common Carrier Bureau