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
	)	
Access Charge Reform	)	CC Docket No. 96-262

REPLY COMMENTS OF BELL ATLANTIC[1] ON FURTHER NOTICE OF PROPOSED RULEMAKING

The comments in this and the related model-input inquiry again make clear what is obvious to any party that has followed the efforts to create a national forward looking proxy cost model – the model does not work. Spending additional resources on "improving" the model is like spending hours shining the headlights on an Edsel – in the end it is still junk. Instead, the Commission should join the commenters in acknowledging that the model is so overly complex and its output so skewed that it is unsalvageable as a public policy tool.

The model also is unnecessary. Because the Commission was only considering applying the model as a way to distribute the high cost fund of the non-rural local exchange carriers, the model was only going to be used to address a small portion of the universal service pie. Those dollars could be reasonably allocated using existing cost data instead.

At the same time, the Commission should resist the siren song that subscriber line charges should be reduced. Shifting the cost recovery burden to access charges does not

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1 The Bell Atlantic telephone companies ("Bell Atlantic") are Bell Atlantic-Delaware, Inc.; Bell Atlantic-Maryland, Inc.; Bell Atlantic-New Jersey, Inc.; Bell Atlantic-Pennsylvania, Inc.; Bell Atlantic-Virginia, Inc.; Bell Atlantic-Washington, D.C., Inc.; Bell Atlantic-West Virginia, Inc.; New York Telephone Company; and New England Telephone and Telegraph Company.

free consumers from paying. Quite the contrary, consumers end up paying more through a multiplicity of charges that are passed through by long distance carriers, with a generous dollop of added charges on top. Consolidating the charges into a single subscriber line charge minimizes the total charge, and provides a safety net for low income consumers by extending the benefit of Lifeline protection to all of those charges, so that those consumers most in need get a true rate reduction.

I. The Commission Should Abandon The Flawed Proxy Model

In the accompanying inquiry, Bell Atlantic and other commenters highlighted the numerous and substantial errors in the current model foundation and inputs. *See, e.g.*, Model Comments of Sprint Corp. at 3 ("There are significant errors in certain of the input methodologies that will affect all companies"); Model Comments of the Rural Telephone Coalition (the coalition is aware of "alarming discrepancies" when comparing model results to "actual" forward looking cost data).

As a result, in this proceeding -- in which commenters were asked to apply those results in order to size and distribute a universal service fund for non-rural local exchange carriers -- there is no consensus as to the other policy parameters, which are themselves dependent on the uncertain results of an, as yet, deeply flawed and unfinished model.

In fact, the comments evidenced growing recognition that the flaws in the model are more fundamental than a simple matter of correcting a few individual inputs. For example, MCI acknowledges that the proposed model "is a blunt, inflexible instrument, incapable of achieving its stated goals in a rational manner." MCI Comments at 18.

The model results also cannot be squared with the Commission's policy conclusion that the fund size should not increase substantially. As the New York Commission explained:

> "Combinations that achieve the Commission's expectations that current funding need not increase appear to provide funding to a mere handful of study areas, and combinations that provide more reasonable distributions among study areas produce unacceptably large funds."

New York Comments at 4. The New York Commission recognized the true source of the problem; the results of the model are "skewed" and as a result the model is not useful for even the limited purpose for which the Commission seeks to rely on it. *Id.*[2]

Because of these fundamental flaws, the New York Commission and numerous other commenters point out that the only rational choice at this point is to "continue to use existing cost for determining high cost funding." New York Comments at 5. As Bell Atlantic explained in its comments on the model inputs, the Commission should apply the existing state-wide costs and translate that support to a per-line amount that either the incumbent local exchange carrier or a new entrant would be entitled to receive for each qualified line it serves. This per-line amount could be disaggregated within a state to the extent that a state has adopted zones with deaveraged unbundled network elements. *See* Bell Atlantic Model Comments at 5.

If the Commission nevertheless seeks to apply some future version of the model results here (which it should not), at the very least it must limit the potential harmful impact

[2] Even if the Commission lawfully could rely on a model that had been shown to be accurate and reliable, it would be arbitrary and capricious to rely on a model that was shown to be inaccurate or unreasonable. *See Chemical Manufacturers Association v. EPA*, 28 F.3d 1259, 1265 (D.C. Cir. 1994) (courts will reverse the application of a regulatory agency model to a party where there is evidence of "a poor fit between the agency's model and that party's reality").

by using it only to *distribute* a pre-set fund amount, and must limit the model to calculating costs measured at the study area level. Because of averaging at the study area level, many of the model's most egregious errors are masked. *See* Bell Atlantic Comments at 5-6. Moreover, running the model at the study area level is more consistent with the Act because it "continues to recognize state responsibility for affordable and reasonably comparable rates." California Comments at 12.

II. Artificial Limits on the Subscriber Line Charge Do Not Benefit Consumers

Several commenters argue that the Commission should place artificial limits on the amount of common line costs that can be recovered through subscriber line charge ("SLC"), and force carriers to recover those common line costs through other rate elements. *See* Comments of the State Members; Joint Comments of Texas Office of Public Utility Counsel, *et. al* ("Joint Comments"). But while these proposals are based on consumer protection theories, the supposed benefits are completely illusory. If common line costs are not recovered through a SLC, then they must be recovered in some other rate and the resulting burden to individual rate payers actually would be greater than if it were a simple single charge.

Today, the Presubscribed Interexchange Carrier Charge ("PICC") – the per-line common line charge imposed on long distance carriers -- is being passed through directly to consumers as an end-user charge on their long distance bill (typically with an added amount to pad the coffers of the long distance carriers thrown in for good measure). As a result, consumers get no benefit from recovering costs through a charge to long distance carriers rather than directly through the SLC. Indeed, the way long distance carriers have been "passing through" the PICC, consumers actually pay a *higher* per-line rate than they would if the cost recovery had been through a SLC instead. For example, when the FCC raised the PICC to just over one dollar for primary residential lines, AT&T raised its fee to over $1.50.

Similarly, recovering common line costs through a per-minute carrier charge (rather than a flat rate charge) would provide no real benefit to consumers. The higher per-minute rates are passed through in the form of higher long distance charges. Moreover, the Commission has repudiated the former practice of collecting the fixed per-line common line costs on a per-minute basis. *See Access Charge Reform*, 12 FCC Rcd 15982, ¶¶ 102-105 (1997). This move is consistent with economic policy judgments that the Commission has long recognized. *MTS and WATS Market Structure*, 97 FCC 2d 682, 686 (1983) (movement toward charging common line cost as a flat end user charge will "enable our society to maximize its efficient use of the telecommunications network and realize the benefits possible from increasing competition in the interexchange marketplace").

In contrast, consolidating common line charges into a single end user charge by the local exchange carrier provides a simple and direct way to recover common line costs. Such a shift has been proposed by an industry coalition made up of local exchange and long distance carriers. *See ex parte* letter from John Nakata, CC Docket Nos. 96-45, 96-262, 94-1, 99-249 (filed July 29, 1999). Moreover, under that proposal, these consolidated charges will be deaveraged and combined with additional universal service coverage for high cost lines. For that reason, there will be new economic incentives for residential competition, especially in higher cost areas where current pricing rules have discouraged new entrants. As one financial analyst explained, this proposal creates a "much bigger opportunity in the local residential market." Sanford Bernstein Report by Todd Jacobs (rel. Aug. 3, 1999). Further, provided they are passed through in long distance rates, the reduction in per-minute charges will reduce the incremental cost of long distance calling, thereby spurring greater use of the network and enhancing consumer welfare.[3]

The shift from a PICC to a consolidated SLC has the added advantage of allowing the Commission to extend its existing Lifeline protection to cover all of the common line charges, thereby reducing the overall cost to those low income customers for whom affordability is of greatest concern. These customers also reap the benefit of lower long distance charges made possible by consolidating common line charges into a single end-user charge. Even for those customers that do not qualify for Lifeline protection, an increased SLC would not impose an unreasonable cost recovery burden on the end user. Under the industry coalition proposal, the SLC would still be subject to a dual limitation. While the overall cap would increase, the SLC would also be capped based on actual common line costs. No customer would pay SLCs above the common line costs for their jurisdiction. As a result, there is no disproportionate burden that would be borne by individual consumers.

The state joint board members argue that some portion of the common line cost should be imposed on other services that need to use the loop to complete the call. But this view of cost allocation is inconsistent with sound economic principles. As Professor Alfred Kahn has explained:

> "Consumers impose the non-traffic-sensitive costs of the loop on a telephone company and on society by the act of subscribing to telephone service—or to basic universal service, as the Commission has defined it. The costs of the loop are emphatically not a joint cost of supplying

[3] There is no reason to expect higher SLC caps to have a negative impact on subscribership levels. Even though the PICC was passed on to consumers in amounts that exceeded what the long distance carriers were paying, subscribership has actually increased in the period since that charge was put in place. *See* FCC Telephone Penetration Statistics (rel. Feb. 1999).

> subscriber dial tone, custom calling features, local or long distance calling."

Rebuttal Testimony of Alfred E. Kahn Before the Pennsylvania Public Utilities Commission at 4, Formal Investigation To Examine And Establish Updated Universal Service Principles And Policies For Telecommunications Services, Docket No. I-00940035 (filed Jan 19, 1998).

Section 254 does not change that basic economic truth. Section 254(k) simply says that services included in the definition of universal service should bear no more than a reasonable share of joint and common costs of facilities used to provide those services. But as Professor Kahn has explained, the costs of the loop are *not* joint and common costs of providing other services. In fact, under current structures, where common line costs are included in switched access rates, even in areas subject to a high degree of competition, the subsidy has flowed the other way. Regardless, imposing the full cost of the common line on the cost causer is not inconsistent with the statutory command.

The Joint Commenters go even further and argue that the current SLC over-recovers the cost of providing service. Given that the local exchange carriers' common line costs serve as a cap on all SLC rates, the only way they can make that argument is to ignore actual costs. Instead, they rely on the output of the Commission's model as a proxy for the actual cost of providing service. But aside from the fact that the model doesn't do what it is intended to do, it was never intended for the purpose of determining cost-based pricing. As the Chief of the Common Carrier Bureau explained at the last open meeting discussion concerning universal service, "I want to emphasize that this model is not going to be used to be setting any prices. This is being used simply to understand what support levels might be necessary for universal service. It is not setting prices." Remarks of Larry Strickling, Chief of the Common Carrier Bureau, on May 27, 1999 Open Meeting, Agenda Items 1 and 2.

It is for good reason that the Commission has disclaimed use of the model to set prices.[4] The costs projected by the model – even if they were consistent with the intended purpose, which they are not – are not the cost of the incumbent carrier, but rather the costs of some hypothetical super-efficient new entrant. Indeed, as one Court has explained, the model posits a "mythical" network limited only by the imagination of its designers. *See U.S. West Communications, Inc., v. Renz D. Jennings*, 1999 U.S. Dist. LEXIS 6821 (rel. May 5, 1999), p. 5. It would be completely arbitrary to rely on those theoretical costs to set cost recovery levels for an incumbent carrier with a pre-existing network and real costs that were far in excess of those model results.

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[4] Instead, for rate regulation the Commission has continued to rely on historical cost levels to set rates. Indeed, in rejecting a replacement-cost methodology for cable-television rates, the Commission confirmed that "[o]riginal cost is the normal, now traditional method used for public utility valuation." *Implementation of Sections of the Cable Television Consumer Protection and Competition Act of 1992; Rate Regulation*, Report and Order and Further Notice of Proposed Rulemaking, 9 FCC Rcd 4527, ¶ 55 (1994).

Conclusion

The Commission should abandon its failed cost model and reject calls to artificially limit the SLC.

Respectfully submitted,

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