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August 5, 1999

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FEDERAL COMMUNICATIONS COMMISSION  
OFFICE OF THE SECRETARY

Ms. Magalie Roman Salas  
Secretary  
Federal Communications Commission  
445 Twelfth Street, S.W.  
Washington, D.C. 20554

RE: Ex Parte  
CC Docket No. 98-166 / Prescribing the Authorized Unitary ROR

Dear Ms. Salas:

On August 3, 1999, I presented the attached analyses to Anthony Dale, Tom David, George Williams, Richard Robinson, William Davenport, Gary Seigel, Louise Klees-Wallace and Andy Mulitz of the Common Carrier Bureau's Accounting Safeguards or Enforcement Divisions. These analyses of the impact on universal service, access and UNE interconnection rates from resetting the authorized interstate rate of return to the current cost of capital are provided illustratively for the entire nonrural LEC industry. If the Commission accepts the proposed coalition agreement on interstate access charges and implicit universal service support, changes in the signatories' interstate access charges or calculations of universal service support to replace support implicit in access charges based on changes in the authorized rate of return would be unnecessary.

Two copies of this Notice are being submitted to the Secretary of the FCC in accordance with Section 1.1206(a)(2) of the Commission's rules.

Sincerely,

*Richard N. Clarke / ha*

Richard N. Clarke

Attachments

cc: Anthony Dale	Tom David	George Williams
Richard Robinson	William Davenport	Louise Klees-Wallace
Gary Seigel	Andy Mulitz	

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# Effects of Resetting the Allowed Interstate Rate of Return to the Nonrural LECs' Cost of Capital

## *1 Universal Service Support*

Currently, the FCC's Synthesis Model for calculating the forward-looking economic cost of basic local service assumes that the nonrural LECs' forward-looking cost of capital equals their currently allowed rate-of-return of 11.25%, set in CC Docket 89-624 (adopted September 19, 1990 and effective January 1, 1991). AT&T has demonstrated in its March 16, 1999 submission in CC Docket 98-166, that the current forward-looking cost of capital to incumbent LECs is, roughly, 8.64%.

If input values to the Commission's 6/2/99 release of the FCC's Synthesis Model are adjusted to reflect this current figure for the incumbent LEC cost of capital, the Synthesis Model's calculated average monthly basic service cost for the nonrural LECs would decline by 10.3%. In general, calculations of required universal service support vary even more dramatically with changes in calculated monthly basic service costs. If, for illustrative purposes, one uses the old federal universal service support calculation embedded in the density zone expense module of the 6/2/99 release of the FCC's Synthesis Model, this projects a 25.7% decline in federal universal service support if the nonrural LECs' cost of capital is reset to 8.64%.

## *2 Interstate Access Charges*

Price cap indicies controlling the nonrural LECs' interstate access rates currently reflect the Commission's stale 11.25% cost of capital – adjusted for intervening changes in GDP-PI. But because the LECs are, roughly, twice as capital-intensive as the average firm in the U.S. economy, GDP-PI adjustments implicit in the nonrural LECs' PCIs have reflected only half of the drop in these LECs' cost of capital since 1/1/91 (see, AT&T's Comments in CC Docket 94-1, filed 5/9/94). If the nonrural LECs' PCIs were adjusted to reflect fully the drop in their cost of capital, this would reduce their current PCIs by about \$650 million per year.<sup>1</sup>

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<sup>1</sup> Given current levels of tax gross-up factors, interstate revenues and average net investment of the nonrural LECs, each percentage point reduction in their allowed rate-of-return reduces their PCIs by about \$500 million. Taking half of the difference between 11.25% and 8.64%, and multiplying this figure by \$500 million yields an approximate annual reduction of \$650 million.

		Adjusted FCC Synthesis Model		
State	Company	Monthly Basic Service Cost @ 11.25% ROR	Monthly Basic Service Cost @ 8.64% ROR	Percent Diff
Alabama	Contel Of The South Db	\$61.00	\$53.18	-12.8%
Alabama	Gte And Contel Of Alabama	\$45.83	\$40.16	-12.4%
Alabama	South Central Bell-Al	\$30.49	\$27.13	-11.0%
Arkansas	Southwestern Bell-Arkansas	\$28.52	\$25.29	-11.3%
Arizona	Mountain Bell-Arizona	\$18.84	\$16.98	-9.8%
California	Contel Of California - California	\$37.22	\$32.75	-12.0%
California	Gte Of California	\$16.64	\$15.08	-9.4%
California	Pacific Bell	\$16.33	\$14.82	-9.2%
California	Roseville Telephone Company	\$18.31	\$16.56	-9.6%
Colorado	Mountain Bell-Colorado	\$21.44	\$19.29	-10.0%
Connecticut	Southern New England Tel	\$19.92	\$17.96	-9.9%
Dist of Columbia	C And P Telephone Company Of Wa Dc	\$12.09	\$11.17	-7.5%
Delaware	Diamond State Tel Co	\$19.93	\$17.93	-10.0%
Florida	Central Tel Co Of Florida	\$26.33	\$23.41	-11.1%
Florida	Gte Floridainc	\$17.86	\$16.16	-9.5%
Florida	Southern Bell-FI	\$17.97	\$16.22	-9.7%
Florida	United Tel Co Of Florida	\$22.13	\$19.80	-10.5%
Georgia	Southern Bell-Ga	\$22.48	\$20.16	-10.3%
Hawaii	Gte Hawaiian Telephone Co Inc	\$17.02	\$15.38	-9.6%
Iowa	Northwestern Bell-Ia	\$22.16	\$19.84	-10.5%
Idaho	Mountain Bell-Idaho	\$26.69	\$23.71	-11.1%
Illinois	Central Tel Co Of Il	\$17.98	\$16.24	-9.6%
Illinois	Contel Of Illinois Inc Db	\$52.05	\$45.48	-12.6%
Illinois	Gte Of Illinois	\$37.27	\$32.80	-12.0%
Illinois	Illinois Bell Tel Co	\$16.39	\$14.90	-9.1%
Indiana	Contel Of Indiana Inc Db	\$48.72	\$42.69	-12.4%
Indiana	Gte Of Indiana	\$28.21	\$25.08	-11.1%
Indiana	Indiana Bell Tel Co	\$21.58	\$19.40	-10.1%
Kansas	Southwestern Bell-Kansas	\$24.13	\$21.51	-10.9%
Kentucky	Cincinnati Bell-Ky	\$25.68	\$22.89	-10.9%
Kentucky	Gte South Inc - Kentucky	\$33.20	\$29.34	-11.6%
Kentucky	South Central Bell-Ky	\$31.19	\$27.59	-11.5%
Louisiana	South Central Bell-La	\$25.47	\$22.66	-11.0%
Massachusetts	New England Tel-Ma	\$17.01	\$15.40	-9.5%
Maryland	C And P Tel Co Of Md	\$18.77	\$16.93	-9.8%
Maine	New England Tel-Maine	\$31.16	\$27.54	-11.6%
Michigan	Gte North Inc-Mi	\$39.95	\$35.15	-12.0%
Michigan	Michigan Bell Tel Co	\$20.06	\$18.07	-9.9%
Minnesota	Contel Of Minnesota Inc Db	\$68.83	\$59.75	-13.2%
Minnesota	Northwestern Bell-Minnesota	\$21.62	\$19.38	-10.3%
Missouri	Contel Missouri Db	\$58.77	\$51.33	-12.7%
Missouri	Gte North Inc - Missouri	\$40.91	\$35.95	-12.1%
Missouri	Southwestern Bell-Missouri	\$22.51	\$20.17	-10.4%
Mississippi	South Central Bell-Mississippi	\$40.70	\$35.84	-11.9%
Montana	Mountain Bell-Montana	\$31.77	\$28.01	-11.8%
North Carolina	Carolina Tel And Tel Co	\$35.03	\$30.92	-11.7%
North Carolina	Central Tel Co-Nc	\$33.91	\$29.96	-11.7%
North Carolina	Contel Of North Carolina Db	\$45.61	\$40.02	-12.3%
North Carolina	Gte South Inc - North Carolina	\$21.19	\$19.07	-10.0%
North Carolina	North State Tel Co-Nc	\$21.40	\$19.24	-10.1%
North Carolina	Southern Bell-Nc	\$22.59	\$20.28	-10.2%
North Dakota	Northwestern Bell-North Dakota	\$25.77	\$22.89	-11.2%
Nebraska	Lincoln Tel And Tele Co	\$33.16	\$29.21	-11.9%
Nebraska	Northwestern Bell-Nebraska	\$26.52	\$23.78	-10.3%
New Hampshire	New England Tel-Nh	\$24.91	\$22.22	-10.8%
New Jersey	New Jersey Bell	\$15.68	\$14.26	-9.1%
New Mexico	Mountain Bell-New Mexico	\$24.85	\$22.17	-10.8%
Nevada	Central Telephone Company - Nevada	\$14.96	\$13.60	-9.0%

		Adjusted FCC Synthesis Model		
State	Company	Monthly Basic Service Cost @ 11.25% ROR	Monthly Basic Service Cost @ 8.64% ROR	Percent Diff
Nevada	Nevada Bell	\$25.14	\$22.25	-11.5%
New York	New York Tel	\$16.81	\$15.19	-9.7%
New York	Rochester Telephone Corp	\$19.72	\$17.69	-10.3%
Ohio	Cincinnati Bell-Ohio	\$18.08	\$16.32	-9.8%
Ohio	Gte North Inc-Oh	\$38.39	\$33.82	-11.9%
Ohio	Ohio Bell Tel Co	\$18.44	\$16.67	-9.6%
Ohio	United Tel Co Of Ohio	\$33.79	\$29.88	-11.6%
Oklahoma	Gte Southwest Inc - Oklahoma	\$36.25	\$31.95	-11.9%
Oklahoma	Southwestern Bell-Oklahoma	\$26.10	\$23.20	-11.1%
Oregon	Gte Of The Northwest	\$24.86	\$22.15	-10.9%
Oregon	Pacific Northwest Bell-Oregon	\$20.90	\$18.77	-10.2%
Pennsylvania	Bell Of Pennsylvania	\$18.48	\$16.68	-9.8%
Pennsylvania	Gte North Inc-Pa And Contel	\$27.93	\$24.81	-11.2%
Rhode Island	New England Tel-Ri	\$18.07	\$16.31	-9.7%
South Carolina	Gte South Inc - South Carolina	\$30.67	\$27.15	-11.5%
South Carolina	Southern Bell-Sc	\$26.04	\$23.19	-11.0%
South Dakota	Northwestern Bell-South Dakota	\$28.93	\$25.58	-11.6%
Tennessee	South Central Bell-Tn	\$26.34	\$23.48	-10.8%
Tennessee	United Inter-Mountain Tel Co-Tn	\$28.10	\$24.97	-11.1%
Texas	Central Telephone Company Of Texas	\$32.47	\$28.69	-11.6%
Texas	Contel Of Texas Inc DbA Gte Texas	\$67.67	\$58.82	-13.1%
Texas	Gte Southwest Inc - Texas	\$28.65	\$25.42	-11.3%
Texas	Southwestern Bell-Texas	\$20.05	\$18.02	-10.1%
Utah	Mountain Bell-Utah	\$19.45	\$17.58	-9.6%
Virginia	C And P Tel Co Of Va	\$20.15	\$18.12	-10.1%
Virginia	Central Tel Co Of Va	\$44.63	\$39.13	-12.3%
Virginia	Contel Of Virginia Inc DbA Gte Virginia	\$34.54	\$30.50	-11.7%
Virginia	United Inter-Mountain Tel Co-Va	\$47.79	\$41.85	-12.4%
Vermont	New England Tel-Vt	\$33.36	\$29.46	-11.7%
Washington	Gte Northwest Inc - Washington	\$23.09	\$20.65	-10.6%
Washington	Pacific Northwest Bell-Washington	\$19.24	\$17.36	-9.8%
Wisconsin	Gte North Inc-Wi	\$47.12	\$41.25	-12.5%
Wisconsin	Wisconsin Bell	\$19.68	\$17.74	-9.8%
West Virginia	C And P Tel Co Of W Va	\$36.11	\$31.82	-11.9%
Wyoming	Mountain Bell-Wyoming	\$35.69	\$31.28	-12.3%
	<i>Weighted Average</i>	\$21.19	\$19.01	-10.3%
	<i>Min</i>	\$12.09	\$11.17	-7.5%
	<i>Max</i>	\$68.83	\$59.75	-13.2%
	<i>Median</i>	\$25.68	\$22.89	-10.9%

**Notes:** "Adjusted FCC Synthesis Model" is 6/2/99 release with CCCFactor calculation references corrected.

"Monthly Basic Service Cost" is from cell USF!M38 in DZ expense module of the Synthesis Model.

"Illustrative Federal USF Support" is from cell USF!M60 in DZ expense module of the Synthesis Model.

It uses an old calculation methodology that sets federal support at 25% of the residual between the modeled basic service cost and \$31 for residence lines and \$51 for business lines.

## Adjusted FCC Synthesis Model

State	Company	Illustrative Federal	Illustrative Federal	Percent Diff
		USF Support @ 11.25% ROR	USF Support @ 8.64% ROR	
Alabama	Contel Of The South DbA Gte South	\$10,994,178	\$8,554,708	-22.2%
Alabama	Gte And Contel Of Alabama	\$8,574,160	\$6,695,790	-21.9%
Alabama	South Central Bell-Al	\$34,360,682	\$25,585,014	-25.5%
Arkansas	Southwestern Bell-Arkansas	\$18,161,987	\$13,769,438	-24.2%
Arizona	Mountain Bell-Arizona	\$8,703,956	\$6,426,243	-26.2%
California	Contel Of California - California	\$10,854,442	\$8,373,987	-22.9%
California	Gte Of California	\$5,784,387	\$4,148,151	-28.3%
California	Pacific Bell	\$30,120,642	\$21,627,604	-28.2%
California	Roseville Telephone Company	\$4,880	\$0	-100.0%
Colorado	Mountain Bell-Colorado	\$16,190,532	\$12,032,420	-25.7%
Connecticut	Southern New England Tel	\$3,020,964	\$1,624,970	-46.2%
Dist of Columbia	C And P Telephone Company Of Wa Dc	\$0	\$0	0.0%
Delaware	Diamond State Tel Co	\$2,458,678	\$1,613,990	-34.4%
Florida	Central Tel Co Of Florida	\$6,385,197	\$4,813,199	-24.6%
Florida	Gte Floridainc	\$1,869,847	\$1,147,917	-38.6%
Florida	Southern Bell-FI	\$10,032,305	\$6,992,327	-30.3%
Florida	United Tel Co Of Florida	\$7,291,020	\$5,100,560	-30.0%
Georgia	Southern Bell-Ga	\$28,679,528	\$20,657,538	-28.0%
Hawaii	Gte Hawaiian Telephone Co Inc	\$903,345	\$628,627	-30.4%
Iowa	Northwestern Bell-Ia	\$11,467,084	\$8,630,024	-24.7%
Idaho	Mountain Bell-Idaho	\$8,712,772	\$6,554,459	-24.8%
Illinois	Central Tel Co Of Il	\$1,140,542	\$842,105	-26.2%
Illinois	Contel Of Illinois Inc DbA Gte - Illinois	\$12,712,602	\$9,944,106	-21.8%
Illinois	Gte Of Illinois	\$23,720,950	\$18,427,731	-22.3%
Illinois	Illinois Bell Tel Co	\$9,045,358	\$6,426,602	-29.0%
Indiana	Contel Of Indiana Inc DbA Gte - Indiana	\$10,373,518	\$8,147,081	-21.5%
Indiana	Gte Of Indiana	\$11,309,542	\$8,195,127	-27.5%
Indiana	Indiana Bell Tel Co	\$12,696,444	\$9,099,445	-28.3%
Kansas	Southwestern Bell-Kansas	\$16,934,915	\$13,250,139	-21.8%
Kentucky	Cincinnati Bell-Ky	\$1,983,737	\$1,422,103	-28.3%
Kentucky	Gte South Inc - Kentucky	\$12,462,846	\$9,461,390	-24.1%
Kentucky	South Central Bell-Ky	\$27,772,001	\$20,768,470	-25.2%
Louisiana	South Central Bell-La	\$29,177,850	\$21,636,134	-25.8%
Massachusetts	New England Tel-Ma	\$4,156,013	\$2,408,416	-42.0%
Maryland	C And P Tel Co Of Md	\$9,204,782	\$5,977,254	-35.1%
Maine	New England Tel-Maine	\$14,622,396	\$10,774,591	-26.3%
Michigan	Gte North Inc-Mi	\$24,528,623	\$17,855,669	-27.2%
Michigan	Michigan Bell Tel Co	\$23,139,260	\$16,101,630	-30.4%
Minnesota	Contel Of Minnesota Inc DbA Gte Minnesota	\$12,952,862	\$10,137,564	-21.7%
Minnesota	Northwestern Bell-Minnesota	\$20,884,224	\$15,824,132	-24.2%
Missouri	Contel Missouri DbA Gte Missouri	\$20,957,362	\$16,633,689	-20.6%
Missouri	Gte North Inc - Missouri	\$5,531,641	\$4,355,820	-21.3%
Missouri	Southwestern Bell-Missouri	\$23,291,739	\$17,638,903	-24.3%
Mississippi	South Central Bell-Mississippi	\$54,922,095	\$42,959,673	-21.8%
Montana	Mountain Bell-Montana	\$9,615,687	\$7,480,875	-22.2%
North Carolina	Carolina Tel And Tel Co	\$29,902,243	\$21,990,000	-26.5%
North Carolina	Central Tel Co-Nc	\$5,691,431	\$4,051,293	-28.8%
North Carolina	Contel Of North Carolina DbA Gte No Carolina	\$6,477,999	\$4,661,396	-28.0%
North Carolina	Gte South Inc - North Carolina	\$841,910	\$516,665	-38.6%
North Carolina	North State Tel Co-Nc	\$312,359	\$161,749	-48.2%
North Carolina	Southern Bell-Nc	\$13,147,168	\$8,598,228	-34.6%
North Dakota	Northwestern Bell-North Dakota	\$5,288,698	\$4,270,774	-19.2%
Nebraska	Lincoln Tel And Tele Co	\$8,346,768	\$6,602,080	-20.9%
Nebraska	Northwestern Bell-Nebraska	\$8,236,084	\$6,640,640	-19.4%
New Hampshire	New England Tel-Nh	\$7,731,694	\$5,398,021	-30.2%
New Jersey	New Jersey Bell	\$2,323,678	\$1,202,972	-48.2%
New Mexico	Mountain Bell-New Mexico	\$9,230,888	\$7,019,584	-24.0%
Nevada	Central Telephone Company - Nevada	\$602,610	\$440,559	-26.9%

## Adjusted FCC Synthesis Model

State	Company	Adjusted FCC Synthesis Model		Percent Diff
		Illustrative Federal USF Support @ 11.25% ROR	Illustrative Federal USF Support @ 8.64% ROR	
Nevada	Nevada Bell	\$4,415,886	\$3,374,516	-23.6%
New York	New York Tel	\$33,011,034	\$23,317,156	-29.4%
New York	Rochester Telephone Corp	\$2,490,127	\$1,697,948	-31.8%
Ohio	Cincinnati Bell-Ohio	\$747,255	\$387,523	-48.1%
Ohio	Gte North Inc-Oh	\$29,156,064	\$21,635,300	-25.8%
Ohio	Ohio Bell Tel Co	\$10,744,747	\$7,404,724	-31.1%
Ohio	United Tel Co Of Ohio	\$14,243,715	\$10,054,182	-29.4%
Oklahoma	Gte Southwest Inc - Oklahoma	\$3,834,376	\$3,006,031	-21.6%
Oklahoma	Southwestern Bell-Oklahoma	\$26,149,775	\$20,074,713	-23.2%
Oregon	Gte Of The Northwest	\$5,641,060	\$4,236,724	-24.9%
Oregon	Pacific Northwest Bell-Oregon	\$10,013,227	\$7,279,524	-27.3%
Pennsylvania	Bell Of Pennsylvania	\$17,981,557	\$12,368,789	-31.2%
Pennsylvania	Gte North Inc-Pa And Contel	\$7,731,188	\$5,424,210	-29.8%
Rhode Island	New England Tel-Ri	\$595,880	\$284,429	-52.3%
South Carolina	Gte South Inc - South Carolina	\$3,618,455	\$2,761,922	-23.7%
South Carolina	Southern Bell-Sc	\$16,083,706	\$11,328,313	-29.6%
South Dakota	Northwestern Bell-South Dakota	\$6,848,053	\$5,459,193	-20.3%
Tennessee	South Central Bell-Tn	\$34,455,862	\$24,936,926	-27.6%
Tennessee	United Inter-Mountain Tel Co-Tn	\$2,977,640	\$2,024,856	-32.0%
Texas	Central Telephone Company Of Texas	\$4,986,652	\$3,905,665	-21.7%
Texas	Contel Of Texas Inc Dbg Gte Texas	\$25,423,517	\$20,220,451	-20.5%
Texas	Gte Southwest Inc - Texas	\$28,221,579	\$22,060,361	-21.8%
Texas	Southwestern Bell-Texas	\$53,360,061	\$39,845,217	-25.3%
Utah	Mountain Bell-Utah	\$3,774,209	\$2,792,574	-26.0%
Virginia	C And P Tel Co Of Va	\$22,343,204	\$16,167,063	-27.6%
Virginia	Central Tel Co Of Va	\$14,773,469	\$11,408,138	-22.8%
Virginia	Contel Of Virginia Inc Dbg Gte Virginia	\$14,900,534	\$11,093,555	-25.5%
Virginia	United Inter-Mountain Tel Co-Va	\$5,994,027	\$4,601,456	-23.2%
Vermont	New England Tel-Vt	\$9,863,590	\$7,346,230	-25.5%
Washington	Gte Northwest Inc - Washington	\$5,518,444	\$4,094,658	-25.8%
Washington	Pacific Northwest Bell-Washington	\$9,133,093	\$6,653,089	-27.2%
Wisconsin	Gte North Inc-Wi	\$26,457,741	\$20,391,390	-22.9%
Wisconsin	Wisconsin Bell	\$8,980,844	\$6,287,554	-30.0%
West Virginia	C And P Tel Co Of W Va	\$26,568,709	\$20,363,907	-23.4%
Wyoming	Mountain Bell-Wyoming	\$7,608,243	\$5,964,925	-21.6%
	<i>Sum</i>	\$1,214,488,626	\$902,552,783	-25.7%
	<i>Min</i>	\$0	\$0	0.0%
	<i>Max</i>	\$54,922,095	\$42,959,673	-21.8%
	<i>Median</i>	\$9,615,687	\$7,019,584	-27.0%

**Notes:** "Adjusted FCC Synthesis Model" is 6/2/99 release with CCCFactor calculation references corrected.

"Monthly Basic Service Cost" is from cell USF!M38 in DZ expense module of the Synthesis Model.

"Illustrative Federal USF Support" is from cell USF!M60 in DZ expense module of the Synthesis Model.

It uses an old calculation methodology that sets federal support at 25% of the residual between the modeled basic service cost and \$31 for residence lines and \$51 for business lines.